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Policy issues for the Asia-Pacific region: inclusive and sustainable economic and social development in Asia and the Pacific through regional economic cooperation and integration

Enhancing regional economic cooperation and integration in Asia and the Pacific

Note by the secretariat

Summary

The Economic and Social Commission for Asia and the Pacific endorsed the Bangkok Declaration on Regional Economic Cooperation and Integration in Asia and the Pacific in its resolution 70/1. In the Declaration, it was recognized, inter alia, that progress had been made by regional groupings and organizations in integrating their subregions, and an agenda was proposed aimed at deepening and broadening economic cooperation and integration in Asia and the Pacific. The agenda consisted of four elements: (a) moving towards the formation of an integrated market, (b) developing seamless connectivity in the region, (c) enhancing financial cooperation, and (d) increasing economic cooperation to address shared vulnerabilities and risks.

In addition to providing a brief overview of the progress so far and lessons learned, the present document includes a discussion of how regional economic cooperation and integration can support the implementation of the 2030 Agenda for Sustainable Development, an assessment of the key challenges to further pursuing regional economic cooperation and integration, and recommendations on the way forward.

The Commission may wish to consider the recommendations contained in this document and provide guidance to the region on how to deepen regional economic cooperation and integration while maximizing the benefits of its synergies with the 2030 Agenda and on how the secretariat could support those efforts.

* E/ESCAP/73/L.1.

I. Introduction

1. At the first Ministerial Conference on Regional Economic Cooperation and Integration in Asia and the Pacific in December 2013, Ministers, senior policymakers, and representatives of members and associate members of the Economic and Social Commission for Asia and the Pacific (ESCAP) adopted the Bangkok Declaration on Regional Economic Cooperation and Integration in Asia and the Pacific. The Bangkok Declaration set an agenda for regional economic cooperation and integration in the Asia-Pacific region consisting of four elements: (a) moving towards the formation of an integrated market, (b) developing seamless connectivity in the region, (c) enhancing financial cooperation, and (d) increasing economic cooperation to address shared vulnerabilities and risks.

2. Thus envisaged, regional economic cooperation and integration is both a multidimensional concept and a process that facilitates shared prosperity through an increased flow of goods, services, capital and people by supporting the development and strengthening of national institutions through the exchange of information, technical assistance and capacity-building and by helping countries coordinate policies and institutional arrangements.

3. Although the overall level of economic integration of the Asia-Pacific region as a whole is relatively high – similar to that of the Americas but lower than in Europe – there is wide variation across its subregions, and East and South-East Asia are the most integrated.¹ Such variations reflect traditional drivers of integration, such as contiguous borders, historical roots and ties, common languages and geography. However, these traditional drivers are enabling and not determining factors for economic cooperation and integration. In particular, the expansion of global value chains and cross-border investment flows, supported by appropriate national trade and commercial policies, can provide enormous opportunities for countries in the region to transcend constraints on their development that are based on geography or small domestic markets. A major goal of regional economic cooperation and integration is to make such opportunities available to all countries throughout the Asia-Pacific region.

4. Further motivation for pursuing regional economic cooperation and integration in the region is driven by the rising importance of Asia-Pacific economies relative to the advanced economies of North America and Europe. This is noticeable when looking at shares of global gross domestic product (GDP). In the period 2001-2005, North America and Western Europe represented 46.3 per cent of world GDP, compared to 27.1 per cent for the ESCAP region. But during the period 2011-2015, the two regions had a similar share of the world GDP: 36.3 per cent for North America and Western Europe and 36.1 per cent for the ESCAP region; approximately \$27 trillion each. With this trend, the Asia-Pacific region is well on its way to becoming the largest market in the world, opening possibilities for further expansion of trade and investment within the region.

5. Recent developments in Europe and North America, such as the vote in the United Kingdom of Great Britain and Northern Ireland to leave the European Union, the withdrawal of the United States of America from the Trans-Pacific Partnership and moves to impose discriminatory increases in

¹ See ESCAP, *Enhancing regional economic cooperation and integration in Asia and the Pacific* (forthcoming).

import tariffs, clearly indicate an increase in protectionist trends for the traditional export markets of the Asia-Pacific region. These trends highlight the importance of strengthening domestic and regional demand. Such rebalancing strategies will require opening domestic markets to economies in the region, thus facilitating regional economic cooperation and integration. Pursuing such strategies, however, may have redistribution implications. Therefore, strong political will and widespread domestic ownership across different groups of stakeholders will remain an important driver of regional economic cooperation and integration.

6. A particularly important new driver of regional economic cooperation and integration in the region is the Belt and Road Initiative of the Government of China. The Initiative aims to promote a multimodal network by connecting road and rail routes with seaports and expanding energy networks through oil and gas pipelines and regional power grids, while extending International Trade Centre fibre-optic links from China through Central Asia and ultimately to Europe. The Belt and Road Initiative places a strong emphasis on the seamless connectivity component of regional economic cooperation and integration, particularly transport, energy, and information and communications technology (ICT) infrastructure. Building such infrastructure is essential for the region to make significant progress in the other components of regional economic cooperation and integration. For instance, without suitable roads linking neighbouring countries, the costs of trade can be prohibitive.

7. The Belt and Road Initiative will need to address other elements of regional economic cooperation and integration, including soft connectivity issues, such as trade and investment facilitation; trade liberalization measures, including lowering non-tariff barriers; financial cooperation to mobilize resources for sustainable infrastructure development; and addressing some shared vulnerabilities and risks by, for example, sharing information on epidemics. Thus, there are strong potential synergies between the Belt and Road Initiative and regional economic cooperation and integration, and it will be useful to discuss how these two initiatives should be operationalized so that they complement each other in the most effective way.

8. The enormous potential of regional economic cooperation and integration to generate income and employment opportunities also makes it a critical enabler of the 2030 Agenda for Sustainable Development in Asia and the Pacific. Such opportunities can contribute to several Sustainable Development Goals, such as Goal 8. A point worth highlighting is that Goal 8 calls for inclusive and sustainable economic growth and productive and decent work for all and not just economic expansion through trade and investment flows and infrastructure development. Thus, for regional economic cooperation and integration to be an effective enabler of the 2030 Agenda, sufficient attention will need to be paid to inclusiveness and sustainability.

9. The large investments in transport, energy and ICT infrastructure required by regional economic cooperation and integration can also contribute directly to Sustainable Development Goals 7 and 9 and their associated targets. For instance, the aim of target 9.1 is to develop quality, reliable, sustainable and resilient infrastructure, including regional and transborder infrastructure with a focus on affordable and equitable access for all. Similarly, regional economic cooperation and integration can also contribute to Goal 17, including target 17.1 (Strengthen domestic resource mobilization) and 17.11 (Significantly increase the exports of developing countries). Finally, the regional economic cooperation and integration

component on shared vulnerabilities can also help to enhance cooperation to address Goal 1, in particular target 1.5 (By 2030, build the resilience of the poor and those in vulnerable situations and reduce their exposure and vulnerability to climate-related extreme events and other economic, social and environmental shocks and disasters).

10. The relationship between regional economic cooperation and integration and the 2030 Agenda is, however, two way. Not only can regional economic cooperation and integration support the attainment of the Sustainable Development Goals, the Goals also have a vital role in guiding the implementation of regional economic cooperation and integration. This can happen, for instance, by ensuring that infrastructure projects have favourable social and environmental, as well as economic, impacts. Ensuring that infrastructure projects connect small, low-income and geographically distant countries with the main markets of the region and according high priority to addressing transboundary vulnerabilities and risks are other ways by which the 2030 Agenda can inform the question of how regional economic cooperation and integration can be most effectively implemented.

11. In a nutshell, stakeholders must remember that effectively pursuing the 2030 Agenda will require a fundamental rethinking of development policies and frameworks, as it requires a transition from growth-centric development to one that incorporates social and environmental considerations in an integrated manner. Such a conceptual transition needs to be complemented by a reinvigorated spirit of multilateralism and cooperation in the Asia-Pacific region. Thus, regional economic cooperation and integration and the 2030 Agenda should be pursued in an integrated manner so as to maximize coherence and coordination among policies and reforms that are required for their success.

12. The present document provides inputs for further deliberations on regional economic cooperation and integration by the Commission. The next section contains an overview of broad lessons from existing subregional economic cooperation and integration initiatives in Asia and the Pacific. The third section provides an overview of specific challenges in each of the four areas of regional economic cooperation and integration in the region. The final section includes some suggestions for broad recommendations on the way forward, for consideration by the Commission.

II. Lessons from existing subregional economic cooperation and integration initiatives in Asia and the Pacific

13. Most of the progress in regional economic cooperation and integration in the region has taken place through a wide variety of subregional initiatives, arrangements and bodies, which differ significantly in their extent, coverage, ambitions and implementation capabilities. Prominent examples include the Association of Southeast Asian Nations (ASEAN), the South Asian Association for Regional Cooperation (SAARC), the Pacific Islands Forum and the Eurasian Economic Union. Analysing their experiences is useful, as they provide broad lessons on advancing the agenda of regional economic cooperation and integration as stipulated in the Bangkok Declaration.

14. **Lesson 1: the progress and the sustainability of regional economic cooperation and integration initiatives are difficult to predict and guarantee.** Unlike in Europe, where regional cooperation and integration has steadily expanded to include more areas as well as deepen the process, in the Asia-Pacific region, and other parts of the world, subregional and regional

economic cooperation and integration initiatives have progressed in different phases and waves over the past several decades. Those phases have been influenced by, among other factors, changing ideas and attitudes towards globalization. Over the past two or three decades, trade and investment liberalization measures in several economies of the region gained momentum, as the potential of globalization to generate economic progress and raise living standards was increasingly recognized. Those policies paid off handsomely, leading to unprecedented economic growth and significant reductions in extreme poverty in the region. More recently, however, it has become increasingly evident that not everyone has enjoyed the benefits. Inequality has increased and continues to do so. Rising trade protectionism is one example of changing attitudes towards globalization and further integration. Thus, it is important to rearticulate the benefits of economic integration and cooperation, while introducing credible policy measures to address the concerns of vulnerable groups and countries. Linking regional economic cooperation and integration explicitly to the 2030 Agenda provides a useful framework for this purpose.

15. Lesson 2: the existence of overlapping organizations is costly in terms of political, human and financial resources. The region's approach to economic cooperation and integration has been pragmatic and flexible, following a gradual, incremental, multitrack, and multi-speed process. This approach has had many advantages, including avoiding a costly and restrictive bureaucracy and maintaining respect for countries' differing needs and sensitivities.² However, it has inadvertently led to many, often overlapping, bilateral and multilateral arrangements in terms of membership or functional areas, and there is a lack of coordination and consultation among the various regional and subregional bodies that organize such programs and initiatives. For instance, in the area of trade, the so-called "noodle bowl" of preferential trading arrangements has led to higher transaction costs due to a lack of clarity as to which agreements are most convenient for exporters, particularly for small and medium enterprises. Similar regulatory burdens and transaction costs have increased due to the plethora of infrastructure agreements and frameworks that have been finalized under various bilateral and subregional initiatives. In addition to the higher transaction costs for the private sector, the existence of multiple, overlapping arrangements has placed a heavy burden on the government agencies in charge of managing them. The diversion of scarce technical and governance resources for that purpose is particularly problematic for small and low-income developing countries. A major lesson from this experience is the need to move towards coordinating, streamlining and eventually consolidating existing initiatives and arrangements. This is a tall order but would be a step in the right direction.

16. Lesson 3: lack of delegation leads to suboptimal outcomes. Regional economic cooperation and integration is always very complex, but lack of delegation makes the challenges even more pronounced. Unlike the case of European integration, national Governments in the Asia-Pacific region have been reluctant to delegate decision-making powers to regional or subregional intergovernmental bodies. While this approach offers some benefits in terms of autonomy and flexibility, and while Asia and the Pacific do not need to follow the European model, a decision-making process built entirely on consensus is time consuming and costly. This has led to a proliferation of bilateral solutions that are often suboptimal. Another

² Asian Development Bank, *Emerging Asian regionalism: A partnership for shared prosperity* (Manila, 2008), p. 243.

detrimental consequence is that it makes the vision and objectives of regional economic cooperation and integration rest disproportionately on the political leadership of the participating countries. Changes in political leadership tend to create setbacks in cooperation and integration processes as priorities change. The question is how to strike the right balance between consensus-based intergovernmental processes and delegated decision-making to regional secretariats or intergovernmental bodies. Therefore Governments in the region need to reflect on and discuss further this complex issue, while pursuing cooperation and integration in the region.

17. **Lesson 4: ownership remains weak – stronger political will and vision are needed.** A number of facilitating institutions, such as bilateral aid programs or international financial institutions, often provide considerable financial resources for various initiatives related to regional economic cooperation and integration. This has led to dependence on external sources, which undermines local ownership. Countries' engagement with a large number of overlapping initiatives contributed to the dissipation of political energy, as well as of human and financial resources. The lesson is that the success of regional economic cooperation and integration requires a long-term vision, strong political will and collective ownership, all of which should be backed by generous financial resources. For that purpose, it is important that regional economic cooperation and integration initiatives be integrated with national development agendas and that they receive wide governmental support beyond specific line ministries. Furthermore, the development of successful national coalitions for regional economic cooperation and integration also requires broad-based support from communities, businesses, civil society organizations, academics and think tanks.

18. **Lesson 5: project preparations and coordination need to be strengthened, particularly to maximize synergies between regional economic cooperation and integration and the Sustainable Development Goals.** Investments in infrastructure, such as for energy, transport and ICT, require ample financial and technical resources for the preparation of projects, plans, programs and implementation strategies. However, the availability of such resources, especially in the public sector, is limited in most economies. In addition, taking advantage of synergies between regional economic cooperation and integration and the 2030 Agenda requires that projects with the most favourable economic, social and environmental impacts at the regional level are prioritized for implementation. The evaluation of such projects, some of which could encompass more than one sector, is a complex task. Moreover, the overall complexity of regional infrastructure projects is exponentially greater than national projects. Thus, an effective partnership between Governments, international financial institutions, pertinent regional and international organizations, and various national stakeholders needs to be forged.

19. **Lesson 6: integrated approaches to infrastructure development are currently missing.** There are synergies waiting to be explored in regional infrastructure projects. For example, transmission lines for the power sector, ICT networks and transport corridors need to be planned in an integrated way so as to improve overall connectivity and trade facilitation in the most efficient and optimum manner. At present, regional projects are prepared within sector frameworks, thus limiting overall impacts. Furthermore, as mentioned above, there is a need to look beyond sectoral issues and their economic impacts; social and environmental considerations must be factored in as well. The benefits of regional economic cooperation and integration could increase many times over if such integrated approaches to infrastructure development, keeping in view the 2030 Agenda, can be developed and implemented.

20. **Lesson 7: the gains from regional economic cooperation and integration need to be fairly distributed among members.** Mutual gains and a fair distribution among the members of costs and benefits of regional economic cooperation and integration initiatives are very important. This is because countries that do not perceive, for a variety of reasons, that they are benefiting tend to prefer to withdraw from such initiatives. The recent vote in the United Kingdom to leave the European Union is a case in point. Such considerations are particularly important if regional economic cooperation and integration is to serve as an important means of implementation of the 2030 Agenda. The spirit of the Agenda calls for leaving no one behind, and thus it is imperative to ensure that regional economic cooperation and integration contributes to reducing inequalities both within and across countries.

III. Specific challenges of the four elements of regional economic cooperation and integration in Asia and the Pacific

21. Regional economic cooperation and integration, as envisaged in the Bangkok Declaration, embodies a four-pronged approach: promoting market integration,³ increasing seamless connectivity,⁴ enhancing financial cooperation,⁵ and addressing shared vulnerabilities and risks.⁶ This section includes a discussion on the challenges faced by the Governments in the region in each of these four areas.

A. Market integration

22. Market integration results in a freer movement of goods, services and factors of production, such as capital or labour, across countries and contributes to enhancing efficiency, disseminating technology and improving welfare. Market integration in the region has been primarily driven by the expansion of global value chains throughout the economies of East and South-East Asia. This expansion was driven by investments by multinational corporations aimed at lowering their costs of production and assembly of goods to eventually be exported to developed country markets in North America and Europe. It was facilitated by the existence of productive capabilities, appropriate physical and soft infrastructure, and relatively low wages in the Asia-Pacific subregions.

23. The main challenges to the process of market integration in the region are posed by the slow recovery of demand in the region's main markets in North America and Europe, together with the existence of high costs (import tariffs, non-tariff or behind-the-border barriers, regulatory and procedural border burdens, and transport costs) associated with bilateral trade within the region. Historically, Asia-Pacific economies relied on multilateral and unilateral trade liberalization to reduce high trade costs and gain access to larger markets. However, the impasse in the World Trade Organization (WTO) Doha round of negotiations stirred Asia-Pacific economies to seek market access through preferential trade agreements, which have been proliferating rapidly in the past two decades. Overreliance on preferential

³ ESCAP, *Enhancing regional economic cooperation and integration in Asia and the Pacific* (forthcoming), chap. 3.

⁴ *Ibid.*, chap. 4.

⁵ *Ibid.*, chap. 5.

⁶ *Ibid.*, chap. 6.

trade agreements has led to inefficiencies, because countries do not usually abolish or annul bilateral agreements when a new multilateral agreement is signed among the same countries. This has led to a multiplicity of overlapping preferential trade agreements, often referred to as Asia's noodle bowl.

24. However, historical evidence suggests that liberalization of trade through free trade agreements does not always lead to more trade. One important reason is that they do not deal effectively with non-tariff barriers and regulatory and procedural obstacles, which surpass tariffs as the most troublesome obstacles to trade. Regulatory obstacles are particularly important in services trade, which plays a key role in facilitating industrial and agricultural trade, as well as countries' participation in value chains.

25. An important recent step in the region towards the reduction of trade costs was the adoption of a region-wide Framework Agreement on Facilitation of Cross-border Paperless Trade in Asia and the Pacific in May 2016. This agreement, which complements the WTO Trade Facilitation Agreement, will help the region focus its attention on next-generation trade facilitation measures and prepare for cross-border e-commerce opportunities.

26. Foreign direct investment (FDI), by combining external financial capital and technology, plays an important role in boosting productive and skills development in the region's developing countries. A substantial amount of FDI is linked to the establishment and development of global and regional value chains, which have been an essential factor in the process of market integration in the region, particularly in East Asia and South-East Asia.⁷ Therefore, obstacles to effective cross-border trade, including the lack of effective trade facilitation, are usually also obstacles to FDI.

27. Furthermore, FDI lacks a global system of governance, although global trade rules under WTO agreements, such as the General Agreement on Trade in Services, cover FDI to some extent. Instead, most of the promotion and protection of investment is regulated through a large number of international investment agreements, either in the form of bilateral or subregional investment treaties or as investment chapters in bilateral or regional trade agreements.⁸ Similar to the situation for trade, the proliferation of such agreements has led to overlaps and duplications, which need some level of consolidation and streamlining. Such an exercise would help improve transparency and clarity in international investment rules and help regional integration.

28. Currently, the only subregion with a clear subregional-level investment regime is the ASEAN region, as a result of the ASEAN Comprehensive Investment Agreement. However, individual ASEAN members continue to maintain their national investment laws and bilateral investment treaties, both with each other and with external partners. Thus, the ASEAN Comprehensive Investment Agreement has been added to existing treaty layers, which could lead to an even more complex network of international obligations, prone to

⁷ WTO and Institute of Developing Economies-Japan External Trade Organization, *Trade Patterns and Global Value Chains in East Asia: From Trade in Goods to Trade in Tasks* (Geneva, 2011).

⁸ At the global level, there are 2,324 bilateral investment treaties and 297 treaties with investment provisions in force, as of January 2017. The corresponding figures for Asia and the Pacific are 968 bilateral investment treaties and 148 treaties with investment provisions.

overlap and inconsistency.⁹ The complexity and non-transparency of the regulatory environment is an obstacle to both FDI and to regional integration.

29. Other important challenges to FDI flows, in particular to intraregional FDI flows involving developing countries of the region, include excessive red tape; lack of effective investment facilitation; absence of required labour skills, infrastructure and technological capabilities; corruption; and other obstacles related to ineffective law enforcement. This explains the need of many investor home countries to seek international investment agreements with host countries that emphasize investor protection. Recently, however, there have been an increasing number of calls for more balanced international investment agreements that also recognize host country development needs and the right of Governments to regulate for development purposes.

30. Despite significant labour migration flows and the importance, from a social perspective, of labor market integration, it is lagging behind other forms of integration in the Asia-Pacific region. Although some policy measures have been put in place in recent years,¹⁰ most migrants tend to have low skills and are, therefore, prone to vulnerable or irregular employment. Moreover, existing mechanisms to promote orderly migration in many countries do not favor an easy matching between demand and supply of migrant labor, which also contributes to irregular migration flows.

31. Politically, labour market integration touches on a core aspect of State sovereignty, namely the right of States to choose who is allowed to enter or reside in their territory. Moreover, migration is often seen as a threat to countries' national security and cultural identity. For these reasons, countries are hesitant to sign international conventions on the protection of migrant workers and are cautious about entering any agreement that may be interpreted as a commitment to opening their borders.

32. Furthermore, public perception of migrants, especially low-skilled migrants, is often negative. This is typically driven, inter alia, by press coverage that tends to highlight issues of illegality, both with regards to migrants' status and to illegal acts carried out by migrants, as well as by debates which focus on the perceived negative economic effects of migration such as migrants "taking" jobs from domestic workers. Even if this is not the case and low-skilled migrants generally complement national workers and add value to national economies, negative perceptions of migrants tend to prevent Governments of key destination countries from discussing opening labour markets to migrant workers.

33. Labour market integration involves significant technical adjustments across a wide range of policy areas. For example, differences in educational systems make it difficult to certify that migrant workers have the required qualifications for specific jobs. Similarly, ensuring that migrant workers are

⁹ Organization for Economic Cooperation and Development, "Southeast Asia investment policy perspectives", 2014. Available from www.oecd.org/daf/inv/investment-policy/Southeast-Asia-Investment-Policy-Perspectives-2014.pdf.

¹⁰ For instance, the Treaty on the Eurasian Economic Union led to the creation of a single labour market through the right to access employment and social protection systems. This can rationalize and regularize long-standing labour migration flows between the countries involved. In a similar vein, the ASEAN Economic Community has enabled mobility of highly skilled workers through mutual recognition of degrees in specific professions.

able to pay into social protection systems and enjoy the benefits of these systems, particularly with regard to acquired rights such as pensions, on their return to countries of origin, requires technical cooperation and agreement on such issues between member States who may have very different systems. With concerted efforts and cooperation initiatives, these challenges can be overcome, with significant benefits for the countries of origin and destination, as well as for the migrants themselves.

B. Seamless connectivity

34. Seamless connectivity encompasses the development of infrastructure in areas such as transport and logistics, energy and ICT. There are three elements of such infrastructure development: (a) hard infrastructure, such as roads, railways, power plants, transmission lines and fibre-optic lines; (b) soft infrastructure, including legal, regulatory and policy frameworks; and (c) services that are enabled by investments in infrastructure.

35. Sufficient integration of cost-effective transport across countries remains a challenge to achieving seamless connectivity. For instance, although East and North-East Asia is one of the world's most vibrant subregions, its intraregional and logistics network is still not sufficiently integrated. Similarly, the smaller and more isolated islands in the Pacific still lack affordable access to regular maritime transport to integrate their markets with neighboring archipelagos. Moreover, to date, only 32 per cent of the Asian Highway Network, which spans 143,000 km of roads passing through 32 member states, reaches the two highest categories of road class, and 11,500 km still need to be upgraded to meet minimum standards. Finally, the Trans-Asian Railway covers 117,500 km of railway lines and serves 27 member States, but has 10,500 km of missing links which prevent the network from functioning as a continuous system.

36. Unlike the transport sector, efforts to build energy infrastructure have remained confined to national economies, partly because in the past, self-reliance, rather than inter-country connectivity, was considered the main way to ensure energy security. However, in view of rapidly rising energy demand and with climate concerns on the rise, Governments of the region now realize that regional connectivity and integration could provide the most appropriate framework to enhance energy access and security. Ensuring access to reliable, affordable, efficient and environmentally sustainable energy services for all, however, will be very challenging, as the Asia-Pacific region is home to 41.8 per cent of the 1.1 billion people in the world that do not have access to electricity, and 70 per cent of the global population that relies on biomass for cooking and heating.

37. ICT is a vital component of seamless connectivity. Besides enabling better communications, ICT facilitates economic activities, delivers social services, facilitates disaster risk management, and makes possible a more sustainable use of resources, while supporting other infrastructure, such as intelligent transport management systems, smart grids and single window systems. However, the development of the full potential of ICT in the region is still limited by the poor availability, affordability and reliability of broadband infrastructure. The current terrestrial networks of fibre-optic cables are typically constrained by limited access to international transit. Furthermore, most countries' backhaul networks are usually poorly meshed and follow a river system pattern in which networks spread from submarine landing stations and thin out into countries' hinterlands; a single point of failure could thus cause a major Internet blackout in the country.

The following paragraphs provide an examination of the challenges to increasing seamless connectivity.

38. **Bottom-up process.** Most cross-border connectivity projects have been negotiated bilaterally. Although such projects may be effective for meeting bilateral objectives, their fragmented nature is not conducive to achieving effective seamless connectivity for the region as a whole. The plethora of agreements and frameworks completed under bilateral and subregional initiatives have led to another so-called noodle bowl, which, like the noodle bowl of trade agreements, increases regulatory burdens and transaction costs.

39. **Asymmetric costs and benefits, externalities and compensation mechanisms.** Regional infrastructure projects invariably involve asymmetric costs and benefits across countries and groups of people. For example, transit countries tend to bear disproportionately larger costs, while the benefits of lower costs of trade and transport accrue to consumers and manufacturers. Regionally accepted, transparent rules and regulations need to be put in place for internalizing externalities so as to ensure a fair distribution of costs and benefits among all stakeholders.

40. **Planning, coordination and cross-sectoral infrastructure synergies.** To expand physical transport, energy and ICT networks, they must be considered as a system, which results in cost and time savings. For instance, the costs of deploying terrestrial fibre networks related to digging, trenching or laying down conduits are reduced when works are along major roads, railways, power transmission lines, pipelines or waterways. Building connectivity networks requires careful planning and coordination, often absent due to lack of resources and appropriate institutional mechanisms, and these challenges are more pronounced when countries have different legal and regulatory regimes.

41. **Vision and political will.** Most infrastructure networks are capital intensive, exhibit economies of scale, require lumpy investments, and are of little use unless their construction is complete and they are well maintained. Together with careful planning and coordination, a strong political will and a shared vision among national Governments are critical for setting up effective coordination mechanisms for infrastructure development.

42. **Financing.** The building blocks of regional seamless connectivity are based on the national infrastructure in each country of the region. Hence, lack of adequate financing resources to undertake infrastructure projects at the national level is a major challenge. To coordinate solutions to this challenge, it is necessary to bring together all stakeholders to a regional platform with the aim of identifying opportunities and solutions for financing regional seamless connectivity.

C. Financial cooperation

43. The availability of financing is not only critical for the development of seamless connectivity in the region but also for a successful pursuit of the 2030 Agenda. A major challenge in this regard is the development of financial markets and mechanisms that can channel savings into financing instruments, including towards developing sustainable infrastructure. An additional challenge is the need to ensure financial stability by strengthening economic surveillance and monitoring schemes and through the provision of short-term liquidity support.

44. With respect to arrangements for the provision of short-term liquidity support, the region has both multilateral initiatives and bilateral swap arrangements. The former includes the Chiang Mai Initiative Multilateralization for ASEAN+3 countries and the Eurasian Fund for Stabilization and Development. Bilateral swap arrangements include the Framework on Currency Swap Arrangements of SAARC countries and a large network of bilateral swap arrangements provided by China. All these arrangements make available a total of more than \$400 billion of short-term liquidity support to a number of countries in the region. However, access to these resources is uneven across countries.

45. Regional financial safety nets offer short-term liquidity outside the International Monetary Fund (IMF) emergency lending programs. In evaluating the efficacy of regional facilities, the following questions need to be considered: (a) are these facilities operationally flexible and can they safeguard or prevent short-term risks associated with financial market volatility in general and/or volatility in capital flows in particular, together with significant fluctuations in exchange rates? (b) should the existing facilities be backed by a more robust framework of regional surveillance, supported by regionally harmonized and enforceable macro-prudential policy frameworks? and (c) will the fragmentation across subregions of facilities and regulatory frameworks make region-wide crisis management difficult?

46. Furthermore, the Chiang Mai Initiative Multilateralization is currently reliant on IMF surveillance for withdrawals exceeding 30 per cent of country quotas. The key then is how swiftly surveillance reports can be developed and, if IMF recommends its standard conditionalities, how to ensure coordination so that Initiative withdrawals are complementary to IMF emergency support. Finally, there remains concern regarding the effectiveness of subregional surveillance and the expediency of funds disbursements, given procedural uncertainty on how to access Initiative resources and that the facility has not been tested yet in emergency situations. Thus, there is a need in the region to develop capacities to formulate and monitor policy conditionality associated with emergency lending.

47. Managing risks associated with financial market and capital flow volatility, together with significant fluctuations in exchange rates, will require furthering cooperation, particularly with regards to monetary and exchange rate policies and the implementation of macro-prudential policies and capital flow measures. Ensuring financial and macroeconomic stability is important to provide a resilient platform for economies to raise the necessary financial resources in support of the 2030 Agenda.

48. Domestic financial markets in most economies are relatively underdeveloped in terms of size, liquidity and maturity, which impedes the channelling of long-term savings into long-term investments. As most financial markets in the region are dominated by banks, one challenge is to develop local currency bond and securities markets. For this purpose, both the demand and supply side of these markets need to be strengthened by facilitating market access to a diverse issuer and investor base. In this context, development of domestic institutional investors with long time horizons, such as insurance companies, pension funds and asset management companies, is particularly important.

49. Similarly, there is a need to enhance financial market infrastructure in order to regulate the issuing and trading of bonds and securities, functioning of payment systems, and cross-border clearing and settlement systems. This, however, is a challenging undertaking for most emerging and small markets

in the region, due to the difficulties in harmonizing regulations, corporate governance requirements and financial products for mutual recognition of their trading transactions.

50. Development of domestic financial markets and institutions, and linking them through cooperation, is critical to facilitate the financing of high-priority, bankable infrastructure projects, with an appropriate mix of debt and equity. However, poor availability of risk capital and long-term finance pose considerable constraints. At the same time, demand for new investment in infrastructure and maintenance of the existing stock continues to rise. Furthermore, improving the process of project selection, so that funding is channeled to high-priority projects, remains a challenge. High-priority projects are those that contribute most effectively to seamless connectivity in the region and to the implementation of the 2030 Agenda by ensuring that infrastructure development is inclusive, climate-friendly and resilient.

51. Cross-border projects often receive lower priority compared to national ones, which have a lower risk profile and a shorter gestation time. The former are, however, critical for achieving regional connectivity. The establishment of dedicated financing mechanisms for these projects could contribute to raising their priority level while serving as coordination platforms among the involved countries. These mechanisms could take different forms such as a project preparation facility exclusively for cross-border projects or loan-grant blending instruments improving their financial viability.

52. Countries should also consider tapping new emerging financing sources, such as the Asian Infrastructure Investment Bank and the New Development Bank. Multilateral initiatives have also burgeoned to support infrastructure project preparation and financing. Examples include the Global Infrastructure Facility led by the World Bank and the Asia-Pacific Project Preparation Facility of the Asian Development Bank.

53. To circumvent limited public budgets and borrowing capacity, Governments can also consider involving the private sector through public-private partnerships to close infrastructure financing gaps. To attract public-private partnership investments, Governments will need to create an enabling environment characterized by a clear policy orientation and a conducive legal and regulatory framework. In this context, it is important to ensure that risks are properly allocated between the public and private partners. Public-private partnership contracts can entail long-term budgetary commitments and contingent liabilities, such as those related to public guarantees. Hence, care is needed to ensure that public-private partnership contracts are affordable to the public purse over the entire period and do not threaten fiscal stability in the long run.

54. Public-private partnership projects are complex and may require skills not available internally. Therefore, to make the most of this type of mechanism, regional cooperation is critical, as countries need to learn from each other's successes and failures. In particular, stepping up capacity-building efforts is required to ensure that public-private partnerships become an effective instrument for delivering infrastructure services. This will also reduce the expertise asymmetry between the private and public sectors when contracts are negotiated. Building Governments' capacities to undertake projects of this type is critical to structure projects that will maximize positive development impacts, allocate risks adequately and ensure the quality of services to be provided. Such capacity can be efficiently built through regional cooperation and networks of experts.

55. The mobilization of domestic public resources is fundamental for the implementation of both the 2030 Agenda and various aspects of regional economic cooperation and integration. A major challenge is posed by low tax revenues collected in the region's developing countries, which was 17.6 per cent of GDP on average during the period 2012-2014, compared to 21.3 per cent for all other developing countries. Raising tax revenues is a complex task and must be based on a broad social contract that links the responsibility of paying taxes with accountable public expenditure that delivers on economic, social and environmental outcomes.

56. To facilitate the achievement of these objectives, the Asia-Pacific region needs to develop a regional approach on and vision for public finance strategies and policies. The vision should leverage the region's own policy lessons and experiences and take into account the local institutional, cultural and historical context. Such an approach will also support national efforts to enhance public revenues and to implement suitable tax and spending policies for sustainable development.

57. For this purpose, an inclusive and region-wide platform, such as that provided by ESCAP, can be considered. Examples of the areas such a platform could focus on include (a) broad regional policy debate, knowledge exchange, peer learning and targeted technical assistance and capacity-building activities for the prioritization of public financing as a key pillar of the regional implementation strategy for the 2030 Agenda; (b) dedicated and focused research on forward-looking tax and public expenditure policies and pragmatic policy design, keeping in view the Asia-Pacific context; (c) strengthening the region's participation in international tax cooperation and norm-setting processes, through substantive and coordinated regional positions and inputs; and (d) providing a mechanism for improved synergy between policy advisory and capacity-building efforts by international organizations and development partners on a voluntary basis.

D. Disaster risk and shared vulnerabilities

58. Many countries in Asia and the Pacific share vulnerabilities to environmental and disaster risks that arise from seismically active fault lines which cross many national frontiers, ocean basins with frequent cyclones, many river basins with flood potential, and climate change, to name just a few. Indeed, the region is one of the most disaster-prone in the world; 500,000 people have lost their lives and approximately 1.4 billion people have been affected, in addition to significant economic losses, by 1,625 reported disaster events over the past 10 years. Economic losses are higher if lost income, increased costs of production, and other financial losses to businesses and households resulting from damages to assets and economic activity are taken into account.

59. Improving the collective management of transboundary natural disasters, which is currently limited and inappropriate in most of the region, is a major challenge that needs to be addressed through regional cooperation. The following paragraphs address some specific challenges.

60. **Information sharing.** Facilitating the sharing of data and information across countries on disaster risks and on impacts and losses at the regional level is a significant challenge. Such data, which should include information on transboundary river basin floods and slow-onset disasters such as droughts, are needed to estimate regional disaster risks and transboundary hazards, as well as to strengthen early-warning systems.

61. **Financial provisioning.** Considering the huge contingent liabilities represented by disasters, a second major challenge is to set aside sufficient resources to meet expected losses. This is particularly important to avoid disruptive impacts of disasters on poverty reduction and progress towards the 2030 Agenda. For that purpose, countries should explore measures such as budgeting for disaster loss and building up reserve funds, contingent credit agreements, insurance, and access to emergency financing. In addition, ex ante financing mechanisms and investment in disaster risk reduction can be expected to significantly buffer economies from negative growth impacts.

62. **Financial infrastructure for risk sharing.** Taking into account the low insurance penetration in a number of the countries that are most vulnerable to disasters, another important challenge is to identify ways to manage risks and to create opportunities to share or transfer disaster contingencies. In this regard, innovative risk-transfer mechanisms, such as index-based parametric insurance and regional risk pooling, have great potential and need to be scaled up. The challenge of building well-functioning risk-transfer systems is even greater in countries characterized by low levels of financial development.

63. **Building urban resilience.** A final challenge is for spatial land-use planning and building authorities in many developing countries to effectively integrate resilient disaster risk management practices into their policies and permits.

IV. Suggestions for moving forward

64. Broad lessons from existing subregional economic cooperation and integration initiatives in Asia and the Pacific provide sufficient ideas for further reflection by the member States while they move forward with regional economic cooperation and integration and keep in view the 2030 Agenda. A brief synopsis of these lessons is provided below:

(a) In the context of rising inequalities and protectionist tendencies, it is important to re-articulate the benefits of economic integration and cooperation and a multilateral approach. Countries will also need to introduce credible policy measures to address the concerns of vulnerable groups and countries. The spirit of the 2030 Agenda is to leave no one behind, and thus it is imperative to ensure that benefits of regional economic cooperation and integration are fairly distributed;

(b) Given the plethora of overlapping and at times mutually inconsistent bilateral and multilateral agreements among countries of the region in the areas of trade, investment and infrastructure connectivity, there is a clear need to move towards coordinating, streamlining and eventually consolidating existing initiatives and arrangements;

(c) Striking a good balance between consensus-based intergovernmental processes and delegated decision-making to regional secretariats or intergovernmental bodies requires further deliberation;

(d) Regional economic cooperation and integration initiatives should be integrated with national development agendas and, in addition to specific line ministries, should be supported broadly by Governments. The development of successful national coalitions for regional economic cooperation and integration also requires broad-based support from communities, businesses, civil society organizations, academics and think tanks;

(e) Taking advantage of synergies between regional economic cooperation and integration and the 2030 Agenda requires that projects with the most favourable economic, social and environmental impacts at the

regional level are prioritized for implementation. The benefits of regional economic cooperation and integration can increase many times over if such integrated approaches to infrastructure development, keeping in view the 2030 Agenda, can be developed and implemented.

65. Simultaneously promoting all four components of regional economic cooperation and integration in an integrated manner should be a key consideration in moving forward. For instance, expanding trade and investment through market integration is one of the major objectives of regional economic cooperation and integration. This in turn would require seamless connectivity in transport, energy and ICT. Achieving seamless connectivity would be demanding without adequate financial resources, deep and connected financial markets, and stable financial and economic conditions. Similarly, vulnerabilities emanating from transboundary environment and disaster risks need to be addressed in an effective manner in order to continue to move forward towards shared prosperity.

66. Most importantly, enhancing regional economic cooperation and integration in Asia and the Pacific has strong potential synergies and complementarities with the 2030 Agenda. Opportunities offered by further market integration for creating jobs and boosting economic growth directly support the achievement of some of the Sustainable Development Goals. Similarly, large investments in transport, energy and ICT infrastructure to achieve seamless connectivity will also contribute directly to some of the Goals.

67. However, regional economic cooperation and integration should not be seen merely as an enabler of the 2030 Agenda. In turn, the 2030 Agenda should also play a fundamental role in informing how regional economic cooperation and integration should be pursued. This could be done, for instance, by ensuring that infrastructure projects maximize favourable social and environmental impacts, as well as economic impacts. Pursuing regional economic cooperation and integration and the 2030 Agenda jointly also means the expansion of opportunities in countries with special needs, such as least developed countries, landlocked developing countries and small island developing States, must be prioritized.

68. To maximize the synergies of regional economic cooperation and integration with the 2030 Agenda, ESCAP can play an overarching role through leveraging its inclusive intergovernmental platform, its normative work and its multisectoral technical expertise. ESCAP is already working to strengthen the constituent pillars of regional economic cooperation and integration through its existing subprogrammes in areas such as transport, ICT, energy, financing for development, trade and disaster risk reduction. ESCAP is also working with subregional cooperation organizations, including ASEAN, SAARC, the Pacific Islands Forum and the Economic Cooperation Organization, and is providing technical cooperation on the Belt and Road Initiative. Therefore, ESCAP is well positioned to accelerate progress across all four pillars of regional economic cooperation and integration simultaneously and to bring together member States, subregional organizations and other relevant institutions working on this issue. For this purpose, ESCAP can draw on its long-standing normative and research work on the constituent elements of regional economic cooperation and integration to forge regional agreements, undertake research to better understand its costs and benefits, and develop cross-sectoral synergies. It can also facilitate connecting regional economic cooperation and integration to global initiatives and frameworks for action on sustainable development, financing for development and climate change.

69. To support member States in moving towards a more integrated Asia-Pacific, ESCAP could continue the process of incorporating and formalizing regional economic cooperation and integration into its own work programme and into the work of its intergovernmental committees. There are a number of options which can be considered. These include instituting a cross-sectoral task force on seamless connectivity under the Committees on Energy, Information and Communications Technology, Science, Technology and Innovation, and Transport, as well as a recurring segment on regional economic cooperation and integration during Commission sessions to engage member States and subregional organizations in a dialogue on how to prioritize and move forward on key initiatives in this area.

70. In light of the enormous significance of the regional economic cooperation and integration agenda for the development of the region, and its ability to both boost and benefit the implementation of the 2030 Agenda, it is hoped that the Commission will pay close attention to the lessons learned and suggestions included in the present document, as well as to the more detailed discussions, assessment and recommendations included in the companion report *Enhancing regional economic cooperation and integration in Asia and the Pacific*. The Commission's comments with regard to the present document and its guidance will be very useful for the further implementation of the Bangkok Declaration on Regional Economic Cooperation and Integration in Asia and the Pacific.
