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# East Asian Regional Integration: From Japan-led “Flying-geese” to China-centred “Bamboo Capitalism”

Li Xing

## Introduction

### *East Asian in perspectives*

Over the past decades, studies in regional integration have become part of the focus and interest of development researches and debate. Among them, the regional integration of East Asia<sup>1</sup> has appeared prominently in these researches. Within the various domains of development studies, East Asia has been applied as valuable comparative parameters due to a number of its significant characteristics:

- East Asia has the world’s largest regional market of almost 2 billion populations, and it is many times bigger than the 25-EU 481 million and NAFTA 405 million populations.
- East Asia has been since the 1960s the fastest growing region in the world. Over the last two decades the region has an average annual economic growth rates of around 7%, which is much higher than the average 5% growth in the rest of the world.
- East Asia has historically had a high domestic savings rate of about 20-45% (it is different from country to country). It is much higher than the EU’s average of about 20%.
- East Asia holds over half the world’s foreign exchange reserves, see Table 2 (China alone has the world largest foreign exchange reserve which passed \$1 trillion in 2006).

The growth of GNP of many economies in East and Southeast Asia has since the 1960s increased more than twice those of the rest of the developing world: first Japan, then the four Asian newly industrialized economies (NIEs), i.e. Taiwan, South Korea, Hong Kong and Singapore), then new generation of NIEs (Thailand, Malaysia and Indonesia) and then China. Japan had in the mid-1980s replaced the USA as one of the world’s largest creditor nations and significant foreign aid donors. Since its economic reform started at the end of 1970s, China has followed the similar development path of Japan and the NIEs and has emerged economically and politically.

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<sup>1</sup> The geographical notion of East Asia is defined in various ways. Some refer it to the Far East, others refer it to Northeast Asia excluding Southeast Asia. Here, the notion of East Asia means the “eastern part of Asia” including Northeast and Southeast Asia.

**Table 1: Selected indicators of the three largest regional economic blocs**

Indicators (2002 unless otherwise specified)	East Asia	European Union	NAFTA
Population (million)	2,014.5	453.3	420.6
GDP (\$ trillion), 2003	7.5	11.0	12.3
Average GDP Growth (%), 1980-2003	7.0	5.0	6.0
Domestic Savings (% of GDP)	28.8	20.2	15.0
Investment (% of GDP)	26.5	18.7	37.5
FDI Flows (\$ billion), 2003			
Inflows	105.5	295.5	36.4
Outflows	57.7	337.0	173.4
Foreign Exchange Reserves (\$ billion)	1,177.0	304.4	116.4
Current Account Balance (% of GDP)	3.20	0.29	(4.10)

(Source: Akhtar, 2004:2)

Largely inspired by the intense curiosity on this first case of rapid industrialization outside the Western cultural sphere, the East Asian newly industrialized economies became the object of various academic studies and interpretations. The World Bank had invested on a special study report on *The East Asian Miracle* (1993), which generated a global debate on the various factors behind the East Asian success. Therefore, an envisioned integration of East Asian economies has been a subject of various researches since the 1980s. However, until now East Asian has not been able to form a full-scale regional integration with common economic and financial policies, and common political and foreign policies. So the puzzling question is: Would it be possible for East Asia to eventually evolve into an institutionalized self-sustaining economic zone, with or without its own characteristics comparable to the EU and NAFTA?

### *Objectives*

This paper has four major objectives in which East Asian regionalism is examined with a combination of the historical context, the geopolitical factors, the major roles of the key powers as well as the post-Cold War transformation of the region's political economy so as to comprehend the dynamics and limits of East Asian integration:

- 1) understand the historical background of the “flying geese” implication and the role of Japan and the United States in the political economy of the region's industrial relations.
- 2) provide some frameworks of understanding the factors, patterns and underlying dynamics of East Asian economic interactions in connection with various interpretations of the “flying geese” metaphors.

- 3) analyze the rise of China as a new engine in promoting the regional integration through trade promotion and institutionalization of multilateral cooperation.
- 4) conceptualize the on-going regionalization processes and progresses as well as deep-seated problems and obstacles which make the regional integration an uneasy task for the time being.

### **The flying-geese model in historical retrospect**

Culturally speaking, the terminology of “flying-geese” has special implications. In Chinese classical literature, the notion implies a symbol of an “order” based on leadership and collective action within a nation-state. The “Λ” geometry of the formation of geese-flying symbolizes two types of qualities: the team-based solidarity and the desire to return home.

The concept of the East Asian “flying-geese” pattern of regional economic integration was originated in the 1930s by a Japanese economist, Kaname Akamatsu (1935) who developed the theory of a multi-tier hierarchical “flying geese” model in which industrialization could be promoted and spread from developed countries to the less developed countries through their economic integration. In a broader sense, this model is often applied to examine the patterns and characteristics of East Asian economic integration.

The hypothesis of the flying-geese pattern suggests that a group of nations in this region are flying together in layers with Japan at the front layer. The layers signify the different stages of economic development achieved in various countries. In the flying-geese model of regional economic development, Japan as the leading goose leads the second-tier geese (less developed countries) which, in their turn, are followed by the third-tier geese (least developed countries).

Japan made the first attempt to lead Asian countries before the Second World War. At that time, the Japanese Government embarked on a brutally expansionist policy the result of which was creation of the first gaggle of “flying geese” under the name of the “Greater East Asia Co-Prosperity Sphere.” During the “flight” Japan militarily invaded and brutally ruled most of the countries in the region, and forcefully imposed its own worldviews and values on the rest of the region. At the same time, the Japanese Government assumed hostile attitude toward Western countries. Japan’s defeat in the Second World War signified the end of flight of the first “flying-geese” gaggle.

After the war, Japan made another attempt at regional integration through establishing a production network in East Asia. Thus the second gaggle of

“flying geese” came into existence. During the flight of the “second gaggle” of geese, Japan and the second flying layer of geese (South Korea, Taiwan, Singapore and Hong Kong) became a member of the western blocs enjoying benefits from the US-led capitalist world system. This type of geopolitically-supported regional economic development came to an end following the end of the Cold War at the end of 1980s. Furthermore, the rapid emergence of China and the Asian economic crisis in 1997 not only interrupted the flight of the “second gaggle” but also started the global debates about the “Asian crony capitalism” and the “Asian values” (Fuller, 2000; Li, et al, 2002; ul Haq, 1998).

Seen from the world system terminology<sup>2</sup>, the structure of Akamatsu’s theory of a regional division of labour could be described as consisting of Japan as the centre, a semi-periphery (the two formal colonies of Korea and Taiwan), and the vast markets and suppliers of raw material of the rest of Asia as the periphery. In essence a reconstruction of this pyramidal structure was the aim of US policy shortly after the war with the principal difference however that the US was to be included as the centre and Japan as the semi-periphery with the rest of Asia as the periphery to the American and Japanese economies.

#### *The political economy of the fly-geese model*

It would be profoundly ahistorical to think that the flying-geese industrial relations in East Asia only occurred since the 1960s. An understanding of the political economy of these relations can only emerge from an approach that posits the systemic interaction of each country with the others and of the region with the world at large. It is accordingly crucial to study the fall of the Chinese empire and the success of Japan’s early industrialization in the 19th century as well as the East Asian political economy from 1900 to 1945 in order to understand the role of Japanese colonialism and capitalism in the evolution of East Asian economic relations.

Japan followed the path of the Western experience of colonization of the non-European world in the past centuries. Witnessing the fall of the Chinese Qing Empire and being afraid of becoming a dependency or perhaps even a colony of the Western powers, Japan resorted to maximize its relative advantages by seeking territories close to the homeland. Although it is clear that the colonial development was directed to serve the Japanese Empire rather than the rest of

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<sup>2</sup> The World System School (Wallerstein, 1982, 2004) maintains that there are global divisions within the capitalist world system: the core, or First World, has an economy based upon the importation of raw materials and exportation of finished goods; the periphery, or Third World, in turn provides the raw materials and a market for the finished goods made from them; in between it is the semi-periphery, or Second World whose economy is a mixture of resource extraction and manufacturing.

the region, some scholars argue that colonialism did have certain positive effect on the later development of such as Korea and Taiwan, and certain changes effected from Japanese colonialism were historic (Cumings, 1987). At least Japanese imperialism had laid an infrastructural foundation for these countries' later industrialization.

Unlike other colonial powers Japan colonized its neighbouring countries in order to establish a close and tight regional economic integration. In Korea and Taiwan, Japan emphasized not only military control but also development under strong state auspices. Japan was also among the few imperial powers to locate modern heavy and light industries in its colonies: steel, chemicals, hydroelectric facilities, railways, roads, rice mills, textile factories, smelters, oil refineries, shipyards in Korea and some heavy industries in Manchuria where even today China's heavy industry still is located. It was during the colonial period that preliminary industrial relations were established in East and Southeast Asia.

Nevertheless, Japan's "Greater East Asia Co-Prosperity Sphere" project was formed and implemented forcibly through the use of military force. Japan aggressively promoted its own ideals and imposed those on other Asian countries. Japan's strong militarist and expansionist policies and its extreme anti-Western sentiment and nationalism could be instrumental in fuelling the country's expansionist policy. As Buzan puts forward very straightforwardly, "There is no question that Japan's policy between 1895 and 1945 was aggressively expansionist and ruthlessly brutal" (1988: 557). Tamamoto also bluntly declares that the proclamation of the "Co-Prosperity Sphere" in East Asia was merely a justification for Japanese military expansion conducted under the pretence of liberalising Asia from the Western imperialism (1991: 583).

East Asia has had "industrialization waves" at different periods. Japan was the only country in Asia that industrialized much earlier than the rest countries. Its modernization initiative and program can be dated back to the Meiji period when Japan faced the danger of Western invasion and colonization. After the Second World War, Japan started the first industrialization wave based on American capitals and technologies. During the post-war period, Japan sought to rely on its recovered economic strength and employed its aid as a means to boost its industrial power and consolidate its production relations in East Asia. Politically, Japan had to keep a low profile in international political affairs and was reluctant to come up with bold political initiatives. During the next three decades Japan took the opportunities of the global economic restructuring, and gradually transformed itself from a defeated nation into the second largest economy in the world right after the United States.



### *The “visible hand” of the United States*

The Japan-based regional flying-geese model was not unfavourable to the objectives of the US post-war policy toward East Asia, that was to cement strategic relations through economic dependence, to strengthen the position of pro-American political elites, and more importantly, to restore and nurture a Japan-centred East Asian economic growth in the hope that this would help immunize the region against communist expansion. In order to reach the objective, Washington pursued a strategic course to create a capitalist world economic system - “a global liberal economic regime” – in which the condition of its own participation implicitly strove to restore a US-cloned “Greater East Asian Co-prosperity Sphere” (Schwarz, 1996: 92-102)<sup>3</sup>. Through providing security, economic support and military aid to Japan and other East Asian states, the American goal was consequently to control and define their roles (including Germany in Europe) within the American-led alliance and prevent them from embarking upon an independent political and military course (ibid).

Considering the extent of the US historical, political and economic influence in the region, nowadays, to discuss about East Asian regionalism without taking consideration the role of the US would be meaningless. The US considers itself not only as a global power in general but also an Asian-pacific power in particular given by the simple fact that the US trans-Pacific trade is bigger than its trans-Atlantic trade. The US can become both a facilitator and a resister to East Asian regional integration depending on a number of crucial factors connecting with American interest. The US long-term strategic interest in East Asia can be understood as having a dual objective: “watching” the role of Japan and “managing” the risk by the rise of China as a global and regional power. The US role and presence in this region as a balance-of-power guarantor are generally welcome by the smaller nations. It is expected that in the foreseeable future the US will remain a key role player in this region’s integration process whether one like it or not.

### **Some unique characteristics of the flying-geese model**

What are the explanations to East Asia’s sustained economic growth in the past four decades? What are the dynamics of East Asian regional economic relations? Many scholars begin to notice some of the interesting features of East Asian economic development and industrial relations contributing to sustained economic growth and spatial expansion in this region. The Japan-led East Asian flying-geese model is precisely summarized by Hiley in a nutshell:

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<sup>3</sup> It is recognized that the US post-war objective in East Asia, as a part of its global strategies, was to restore the functioning of the capitalist world system, which was fundamentally different from the fascist-militarist Japanese agenda during the Second World War.

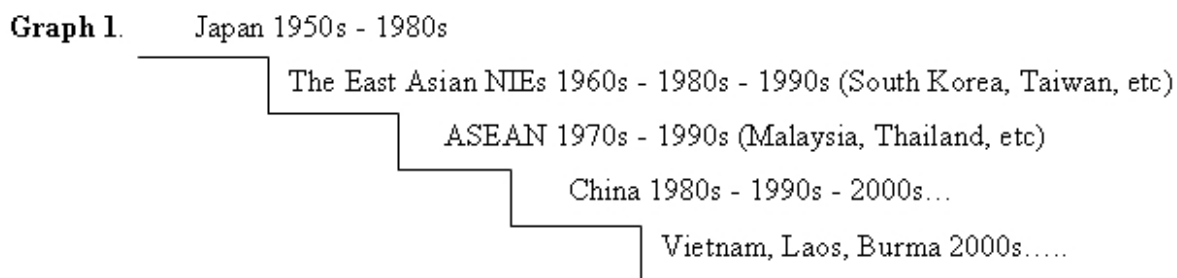
It therefore better describes the situation of a developing country, where the cycle begins when the product is introduced through imports: the economic growth of the developing countries is explained through mutual interaction between developing and developed countries based on leadership and emulation. The paradigm presupposes dynamic changes in economic relations among advanced (leading) and developing (catching-up) countries. The significance of the paradigm lies in its analysis of the linkages between the different countries in a regional hierarchy, the mechanisms by which development is transmitted from one country to another, the respective roles of policy and markets in this process, and the stability and sustainability of the process itself. ....

The basic idea of the paradigm is that a developing country, in an open-market context, industrialises and goes through industrial upgrading, step by step, by capitalising on the learning opportunities made available through its external relations with the more advanced world

(1999:81)

By a closer look, some unique dynamic phenomena of this model can be analyzed from three inter-related and somehow overlapped types of economic relation: 1) The dynamics of “take-over”, “ladder” and “chain” pattern of intra-regional economic relations; 2) The dynamics of intra-regional market and trade; 3) intra-regional investment.

### **Ladder-form regional economic growth**



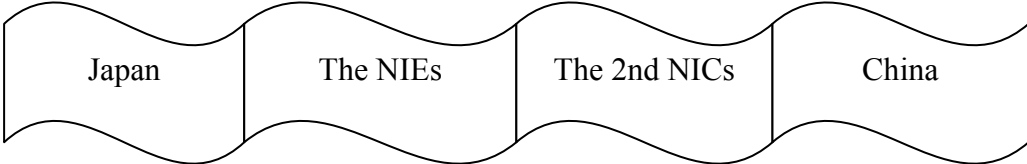
The above graph indicates that East Asia’s ladder-type of intra-regional economic relations is well formulated both in time and space. In terms of development level Japan always stands at the top ladder whereas the rest are followed at low or lower levels. In terms of industrial relations countries at the lower end of the ladder inherit the “left-over” from countries at the top of the ladder by overtaking their industries and importing their technologies. This kind of closely linked intra-regional economic structure also explains the reason why economic growth is also “inherited” in East Asia. This peculiar phenomenon has been possible because the region has continuously produced, but never simultaneously, new economic players in the world economy (Kim, 1991).

Thus, we can observe the interesting fact that countries in this region are at different stages of economic development, but they all share some fundamentally identical path of economic development.

*Regional industrialization waves*

Japan’s economic advancement in the past four decades was the main source of aspiration in stimulating East and Southeast nations to follow its suit. Japan was the model for imitation for East Asian late-comers. They basically learned the development formula from Japan: low wages, good education and training, high saving rates and strong government guidance of the private economy. Historically, there have been three main elements in East Asian industrial development which were based on Japanese model. The first was the development of a highly competitive manufacturing sector. The second was the deliberate restructuring of industry toward higher value-added and high-productivity industries, and in the late 1980s, these were mainly knowledge-intensive tertiary industries. The third element was aggressive domestic and international business strategies. When Japan entered a later stage, it passed the earlier phase to the next Asian NIEs who, in turn, passed their earlier stages to other developing countries as they entered a higher level.

**Graph 2.**



Both Graph 1 and here Graph 2 imply that during each ladder-period there had always been one or more new “engines” for generating economic growth with a spill-over effect to the rest of the region. After Japan the East Asian NIEs played the key role in generating the second industrialization wave in which they inherited Japanese capital, technologies and mode of production, and within several decades they succeeded in achieving industrialization. Again, the three ASEAN countries presented the third industrialization wave by taking the opportunities in the adjustments of production structure in Japan and the Asian NIEs and by absorbing their investments and technologies. These three ASEAN nations are leading the global economic growth and they have been labelled as the “second generation of NIEs”. What is the far-reaching importance for the whole region is China’s economic take-off alleviated by its reform program since the 1980s, which is regarded as the fourth industrialization wave in East Asia.

### *Regional divisions of labour*

The regional division of labour in East Asia was not only a part of larger global process of specialization (between Japan and the core states, and between Japan-the NIEs-the core states), but also a good example of regional labour division (Japan-the NIEs-China/AESEAN). The most interesting factor explaining the regional labour division is that in East Asia there are strong differences in the allocation of natural resources and industrial development level. Some industrially powerful countries are resource-poor ones. Some resource-rich countries are industrially weak. Even among the industrialized countries, some are relatively more advanced in the level of industrialization than others.

Therefore, labour division in East Asia has been structured both vertically and horizontally. The vertical labour division explains that the advanced economies in this region are the host countries for technologies and high-tech industries, whereas the less developed economies are the suppliers of cheap labour and resources. The horizontal labour division indicates that the shedding effects from the advanced economies can be a great input to the less advanced economies in form of foreign direct investment, partial and gradual technology transfer and international subcontracting.

Taking into consideration the factors of resource, labour, capital and technology, East Asian sustained economic growth is a phenomenon based on rational flow of capitals, mutual assistance and comparative advantage. Therefore, the characteristics of international labour division in East Asia pave the foundation for sustained regional economic cooperation and economic growth.

### *The chain-pattern economic relations*

The so-called chain-pattern economic development in East Asia is clearly the product the interactions of the four industrialization waves. It has certain overlaps with the flying geese pattern of economic development put forward by Japanese leaders and intellectuals in the 1980s. The flying geese pattern mainly refers to the development levels and stages between countries in the region while the chain-pattern reveals the structure of industrial production relations among countries in the region.

The hypothesis of chain pattern indicates that many products are going through processing in a number of countries, and economies in the leading position will gradually move some of their industries or industrial sectors to the next layer of countries because of changing comparative advantage over time. However, it is necessary to point out that this pattern of economic development is largely centred on Japan and based on its production system.

When the Japanese economy entered a higher development stage focusing on high-tech industries and high value-added products, it transferred its labour-

intensive and part of its capital- and technology-intensive manufacturing industries to other East Asian countries, thus leaving itself at the far end in the spectrum of manufacturing and strengthening the character as a service-oriented economy. Following the rapid economic development of the first generation of East Asian NIEs and the rise of their labour cost, they too transferred their labour-intensive and part of its capital- and technology-intensive industries to countries of Southeast Asia.

The chain-pattern of production relations in the region increases intra-industrial and intra-company cooperation. Gradually, more products are produced through different stages and sections in different countries based on comparative advantage. There are four stages of chain-pattern of production relations: 1. Early stage (food processing, textile and leather products); 2. Middle stage (non-metallic minerals, rubber products, wood products, chemical and petroleum refining, etc.); 3. Late state (clothing, basic house electronics, capital and intermediate goods); 4. High-tech stage (biology, information technology, hi-technology and material sciences). Japan is the only country which has entered the high-tech stage judging from its overall economic performance. The East Asian NIEs have both the late and high-tech stages at the same time while the catching-up NIEs have entered the late stage.

This take-over relation is formulated not in the form of rapid transfer of a total industry from one country to another but in the form of transferring some particular industrial sectors or certain production processing units. The content of these transfer interactions can be described as “tutor-pupil” relationship. The economies which transfer their industries or sectors to other countries will simultaneously pass on their competitive technologies and management to them. As a result, based on their own comparative advantages those recipient countries will use the inherited industries to strengthen their competitiveness in the international market. The “learning effect” will eventually develop the “catching-up effect”, and those late-comers will be able to advance their economic development and narrow the gap of income level and living standard with those of developed economies. Of course, it is important to point out that during the catching-up period, many factors play vital roles in the process of industrialization, i.e. the role of the state, culture, education, labour, etc., although they are not the subjects of discussion here. The first generation of Asian NIEs, Taiwan, South Korea, Singapore, is an example of such an effect.

The chain-pattern of production relation among East Asian states also reveals a similar model of their labour relations. The international labour division of production is well-defined among Japan, the NIEs and ASEAN states. In the past few years, a very sophisticated pattern of specialization has emerged. While Taiwan and South Korea have specialized in the highly capital and technology-

intensive productions; Hong Kong and Singapore have done so in the highly skill and equipment-intensive design and testing stages; and on the other hand, the Philippines, Thailand and Malaysia have concentrated on the highly labour-intensive assembling stage (Chen, 1989).

In this connection, one interesting point worth of mentioning is China's production and labour relations with other Asian states. As it is mentioned before, the nation's vast size and unbalanced development level between regions indicate that it is flying in different layers simultaneously and has multiple chain production and labour relations with many countries. This situation is obviously an advantage because it enables China to cooperate with other countries in almost all industrial sectors. On the one hand, China is capable of cooperating with Japan and the NIEs in developing high-tech industries while it can inherit labour-intensive industries from them. On the other hand, it can also export capital, intermediate products and some of its labour-intensive light industries to less developed countries in the region. Based on these closely linked economic relations, Chinese economy is increasingly integrated with the regional economy. "In contrast to the fears of China as an economic competitor, which dominated perceptions of China's role at the beginning of the modernization program, Asia-Pacific countries in general have found that they have successfully adjusted to China's integration into the regional economic system without serious negative repercussions to them" (Morrison, 1992: 456).

#### *Intra-regional trade and investment*

Various studies have indicated that a network of interdependence and intra-regional trade is emerging. Although East Asian economies still rely on exports to the industrial countries as an important engine for growth, intra-regional trade and internal demand play an increasing role in their development. Domestic markets have been driven by the rapid growth in personal incomes and by needed infrastructure investments. If we look at the whole Asia-Pacific region, trade within the region has been increasing dramatically in comparison with other parts of the world. In 1992, the total US trade volume in the Asia-Pacific region reached \$534 billion in which its trade with East Asia accounts for \$348 billion. This was far more than the US trade with Canada and Mexico (\$265 billion) and Europe (\$227 billion) (Li, Changjiu, 1994:44). During the end of 1980s, 70 per cent of Asian NIEs' export and 68 per cent of its import were conducted with the region. Similar indications of increasing intra-regional trade can be found with 72 per cent of ASEAN export and 63 per cent of its import; 62 per cent of Japan's export and 57 per cent of its import; 46 per cent of the US export and 53 per cent of its import; 82 per cent of Canada's export and 77 per cent of its import; China, whose total trade volume was \$111.6 billion in 1989 in which its Asia-Pacific trade was 66 per cent of the total import volume and 75 per cent of the total export volume (Zhang, 1994: 25).

**Table 2. Intra-regional trade ratios in comparison**

Region	1980	1985	1990	1995	2000	2001	2002	2003
East Asia, including Japan	34.7	40.2	45.6	55.5	54.0	55.4	57.3	54.0
Developing East Asia	21.6	29.1	36.4	43.7	43.4	45.6	47.5	44.1
NIEs	7.7	10.7	14.3	18.1	16.4	17.5	17.1	16.1
ASEAN	18.0	20.3	18.9	24.1	25.7	24.1	24.4	24.0
NAFTA	33.8	38.7	37.9	43.2	48.7	49.0	48.3	46.0
European Union 15	52.4	52.5	58.6	56.8	62.2	62.1	62.4	64.4

ASEAN = Association of Southeast Asian Nations, NAFTA = North American Free Trade Agreement.  
Notes: East Asia comprises Japan, ASEAN, PRC, newly industrialized economies (NIEs) of Hong Kong, China; Korea; Singapore; and Taipei, China. Developing East Asia excludes Japan.  
Source: Kawal 2005.

(Source: *Asian Development Bank*, 2006: 272)

The above table indicates that although East Asian intra-regional trade ratios in 2003 were lower than EU but higher than the rest of regions. According to the recent speech by the Director of Asian Development Bank, intra-regional trade in East Asia has risen from 45% of total trade in the early 1990s to 55% in 2005, which is only modestly lower than the 62% figure for the 15 European Union countries (Kuroda, 2006). What is more important to notice is the fact that such high regional trade ratios are achieved without formal regional institutionalization of political and economic unity.

East Asian intra-regional trade is expected to continue to grow following the on-going establishment of regional free trade agreement between China and ASEAN and between China-Japan-South Korea and ASEAN. While the expansion of world trade has slowed down and the extent of protectionism has increased in most developed countries, it is however very remarkable that East Asian states are creating new markets in their own region. Intra-regional trade expansion in East Asia is particularly evident in the areas of the Golden Triangle of Southeast Asian (consisting of parts of Malaysia, Indonesia, and Singapore), in the South China Zone comprising Hong Kong, Taiwan and China's southern provinces, and in the area of the Yellow Sea including Japan, South Korea and China's northern provinces.

Intra-regional investment in East Asia is also worthy of attention. According to the Asian Development Bank, FDI inflows into East Asia including Japan have more than quadrupled since 1980 and in 2004 FDI inflows in the region reached 21% as a share of world total. Over the same period, the share of East Asian FDI outflows also increased substantially from 5% to 14% of the world total (Kuroda, 2006: on-line). Intra-regional FDI flows accounted for much of this increase. The Asian Development Bank data shows that the main sources of FDI in East and Southeast came from the region itself. Between 1986 and 1992, the four East Asian dragons (South Korea, Taiwan, Singapore and Hong Kong)

were the largest single FDI sources for China, Indonesia and Malaysia; and they accounted for 48% of total FDI flows to ASEAN and China between 1990 and 2002 manifesting a mutually reinforcing relationship between the region's FDI and trade (Kuroda, 2005: on-line).

### **China-centred regional bamboo capitalism**

#### *The shift of flying-geese in East Asia*

If the failure of Japan's first attempt of the "flying-geese" process of industrialization in East Asia was connected to among others the victory of the Chinese Revolution in 1949 and the defeat of Japan in the Second World War. It is an irony of history that a contributing factor to the deformation of Japan's second attempt of flight for the "flying-geese" pattern of regional development is again connected to the rise of China as one of the key regional and global economic actor. China's continuous economic dynamism and increasing FDI flow to China despite the geopolitical turbulences following the end of the Cold War and the heavy pressure of the regional financial crisis in 1997. Since then, Japan was gradually no longer the central "locomotive" of the regional economic growth.

In terms of intra-regional economic relations in Asia, it was witnessed that a shift away from the previous Japan-led "flying geese" model of vertical economic integration through investment, technological transfer and supply of manufacturing parts which was based on a hierarchical market exchange and a clear regional division of labour and production networks.

China's open-door has attracted a large amount of foreign investment and many labour-intensive and capital- and technology-intensive industries have been moved to China. For instance, Hong Kong has almost moved its entire manufacturing industries to Mainland China while continuing to act as a financial and service centre. Taiwan and Mainland China have developed similar highly dependent economic relations in recent years. As a result of these shifts, the regional growth pattern and convergence structure was also beginning to change.

#### *The new development of East Asian regionalism*

Since the 1990s the region witnessed a gradual shift away from the vertical "flying-geese" model of to a new horizontal modelling of regional economic integration. The new pattern of FDI inflow played a key role in creating a phenomenon of "bamboo capitalism":

This regional model appears to be shifting towards that of "bamboo capitalism" or "parallel development." Based on foreign direct investment



(FDI) flows in the region, which create intricate intra-regional production networks, “bamboo capitalism” also focuses on the exchange of parts, components and other intermediate products, and hence a “horizontal network of trade and capital” – with China at its core.

(Cheow, 2004:3-4)

The new engine of regional economic growth is driven by FDI-directed supply chain which has created a pattern of “parallel development” for the region in many ways. It has not only generated diverse and vibrant networks of local enterprises and industries around the whole region, but also further decomposed and extended the supply chains geographically. This kind of network-based exchange of trade and capital has profound impact to East Asian economic convergence because the new situation necessitates governmental cooperation and institutional building. One of the key actors in generating dynamic intra-regional industrial and economic integrations is the overseas Chinese communities.

#### *The role of overseas Chinese Diaspora*

The role of ethnic Chinese networks (Chinese Diaspora) has been significant in regional economic integration not only in terms of being the major source of FDI contributing to China’s economic growth but also in terms of being the network connector linking the Chinese market with the rest of the region (Peng, 2000).

Among the major investors, the overseas Chinese networks and the Chinese-dominated regions such as Hong Kong and Taiwan have been playing a decisive role since the very beginning of the economic reform. The capital, technology, entrepreneurial ability, marketing skills and international trading experience of the overseas Chinese made a formidable combination with the advantages of cheap land and abundant supply of low-priced disciplined labour in the mainland. Not only in China, ethnic Chinese are also major and sometimes prime sources of capital and entrepreneurship of most of the Southeast Asian countries.

The spill-over effect of the regional network-based “bamboo capitalism” can be partly illustrated by the role of the hundreds of successful ethnic Chinese family business and networks connecting interlocking, medium-sized businesses in many countries in the region. Overseas Chinese entrepreneurs, business executives, traders and financiers are the major players linking local economies with that of the region.

### *The China-driven economic integration*

China's "core" position can be explained in this way that the country's vast size and unbalanced development levels between its internal regions with their respective levels of industrial stages and comparative advantages enables China to cooperate with the rest countries of the region and even the whole world, rich and poor, advanced and underdeveloped both vertically and horizontally. This is to say that on the one hand, this signifies the unbalanced development of China's domestic economy in different regions, on the other hand, the advantages of China's multi-level economy enable it to cooperate with countries of different stages at the same time; and different Chinese provinces can give full play to their comparative advantages with all countries in the East Asian region, i.e. a China-driven vertical and horizontal market network of trade and capital.

When global FDI began to horizontally spread to China and other East Asian countries, the early form of flying-geese and ladder-patterned intra-regional industrial, trade and the linkages with global FDI was transformed into a relationship of competition in which countries in this region are competing with one another for capital and financial resources as well as for export market. Moreover, the insecure feeling on the rise of China points to the fact that many enterprises or industries are facing direct competition with Chinese products. To some scholars, the emergence of China's economic strength was among the factors contributing to the financial and economic turbulence in the region in 1997 (Li, et al, 2002).

The rise of China has met different response from different corners of the world. The immediate feelings of China's impact are nowhere more manifest than in Asia where China's emergence has been felt most strongly due to obvious geopolitical and economic factors and cultural and historical ties. China's rapid economic growth and active regional diplomacy have already transformed Asia in many ways. Economically, China's commercial and energy ties with all major regions of the world are expanding. China is one of the main driving forces proliferating regional and bilateral trade agreements. Politically, it is often interpreted that China seeks to shape the region's emerging political-institutional contours, encouraging movement toward an East Asian community balancing the declining influence from the United States.

Today there is a consensus in East Asia that the quick rise of China's economic power especial its growing domestic market is a major engine for growth boosting regional trade growth and economic integration. Even Japan has acknowledged that its recent economic recovery has been due in a large part to its massive exports to the Chinese market shifting its traditional trade deficit to surplus. Japan has remained China's largest trading partner and import source as well as third largest export market for 10 consecutive years. In terms of South

Korea, China (excluding Hong Kong and Macao) finally surpassed the United States as its top export market in 2003.

Following the financial crisis in 1997 which deteriorated the regional economy, it was recognized that China, not the United States or Japan, played the most important role in the region's economic recovery. It did so through drawing on its extensive foreign exchange reserves to assist distressed nations. It also refused to devalue its currency and refused to withhold its committed aid as Asian nations that tried to rebuild their vulnerable economies.

In Southeast Asia, bilateral trade volume between China and nations in this region has reached 40 billion US dollars a year and the region's exports to China are bigger than those to any other place in the world. Chinese statistics show that from 1990 to 2005, China-ASEAN trade volume surged at an average of 22% on year-on-year basis, four percentage points higher than the growth rate of China's overall foreign trade volume in the corresponding period. Currently China and ASEAN are each other's fourth largest trading partners and trade experts estimate that China-ASEAN trade may reach the 200 billion US dollar target by 2008 (People Daily online, October 30, 2006). China and ASEAN countries have been committed to the goal of establishing a free trade area by 2010 as scheduled - ASEAN-China Free Trade Area (ACFTA). The rise of China changed the East and Southeast regional landscape in two ways. On the one hand, China's new role as a link in the production network contributed to the growth of intra-regional trade. On the other hand, China became an active player in developing institutional frameworks to promote regional integration.

There is no dispute today that China is increasingly looked as the locomotive of the region's economic growth and development. While having a large surplus in its trade with the United States and the EU, China actually has trade deficits with most Asian countries. China's import is helping to fuel the economic recovery and growth of its smaller neighbours. Even Japan has acknowledged that its economic recovery last year has been due in a large part to its massive exports to the Chinese market. China displaced the United States as the largest source of Japan's imports for the first time ever in August 2001. Due to its internal regional differences in economic development, China's economic growth is expected to last for a long period due to the "catching-up" process from within.

The positive integration trend led by China-driven regional economic growth is confirmed by a study result on the spill-over effect on the economic growth in the home country generated by openness, market size, and level of development of neighbouring countries in the same region, and the conclusion shows that "the economies of countries near large and open economies grow faster. Also, the

level of development of neighbouring economies, especially when they are open, has significant positive spill-over effects” (Vamvakidis, 1998:265)

### **On-going integration processes, difficulties and challenges**

So far, there is no consensus on a full regional integration among all countries in the region. There are currently two processes driving further towards to Asian regionalism at sub-regional levels: top-down regional and governmental cooperation fostered by organizations like the Association of Southeast Asian Nations (ASEAN), and other bottom-up economic integration through cross-border investment and the establishment of regional production networks.

The Asian Financial Crisis of 1997-98 played also a role in pushing the region into forming trade and financial agreement in one way or another. Since then, the ten ASEAN countries have initiated a regular series of meetings at the cabinet and head-of-government levels with their counterparts from Japan, China, and Korea. These meetings are held at a yearly basis with two parallel structures: ASEAN10+1 (ASEAN 10 countries + China) and ASEAN10+3 (ASEAN 10 countries + China, South Korea and Japan) including annual meetings of the ASEAN ministers of foreign affairs, trade, investment and finance.

A good example is ASEAN – China Free Trade Agreement (FTA). According to *Asian Economic News* (Dec 13, 2004), economic ministers from the ASEAN 10 and China signed a free-trade agreement that will phase out tariffs on most goods traded between them during the five-year period starting in July 2005. It is expected that the total elimination of tariffs on traded commodities will be completed by 2010.

### *The geopolitical transformation of the US strategic objective*

The restoration and prosperity of the key economic powers of East Asia (Japan, South Korea, Taiwan) in the post-war period were realized as a result of the impact of restoring global stability alleviated by reconstruction funds provided by the United States whose post-war foreign and economic policies were aimed at fostering developmentalist, authoritarian and anti-Communist states in different parts of the world.

In Europe American “Marshall Aid” was used to revive the Western European industries within the possibly shortest time so as to eventually block Communist expansion. In East Asia the pivotal object of American post-war policy was basically the same as its policy in Europe: that is to revive the Japan-centred capitalist regional economies including South Korea and Taiwan. Under American protection, external military threats and the internal danger of

communist expansion were substantially reduced in these two regions. The burden of the allied countries' military expenses was also greatly reduced by the American military presence. American military bases have been documented to have not only protected these countries but also provided them with economic benefits such as employment. Even now, the withdrawal of American military forces would be considered as a substantial economic loss.

The end of the Cold War is also the end of the necessity of the geopolitical mechanism for the region's take-off and prosperity. America's current global strategic policy is based on deregulation (Haass,1997), i.e. no longer regulated by superpower rivalry and *transnational liberalism* (Agnew and Corbridge,1995) in which nations interact in compliance with the rules and standards endorsed by Washington Consensus. Thus, it is argued that the shift of the power base of the new US hegemony from hegemonic order/stability (*balance of power* under nation-state structure in a bipolar world) to hegemonic liberalism and market economies (*imbalance of power* under transnational structure in a multipolar global economy) is one of the important factors contributing to the East Asian financial crisis in 1997.

Therefore, it is even legitimate to ask the question: whether East Asian regionalism can be realized without the United States? Even today, the US is still the largest export market for the key countries in the region. In addition, the US has much more closer political and military alliance with South Korea and Japan. Apart from the economic rationalities, the United States will have to both involve in and regulate East Asian affairs in order to make sure, for the sake of its own global interest, that China is becoming a responsible regional player in East Asia and a rational stakeholder in the international system.

#### *Institutionalization of East Asian regionalism*

The EU regional integration has been driven by the desire to foster political and social cohesion. Interdependence in political and economic ties within the EU was seen as an effective approach way to resolve security conflicts in the region. In retrospect, the evolution of the European Union has a history of a more than 50-year process. It can be argued that the EU began with the Bank for International Settlements, and then the European Coal and Steel Community. Later on the European Common Market was upgraded to the European Economic Community. Finally and now the European Union and the Euro Zone has become a reality. Again in retrospect, the Japanese wishful thinking of a flying-geese "Great East Asia Co-Prosperity Sphere" can be dated back to the 1930s, the achievements of East Asian regionalism can hardly be compared with the EU both in depth and width. There are still many challenging obstacles which need to resolve, without which an EU-like full institutionalized regionalization is impossible.

In contrast, East Asia has not been able to develop a common vision and mandate for regional cooperation. The East Asian region is one of the regions with intensified economic interactions and interdependence that have not established any institutionalized arrangement in the process of regional integration. East Asian intra-regional economic relations have been constructed under the absence of formal institutional framework. Even the three major economic powers – China, South Korea and Japan – are not able to conclude a FTA between themselves.

Are the people and government in East Asia able to establish formal institutional framework of regional integration beyond national sovereign and political ideologies? Despite the increasing economic integration and interdependence in East Asia, there is no formal institutionalized regional integration agreement which is similar to EU and NAFTA, except ASEAN. Even the sub-regional organization, ASEAN, cannot be compared with the European Union, and it lacks infrastructure and institution to lead the process. Three big economies in North East Asia; Japan, China and Korea do not have a free trade agreement (FTA) among themselves nor do they belong to any regional integration. EU in Europe and NAFTA in North America are developing steadily although many obstacles need to remove. East Asia as a whole is not moving decisively towards establishing economic zone, although there are growing sentiments among member countries of East Asia to move towards its establishment.

#### *Political, territorial and historical obstacles*

Will common regional economic interests pressure governments to look beyond territorial disputes, historical memories and nationalism? Since Japan's historical crime is still not clearly and sincerely acknowledged by the Japanese government creating fundamental political distrust among major powers of the regional, otherwise, regionalism in East Asia can only remain purely market-based economic cooperation without political and cultural foundation.

Globalization and the post-Cold War power relations in East Asia with the disappearing of the balance of power necessity among world powers are paving the way for traditional international conflicts over territories and natural resources. Furthermore, severe economic competition and rapid economic growth in this region have intensified rising competition for fish, petroleum, gas and other resources and at the same time are spurring emotional nationalism in the region especially among China, Japan and South Korea, leading to the aggravation of long-standing disputes over territorial claims and history interpretations. Countries in this region, weak or powerful, rich or poor, are seeking ways to extend their power beyond their territorial waters. The South China Sea, the East China Sea Shore and the Spratly Islands are at present the hot spots for possible confrontations among a number of countries.

Historically China was the dominant regional power both politically, economically and culturally, whereas Japan began to emerge as a military and economic power since the *Meiji Restoration*<sup>4</sup> of the later 19<sup>th</sup> century. Right now, it is first time in the history of East Asia that Japan and China are becoming “two tigers in the same mountain” – a rivalry competition. The growing economic interdependence between China and Japan and between Japan and South Korea since the end of the Cold War period has not been matched by a corresponding improvement in relations in socio-political and socio-cultural spheres. Without substantial foundations and levels of social, intellectual and political trust these three great countries will not be able to overcome the historical problems making a true full-fledged regionalism in East Asia unreachable. Other countries in the region do not have sufficient confidence, nor do they have the economic power to play the leadership role.

*Contradictions in economic levels, divisions of labour and other diversified factors*

Unlike the EU and NAFTA, economies of East Asia are too diversified in terms of economic size and development level as well as living standard. On the one hand, the region has two of the global economic giants – Japan and China, more advanced economy – South Korea, Singapore, etc; on the other hand, it also has world’s poorest countries – Cambodia, Laos and Burma, etc. Many countries are still struggling with political stability and with serious poverty concerns.

Although intra-regional economic interdependence in East Asia has the appearance of a well-organized structure, further studies and examinations can disclose some embedded contradictions. The fact that the final products of different stages go through production processes in many countries in the region - indicates that this new division of labour is both horizontal in the sense that the entire industry or production line is passed on, and vertical in another sense that the sub-processes may be passed on to other countries. It must be seen that the region's economies are not in well-balanced harmony but are more in competition with one another than complementary in labour cost, labour talent, seeking markets for export, technological upgrading, etc.

Other obvious factors blocking a full regional integration are vast differences in many key areas, such as political systems, social structure and cultural values, which make it impossible to reach basic consensus in order to form a region-based foreign, economic and financial policies. Most underdevelopment countries in the region are diversified in ecosystem, population, ethnicity, religion. Rather than integration obstacles they are facing more serious internal

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<sup>4</sup> Refers to the period of Enlightened reign of Emperor Meiji (1868-1912) during which Japan started a series of modernization processes and rose to world power status.

development problems such as emerging income gaps, environmental degradation, urbanization and congestion, and various social evils.

### **Conclusion**

This paper analyzes the unique features of East Asian regionalism which are historically constructed in terms of waves of industrialization, intra-regional industrial relations, trade, and investment and so on. These historical features are further developed, and new forms of integration driving forces are generated by the rapid globalization process and especially by the rise of China.

However, East Asia is still far away from a full regional integration to the similar scale in comparison with the EU. Many fundamental differences with deep-seated difficulties and obstacles between countries in the region are too wide to be bridged. Currently, some sub-regional integration movements of free trade are undergoing between or among groups of countries. It is interesting to observe whether these sub-regional movements can generate the positive spill-over effect to eventually reach the regional integration at high institutionalized levels.



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