

## **Asia-Pacific Cooperation and Its Contribution: Historical and Future Perspectives**

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### **I. Lessons from the Forty Years of Pacific Cooperation**

I am pleased to have been given the opportunity to make the anchor speech for this conference. In this conference, we discussed the present situation and future prospects of the Pacific basin economy in comparison with that of Latin America from various angles. This paper considers the Pacific basin from the angle of regional cooperation. I would like first to reconsider what we have learned from the history of the Pacific cooperation; second, to examine the drastic change in the world economic system since the 1985 Plaza Agreement, which is posing a new challenge to the Pacific cooperation; third, to analyze the structural background of the Pacific cooperation; and finally, to make some concluding remarks about the future of the Pacific cooperation.

It has been more than forty years since the foundation of the South Pacific Commission and ECAFE in 1947, twenty-one years since the start of PBEC and PAFTAD in 1968, and about ten years since the first PECC assembly was held in Canberra in 1980. During these years different types of forums on the Pacific cooperation have been organized. Today Pacific cooperation is taken for granted as 'needs of time' and is becoming an active global movement. As many people may agree, the recent upsurge in the Pacific cooperation movement is approaching something similar to a fever. Therefore, it is now appropriate for us to cool down our enthusiasm and reconsider the genuine role of Pacific cooperation in 1989 and beyond. In this regard, this conference, I believe, is outstanding for its broad perspective and the in-depth insights held by all the distinguished participants.

### **1. First phase: organizations for cooperation for the implementation of regional development projects established after World War II**

Activities relating to Pacific Cooperation can be classified into four phases, the first phase began after the Second World War, when two organizations, the South Pacific Commission (SPC) and the UN Economic Commission for Asia and Far East (ECAFE) were set up in 1947. The former was the result of the Australian government's initiative in which five former colonial powers in the Pacific region participated and played a dominant role in solving the economic, social, educational and medical problems of the region. The latter, which is a United Nations organization, sponsored a large number of regional development projects. In the early stage, for example, ECAFE concentrated its activities on the development of major Asian river-basins such as the Mekong River Development Project.

These experiences with the activities of SPC and ECAFE left us with the following two lessons.

*Lesson 1.* Regional cooperation is vital to region-wide development. In other words, economic development can be achieved not only by national policies but also by regional cooperation.

*Lesson 2.* One of the core objectives of regional cooperation is to promote joint efforts for the implementation of concrete development projects.

Regrettably, we are now losing sight of such a target of regional development in the recent discussions relating to Pacific cooperation.

### **2. Second phase: organization of three Pacific cooperation conferences**

In 1965, Professor Kiyoshi Kojima proposed the concept of Pacific Free Trade Area (PAFTA) which triggered the organization of a series of conventional Pacific cooperation forums. In January 1968, the Pacific Trade and Development Conference (PAFTAD) was first held with the participation of scholars from five major Pacific rim countries, namely, Australia, New Zealand, Canada, the U.S. and Japan, and in May of the same year groups of businessmen from the five countries started the annual gatherings of the Pacific Basin Economics Council (PBEC).

In 1979, Japan's late prime minister Ohira proposed the concept of a forum on Pacific cooperation, and Japan's former Minister of Foreign Affairs Okita and his colleagues in Australia and the U.S. contributed to the organization of the Pacific Economic Cooperation Conference (PECC), which was first held in Canberra in September 1980.

These three separate organizations shared some common characteristics. First, they were informal and loosely linked organizations composed of scholars, businessmen, statesmen, and civil servants. Second, these three conferences discussed the possibility of Pacific cooperation as the key measure for promoting growth and stability in the region and the world. Third, they were characterized by the detached and rather reluctant attitude of the United States until 1983 at latest. This last factor, unfortunately, reduced the impact of the discussions held during these three

major conferences on the national and international policies until 1983. The experience gained in the efforts in the second phase gave us the following lessons.

*Lesson 3.* The Pacific cooperation can be the key instrument to growth and stability of the economies in the region.

*Lesson 4.* In the early stage of such a type of regional cooperation, informal exchanges are more useful than resolutions adopted by an official organization.

However, in order to promote economic growth in the Pacific region through more pragmatic cooperation such as regional development projects, multilateral investment programs, and intra-regional technology transfer, informal exchanges are not sufficient.

### **3. Third phase: the U.S. factor**

In 1983, the U.S. faced drastic changes in her political and economic environment. Military and security tension escalated both in the Caribbean Sea and in Vietnam (Cam Ranh Bay). Thereafter, the U.S. adopted a more constructive attitude in the reorganization of security and economic cooperation in both the Caribbean and the Pacific regions. In the Caribbean region, the U.S. enacted the 1983 Caribbean Economic Reconstruction Act and implemented other measures known as CBI, or Caribbean Initiative. In the Pacific area, the Philippines-based U.S. force increased its activity to cover the sea lane around the Cam Ranh Bay and Japan's then Prime Minister Nakasone announced his intention to collaborate with the USA in the sea lane security to safe-guard Japanese interests, though this proposal was met with strong criticism on the part of Japan's opposition parties.

At the same time, in 1983, the U.S. began to suffer from the persistent twin deficits, namely trade deficit and government budget deficit. The huge U.S. trade deficit occurred simultaneously with the trade surplus against the U.S. within the West Pacific Asian countries, namely Japan, Asian NIEs and some ASEAN countries. Thus, the U.S. leaders became aware of the importance of the Pacific cooperation for the U.S.'s own interests.

This change in the attitude of the U.S. leaders has been clearly noted in their addresses, such as that made in March 1983 by Secretary of State Schultz at the World Affairs Council of Northern California to the effect that the U.S. was already closely linked with the dynamic Asia Pacific economy which had started to account for one sixth of the world trade at an unprecedentedly rapid pace. Similar addresses were made by the Deputy Secretary of State Eagleberger in January 1984 at John Davis Lodge International Center, and in March 1984 at the National Press Association in Washington D.C. Secretary of State Schultz again in July 1984 gave an address in Honolulu on the importance of the Asia Pacific cooperation, recognizing that the Asia Pacific region had become the growth center of the world economy and the most concentrated area of military tensions.

At the same time, appointments of Asian experts were made to important policy-related positions within the U.S. government. In March 1984, the U.S. government appointed the former Ambassador to the Philippines Armacost as Deputy

Table 1. GROWTH RATES OF REAL GDP IN PACIFIC BASIN AND LATIN AMERICA  
(%)

	1980	1981	1982	1983	1984	1985	1986	1987	1988
Korea	-3.5	7.4	5.7	10.9	8.6	5.4	11.7	11.8	11.0
Taiwan	7.3	6.2	2.9	7.8	9.6	4.4	10.6	12.4	6.8
Hong Kong	10.9	9.4	3.0	6.5	9.5	-0.1	11.2	13.6	7.4
Singapore	9.7	9.6	6.9	8.2	8.3	-1.6	1.8	8.8	11.0
Thailand	4.8	6.3	4.1	7.3	7.1	3.5	4.7	8.4	11.0
Malaysia	7.8	6.9	5.9	6.3	7.8	-1.0	1.2	5.2	7.8
Indonesia	9.9	7.9	2.2	4.2	6.0	2.5	4.0	3.6	4.1
Philippines	5.2	3.9	2.9	0.9	-6.0	-4.3	1.5	4.7	6.6
China	6.5	4.6	8.7	10.2	14.5	13.0	8.3	10.6	11.2
Mexico	8.3	8.8	-0.6	-4.2	3.6	2.6	-3.8	1.5	1.1
Brazil	9.3	-4.4	0.6	-3.5	5.1	8.3	7.6	3.6	-0.3
Argentina	1.1	-6.8	-4.6	2.8	2.6	-4.5	5.7	1.6	-1.0
Japan	4.4	3.8	2.9	3.2	5.0	4.4	2.4	4.2	4.9
USA	-0.1	2.0	-2.5	3.7	6.8	3.2	3.0	3.4	3.9

Sources: IMF, *International Financial Statistics*, various issues, and publications from each country's statistics bureau. Figures of 1988 are estimated by OECD, ESCAP, and other institutions.

Secretary of State. Simultaneously, Fairbanks was assigned as Ambassador in charge of the Pacific Affairs and the chairman of the newly established U.S. Pacific Economic Cooperation Committee. This change in the U.S. attitude greatly revitalized the Pacific cooperation forums, especially, PECC. This gives us:

*Lesson 5.* The commitment by a major country, especially the U.S., is crucial to the effectiveness of Pacific cooperation.

#### 4. Fourth phase: debt adjustment with tacit regional coordination

Looking back at the economic performance during the period 1980 and 1985 of the member countries of the Pacific cooperation, in addition to the well-known U.S. twin deficits, we can observe a contrast between the Asian success and the Latin American failure. After the second oil crisis during the period 1979 and 1980, most of the Asian and Latin American countries suffered from a serious slow down in industrialization and economic growth as shown in Table 1. During 1981 and 1983 most of these countries, especially the Asian developing countries, achieved growth by promoting development policies that accelerated public and private investment.

However, such active development policies were associated with a considerable increase of the debt burden. 1983 was the most critical turning point for all debtor countries both in Asia and Latin America. While some of the Latin American countries were on the verge of declaring default, most Asian countries succeeded in

avoiding the crisis by adopting active adjustment policies. For example, Thailand whose debt increased sharply in 1982 and 1983 enforced very tight adjustment policies in 1984 and 1985 by reducing the budget for development plans and regulating public and private investment. Although these policies naturally led to a very low, or even negative growth rate among the Asian countries in 1984 and 1985, as shown in Table 1, the need to borrow from abroad was successfully reduced. The capability of adopting positive debt adjustment policies was the main reason for the contrast between the Asian success and the dismal failure in Latin America.

Despite the often raised claims that the dialogue at every level among the leaders of the West Pacific countries with the U.S. and Japan had had some influence on the policies adopted by the leaders of the Asian countries, especially regarding the concerted efforts of macroeconomic policy adjustment, it is still questionable whether such an influence had been significant enough to effect the policy change towards active economic adjustment in each member country. Nevertheless, it is becoming evident that the macro adjustment policies which are the most urgent task for every country can effectively be implemented only when interlinked neighboring countries are able to coordinate their efforts to harmonize regional adjustment policies and plans. The last lesson we learnt through the turbulent time of 1983 – 85 is the following.

*Lesson 6.* As long as it remains merely an informal forum, the present system of Pacific cooperation is too weak to make any substantial contribution to the stable growth of the economy of the member countries.

## II. The Coming Storm

The dramatic changes which have occurred in the world economic system since the 1985 Plaza Agreement present a new challenge to the Pacific cooperation. Although the currencies of most of the Pacific countries fell against the Japanese yen, they were later forced to appreciate against the U.S. dollar. This has caused a drastic shift in the region's trade. Although export growth of Asian manufactured goods to the U.S. did not slow down, the appreciation of the currencies against the dollar and the emerging protectionism in the U.S. caused a diversion of the export of manufactured goods to the Japanese market during the period 1986 and 1988. This trend was further promoted by the reduction of interest rates since March 1986, and by the decline of the oil prices. Thus, this situation led many people in most of the Pacific cooperation discussions to talk about the "dream" that the Pacific Age, or Age of Pacific Prosperity, was being realized.

As long as this self-sustained expansion in the Asian Pacific region continues, due to the exchange reform, lower interest rates and decrease in the price of raw materials, many people may have the illusion that the present system of Pacific cooperation plays a substantial role in maintaining the growth, stability and harmony in the Pacific region. But should a storm hit our region, mere dialogue would

turn out to be fruitless. I regret to have to raise this topic concerning the coming storm over the Pacific region, which is based on the following three factors.

First, all the previously favorable conditions which prevailed during the 1986–88 period are changing: the U.S. exchange rate has rebounded and consequently the value of the Asian and Latin American currencies against the yen has also rebounded; the interest rates which had fallen since March 1986 and thus promoted investment have risen again, and so have the prices of oil and other raw materials. This reverse trend may lead the Asian developing countries back to their original position of vulnerability, and the Latin American countries towards a new catastrophe. We have to be aware that the apparently successful export-led growth of these countries which gave cause for such optimism in 1986–88 may easily turn out to be short-lived and fragile. For the Pacific cooperation forums, the time of friendly exchange of amenities and good-will may soon come to an end, and the new stage of difficult negotiations and coordination between the conflicting national interests will emerge.

Second, symptoms of protectionism and trade-block regionalism are apparent, and consequently, we are facing a critical turning point of the IMF-GATT system. The crisis originates mainly from the decline of U.S. leadership in the global economy and security, and subsequent transition of the political power over foreign trade policies from the U.S. president to Congress.

The U.S. had been the flagbearer of global free trade since 1922 when she shifted her trade principle from bilateralism toward multilateralism by enacting the Fordney McCumber Tariff Act. And in 1934 the Congress' authority over foreign trade negotiations was entrusted tentatively to the President by the 1934 Reciprocal Trade Agreement Act. In the early 1970s the U.S. began to revert to her original bilateralism and protectionism, and this reversion has clearly escalated. During the early 1970s, difficult bilateral negotiations were actually held to protect the American textile and steel industries against imports from Japan and Europe. Subsequent series of bilateral negotiations were held for automobile and color TV sets in the late 1970s, and for the semi-conductors and other electronic products in the early 1980s. These bilateral negotiations took the form of Voluntary Restraint Agreement (VRA), and Orderly Market Agreement (OMA).

The unilateral preferential tariff and tax scheme enacted in 1983 led to the end of multilateralism. In September 1985 President Reagan in his address entitled "Integrated Trade Policies," declared the adoption of the notorious fair trade principle, by which the U.S. reserved herself the liberty to identify trade practices and trade partners as "fair," or "unfair." In August 1988, President Reagan signed the 1988 Omnibus Trade Competitiveness Act. This was close to a death blow to GATT's principle of free and non-discrimination trade.

Another threat to the GATT system is the American regionalism which is taking the new form of bilateral Free Trade Agreement (FTA). In January 1989, the U.S.-Canada FTA came into effect. It is reported that the U.S. and ASEAN are now considering the U.S.-ASEAN initiative, UAI, as the next version of bilateral FTA. Recently, former Ambassador Mansfield, backed by the Treasury Secretary

Table 2. INPUT-OUTPUT STRUCTURE OF PACIFIC BASIN  
INTERNATIONAL INPUT-OUTPUT TABLE, 1985

(US\$ million)

	United States	Japan	Asia NIEs <sup>4</sup>	ASEAN <sup>4</sup>	China	Latin America 3
United States	2,632,624	20,174	9,189	2,499	1,520	9,764
Japan	28,580	1,443,248	14,329	6,329	4,242	831
Asia NIEs <sup>4a</sup>	20,572	8,839	181,286	7,403	6,853	205
ASEAN <sup>4b</sup>	8,250	16,374	3,622	111,209	498	100
China	2,039	5,169	4,959	398	233,672	335
Latin America 3 <sup>c</sup>	11,935	2,666	240	252	599	434,201
Other	221,042	66,177	29,544	13,813	10,444	12,146
Value Added	3,957,000	1,239,549	192,903	188,143	238,319	469,758
Gross Output	6,882,041	2,802,195	436,072	330,045	496,147	927,339

Source: Our own estimation.

<sup>a</sup> Asia NIEs<sup>4</sup> consists of Korea, Taiwan, Hong Kong, Singapore.

<sup>b</sup> ASEAN<sup>4</sup> consists of Thailand, Malaysia, Indonesia, and the Philippines.

<sup>c</sup> Latin America 3 consists of Mexico, Brazil, and Argentina.

Baker and Commerce Secretary Verity, suggested the establishment of a U.S.-Japan FTA. It appears that the U.S. is now thinking of constructing a network of FTAs with other Pacific countries. There is a danger that trade-block regionalism in the form of FTA networks may invite the destruction of GATT's free trade system in this region.

Third, the threat of political turbulence in some countries in this region. The recent political turmoil in China has a tremendous long-term impact on the economic prospect of the region. Apart from the resulting sudden growth in political tension, the turbulence in China will have a dampening effect on the exports of many countries to one of the world's largest markets. The hardest hit will be Japan and the Asian NIEs, which have tried to divert their exports away from the U.S. and Europe where there is a rise in protectionism. Furthermore, the harshness of the political suppression in China has prompted the U.S. and other major countries to adopt of economic sanctions against China.

Moreover, the uncertainty concerning the political future of Hong Kong and Taiwan is casting a shadow on their economic prospects. Furthermore in ASEAN with the approaching elections for national leaders in the Philippines and Indonesia, there are doubts about the resulting political stability in those countries.

### III. Structural Background of Pacific Cooperation — Interdependence and Dichotomy —

The current dialogue on the Pacific cooperation is characterized by an optimistic view of the "Pacific Age," and an illusionary conviction about the structural linkage among the economies of the Pacific countries. In reality, based on our empirical study we discovered close links among the U.S., Japan and other Asian Pacific

countries, but a dichotomy between Latin America and the rest of the Pacific-rim countries. In this chapter, we examine the topic concerning interdependence and dichotomy.

### **1. Interdependence in production and trade**

In order to observe the production and trade interdependence within the Pacific countries, we have compiled a Pacific Basin Regional Input Output Table for 1985,<sup>1</sup> which includes 14 countries.<sup>2</sup>

The Pacific Basin I-O Table deals with 23 industries for each member country. Table 2 is a summary of the Pacific Basin I-O Table, obtained by pooling all the industries in the classification, and by grouping some countries into a subregion,<sup>3</sup> in which only the total figures for production and trade of each member country are shown. Table 2 illustrates the following aspects. First, the United States and Japan show the largest interdependence. Second, the U.S. and Asia NIEs and ASEAN countries show strong interdependence. Third, the trade pattern of Asia NIEs and ASEAN countries is different. Although both groups import more from Japan than from the U.S., the ASEAN countries export more to Japan than to the U.S. while Asia NIEs export more to the U.S. than to Japan. Fourth, the interdependence between the U.S. and Latin America is not significant, and Latin America's exports to the U.S. exceed their imports from the U.S. Fifth the interdependence between Latin American and Asian countries including Japan is minimal.

Table 3 shows the result of a simulation of the effect of GDP increase in the U.S. and Japan on the GDPs of countries in Asia<sup>4</sup> and Latin America based on the Pacific Basin I-O Table. It shows that 1000 units of GDP increase in Japan induces an increase of 34.4 units of GDPs in the U.S., 48.2 units in Asia and 4.5 units in Latin America.<sup>5</sup> Clearly Asia is by far the greatest beneficiary from an increase in Japan's GDP. Latin America's link with Japan is smaller than that with the U.S. A GDP increase of 1000 units in the case of Japan gives Latin America only a GDP rise of 4.5 units, in contrast to the case of the U.S. which raises Latin America's GDP by 9.8 units. The link between the U.S. and Asia is even more pronounced. A 1000 unit increase in U.S.'s GDP raises the income in Japan by 40.3 units and in Asia by 29.1 units.

The observations above also illustrate the role of the U.S. and Japan, as the engine of growth in the world economy. The rise of 1000 units in GDP of the U.S. and Japan pulled the income in other parts of the world by 79.2 and 87.1 units, respectively.

### **2. Financial interdependence**

There is a bias in the interdependence of international financing among the Asia Pacific countries and Latin American countries. Table 4 shows the financial interdependence among the U.S., Japan, Asia and Latin America. Throughout the first half of the 1970s, concessional official funds from the U.S. and Japan including ODA, provided the bulk of assistance to the Asian and Latin American

Table 3. SIMULATION OF GDP INCREASE IN VARIOUS COUNTRIES: INDUCED BY 1000 UNIT INCREASE IN JAPAN AND THE UNITED STATES

(Unit: US\$)

	Total Induction (Direct and Indirect GDP Increase) in				
	Japan	United States	Asia	Latin America 3	Total
Case of 1000 unit increase in Japan's GDP through direct increase in					
Japan		15.3	29.3	2.0	46.6
United States		18.3	0.2	0.1	18.6
Asia		0.6	18.8	0.1	19.4
Latin America 3		0.1	0.0	2.4	2.5
Total		34.4	48.2	4.5	87.1
Case of 1000 unit increase in the United States' GDP through direct increase in					
Japan	33.4		0.8	0.1	34.2
United States	5.6		7.6	3.5	16.7
Asia	1.3		20.8	0.0	22.1
Latin America 3	0.0		0.0	6.2	6.2
Total	40.3		29.1	9.8	79.2

Source: Our own estimates.

Note: Asia consists of Korea, Taiwan, Hong Kong, Singapore, Thailand, Malaysia, Indonesia, the Philippines, and China. Latin America 3 consists of Mexico, Brazil, and Argentina.

developing countries. As a result of the U.S. banks' active recycling of petro-dollars, a large amount of private funds flowed to Latin America in the second half of the 1970s. In Asia, too, flows of private funds increased due to the rapid industrialization of the newly industrializing economies (NIEs).

Following the Mexican debt crisis in 1982, the U.S. official development assistance and private funding, which had sustained the economic development of Asia and Latin America, began to decrease, and the slow-down became considerable in 1985. The amount of U.S. private funds decreased markedly, resulting in a worldwide decrease in development finance.

The U.S. has also cut back its provision of official assistance, and reduced its ODA budget year after year to as little as \$8.8 billion in fiscal 1988. Although it is anticipated that U.S. ODA will rebound to \$9 billion, this is still less than Japan's \$9.7 billion. The U.S. retreat in development financing, both official and private, creates a vacuum that endangers the Pacific and Latin American economy.

Thus, the U.S. request to, or pressure on, Japan to take over the responsibility of providing official development assistance, private funds, and relief to ease the debt burden of Latin American and Pacific countries has become one of the most important issues of the Pacific cooperation. The dialogue on this topic of development financing and reduction of debt burden requires serious attention.

Pacific development financing and the Latin American debt crisis involve both

Table 4. FINANCIAL FLOWS: OFFICIAL AND PRIVATE FLOWS FROM JAPAN AND THE UNITED STATES TO ASIAN NIEs4, ASEAN4, AND LATIN AMERICA

(US\$ Million)

		Asia NIEs4 <sup>a</sup>		ASEAN4 <sup>b</sup>		Latin America <sup>c</sup>	
		Official	Private	Official	Private	Official	Private
Japan	1983	- 1.3	619.2	942.9	1,198.0	435.6	547.9
	1985	5.0	1,068.0	778.9	560.4	361.1	295.0
	1987	- 833.6	2,435.5	2,176.6	701.2	528.4	1,025.0
United States	1983	377.0	912.0	472.0	1,157.0	- 309.0	7,803.0
	1985	- 363.0	- 957.0	281.0	197.0	727.0	- 5,062.0
	1987	- 2,050.0	1,340.0	219.0	- 598.0	853.0	- 4,439.0

Source: OECD, *Geographical Distribution of Financial Flows to Developing Countries*, various issues.

<sup>a</sup> Asia NIEs4 consists of Korea, Taiwan, Hong Kong, and Singapore.

<sup>b</sup> ASEAN4 consists of Thailand, Malaysia, Indonesia, and the Philippines.

<sup>c</sup> Latin America consists of Brazil, Argentina, Uruguay, Paraguay, Chile, Bolivia, Peru, Ecuador, Colombia, and Mexico.

the developed and developing countries engaged in the Pacific cooperation dialogue. As for the former, we have to discuss how to revive the U.S. role of official and private financing in this region, together with how to increase Japan's burden sharing. As for the latter we should analyze the reasons for the increase of debts in Asia and Latin America and how these debts should be managed.

The figures on the factors related to the increase and decrease of the debt in the Asian NIEs, ASEAN, and Latin American countries are compiled in Table 5 for 1983, 1985 and 1987 according to the decomposition formula.<sup>6</sup> Important considerations can be derived as follows:

(1) In the Asian NIEs, the rate of increase of debt has been declining and in some cases a country has turned from borrowing to lending funds on a net basis. The debt increase, net, for Korea in 1985 was as large as US\$5.1 billion but in 1987 Korea lent out over US\$6.3 billion. Although Taiwan was providing credit amounting to US\$770 million in 1985, it became a net borrower of US\$4.5 billion in 1987. This can be attributed to the inflow of private foreign funds resulting from Taiwan's increased economic credibility.

(2) Among the ASEAN countries the debt increase has been more or less controlled. For Thailand and Malaysia, the yearly increase ranges between US\$1.6 - 3.2 billion. However, Indonesia's debt increase in 1987 rose to almost US\$10 billion. The debt increase has remained limited despite the fact that most countries are still suffering from some deficits in their trade accounts.

(3) There is a persistent tendency of debt increase through borrowing among the countries in Latin America. The debt increase in 1987 for Argentina, Brazil and Mexico reached US\$7.1 billion, 11.2 billion, and 6.8 billion, respectively. The

sharp increase of Latin America's borrowing occurred in spite of large trade surpluses for most of the countries. This obviously indicates that the main reason for the Latin America's debt increase is not the trade deficit but the large amount of financial leakage caused by debt service, foreign remittance of profit, and capital flight.

(4) The leakage of funds, which is calculated as a residual figure in the formula shown in the Note 6 and includes remittance of profit and capital flight but excludes debt services, appears to be very large in the Latin American countries when compared with the annual debt increase shown in the sixth column of Table 5. For example, in 1987, Indonesia's leakage of funds reached US\$11.4 billion while the debt rise was US\$9.5 billion; Mexico, on the other hand, had a leakage of US\$7.1 billion while its debt increased by US\$6.8 billion.

(5) Debt service commands a large amount of funds, compared to the annual debt, in all the countries of Asia and Latin America. However, for Asian NIEs and ASEAN, most of the debt service is directed to amortization in sharp contrast with the Latin American case where interest payments account for more than twice the amount of amortization. It should be noted also here that the interest rates charged for loans to Latin American countries are usually 2–3% higher than those charged for ASEAN. For example, in 1987 Argentina paid an average of 8.2% for all types of credits while Thailand was charged only 5.3%.

#### **IV. A Case Study of Pacific Cooperation — Simulation of Integration of Latin America into the Pacific Trade Circle —**

Through these observations we have revealed the unfortunate dichotomy between Latin America and the rest of the Pacific-rim countries. Therefore, it is obvious that the new task of the Pacific cooperation, among others, is to try to integrate the Latin American economy into the Pacific economy. By assuming the same production structure in each country but the doubling of the trade flow between Latin America and the Asian Pacific countries including Japan, a promising outlook for the future of Latin America could be revealed.

By our simulation, as shown in Table 6, doubling of exports from Latin America to Asia boosted the GDP in Latin America by 1.877% while a doubling of imports from Asia by Latin America raised the income among the Latin American countries by 0.004%. Therefore, the total increase of GDP in Latin America will be as high as 1.881% as trade in both exports and imports between Latin America and Asia doubles.

Thus, the policy implication, suggested by this simulation on how to improve the Latin American economic condition hurt by the debt crisis, is for Asia to open its market widely to goods from Latin America. And, such a policy target could efficiently be pursued in the Pacific cooperation dialogue.

(US\$ million)

Table 5. DEBT INCREASING AND DECREASING FACTORS

	Debt Increasing Factors										Debt Decreasing Factors			
	Increase of Debt (-ΔD)	Trade Balance (-M-X)	Debt Service			Leakage of Fund and Other Factors (-L&O)	Increase of Reserve (-ΔR)	Direct Investment (DI)	ODA Grant (ODG)	Use of IMF Credit (IMF)	Debt Increasing Factors		Debt Decreasing Factors	
			Total (-DS)	Amortization (-AMO)	Interest Payments (-INT)						(-ΔD)	(-ΔR)	(DI)	(ODG)
Korea	1983	-3,090.0	-1,763.0	-4,944.0	-2,664.0	-2,279.0	366.9	460.6	-57.0	30.4	151.1			
	1985	-5,061.0	-19.0	-7,181.0	-4,405.0	-2,776.0	-2,160.3	-115.7	200.0	35.9	-225.9			
	1987	6,269.0	7,659.0	-15,469.0	-13,094.0	-2,375.0	1,660.2	-264.1	418.0	67.4	-896.5			
Taiwan	1983	-256.0	6,268.0	-1,976.0	-1,111.0	-865.0	-2,309.5	-3,478.0	130.0	-1.5				
	1985	770.0	11,170.0	-2,059.8	-1,268.9	-790.9	-2,828.8	-7,040.0	260.0	-0.3				
	1987	-4,517.0	20,212.0	-2,357.8	-2,086.4	-271.4	7,348.2	-31,819.0	11.0	2.2				
Hong Kong	1983	-845.0	-575.4	-318.9	-30.1	-288.8	-1,087.7		1,097.5	9.4				
	1985	-781.0	1,904.8	-333.3	-47.3	-286.0	-2,278.1		-142.1	20.4				
	1987		2,483.1						2,868.2	19.1				
Singapore	1983	-174.0	-610.0	-689.0	-486.0	-202.0	316.2	-784.4	1,085.0	21.2				
	1985	-116.0	-4.0	-1,045.0	-793.0	-252.0	1,733.8	-2,430.6	809.0	27.8				
	1987	-616.0	539.0	-877.0	-572.0	-305.0	424.3	-2,288.0	982.0	31.7				
Thailand	1983	-1,670.0	-2,861.0	-1,760.0	-1,012.0	-748.0	1,217.2	-69.0	348.0	211.8	231.0			
	1985	-2,547.0	-1,332.0	-2,590.0	-1,679.0	-911.0	-582.7	-269.0	162.0	263.7	122.0			
	1987	-2,161.0	-386.0	-2,949.0	-1,891.0	-1,057.0	144.0	-1,203.0	182.0	322.0	-163.0			
Malaysia	1983	-3,223.0	432.0	-1,653.0	-714.0	-940.0	-4,091.3	-16.0	1,261.0	64.3	67.0			
	1985	-2,159.0	3,577.0	-5,142.0	-3,649.0	-1,492.0	-3,696.6	-1,189.0	695.0	102.6	-156.0			
	1987	-1,676.0	5,886.0	-4,158.0	-2,697.0	-1,461.0	-5,401.0	-1,408.0	575.0	133.0	0.0			
Indonesia	1983	-3,638.0	963.0	-3,658.0	-2,023.0	-1,635.0	-3,425.1	-574.0	292.0	316.1	425.0			
	1985	-4,047.0	5,822.0	-5,027.0	-3,107.0	-1,920.0	-8,017.2	-201.0	310.0	338.2	-379.0			
	1987	-9,542.0	4,968.0	-6,482.0	-3,734.0	-2,748.0	-11,470.6	-1,541.0	307.0	479.6	463.0			

Table 5. (Continued)

	Debt Increasing Factors										Debt Decreasing Factors			
	Increase of Debt (-ΔD)	Trade Balance (-M-X)	Total (-DS)	Debt Service			Leakage of Fund and Other Factors (-L&O)	Increase of Reserve (-ΔR)	Direct Investment (DI)	ODA Grant (ODG)	Use of IMF Credit (IMF)			
				Amortization (-AMO)	Interest Payments (-INT)									
Philippines	1983	175.0	-2,485.0	-1,769.0	-831.0	-938.0	2,949.4	141.0	105.0	258.6	144.0			
	1985	-1,832.0	-482.0	-1,523.0	-592.0	-931.0	-833.7	-13.0	12.0	244.7	171.0			
	1987	-1,109.0	-1,017.0	-2,372.0	-876.0	-1,497.0	114.9	760.0	186.0	461.1	-117.0			
Argentina	1983	-2,291.0	3,716.0	-3,781.0	-1,364.0	-2,417.0	-6,258.2	1,334.0	183.0	30.2	1,121.0			
	1985	-468.0	4,878.0	-5,407.0	-1,018.0	-4,390.0	-866.7	-2,030.0	919.0	37.7	984.0			
	1987	-7,098.0	968.0	-4,470.0	-695.0	-3,775.0	-5,926.6	1,101.0	-19.0	78.6	475.0			
Brazil	1983	-5,562.0	6,469.0	-11,245.0	-3,582.0	-7,664.0	-7,428.5	-427.0	1,373.0	88.5	2,027.0			
	1985	-1,558.0	12,466.0	-10,266.0	-2,935.0	-7,331.0	-8,905.6	903.0	1,267.0	107.6	-65.0			
	1987	-11,153.0	11,158.0	-9,516.0	-3,682.0	-5,834.0	-16,346.8	-496.0	1,087.0	155.8	-877.0			
Mexico	1983	-6,946.0	13,762.0	-12,988.0	-4,837.0	-8,151.0	-11,024.6	-3,079.0	461.0	82.6	1,003.0			
	1985	-1,967.0	8,451.0	-14,515.0	-5,122.0	-9,393.0	-4,302.8	2,366.0	491.0	125.8	295.0			
	1987	-6,828.0	8,433.0	-11,425.0	-4,333.0	-7,091.0	-5,084.2	-6,794.0	3,248.0	140.2	320.0			
Venezuela	1983	-5,386.0	8,162.0	-3,791.0	-1,653.0	-2,138.0	-10,432.0	-1,064.0	86.0	—	—			
	1985	1,764.0	7,130.0	-2,765.0	-996.0	-1,769.0	-2,315.0	-1,350.0	68.0	—	—			
	1987	-1,810.0	1,735.0	-4,107.0	-1,589.0	-2,518.0	-1,522.0	474.0	21.0	—	—			

Sources: World Bank, *World Debt Tables*, 1989; IMF, *International Financial Statistics*, various issues; ADB, *Key Indicators of Developing Member Countries of ADB*, July 1988; OECD, *Geographical Distribution of Financial Flows to Developing Countries*, various issues.

Note: 1. ΔD in this table is defined as an increase of Debt Stock.

2. Changes of exchange rates and other factors which affect Debt Stock are included in Leakage of Funds and Other Factors.

Table 6. SIMULATION OF GDP INCREASE IN VARIOUS COUNTRIES INDUCED BY DOUBLED TRADE FLOWS BETWEEN ASIA AND LATIN AMERICA

(%)

	Asia				United States	Latin America <sup>3c</sup>	Total
	Asia NIEs-4 <sup>a</sup>	ASEAN <sub>4</sub> <sup>b</sup>	China	Japan			
Doubling Asia's exports to Latin America	0.225	0.168	0.379	0.196	0.003	0.004	0.080
Doubling Latin America's exports to Asia	0.001	0.009	0.002	0.001	0.012	1.877	0.150
Doubling both	0.226	0.177	0.380	0.197	0.016	1.881	0.230

Source: Our own estimates.

<sup>a</sup> Asia NIEs4 consists of Korea, Taiwan, Hong Kong, and Singapore.<sup>b</sup> ASEAN4 consists of Thailand, Malaysia, Indonesia, and the Philippines.<sup>c</sup> Latin America 3 consists of Mexico, Brazil, Argentina.

## Concluding Remarks

The spirit of cooperation that has been fostered among the people of the Pacific region throughout the past forty years is a very valuable asset of the free economic system of the world. Without this spirit, we would have never had the opportunity to meet and discuss matters in this conference. However, sufficient discussions have already been held concerning the needs to promote a closer cooperation among the countries of the Pacific area, and I believe that the time is ripe for the next stage of concrete action. The urgency of action is being felt more acutely due to two main issues that are threatening the survival of the free world's economy.

First is the chronic third-world debt problem, especially in the Latin American countries. This problem is closely linked to many others and if not solved, may trigger an economic disaster throughout the world. Debt default and the termination of financial flows into these countries may lead to a deep recession with political consequences, which will not be limited to the debtor nations. The U.S. used to be content in the past when it enjoyed large trade surplus against Latin America. However, the loss of this Latin American market, following the deterioration of the debt problem and the loss of the region's purchasing power, has prompted the U.S. to direct its discontent to the Asian Pacific nations which experience fast growth and, unquestionably, this has been an important factor that triggered the rise of protectionism in America.

This leads us to the second problem concerning the surge protectionist mood and the dangerous trend towards trade-block regionalism. One should not forget that the policy of "begging thy neighbors" was mainly responsible for the decline in the world trade that led finally to the Great Depression of the 1930s. The present

level and the future growth of the global trade volume can be maintained only by the system of free world economy based on the benevolent spirit of GATT. Setting up blocks of trading partners is equivalent to the dismantling of the achievements of GATT which were the works of many years of toil and negotiations. It can be compared to killing the goose that has been laying golden eggs for us.

Whether the dream of a prosperous Pacific region will be realized or not depends much on the development of the two serious issues mentioned above. I believe that the solution of these problems is an urgent task for all of us here. And this can be achieved only through greater policy coordination among the countries in the Pacific region together with other areas of the world. Recently, the way of reaching this objective has become clearer with the proposals put forth by two leading politicians, namely Australia's Prime Minister Hawke who suggested the creation of a ministerial assembly of the OECD-type, and U.S. Secretary of State Baker who also proposed the creation of a cooperative organization shaped after the OECD.

However, in my opinion, there is a need for adopting more concrete and practical measures to achieve real policy coordination among the Pacific Basin countries. I would like to suggest, based on the past discussions of the Pacific cooperation, that the existing informal networks be institutionalized into a cooperative body in which the Pacific countries can coordinate their domestic macroeconomic adjustment, trade policy, and debt control. For this purpose, the OECD-type of institutionalization which is characterized by an international bureaucracy is not suitable. An assembly or a parliament composed of scholars, businessmen, statesmen and bureaucrats representing each member country, could fulfill the function of effective coordination. Such an organization may help defuse the time bomb of third-world debt crisis and worldwide protectionism. And, only then, can we reach the dream of the Pacific Era.

## NOTES

1. The author fully owes Y. Akiyama, assistant professor of Keio University, for the compilation of the Pacific Basin Regional Input Output Table.
2. The 14 countries are the U.S., Japan, Korea, Taiwan, Hong Kong, Singapore, Thailand, Malaysia, Indonesia, the Philippines, China, Mexico, Brazil and Argentina. Among these 14 countries, only Japan and Korea have their own 1985 I-O tables. For the rest of them, we estimated their 1985 I-O table by applying the RAS method on the most recently available I-O tables and the total demand statistics of 1985. For Hong Kong, which does not have its own I-O table, we assumed the input-output coefficients to be the same as those of Singapore. We are planning to include Canada, Australia, New Zealand, and some other Pacific-rim Latin American countries such as Chile and Peru into our table. Although Brazil and Argentina are not on the Pacific rim, their linkage with U.S. and Japan through the real economy, especially trade, and through the financial flow calls for their inclusion into the I-O linkage.
3. Grouping of countries: Asia NIEs 4 includes Korea, Taiwan, Hong Kong and Singapore, ASEAN 4 includes Thailand, Malaysia, Indonesia and the Philippines, and Latin America 3 includes Mexico, Brazil and Argentina.

4. In Table 4 "Asia" includes Asia NIEs, ASEAN and China.
5. 1000 units can be interpreted as either "million" or "billion" dollars according to the purpose of analysis.
6. The decomposition of the debt increase ( $\Delta D$ ) is shown in the following formula.

$$\Delta D = (M - X) + DS + (L\&O) + \Delta R - (DI + ODG + IMF) - (AMO)$$

(Debt increasing factors)

$\Delta D$  : Increase of Debt

$M - X$  : Trade balance (deficit)

$DS$  : Debt service (= Amortization + Interest Payment)

$L\&O$  : Leakage of Fund (includes Capital Flight) and Other Flows\*

$\Delta R$  : Increase of Reserve

(Debt decreasing factors)

$DI$  : Direct investment

$ODG$  : ODA Grant

$IMF$  : Use of IMF funds

( $AMO$  : Amortization)

\*L&O is calculated as the residual of the balance equation.