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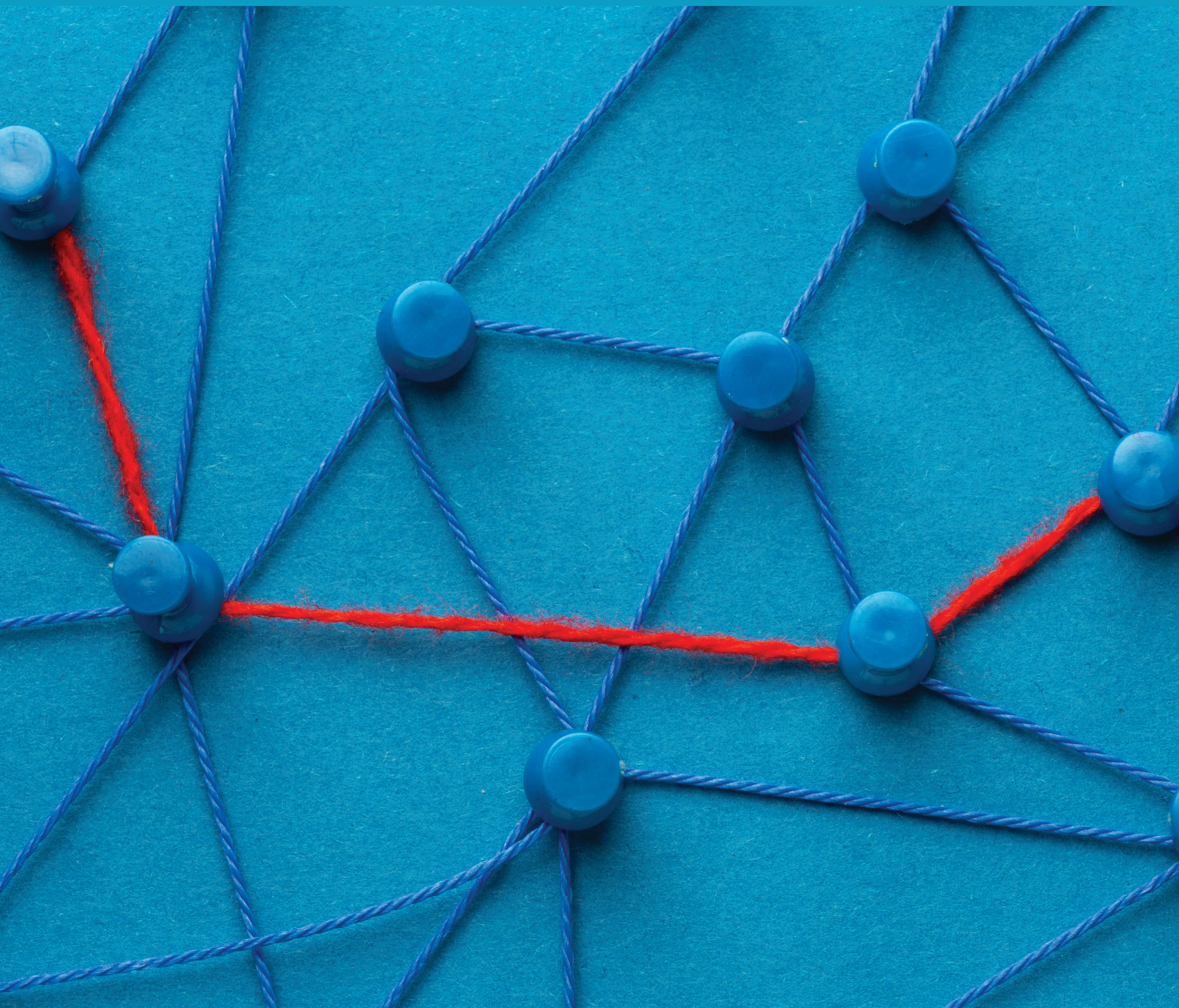
CONNECTIVITY, COOPERATION, and NEW SUPPLY-CHAIN LINKAGES

Edited by

ANITA PRAKASH



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Observer Research Foundation
20 Rouse Avenue, Institutional Area
New Delhi 110002
India
contactus@orfonline.org
www.orfonline.org

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Preface

Opportunities and disruptions arising in the Indo-Pacific region can be addressed through economic cooperation strategies that can recognise and include different stages of industrial development in countries in Asia, the Pacific, Africa, Europe, as well as the United States (US). The Indo-Pacific economic architecture responds to the different policy and plan needs of developing and developed parts of Asia and the Pacific. Along with the need for achieving high and sustained growth in developing countries and least developed countries in the region, there is greater recognition for ensuring equitable, spatially even, and inclusive economic growth amongst all stakeholders.

It is often said that change is a recognition of and adaptation to new needs. The Asia-Pacific represented the post-war construct of the economic rise and institutional maturing in several countries in East and Southeast Asia. The phenomenal economic gains of the Asian Tigers, the political and economic success of the Association of Southeast Asian Nations (ASEAN) community, and the growing importance of the Pacific Island countries all contributed to the successful construct of economic cooperation in the Asia-Pacific region. During this phase, the US and, to a lesser degree, the European Union (EU), were important guarantors of the strategic and economic interests of most countries in the region.

Along this growth trajectory, the rise of China aided the economic dynamism of the region for nearly two decades. China's economy helped Asia remain a bright spot of growth even during the global financial crisis of 2008. Asia and the Pacific provided tailwinds to the global economy during this time. The 2008–2015 period was also when most developed economies took time-out to offset the adverse effects of the financial crisis on their financial, political, and social institutions.

Around the same time, developed and developing Asia, despite relative comfort in terms of growth and prosperity as well as trade openness, became vulnerable to a unilateral interpretation of the status quo in the South and East China Sea. The strategic activities in the two seas caused ripple effects on the economic linkages in Southeast and East Asia. The deep global value chain (GVC) connectivities amongst Southeast Asian countries and China, and between Japan and China, as well as the exchange of investments amongst them all created a ground for dissatisfaction with the existing economic architecture, notwithstanding the ensured economic returns from existing trade integration with China and the complexity involved in unravelling the backward–forward integration of exports in several important sectors.

The introduction of the Belt and Road Initiative in 2015 (and its critical evaluation) could be viewed as the policy convergence point for governments in Asia and Europe as well as in the US to mobilise support for the Indo-Pacific economic architecture in which strategic and economic interests are brought closer than what most trade economists would favour. In other words, the emergence of the Indo-Pacific economic architecture is similar to the conditions when Japanese and US investment initiatives in Southeast Asia during the post-war period galvanised the Asia-Pacific. Policy and political leadership are the primary movers of the new architecture, which will eventually be supervised by economic returns.

To say that the evolution of the Indo-Pacific economic architecture is aimed at the containment of China is a simplistic explanation. The Indo-Pacific undoubtedly addresses China centrality in production sharing in the region and the dependency of the EU and the US on the supply chains of China. From a policy research perspective, the Indo-Pacific economic architecture is more than a reaction to the existing production networks and investment channels in the region. The evolution of this architecture is a preparation for new economic demands before all countries in the region. Structural transformation and employment generation policies in developing Asia and the Pacific must understand, prepare, and respond to the new digital economy, as the latter will affect the patterns and geographical location of industries, employment, trade, and economic growth. Increased industrialisation and participation in GVCs are important for growth and employment generation in several less developed countries. The future of work is vulnerable to decreased investments in manufacturing, and jobs being replaced by automation, robotics, and artificial intelligence, especially for countries that are not deeply integrated in regional or global value chains.

Geographical inclusiveness is an important aspect of the Indo-Pacific architecture. The role of smaller countries—especially the Pacific Island states, which are new entrants to the regional connectivity plans—is particularly recognised in this study and for the future monitoring of economic performance in the Indo-Pacific. Human resources and the movement of people are equally linked with the new digital economy as well as the future of work. Interweaving these elements of cooperation into economic cooperation in the Indo-Pacific will prepare the region for the future.

The COVID-19 pandemic reinforced the need for more equitable distribution of infrastructure and capacities and investments in new centres of production, supply chains, and consumer/

supplier clients. While there are several interpretations of the effects of the pandemic on supply chains, two extreme examples underscore the need for a more enabled, equitable, and inclusive economic cooperation model for the region. The breakdown of the supply of medical equipment and kits from China during the pandemic and the regional distribution of vaccines produced in India in the latter part of the pandemic are emblematic of the problems and solutions before the Indo-Pacific economic architecture.

Trade and investment have underwritten the growth story in the Indo-Pacific. The digital economy is, however, here to stay. As industries, employment, trade, and economic growth continue to change under the influence of digitalisation, the Indo-Pacific region must reap the benefits of this progress. The Indo-Pacific architecture must ensure that digitalisation promotes inclusiveness, especially for youth and women. Asia, Europe, and the US have different levels of digital infrastructure. However, cooperation for the development of services, human capital, regulations for data protection, e-commerce, and taxation require greater institutional linkages amongst all stakeholders. The emergent supply chains and cooperation frameworks will bridge these needs in the Indo-Pacific.

The Indo-Pacific economic architecture is linked to restoring multilateralism that recognises diversity yet leaves no one behind. It is worth noting that multilateralism has provided stability and prosperity to a great number of countries for nearly a century. Global governance of connectivity is also a new challenge, as countries contest and compete for technology that provides interconnections. Managing the internet is most apparent, but the technology underlying electronic commerce and the financial system is much more significant. The traditional chapters of trade agreements—on goods, services, and investment—while still contentious, are now subordinate to the field of technology. The Indo-Pacific economic architecture has no choice but to undertake global actions which aim to resolve this challenge.

In the end, neither multilateralism nor global governance exists for its own sake. The ultimate test for both is to create prosperity that is inclusive and sustainable. The Indo-Pacific economic architecture must consolidate its initiatives, spell out the principles of cooperation, and provide action on its preferred aspects of plurilateral/multilateral economic cooperation and global governance.

This study is an attempt to consolidate information on the Indo-Pacific economic architecture along six important verticals: infrastructure, GVC integration, development cooperation, digital economy, human resources and the movement of people, and geographical inclusiveness for the Pacific. The rebalancing of old elements of trade integration and the introduction of new elements of cooperation in which strategic and economic interests are brought closer to principles of governance, transparency, equity, and inclusiveness emerge as the core of the emergent architecture in the Indo-Pacific.

The Indo-Pacific is a plurilateral component of the international economy in which regions and countries find it mutually advantageous to work cooperatively. However, it brings the Atlantic and Pacific powers much closer to the Indian Ocean to emphasise cooperation and international production sharing that involve services as much as goods. The transformations brought about by this cooperation architecture must fulfil the objectives of mutual trust and mutual growth. The challenge is not to maintain a rules-based system but to create and operate institutions that evolve and sustain rules in the face of change, and the relationships must all be inclusive. To that extent, 'Connectivity, Cooperation, and New Supply Chain Linkages' will be central to the agenda of the Indo-Pacific economic architecture.

Emerging Economic Architecture in the Indo-Pacific: Asia and the Pacific at the Centre of Trade, GVC Integration, and Economic Cooperation of the Future

The evolving economic architecture in the Indo-Pacific rests squarely on the post-war construct of the Asia-Pacific, which has been in existence for six decades but is undergoing changes in the established patterns of economic integration and supply chain linkages. There are without doubt opportunities and challenges in the new policy alignments for institutional support, and (different levels of) willingness amongst governments over such changes in the supply chain linkages and investments—both in Asia and outside Asia—to materialise a newer construct of trade and economic cooperation. The raison d'être of building a new construct lies in the re-evaluation of the existing trade and investment linkages—in Asia, between Asia and the Pacific, between Asia and Europe, and between Asia and Africa—and in the re-calibration of these linkages, along with economic and technical cooperation activities, to reflect the emergent economic and strategic alignments amongst countries and regions. The economic dynamism of Southeast and East Asia, and now increasingly of South Asia, has been at the centre of all economic and strategic cooperation plans, both bilateral and plurilateral, amongst countries in the region and with interregional partners such as the United States (US), the European Union (EU), the United Kingdom (UK), Canada, and even some parts of Africa. Added to this is the opportunity of including the Pacific Island states in the economic linkages in a more vibrant and inclusive manner. To understand the emergent economic architecture in the Indo-Pacific, it is important to evaluate the current state of trade and investment in the wider region from a growth perspective, as well as the strategic importance of regional value chains and global competitiveness for dominating the new technologies that influence both the existing and new centres for the production and consumption of goods and services.

Indo-Pacific: A Long Way from the Far East, East Asia, and Asia-Pacific

In Urata et al.'s (2019) seminal research study *ASEAN Vision 2040* (Tay et al. 2019), the authors described the evolution of trade and supply chain linkages in the Asia-Pacific, which are based on the trade and investment policies of the major economic players and reflect changes in the strategic interests of the countries in Southeast and East Asia.

In the post-war period, when leadership of world affairs rested in the North Atlantic region, the countries of Southeast Asia were often seen simply as part of the 'Far East'. In the third quarter of the 20th century, the Association of Southeast Asian Nations (ASEAN), then with six members, played a key role in making familiar the concept of the 'Asia-Pacific' (Urata et al. 2019). The Asia-Pacific was understood in different combinations of countries and regions. Urata et al. (2019) elaborated on the different understandings of the geography of the Asia-Pacific in terms of economic linkages, trade and investment, and movement of people, although political history and strategic interests prevail upon these linkages to varying degrees. The Japanese word order was 'Pacific Asia', which included the eastern and south-eastern edge of Asia, Australia and New Zealand, and the US, due to the importance of its security relationship with the region. Canada was also included, by analogy with the US, and Mexico and South America came later, mostly as a by-product of the North American Free Trade Agreement and the subsequent trade agreement with Chile. The American understanding of 'Asia-Pacific' was similar, along with the identification of the US as a Pacific power after World War II. The British and European understanding of the Asia-Pacific was more likely to include India, while in Australia and New Zealand it was usually read as 'Asia and the Pacific' to include the Pacific islands.

The Asia-Pacific, however, was more than a geographical understanding (which is also true for the current theme of economic cooperation in the Indo-Pacific—a concept that lacks geographical continuity but professes cooperation over trade and investment, and infrastructure and institutional connectivity). The Japanese-led economic integration in the region was characterised by business leadership and diplomatic and official processes ensuring several trade and investment facilitation measures, followed by business decisions on investment and the location of operations. Japan's experience with export-led growth was quite unlike the prevailing policies in most Asian economies, which favoured import substitution. This growth model was soon followed in the Republic of Korea (henceforth, Korea), Taiwan, Singapore, and Hong Kong in the renowned 'flying geese' formation.[1] Thailand, Indonesia, and other Southeast Asian countries followed. China was too big to be a single goose in a flock, and its opening to international integration after 1978 ushered in a new phase of regional growth. This growth experience was located in the 'Asia-Pacific'.

1 The "flying geese pattern of development" was coined by Kaname Akamatsu in 1930s articles in Japanese, and presented to world academia after World War II in 1961 and 1962 articles in English. The flying geese model explains the catching-up process of the industrialisation of latecomer economies from the intra-industry aspect (product development within a particular developing country, with a single industry growing over three time-series curves, i.e. import (M), production (P), and export (E)); inter-industry aspect (sequential appearance and development of industries in a particular developing country, with industries being diversified and upgraded from consumer goods to capital goods and/or from simple to more sophisticated products); and international aspect (subsequent relocation process of industries from advanced to developing countries during the latter's catching-up process).

The founding of ASEAN in 1967 helped shape the conception of the region from being the 'Far East'—far away from the global centre (the North Atlantic)—to the more familiar 'East Asia', which is increasingly seen as the global centre of manufacturing, and consumption of goods and services. The institutional basis for the Asia-Pacific was supported to varying degrees by the non-official Pacific Economic Cooperation Council (founded in 1980) and the Asia-Pacific Economic Cooperation (APEC) process, which was established in 1989 and extended to leader-level summits in the early 1990s.

ASEAN played an important role in the early history of APEC. Its members were crucial in the endeavour to develop a governmental process from the Track II processes of the Pacific Economic Cooperation Council. The six ASEAN Member States (AMS), which represented half the membership of APEC, initially staged half the annual meetings, and generally provided one of two co-chairs for all significant APEC committees. The inclusion of China, Hong Kong, Taiwan, and Latin American members diluted the role of ASEAN and, although Viet Nam became a member of APEC, other new members of ASEAN—i.e. Cambodia, the Lao People's Democratic Republic, and Myanmar—did not (Urata et al. 2019).

The Asian financial crisis in 1997 reshaped the intra-regional relations to a great degree. The dissatisfaction of ASEAN with financial agencies such as the International Monetary Fund and the World Bank extended to institutional platforms such as APEC, even though financial issues were not central to the role of APEC. The Asian members found the cooperative principles and assistance from other members missing during the crisis. APEC soon ceased to be the unrivalled institutional platform for economic cooperation in the Asia-Pacific, as ASEAN created its own regional trade and economic cooperation mechanisms for strengthening its own economic community objectives, as well as driving the regional economic integration process in Southeast and East Asia region from a position widely known as 'ASEAN centrality' in the post-crisis years.

ASEAN's Evolving Role in East Asia and the Indo-Pacific

In 1999, the institutionalisation of the ASEAN+3 grouping marked a pivotal moment in East Asian cooperation. Over time, this collaboration expanded into the East Asia Summit (EAS), reflecting the region's changing economic and strategic dynamics. The EAS became a platform for addressing trade, economic, and technical cooperation, bridging gaps between original members and new entrants like India, Australia, and New Zealand.

The dichotomy between trade and investment cooperation and strategic security issues within the EAS became apparent, with the US attempting to position it as a "political and security" institution. However, this blurred distinction did not align with the original vision of ASEAN+6 EAS members.

Japanese leadership played a crucial role in aligning the narratives of the Asia-Pacific and East Asia. Prime Minister Shinzo Abe's speech at the United Nations General Assembly in October 2017 set the tone for regional cooperation for exploring new markets, securing strategic interests, and investing in new supply chains. In 2018, he set forth the idea of a 'Free and Open Indo-Pacific', highlighting economic linkages and cooperation in the region.

While the term 'Indo-Pacific' was initially met with scepticism due to perceived security connotations, Prime Minister Abe's vision laid the groundwork for economic cooperation in the region, fostering connectivity between Asia, Africa, and Europe. He separately revived the Quadrilateral Security Dialogue or Quad, bringing in the US as a major economic partner in the region—underplaying the security partnerships of the US and actively engaging with Australia and India, with ASEAN playing an important link in between though not at the table.

In 2019, ASEAN introduced the ASEAN Outlook on the Indo-Pacific, recognising its centrality in the evolving architecture, just as ASEAN had driven the ASEAN+1, ASEAN+3, and EAS meeting process. In practice however, ASEAN's centrality in the Indo-Pacific requires greater deliberation, given the challenges in balancing the strategic interests of several of its Member States or the Dialogue Partners.

The role of India in this narrative becomes crucial, considering its growing importance in the Indo-Pacific. India's participation in the EAS, despite initial reservations from some members, reflects the dynamic nature of the term 'East Asia'. Its deep historical and cultural linkages with Southeast and East Asia, combined with its Act East policy (prior to 2014, Look East policy), facilitated its entry into regional institutional arrangements.

India's trade integration with East Asia, especially with ASEAN, strengthened over the years. The Framework Agreement on Comprehensive Economic Cooperation between India and ASEAN in 2005, followed by the ASEAN-India Trade in Goods Agreement, laid the foundation for deeper economic ties. India actively participated in regional dialogues on economic and strategic cooperation—first in the EAS and later in the broader Indo-Pacific context.

India's rate of growth has remained impressive, attracting the interest of East Asia, especially Japan, Korea, Indonesia, Singapore, Thailand, and Viet Nam. The increasing trade imbalance with China, and India's unresolved strategic interests gave India the impetus to participate actively in regional dialogue on economic and strategic cooperation, first in the EAS and now in the Indo-Pacific. India has also promoted its bilateral relations with Japan, Indonesia, Singapore, and Viet Nam, amongst others, to forge a layered trade integration that actively supports its strategic interests in the region. While most members of East Asia share oceanic distance, India is the only country that shares a land border with China with a history of border conflicts. India's inclusion in the East Asia group and its leading role in the Indo-Pacific (and the Quad) is therefore more complex than the tick boxes of contiguous geographical or oceanic region and the extent of trade integration.

In the broader Indo-Pacific context, India's inclusion in the East Asia group, its leadership role in the Quad, and the US's strategic interests in South and West Asia further deepen the intricacies of regional dynamics.

As ASEAN navigates its role in the evolving Indo-Pacific landscape, understanding the complexities brought forth by India's participation becomes paramount. The region stands at the intersection of economic cooperation, strategic partnerships, and geopolitical considerations, with ASEAN playing a central yet challenging role.

Framing the Shift in Economic and Strategic Outlook

Before the Indo-Pacific captured the imagination of observers from across the globe, policy researchers covering this region had explained the essence of the EAS as a first political attempt to balance China centrality in the supply chains of Southeast and East Asia and to forge a rules-based partnership in the East Asia region. ASEAN centrality and the ASEAN Summit, as the drivers of the EAS, were a conscious decision by all members of the EAS to create this balance in an inclusive manner, where no member country could claim exclusion or be singled out. Between 2005 and 2010—the year the US and Russia became EAS members during Viet Nam's chairmanship of ASEAN—the cooperation element was predominant in the EAS.

The following years of the EAS witnessed three important features. First, China's economy grew at an average of 10 percent during this decade as it rapidly climbed the value chains of production. Several AMS, as well as Japan, the US, Korea, and the EU, were closely integrated with supply chains in China. The Australian economy thrived largely due to commodities exports to China. These economic linkages were, however, being tested by the strategic interests (and intents) of China in the South and East China Sea through unilateral measures of infrastructure development and economic activities. Second, the US had returned its attention to this region after its prolonged engagement and preoccupation with West Asia. The renaming of its US Pacific Command to the US Indo-Pacific Command in 2018 was a significant signal of its intent for the region, although its strategy was as yet un-delineated. From a trade and economic cooperation perspective, this gave policy watchers an opportunity to link the Indo-Pacific with US security interests in the region and as a potential threat to the existing economic dynamism of East Asia. It has taken the US a decade to arrive at a more nuanced version of the Indo-Pacific, served by its huge foreign direct investment in the region. The US is now more integrated with the region than before. Japan's efforts to link the Indo-Pacific with economic cooperation in East Asia and with partners outside Asia notwithstanding, the US's participation in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (eventually pulling out from the final agreement during the Trump presidency) and the launch of the Indo-Pacific Economic Framework for Prosperity negotiations signify the alignment of the US's economic and strategic interests in the region. The arrival of the digital economy and technology platforms has made the US's presence in East Asia more keenly felt than ever before.

Third, the unravelling of globalisation since 2016, when 'Brexit' and 'America First' echoed in other economies, affected policy sentiment in most countries. The US–China trade tensions, which were initially confined to tariffs, have escalated to control of the technologies that underlie the manufacturing value chains. This narrative was compounded in recent years by the onset of the COVID-19 pandemic, which originated in China and created severe supply chain disruptions, at least in the initial few months of the pandemic in 2020. Social and health measures in most countries sustained these disruptions for longer. The existing supply chain dependency and efficiency are therefore being re-examined and sometimes rebuilt with bilateral and trusted partners. New policy watch words such as 're-shoring' and 'friend-shoring' are used extensively, and bilateral and trilateral relations are being explored to alter supply chains and investments in favour of friendly countries. In its inception phase, the emergent economic architecture of the Indo-Pacific reflects some or all these phenomena in varying measures.

The reality, however, is that the Indo-Pacific region is an economic construct along the Indian Ocean, in which several alternative plans and groups of countries are working on their mutual relations and combined strengths. The new plans aim to create new or alternative supply chains or to strengthen existing ones—in order to address changing political and economic needs in Asia, incorporate the opportunities arising from the digital economy and Industry 4.0, expand the location of the global value chains (GVCs) and new markets, ensure inclusive growth, bridge the fault lines in supply chains exposed during the pandemic, and accommodate partners' interests from within and outside Asia. The presence of the US as the largest economic and strategic partner is meant to be a guarantor of these objectives and consensus-based changes in the region.

Imperatives for Indo-Pacific Coming from Outside of East Asia

Japan's efforts to draw the economic landscape of the Indo-Pacific were complementary, and even necessary, to address the unilateral changes in the status quo in the South and East China Sea by a rising China. Abe's call for a Free and Open Indo-Pacific struck a chord with several major trading partners of China, whose reliance on Chinese imports and their greater trade integration (and value chain dependency) with China were being challenged in the political realm, if not by the businesses themselves. As stated above, after the general recovery from the global financial crisis, and especially since 2015 when China announced the Belt and Road Initiative for infrastructure development, the political and public discourse on China centrality in regional supply chains, principles of reciprocity and fair competition, market access, problems of overcapacity, and protection of intellectual property were uppermost in the policy platforms of major economies in Asia and Europe, and in the US, including those in Southeast and East Asia. The EU's current approach towards China, set out in the 'Strategic Outlook' Joint Communication of 12 March 2019 remains valid (EEAS 2022). The EU continues to deal with China simultaneously as a partner for cooperation and negotiation, an economic competitor, and a systemic rival.

With the EU, the changing nature of China's supply chains and China's ascent of GVCs also affected EU member states' integration with each other in terms of trade in intermediate goods. In fact, while the size of the intra-EU value chain has shrunk (countries are more loosely bound to each other in their exports of intermediate goods), EU member states were increasingly linked to China for intermediate goods (EU 2020). The EU, therefore, has shown open support for the new policy discourses in East Asia and has stopped using the term Asia-Pacific in its leadership statements. Ursula von der Leyen, President of the European Commission, attended the Asia–Europe Meeting in Cambodia in November 2021. She referred to the region only as Indo-Pacific in her speech. The leaders of all the EU member countries addressed the summit using the same nomenclature. The EU has also put in place its Global Gateway programme.

'Indo-Pacific' is a well-established term in discussions on international security in venues such as the ASEAN Regional Forum and its Council for Security Cooperation in the Asia Pacific. The significance of the Strait of Malacca and its role as a fulcrum between the Indian Ocean, the South China Sea, and the Pacific Ocean make 'Indo-Pacific' a natural term of discussion in Southeast Asia. This is especially true for Indonesia, but also for other AMS that have territorial issues in the South China Sea, with contestations of free movement of goods in the oceans surrounding the ASEAN region. A school of thought regards the current use of Indo-Pacific as a rather transparent effort to create a forum for the promotion of leadership in Asia, excluding China. This study evaluates this claim in the context of the evolution of the Asia-Pacific; the expansion of East Asia; the robust supply chains in East Asia, and between East Asia and the EU and the US; and the balancing of economic and strategic interests amongst these economic partners. In a real sense, the Indo-Pacific is the quest for more inclusive and rules-oriented trade and economic cooperation where places of production and consumption are diversified and advantageous for all stakeholders.

Trade and Investment: Hallmarks of Indo-Pacific Economic Architecture

Southeast Asia and East Asia are at the centre of the Indo-Pacific's economic vibrancy. This region has, over the years, provided buoyancy to international trade and has been the largest recipient of investment (Table 1.1). The RCEP agreement estimates that the 15 member countries[2] of Southeast and East Asia contribute US$26.3 trillion to global gross domestic product (GDP). If India were added, this region would account for nearly one-third of global GDP. It is no surprise, then, that important global economies such as the US and the EU (and the post-Brexit UK) are keen on an Indo-Pacific partnership that allows for sharing the economic dynamism of the region through its production facilities, markets, and vast human resources capacity. The Indo-Pacific emerges as a plurilateral component of the international economy. Nobody is thinking in terms of a 'bloc'. The development of production networks, including the third unbundling, likely makes the blocs of earlier eras impossible. A plurilateral Indo-Pacific would simply be a region that finds it mutually advantageous to work cooperatively.

Table 1.1: Trade in Goods among the Major Economies of Indo-Pacific (US$ billion)

	ASEAN	China	Japan	Korea	India	Australia	NZL	EU	US	UK	EAC	South Africa
ASEAN		417.81	238.91	191.25	91.83	80.96	11.15	282.01	373.79	32.27	3.67	10.66
China	417.81		371.35	362.29	125.65	230.11	24.72	828.48	758.10	112.68	15.27	54.09
Japan	238.91	371.35		84.69	19.01	67.53	5.70	155.86	219.06	17.39	1.87	12.48
Korea	191.25	362.29	84.69		23.66	42.66	3.46	129.63	169.93	11.77	0.61	3.62
India	91.83	125.65	19.01	23.66		22.02	0.88	104.89	112.90	17.12	7.19	17.06
Australia	80.96	230.11	67.53	42.66	22.02		13.55	50.26	37.67	8.79	0.39	1.66
NZL	11.15	24.72	5.70	3.46	0.88	13.55		10.56	8.81	2.10	0.01	0.22
EU	282.01	828.48	155.86	129.63	104.89	50.26	10.56		771.61	390.23	7.20	53.41
US	373.79	758.10	219.06	169.93	112.90	37.67	8.81	771.61		118.95	2.00	21.46
UK	32.27	112.68	17.39	11.77	17.12	8.79	2.10	390.23	118.95		1.21	12.50
EAC	3.67	15.27	1.87	0.61	7.19	0.39	0.01	7.20	2.00	1.21		1.96

2 The RCEP consists of 15 member countries: the ASEAN 10, Australia, China, Japan, Korea, and New Zealand. India's participation in the RCEP is on hold until certain demands from India and the rest of the members are resolved to their mutual satisfaction.

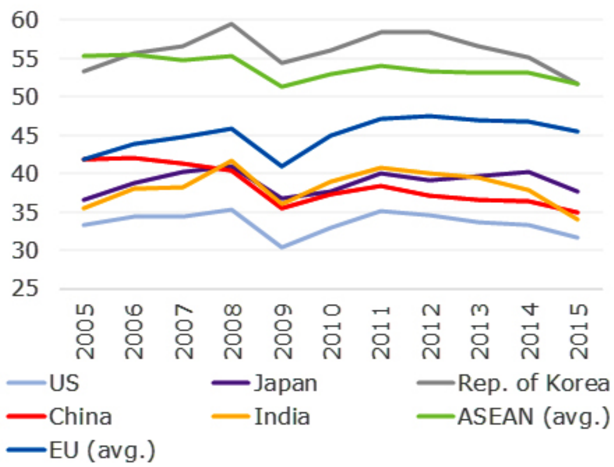
	ASEAN	China	Japan	Korea	India	Australia	NZL	EU	US	UK	EAC	South Africa
South Africa	10.66	54.09	12.48	3.62	17.06	1.66	0.22	53.41	21.46	12.50	1.96	

ASEAN = Association of Southeast Asian Nations, Korea = Republic of Korea, EAC = East Africa Community, EU = European Union, NZL = New Zealand, UK = United Kingdom, US = United States.

Source: International Trade Centre (2022). Author's own arrangement of data.

As with trade, the supply chains in the Indo-Pacific are equally vibrant and the China centrality in the supply chains is visible in most sectors of production. Countries' participation in GVCs, as measured by the value added generated in a country that crosses at least two borders in international trade relative to gross exports, reached a peak at the global level in 2008 and declined progressively afterwards. This feature also included Asian economies and the ASEAN region (Figures 1.1 and 1.2 below). The ASEAN example is particularly important as it provides a snapshot of trade integration between the largest economy in Asia and an economic community of member states that have differently sized economies, industrial bases, and levels of participation in the regional value chains. Moreover, ASEAN has been the fulcrum of trade and investment linkages from partners within and outside Asia. It is one of the most open economic regions in the world, and its economies are growing faster than the rest of the world and are converging in terms of production capacity as well as purchasing power.

Figure 1.1: GVC Participation by Economic Area (% of gross exports)

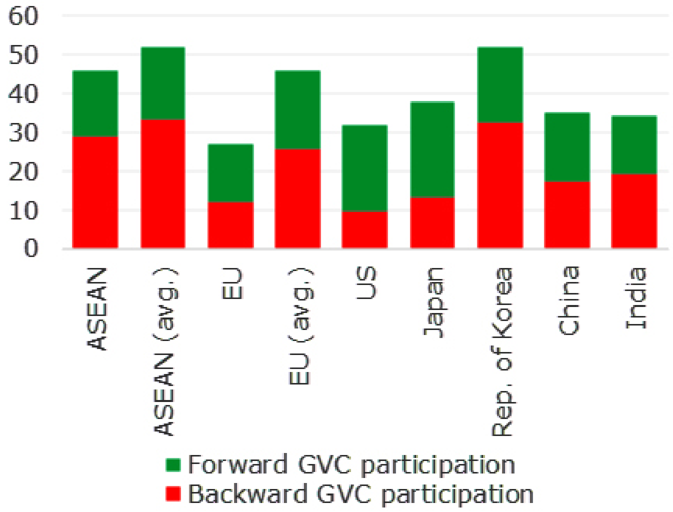


ASEAN = Association of Southeast Asian Nations, avg. = country weighted average, EU = European Union, GVC = global value chain, US = United States.

Notes: ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam. EU refers to the member countries as of 2013–2019.

Source: OECD (2018).

Figure 1.2: GVC Participation by Economic Area and Type, 2015 (% of gross exports)



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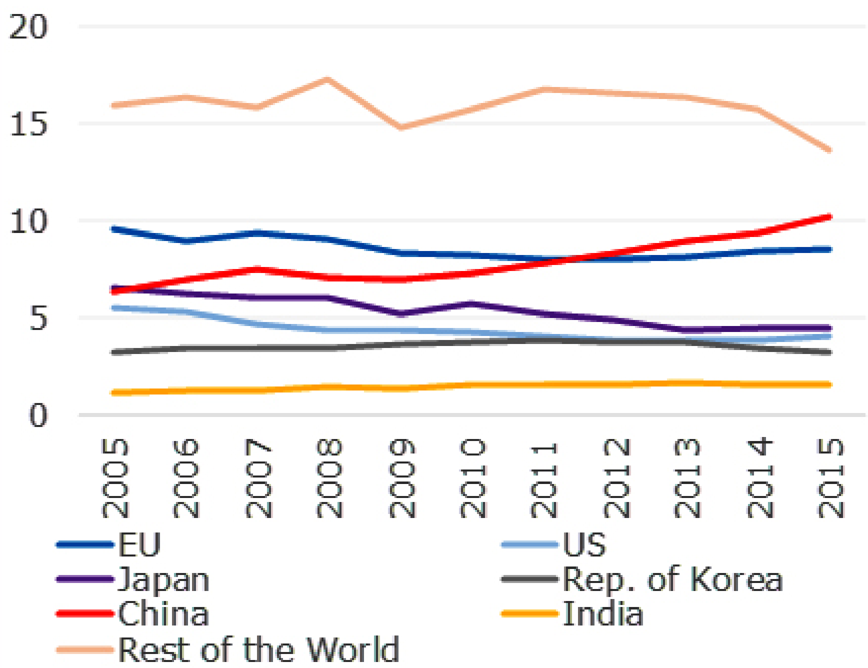
Notes: ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam. EU refers to the member countries as of 2013–2019.

Source: OECD (2018).

The ASEAN+3 region—comprising the 10 AMS, China, Japan, and Korea—provides the most vibrant GVC integration in the Indo-Pacific region. Indeed, these economies exemplify what are called regional value chains. ASEAN integration with the main developed economies has declined since its peak in the late 2000s, maintaining a steady negative trend vis-à-vis the US and Japan, but there has been a partial recovery with respect to the EU. On the other hand, ASEAN has become increasingly integrated with the two largest Asian economies, particularly with China, which has become the main individual partner in GVCs.

ASEAN integration has progressively shifted away from developed to developing economies, particularly reflecting what is known as 'China centrality' in GVCs (Figure 1.3). With developed economies, a steady negative trend has been observed for ASEAN integration with the US and Japan since its peak in the late 2000s. In contrast, a partial recovery has taken place in recent years with respect to the EU, which remains the main integration partner for ASEAN amongst developed economies.

Figure 1.3: GVC Participation of ASEAN, by Partner (% of Gross Exports)



ASEAN = Association of Southeast Asian Nations, EU = European Union, GVC = global value chain, US = United States.

Notes: ASEAN refers to eight of its 10 Member States: Brunei Darussalam, Cambodia, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam (no data were available for the Lao PDR and Myanmar). EU refers to the member countries as of 2013–2019.

Source: OECD (2018).

The China centrality in the GVCs was evident during the outbreak of the COVID-19 pandemic in Wuhan, which later spread to the rest of the world. The first instance of supply shocks emerged from China, especially for medical supplies, leading to a breakdown of entire production and consumption lines in Asia and the rest of the world. While the GVC participation rates had slowed since the global financial crisis in 2008, the COVID-19 experience of supply and demand shocks has given impetus to further balancing of GVCs and investments in supply chains in terms of distance, reliability, and vertical integration. These aspects of GVC participation predate the US–China trade tensions and the COVID-19 related shocks to supply chains. The latter two have only intensified policy actions amongst governments to establish a network of trade and investment in the Indo-Pacific which integrates the strategic and economic interests under similar if not the same rules of engagement.

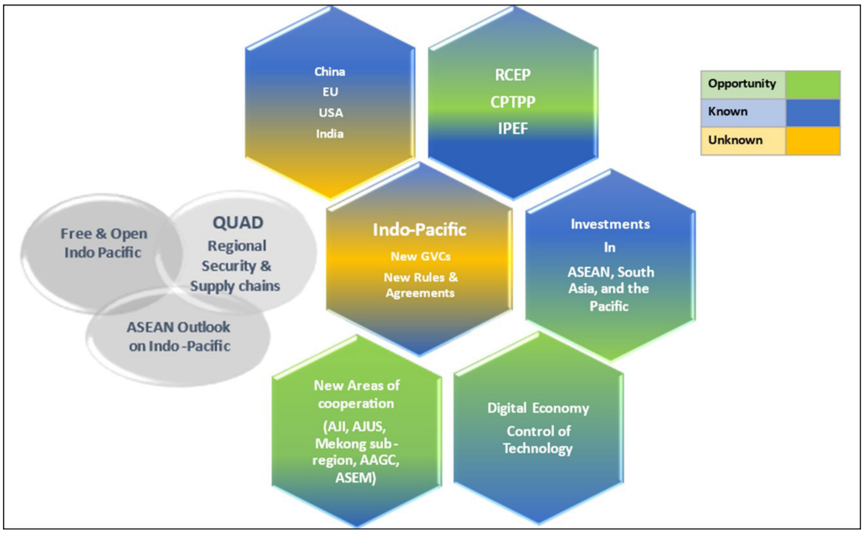
This, effectively, is the antithesis of economic integration with China, and in the larger Indo-Pacific region. When China joined the World Trade Organization in 2001, the labour dividend in China was available to regional economies as well as businesses in developed markets. China's vertical integration leads to China's reduced dependence on Asian regional value chains. As discussed above, Europe's value chain became increasingly dependent on China at the expense of its own regional integration. The US encountered rising dependency on Chinese intermediates while facing declining exports of intermediates not only to China but also the rest of the world. Reshuffling of supply chains to Southeast Asia in response to China's vertical integration has been the intermediate response, as seen in the increased investments of the EU and the US in ASEAN since 2010 (Herrero 2019).

The Indo-Pacific economic architecture is therefore a longer-term response for the balancing of trade and investment partnerships amongst the major economies of the world, with Southeast Asia, East Asia, and the Pacific at the core. The Indo-Pacific is also differentiated by a larger role of South Asia, especially India, in the alignment of strategic and economic interests with the rest of the major players in the architecture. When seen as an oceanic construct, the Indo-Pacific also envisages trade integration and production sharing with countries along the eastern seaboard of Africa as well as the major economies in East, North, and South Africa (Chaturvedi, Prakash, and Dash 2020).

Raising the Indo-Pacific Architecture on Firm Grounds

The Indo-Pacific economic architecture builds upon existing capacities in manufacturing, innovation, trade, and investment—leading to new policy alignments over strategic interests, new production locations, and markets. COVID-19 and the US–China trade tensions have given a new impetus to the rule-setting process around trade and investment (Figure 1.4).

Figure 1.4: Building Blocks for the Indo-Pacific Economic Architecture



AAGC = Asia Africa Growth Corridor, AJI = Australia Japan India Supply Chain Resilience Initiative, AJUS = Australia Japan US Trilateral Partnership, ASEM = Asia–Europe Meeting, CPTPP = Comprehensive and Progressive Agreement for Trans-Pacific Partnership, EU = European Union, IPEF = Indo-Pacific Economic Framework for Prosperity, GVC = global value chain, RCEP = Regional Comprehensive Economic Partnership, Quad = Quadrilateral Security Dialogue, US = United States.

Source: Author's own.

Supply chains in ASEAN, East Asia, and South Asia are likely to remain intact in the post-COVID-19 period. It is still early to say to what extent GVC integration has been affected by the COVID-19 pandemic, as rigorous data will only be released after a delay of some years (Shepherd and Prakash 2021). Besides the policy conversation (and agreements) for restructuring of supply chains along elements of distance and reliability, and an increased policy weightage to domestic production centres, the Indo-Pacific economies are now more engaged in rebuilding and rebalancing trade and investment. The region is also aware of the major potential change in conditions facing GVCs in the rise of the digital economy, environmental products, electric vehicles, or goods suited for increasingly carbon-neutral societies. Recovery programmes in high-income markets will favour this shift through incentives and other measures. East and Southeast Asia is well positioned to take advantage of these opportunities, with some important incentives of retooling. Keeping markets relatively open, an effective supplier network, and integrated GVCs could be an important advantage for the Indo-Pacific region in developing the GVCs of the future.

The ASEAN and East Asia region has shown, so far, that supply chains have been able to withstand the supply and demand shocks emanating from the pandemic-induced disruptions and delays. The implications of the pandemic are mainly macroeconomic, with some difference across sectors. From a supply chain integration standpoint, technology (digital, robotics, and automation) has the potential to move production closer to the location of final consumption. The pandemic experience will likely lead to a reassessment of the risks associated with dispersed production and just-in-time management practices. The US–China trade tensions over control of technologies and redistribution of investments, together with new rules of economic engagement, will likely facilitate a rebalancing of GVCs amongst the trading partners, and the Indo-Pacific will represent these changed dynamics of cooperation and change.

Trade and investment policies will assume more significance in the coming months as they determine the ability of firms to contest markets or to source intermediate inputs from foreign suppliers. For ASEAN, East Asia, and South Asia, trade and investment facilitation will be crucial as it can increase backward and forward linkages and deepen trade integration. Nurturing the business environment will also play a role in structuring trade relations in the Indo-Pacific. The trade agreements of the RCEP, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership, and the Indo-Pacific Economic Framework for Prosperity will be expected to play a crucial role in trade integration and investments in the Indo-Pacific region.

An Indo-Pacific trade and economic cooperation plan must consider China. In 2019, China became ASEAN's largest trading partner (surpassing intra-ASEAN trade) and is now the fifth largest investor in the region. Closely integrated value chains between China and ASEAN have cast a shadow on some trade and investment partnerships with ASEAN, e.g.

with Japan, the EU, and most noticeably with India. The negotiations on trade in goods in the RCEP reflected these concerns at several points before the conclusion of the FTA. It is also an important reason why India stayed out from the conclusion of the RCEP. The emerging economic architecture in the Indo-Pacific, in which ASEAN has a central role, will also face the inevitability of supply chain integration between ASEAN and China, and the EU and China, amongst others. The lessons from the pandemic and the advent of the digital economy underline both the scope of, and immediate need for, efficient and trusted partners. Equally, value chains of the green economy, high-tech production, research and development, and financial markets are other strong prospects for the Indo-Pacific region. Investments in infrastructure for the digital economy and cybersecurity are the two most pressing needs in the region for it to grow as a digital economy hub. The Indo-Pacific region should be ready and able to fulfil both the capacity needs and trust issues required in these areas of cooperation.

The Indo-Pacific region is home to some of the most open markets for both trade and investment. Its economic dynamism is becoming contemporary and future-ready through the cooperation plans for new GVCs and investments, and rules of engagement.

In the following sections, readers will find evidence supporting the cooperation plans along several verticals of economic and strategic interests in the Indo-Pacific. The building blocks of the new economic architecture in the Indo-Pacific are already in operation, with the caveat that there are several opportunities, some certainties of success, and a few unknown gaps that will shape progress towards the future.

Connectivity Plans in the Indo-Pacific:

Infrastructure for Expanded Supply Chains and Resilient Growth

In the 21st century, all connectivity plans have Asia at its core. This is not a coincidence. Asia, particularly Southeast and East Asia, has been a model of trade and economic cooperation, and much of this region's prosperity is due to its hard and soft connectivity efforts. 'Connectivity'—like 'open regionalism', 'comprehensive and cooperative security', and even 'Asia-Pacific'—has become a concept with a substantial Asian origin (Hawke 2007). The merits of such linkages continue with the Indo-Pacific too.

Asia is the centre of pan-regional connectivity initiatives in the Indo-Pacific. The MPAC, Belt and Road Initiative (BRI), Asia–Africa Growth Corridor (AAGC), The EU's Global Gateway, and the Asia–Europe Meeting (ASEM)—all connectivity plans—aim to deepen Asia's economic dynamism and extend it to trans-regional partners. Mega-regional integration initiatives like the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and the Regional Comprehensive Economic Partnership (RCEP) are also integral to this region. The European Union (EU) has also put in place building blocks for an EU strategy on connecting Europe and Asia, with concrete policy proposals and initiatives, including through interoperable transport, energy, and digital networks. The European strategy aims for sustainable, comprehensive, and rules-based connectivity. The initiatives aim to improve connections between Europe and Asia by establishing partnerships for connectivity based on commonly agreed rules and standards and contributing to address the sizeable investment gaps through improved mobilisation of financial resources and strengthened international partnerships. The United States (US) initiated the Infrastructure Transaction and Assistance Network to improve capacities in partner countries' project evaluation processes and project implementation, provide advisory services to support sustainable infrastructure, and coordinate US assistance support for infrastructure in the region. The Asia Reassurance Initiative Act, 2018 is an important part of US connectivity policy in Asia. The Partnership for Global Infrastructure and Investment (PGII) is the latest initiative among the G7 countries, led by the United States, for funding infrastructure projects across the world, especially among the developing regions.

The challenge before Asia, and the Indo-Pacific region, is how to ensure greater cooperation amongst the connectivity initiatives in the region, i.e., "connecting the connectivities". The importance of connecting the connectivities is not limited to converging different connectivity plans in Asia, between Asia and Africa, and between Asia and Europe around the principles of governance and accountability, quality and sustainable financing, and alignment with national and regional plans. An important economic justification lies in the fact that the connectivity plans will aid the deepening of the supply chain networks, create new efficiencies for trade and movement of people, and help to construct the new economic architecture that is emerging in the Indo-Pacific. Most of the important connectivity infrastructure plans of Asia are explained in this section.

The Master Plan on ASEAN Connectivity

The MPAC 2015 is based on twofold objectives:

i. Enhancing intra-regional connectivity will promote economic growth, narrow the development gaps by sharing the benefits of growth with poorer groups and communities, enhance the competitiveness of ASEAN, and connect ASEAN Member States (AMS) within the region and with the rest of the world.

ii. The concept of ASEAN connectivity would complement and support integration within ASEAN and within the broader regional framework in East Asia and beyond. The deepening and widening of connectivity in the region would reinforce ASEAN's position as the hub of the East Asian region and preserve the centrality of ASEAN.

The ASEAN approach to connectivity uses the context of community building and the objective of "a well-connected ASEAN that will contribute towards a more competitive and resilient ASEAN, as it will bring peoples, goods, services and capital closer together" (ASEAN 2011, i). The MPAC contemplates physical, institutional, and people-to-people components. The MPAC 2025 broadens this vision to "achieve a seamlessly and comprehensively connected and integrated ASEAN that will promote competitiveness, inclusiveness, and a greater sense of Community" (ASEAN 2017, 7). Although the vision continues to operate under the three pillars listed above, the emphasis of its actions has greater economic and institutional connotations than those of the MPAC 2015. These actions are as follows: (i) sustainable infrastructure, (ii) digital innovation, (iii) seamless logistics, (iv) regulatory excellence, and (v) mobility of people.

The infrastructure component in MPAC has been subject to budget constraints and competing demands for resources. To help accelerate investment in infrastructure in the region, the MPAC 2025 recommended the establishment of "a rolling priority pipeline list of potential ASEAN infrastructure projects and sources of funds" (ASEAN 2016, 7). As an

ASEAN regional process is not yet in place for identifying and prioritising infrastructure projects, the ASEAN Secretariat engaged the World Bank, with the support of the ASEAN–Australia Development Cooperation Program Phase II, to provide technical assistance in developing a rolling priority pipeline of potential ASEAN infrastructure projects across the transport, energy, and ICT sectors. The pipeline is intended to be a list of well-structured and economically viable physical infrastructure projects that enhances the movement of people, services, goods, and innovations within ASEAN; and that contributes to ASEAN's objectives of improving access to and increasing connectivity in and amongst the AMS.

The Trilateral Highway

Greater connectivity between India and ASEAN has long been both an economic and strategic objective for the ASEAN–India partnership. The Trilateral Highway (TLH) underlines ASEAN–India partnership in which trilateral connectivity between India, Myanmar, and Thailand is linked with ASEAN's connectivity plans. The TLH was conceived at the Trilateral Ministerial Meeting on Transport Linkages in Yangon in April 2002, where India, Myanmar, and Thailand agreed to make efforts to establish trilateral connectivity by 2016. The Chair's Statement of the ASEAN–India Summits in 2010 and 2012 acknowledged the importance of linking the TLH with ASEAN's connectivity plans, and its extension to the Lao People's Democratic Republic (Lao PDR), Cambodia, and Viet Nam. Prime Minister Narendra Modi stated in the ASEAN-India Summit in Jakarta in September 2023 that the implementation of the TLH will be important element of the ASEAN-India connectivity (MEA 2023).

The original alignment of the TLH starts at Moreh in India, crosses Myanmar from northwest to southeast passing Mandalay and Yangon, and ends at Mae Sot in Thailand. A major part of the TLH is the road network in Myanmar, together with border crossing facilities at two terminals in India and Thailand.

The Trilateral Highway and its Extension to Cambodia, the Lao PDR, and Viet Nam

Following the ASEAN–India Summit Meeting of 2018, the Government of India commissioned the Economic Research Institute for ASEAN and East Asia (ERIA) to undertake a study on the feasibility of establishing a seamless, efficient, and end-to-end transportation corridor along the existing TLH and its extension towards Cambodia, the Lao PDR, and Viet Nam. The first phase of the study is complete; and it offers physical, institutional, and economic pathways, along with policy recommendations for the development of the TLH and its eastward extension (Kimura, Umezaki, and Prakash 2020).

Greater connectivity between India and ASEAN has long been both an economic and strategic objective for the ASEAN–India partnership. Based on the Thai proposal at the

16th ASEAN Highway Sub-Working Group Meeting in August 2018 and other existing initiatives—such as the Greater Mekong Subregion (GMS), Ayeyawady–Chao Phraya–Mekong Economic Cooperation Strategy, MPAC 2025, and the ASEAN Highway Network—as well as the recognition that connectivity to international ports is an important factor for the development of economic corridors, this study considered the original alignment of the TLH (Moreh–Tamu–Kalewa–Monywa–Mandalay–Nay Pyi Taw–Bago–Myawaddy–Mae Sot) with two possible routes for eastward extension:

- the northern route from Meiktila in Myanmar to Ha Noi and Hai Phong in Viet Nam via the Myanmar–Lao PDR Friendship Bridge; and
- the Southern route from Mae Sot to Aranyaprathet via Bangkok in Thailand to Phnom Penh/Sihanoukville–Bavet in Cambodia and Moc Bai—Ho Chi Minh City—Vung Tau in Viet Nam.

The TLH, including its eastward extension, would primarily be a transport corridor as the vibrant economic agglomerations are mainly at one end (e.g. Bangkok, Ho Chi Minh City, and Ha Noi).

Mekong–India Economic Corridor

During an ASEAN+6[3] meeting, the Economic Ministers endorsed the idea of an East Asia Industrial Corridor (EAIC) to be studied by the ERIA as a model for the integration of East Asia. The EAIC is envisioned as a region-wide comprehensive development plan, affirming the importance of linking infrastructure development and industrial development planning.

The EAIC aims to facilitate and enhance economic growth by linking economies in East Asia. It is envisaged to be realised through the development of several interregional industrial belts such as the Delhi–Mumbai Industrial Corridor, the EWEC, and the SEC.[4] Linking India with the Mekong region is an important component of the integration of East Asia under the EAIC umbrella project. The ERIA conceptualised the Mekong–India Economic Corridor (MIEC) as a step in this direction.

The MIEC involves the integration of four Greater Mekong Countries—Myanmar, Thailand, Cambodia, and Viet Nam—with India through its east coast. It proposes to connect Ho Chi Minh City (Viet Nam) with Dawei (Myanmar) through Bangkok (Thailand) and Phnom Penh (Cambodia), linking further to the east coast of India (Figure 2.1). The integration with India is likely to benefit the corridor development in view of the growing trade and investment linkages between India and the Mekong countries.

3 ASEAN+6 refers to the AMS plus China, India, Japan, the Republic of Korea, Australia, and New Zealand.
4 Conceptualised by ADB.

Figure 2.1: The Mekong–India Economic Corridor

Source: ERIA (2009)

The MIEC is expected to enhance trade with India by reducing the travel distance between India and the MIEC countries and removing supply-side bottlenecks.

The Greater Mekong Sub-Region Economic Corridor

The GMS countries adopted the economic corridor approach at the Eighth GMS Ministerial Conference in Manila in 1998 to accelerate subregional development. The EWEC, NSEC, and SEC were subsequently designated as flagship programmes under the 10-year GMS strategic framework, 2002–2012. Thus, complementary efforts such as trade and transport facilitation, border and corridor towns development, investment promotion, and enterprise development have mainly focused on the EWEC, NSEC, and SEC. The development of GMS corridors as economic corridors continued to be at the centre of the GMS programme under the GMS strategic framework, 2012–2022.

The original alignment of the TLH is a subset of the GMS NSEC. The primary considerations for including specific routes as part of the EWEC, NSEC, and SEC in the current configuration were their potential to become trade, investment, tourism, and transit corridors; and the presence of significant sections that can be developed into hubs for regional trade, investment, and tourism.

The GMS economic corridor is an integrated system of road, rail, and ports interconnecting (i) GMS country borders; (ii) production centres (manufacturing hubs, industrial clusters, and economic zones); (iii) demand centres (capitals and major urban centres); and (iv) gateways (important seaports used for intra-regional and international trade). The areas of influence of GMS economic corridors extend beyond a single route, encompassing an economic zone running in parallel with the main transport artery.

Economic corridors can attract investment in economic activities along and around their main routes, thus generating additional demand and increasing their viability. They are critical for economic integration in the GMS because they not only facilitate cross-border movement of people, goods and services, labour, and capital along the corridors, but also promote the development of areas that can be accessed through improved connectivity.

Asian Highway Network

The Asian Highway Network is a regional transport cooperation initiative aimed at enhancing the efficiency and development of road infrastructure in Asia, supporting the development of Euro–Asia transport linkages, and improving connectivity for landlocked countries. It comprises more than 141,000 km of roads passing through 32 member countries. The network extends from Tokyo in the east to Kapikule (Turkey) in the west and from Torfyanovka (Russia) in the north to Denpasar (Indonesia) in the south.

The Asian Highway project was initiated in 1959 with the aim of promoting the development of an international road transport system in the region. From 1960 to 1970, potential routes were identified and analysed. However, the progress was slow until political and economic changes in the region spurred renewed interest in the network in the late 1980s and early 1990s. Under a renewed UNESCAP initiative, the Asian Land Transport Infrastructure Development Project was launched in 1992.

The formalisation of the network was initiated in 2002. The UNESCAP Secretariat worked with national governments to develop the Intergovernmental Agreement on the Asian Highway Network, which was adopted on 18 November 2003 and entered into force on 4 July 2005. The agreement includes a list of Asian Highway routes and classification and design standards. UNESCAP maintains the Asian Highway Database, which includes detailed information on the road conditions.

Trans-Asian Connectivity Plans

Regional connectivity is on the rise worldwide. Asia, Africa, Europe, and the other continents are becoming increasingly interlinked through pan-regional initiatives. Asia is the trailblazer in this regard, and most connectivity plans have Asia at its core. Asia is also the centre of pan-regional connectivity initiatives. The MPAC, BRI, Asia–Africa Growth Corridor, and Asia–Europe Meeting (ASEM)—all connectivity plans—aim to deepen Asia's economic dynamism and extend it to trans-regional partners. Mega-regional integration initiatives such as the CPTPP and the RECP are also integral to this region.

The Belt and Road Initiative

President Xi Jinping launched the BRI as a signature foreign policy initiative during his official visit to Kazakhstan in 2013. The BRI is envisioned as a grand development plan to increase global connectivity, with China at its centre. The BRI aims to promote connectivity amongst the Asian, European, and African continents and their adjacent seas. It also aims to establish and strengthen partnerships amongst the countries along the Belt and Road; set up all-dimensional, multi-tiered connectivity networks; and realise diversified, independent, balanced, and sustainable development in these countries (Xinhua, 2017). The framework covers the area of the ancient Silk Road, but it is open to all countries.

The BRI has two components: (i) the land-based Silk Road Economic Belt, and (ii) the Maritime Silk Road. It will focus on building a new Eurasian land bridge; and developing China–Mongolia–Russia, China–Central Asia–West Asia, and China–Indochina Peninsula economic corridors. To do so, it will take advantage of international transport routes, rely on core cities along the Belt and Road, and use key economic industrial parks as cooperation platforms. Many of China's bilateral infrastructure projects in Asia, Europe, Africa, the Indian Ocean islands, and the Pacific Islands have been brought within the BRI (Figure 2.2).

Figure 2.2: Belt and Road Initiative: A Snapshot

2013	The year the BRI was announced	451	The number of projects that are part of the BRI (as of December 2019)
2017	The year the BRI was officially enshrined in China's constitution	1 trillion	The amount of US dollars that China has pledged in BRI funding
138	The number of countries officially part of BRI	80 billion	The amount of US dollars that China has directly invested in the BRI

BRI = Belt and Road Initiative, US = United States.
Source: Prakash (2021)

The aim of improving connectivity across Asia–Europe is at the core of the initiative. Most of the projects and activities under the BRI focus on transportation infrastructure within and between Asia and Europe. Still, it should be noted that the BRI's geographic scope is near-global, as it also encompasses Africa, Oceania, and Latin America. Moreover, apart from transportation connectivity, energy and communication infrastructure are also key BRI sectors. The BRI has major implications for economic and financial integration, multilateral governance, and people-to-people ties across Asia–Europe and beyond. Many, though not all, countries in Asia and Europe have concluded bilateral memoranda of understanding with China for closer cooperation on BRI-related activities (Green Finance and Development Center, 2020).

While the BRI is President Xi's signature foreign policy plan, it is not a centralised strategy. A central task force—the Leading Small Group on Advancing the Construction of the Belt and Road—was created in 2015 to improve BRI coordination amongst various Chinese actors involved in the BRI. However, despite these efforts, the BRI at times still suffers from coordination issues due to its scope and the multitude of actors involved.

Strong financial commitments from China support the BRI. China has launched a US$40 billion Silk Road Fund, which will directly support the initiative. Additional financial resources for the initiative will be provided by the Asian Infrastructure Investment Bank (AIIB), which was primarily set up to address the infrastructure funding gap in Asia (estimated by ADB to total $8 trillion between 2010 and 2020) (ADB 2017).

The scope of the BRI is unprecedented as it aims to link many of the economies of Asia and Europe and reach out to others. The Chinese government has earmarked up to US$1 trillion for investments. Decision-making on infrastructure projects is based on bilateral agreements with other governments. Many early investments are already under way, and focus on building on and improving existing infrastructure.

Activities under the BRI relating to transport infrastructure can be subdivided into financing and construction, rail transport, maritime transport, and air transport. In addition to transport infrastructure, the digital domain is a key connectivity feature of the BRI.

The early phase of the BRI has focused on investment in the hard infrastructure of transport, communications, and energy networks. The developmental and fiscal results in some of the countries hosting BRI projects has brought the BRI under immense global scrutiny, especially on its policy coordination role with the host country. The BRI needs to transform from an infrastructure programme to a connectivity programme by embracing the multidimensional aspects of connectivity and go where they are needed. The BRI in the Indo-Pacific architecture must adhere to these principles and aim to avoid a hegemonic race for infrastructure projects.

Asia–Africa Growth Corridor

Asia–Africa relations are both historical in terms of their common past and contemporary in terms of their aspirations. The Asian economy, especially that of East Asia, has demonstrated resilience and provided a robust drive for the global economy, and it continues to provide the tailwinds thereof. Africa, on the other hand, is on the path to growth. Its young demography and economy require integration and expansion into the GVCs of production that exist in Asia. The two regions account for 70 percent of the global population and 37 percent of global gross domestic product (GDP). Conjoined by the Indian Ocean, the two regions provide a renewed opportunity for partnership for sustainable development. As developing regions, both continents are committed to promoting strong, balanced, sustainable, and inclusive growth, at both the national and international levels.

The vision document of the AAGC—the Asia Africa Growth Corridor: Partnership for Sustainable and Innovative Development—was presented at the African Development Bank annual meeting on 25 May 2017 in Ahmedabad, India. The AAGC foresees Africa's integration with Asia, in which South Asia, West Asia, Southeast Asia, East Asia, and Oceania play an important part. The AAGC proposes four major pillars of connectivity and cooperation to bring peoples, goods, services, capital, and institutions closer together to realise the objective of an Asia–Africa partnership for sustainable and innovative development. These pillars are (i) development and cooperation projects, (ii) quality infrastructure and institutional connectivity, (iii) enhanced capacities and skills, and (iv) people-to-people partnership.

These will facilitate and enhance economic growth by linking economies in Asia and Africa through the development of institutional and human capacity, connecting institutions and people, building capacities for planning and executing projects, facilitating trade, developing human resources, and improving the technology and infrastructure (ports, airports, industrial parks, telecommunications, and information technology) of the two continents. The AAGC emphasises capacity building and expanding the manufacturing base and trade between Africa and Asia. The aim is to transform the region into a growth corridor to embed development processes and value chains in Africa and Asia. It will enable the connected economies to integrate further and collectively emerge as a globally competitive economic region.

The AAGC provides new supply chain linkages between two developing regions and offers a multidimensional approach to industrialisation, trade, and integration in the regional and global value chains in which industrial development is matched with higher spending on education and the development of skills and training for adapting to digital age technologies and improved productivity. With improved productivity and rising wages in important East Asian economies, labour-intensive manufacturing jobs are likely to move to the developing regions of South Asia, Africa, and even Central Asia. The AAGC and the TLH together will provide the new economic linkages and GVC integration between Asia and Africa.

Europe–Asia Connectivity

The European Commission proposed building blocks for an EU Strategy on Connecting Europe and Asia, with concrete policy proposals and initiatives to improve connections between Europe and Asia, including through interoperable transport, energy, and digital networks.

The EU–Asia connectivity strategy is built on the belief that the EU and Asia should ensure efficient and sustainable connectivity because it contributes to economic growth and jobs; global competitiveness and trade; and the movement of people, goods, and services across and between Europe and Asia. It has outlined concrete policy proposals and initiatives to improve connections between Europe and Asia, including through interoperable transport, energy, and digital networks. The EU promotes an approach to connectivity with Asia which is sustainable, comprehensive, and rules-based. In addition, the EU will engage with its Asian partners along three strands:

i. by contributing to efficient connections and networks between Europe and Asia through priority transport corridors, digital links, and energy cooperation at the service of people and their respective economies;

ii. by establishing partnerships for connectivity based on commonly agreed rules and standards, enabling better governance of flows of goods, people, capital, and services; and

iii. by contributing to addressing the sizeable investment gaps through improved mobilisation of resources, reinforced leveraging of the EU's financial resources, and strengthened international partnerships.

EU's Global Gateway

In the 2021 State of the Union Address by President von der Leyen, the EU has presented its new connectivity strategy called Global Gateway (European Commission 2021a). In this strategy, the EU proposes to build Global Gateway partnerships with countries around the world, including Asia. The EU is offering investments in quality infrastructure for connecting goods, people, and services around the world.

The European strategy stands for sustainable and trusted connections to tackle the most pressing global challenges, from climate change and protecting the environment, to improving health security and boosting competitiveness and global supply chains. Global Gateway aims to mobilise up to Euro 300 billion in investments in critical connectivity projects during the period 2021 to 2027 and it is expected that Asia and Africa will be important beneficiaries of this strategy (European Commission 2021b). Over 90 projects have been identified in Africa, Latin America and the Caribbean, Asia and the Pacific, and in the Western Balkans.

EU–Japan Partnership on Sustainable Connectivity and Quality Infrastructure

Japan's plan for quality infrastructure and sustainable development is the basis of its connectivity partnerships in the region. Quality infrastructure is central to all of Japan's infrastructure and connectivity initiatives. In 2019, Japan and the EU affirmed their commitment to establishing a connectivity partnership based on sustainability as a shared value, quality infrastructure, and their belief in the benefits of a level playing field. In the EU–Japan Partnership on Sustainable Connectivity and Quality Infrastructure, the EU and Japan intend to work together on all dimensions of connectivity, bilaterally and multilaterally, including digital, transport, energy, and people-to-people exchanges (Ministry of Foreign Affairs, Japan 2019). The connectivity plans will fully take into account partners' needs and demands, and pay utmost attention to their fiscal capacity and debt sustainability. The EU and Japan will coordinate their respective cooperation on connectivity and quality infrastructure with partner third countries, notably in the regions of the Western Balkans, Eastern Europe, Central Asia, and the Indo-Pacific, as well as Africa.

In view of their commitment to promoting rules-based connectivity globally, both sides intend to cooperate in international and regional bodies, including international fora such as the G7, G20, the Organisation for Economic Co-operation and Development, the World Bank, the International Monetary Fund, the European Bank for Reconstruction and Development, and ADB. Together with the Japan–EU Economic Partnership Agreement, promoting regulatory cooperation for free, open, rules-based, and fair trade and investment is an important institutional component of this connectivity partnership. Both the EU and Japan have underlined digital connectivity as a powerful enabler of inclusive growth and sustainable development, including through digital and data infrastructure as well as policy and regulatory frameworks, in developing countries. Japan and the EU emphasise that the development of a digital economy depends on an open, free, stable, accessible, interoperable, reliable, and secure cyberspace; and on "data free flow with trust" (as declared by the G20 leaders in Osaka). Japan and the EU plan to use the existing Japan–EU Transport Dialogue as a framework for engaging in and cooperating on all modes of transport and horizontal issues. The Japan–EU High Level Industrial, Trade and Economic Dialogue will function as a platform for strategic discussions under the connectivity partnership.

The US Initiative

The US initiated the Infrastructure Transaction and Assistance Network, which provides capacity building programmes to improve partner countries' project evaluation processes and project implementation capacities, advisory services to support sustainable infrastructure, and coordinate US assistance support for infrastructure in the region. The US has deployed the Transaction Advisory Fund and the Global Infrastructure Coordinating Committee in the region for technical assistance and development finance. The Asia Reassurance Initiative Act, 2018, providing US$1.5 billion for 5 years until 2023, is an important part of US policy for the Indo-Pacific.

Eurasia and Northeast Asia

The Greater Tumen Initiative (GTI) (originally known as the Tumen River Area Development Program) is an intergovernmental cooperation mechanism amongst four countries—China; Mongolia; Korea; and Russia—supported by the United Nations Development Programme (Dulambazar 2015). In 1995, the member governments signed agreements to establish the GTI mechanism, aimed at strengthening economic and technical cooperation, and attaining greater growth and sustainable development in Northeast Asia, especially the Greater Tumen Region (GTR). The GTI focuses on the priority areas of transport, trade and investment, tourism, agriculture, and energy, with environment as a cross-cutting sector.

The GTI effectively converges the BRI initiated by China, the Eurasia Initiative proposed by Russia, and the Grassland Road undertaken by Mongolia, in building the China–Russia–Mongolia transport corridor in the GTR. Some of the important projects in the Trans-GTR Transport Corridor are the Tumen Road Corridor, Tumen Rail Corridor, Suifenhe Transport Corridor, Siberian Land Bridge, Dalian Transport Corridor, Korean Peninsula West Corridor and East Corridor, and the China Land Bridge Transport Corridor connecting Asia with Europe via Kazakhstan. In 2013, two additional transport channels between Ulaanbaatar and Bichigt were added in the Tumen transport area. The GTI Common Fund, contributed by the member countries, is a United Nations Development Programme Trust Fund to finance the operation of the GTI Secretariat.

Similarly, the Central Asian Regional Economic Cooperation (CAREC) offers connectivity between Northern Asia and Central Asia. Korea’s New Southern Policy leverages ASEAN and India as its key regional partners and as a strategic priority for Korea.

Partnership for Global Infrastructure and Investment: A Game Changer?

The Partnership for Global Infrastructure and Investment (PGII)—a United States led initiative for funding infrastructure projects across the world—is being increasingly seen as a counter to China’s Belt and Road Initiative (BRI).

The infrastructure plan was first announced in June 2021 during the G7 (or Group of Seven) summit in the UK. The G7 countries include the United Kingdom, the United States, Canada, France, Germany, Italy, Japan, and the European Union (EU).

In 2022, during the G7 summit in Germany, the PGII was officially launched as a joint initiative to help fund infrastructure projects in developing countries through public and private investments. US President Joe Biden called it the Build Back Better World (B3W) framework and extended it as a collective programme with an aim to mobilise nearly US$600 billion from the G7 by 2027 "to invest in critical infrastructure that improves lives and delivers real gains for all of our people" (The White House 2022b).

As the G7 recognises the contours of China-led programmes for infrastructure funding among the developing countries under the BRI, the PGII is the G7's alternative mechanism to help secure funding for countries to build critical infrastructure such as roads, ports, bridges, and communication setups, to enhance global trade and cooperation.

During India's G20 presidency, Prime Minister Narendra Modi brought the Global South to the forefront of the development efforts in the G20. Working closely with the G7 members, Prime Minister Modi announced that the PGII can contribute towards reducing the infrastructure gaps in the Global South countries.

On the sidelines of the G20 Summit in New Delhi, a Memorandum of Understanding (MoU) was signed between the governments of India, the US, Saudi Arabia, the EU, the UAE, France, Germany, and Italy to establish the India–Middle East–Europe Economic Corridor (IMEC).

The IMEC is being envisioned as a network of transport corridors, including railway lines and sea lanes, that is expected to aid economic growth through integration between Asia, the Arabian Gulf, and Europe.

Before the G20 Summit, Prime Minister Modi attended the ASEAN-India Summit in Jakarta on 7 September 2023, where he stated his vision to prepare a Multi-Modal Connectivity and Economic Corridor which connects Southeast Asia, India, West Asia, and Europe, which will focus on logistics, supply chains, infrastructure, clean energy, and solar grid connectivity. In this plan, the Trilateral Highway and the IMEC will be the connecting infrastructure for bringing Asia and Europe as well as the developing countries of the Indo-Pacific closer through inclusive, transparent, and diversified connectivity.

Funding the Connectivity Plans

Asia is one of the world's most dynamic and productive regions, but it is held back from realising its full potential by huge constraints in crucial infrastructure caused by a lack of investment. ADB has estimated that developing Asia will need to invest US$26 trillion for infrastructure from 2016 to 2030, or US$1.7 trillion per year. This would allow the region to maintain its growth momentum, eradicate poverty, and respond to climate change. Without climate change mitigation and adaptation costs, US$22.6 trillion, or US$1.5 trillion per year, will be needed (ADB 2017).

Infrastructure investment varies considerably by sector (Table 2.1). The power and transport sectors require the largest investments, accounting for 52 percent and 35 percent, respectively, of total infrastructure investments. Telecommunications and water and sanitation are no less important for an economy or for individual welfare, and therefore require investment. Each of these sectors has varying levels of regulatory, governance, and sustainability challenges in different countries.

Table 2.1: Infrastructure Investment Needs by Sector in 45 ADB Developing Member Countries, 2016–2030 (US$ billion in 2015 prices)

Sector	Baseline Estimates			Climate-adjusted Estimates			Climate-related Investments (Annual)	
	Investment Needs	Annual Average	Share of Total	Investment Needs	Annual Average	Share of Total	Adaptation	Mitigation
Power	11,689	779	51.8	14,731	982	6.76	3	200
Transport	7,796	520	34.6	8,353	557	6.56	37	-
Telecommunications	2,279	152	10.1	2,279	152	5.12	-	-
Water and sanitation	787	52	3.5	802	53	3.31	1	200
Total	**22,551**	**1,503**	**100.0**	**26,166**	**1,744**	**1.02**	**41**	

ADB = Asian Development Bank

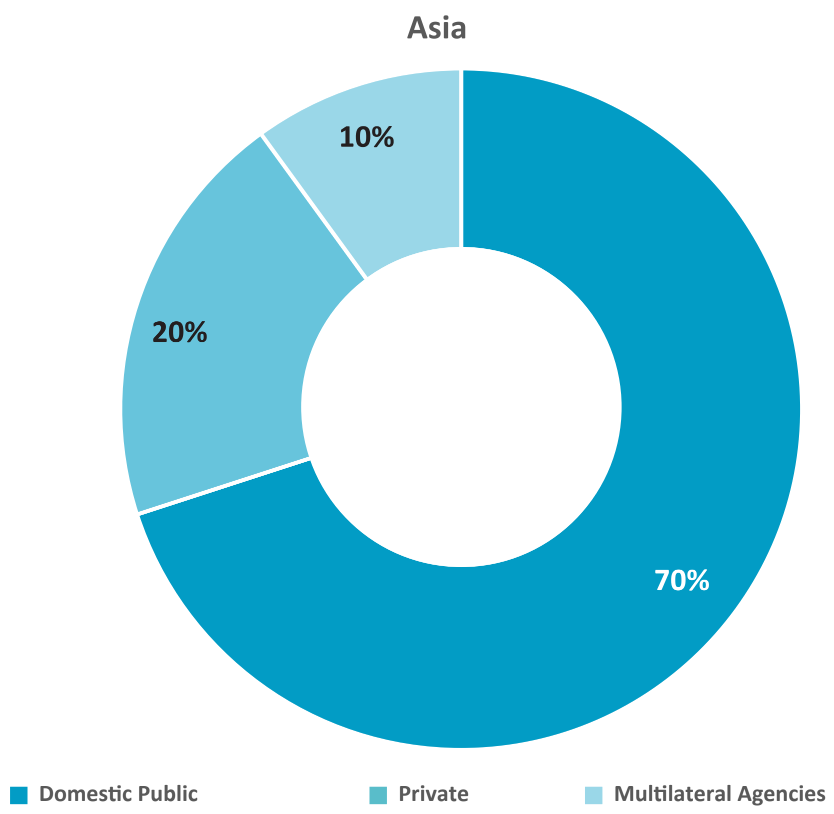
Note: Numbers may not total exactly because of rounding.

Source: Asian Development Bank estimates (2017)

Funding Agencies and Partnerships

Infrastructure projects focused on cross-border connectivity present significant investment opportunities and are vital for long-term growth in Asia. Much of the funding would continue to come from public resources, through better domestic revenue mobilisation, cost recovery, and better prioritisation of fiscal resources. Yet, it is also clear that more private sector financing is required. While public spending still provides the bulk of needed infrastructure investments, fiscal constraints and debt sustainability considerations limit the extension of public finance (Figure 2.3). Various multilateral development banks (MDBs) have also made mobilising private capital a priority. ADB emphasises private participation in infrastructure and capital market development in its private sector operations framework. The World Bank also takes an approach of "maximizing finance for development" to leverage all sources of finance systematically. The AIIB has a more focused mandate on infrastructure project financing and does not offer concessionary financing. It aims to create infrastructure projects as an asset class for private sector investors by increasing the level of data quality. This helps market participants to make informed financing decisions.

Figure 2.3: Composition of Infrastructure Financing



Source: Subhanij, 2018

Besides the MDBs and public–private financing in Asia, the ASEAN Infrastructure Fund (AIF) promotes regional infrastructure financing and financial resilience to support the long-term development of the AMS. The AIF is dedicated to meeting some of the region's infrastructure investment needs. ADB has invested US$150 million and administers the AIF and provides technical support.

Given the plethora of connectivity plans in Asia and their trans-regional nature, the future of financing of these projects may well remain in multilateral cooperation partnerships. The Multilateral Cooperation Center for Development Finance (MCDF) was set up through a memorandum of understanding between China's Ministry of Finance, the AIIB, ADB, the European Bank for Reconstruction and Development, the European Investment Bank, the New Development Bank, and the World Bank to promote infrastructure and connectivity. The MCDF will act as a platform to foster high-quality infrastructure and connectivity for developing countries. It multilateralises infrastructure financing and advocates for a transparent, non-discriminatory, and predictable financing environment, taking into account debt sustainability in mobilising finance. Information sharing, capacity building, and project preparation are the focus areas of the MCDF.

Addressing the Financing Gap

Project governance and sustainability increase the cost of infrastructure but are important for attracting financing from financial institutions (Prakash 2020a). The financing gap for infrastructure is, in large part, the result of inadequate policies and processes and a lack of familiarity with projects. Governments play a central role in most infrastructure projects because infrastructure has strong public good characteristics, requires large-scale capital mobilisation, and is highly sensitive to local politics. However, the scale of infrastructure spending required over the next 10–15 years, coupled with widespread public sector fiscal constraints, means that private finance will be increasingly important. A positive "enabling environment"—that is, one characterised by sound policies, effective institutions, transparency, reliable contract enforcement, and other sector-specific factors—makes it easier to mobilise private finance. Conversely, a poor enabling environment—one characterised by distorting subsidies, unreliable counterparties, and flawed procurement processes—can raise the cost of private finance to the point where infrastructure projects are no longer economically viable (Bielenberg et al. 2016).

Trans-regional plans such as the BRI, AAGC, MPAC, and EU–Asia connectivity are seeking greater emphasis on governance, standards, transparency, and sustainability to varying degrees. Institutions such as the Asian Development Bank Institute and the African Development Bank have helped to further this objective by providing climate adaptation and mitigation adjusted costs for infrastructure. Transparency in project preparation and accountability in project execution are important global concerns emerging from the financing and implementation of infrastructure plans. Global attention has been drawn towards issues of planning and project design, financing and debt sustainability, territorial integrity, and people's choices.

Multilateral Cooperation for Investment in Connectivity Plans

A multilateral cooperation programme amongst Indo-Pacific countries and MDBs could facilitate global investment in infrastructure for connectivity by creating more efficient, informed, transparent, and predictable investment conditions around infrastructure plans and projects. Development banks feature prominently in this multilateral cooperation because they have the mandate, motivation, and means to influence financing flows and shape markets and have experience in infrastructure funding that could help other actors, such as private sector and institutional investors, in taking on the projects (Prakash 2020b). Such cooperation works best when undertaken at a regional level, as is seen in the case of connectivity infrastructure projects in Asia and Africa. This is also important because it helps policymakers to find synergies between national and regional development strategies.

Finding the Convergence among Connectivity Plans in Indo-Pacific

ASEAN and East Asia are manufacturing hubs with close trade relations within the region, and with important markets in the EU and the US. Such trade integration has been achieved through supply chain efficiencies and market demands in which seamless connectivity plays an important role. Supply chains in ASEAN and East Asia rest on a stable foundation of trade and investment links. To the extent that there are risks, they are primarily at a micro level.

The COVID-19 pandemic, prevailing trade tensions, slowdown in trade in goods, and the onset of digital economy have brought the focus on new connectivity strategies that would help the supply chains in Asia remain resilient to changes in the international trade dynamics.

Seeking convergence amongst competing connectivity plans is based on the notion that all connectivity plans have similar objectives. The contours of the MPAC, AAGC, BRI, and other connectivity plans will show that this is not always the case. There are inherent differences in each of these plans, given their origins, partnerships, resources, and the political and economic priorities of the promoters. Given these competitive differences, a consensus amongst governments, businesses, and people is emerging to set up governance mechanisms that would place different connectivity plans behind globally agreed development goals. This will help to create common objectives and create synergies amongst the different connectivity plans.

Finding the global standards for connectivity projects and activities is difficult but not impossible. Global development programmes and the impetus for multilateralism can provide a way to create greater interlinkages between connectivity plans through governments, and regional and multilateral institutions. For this reason, the Indo-Pacific economic architecture is ideal for setting the governance standards in connectivity projects.

The COVID-19 pandemic has revealed the vulnerability of connectivity and GVCs. Connectivity between new production locations and markets will strengthen the resiliency of inter-regional connectivity and the GVCs, and improve trade integration. In the post-COVID-19 phase, it will also support restructuring and diversification of supply chains and markets. Indo-Pacific has high stakes in the new supply chain led connectivity projects. Restructuring, understanding, and preparing for a connected Indo-Pacific will ensure stable and inclusive growth in the region.

An Enhanced Role for the Pacific in the Indo-Pacific Economic Architecture

The Pacific Island countries (PICs) in Melanesia, Micronesia, and Polynesia, though spanning the Western Pacific, face a unique set of challenges. While their vast exclusive economic zones (EEZs) mark them as "large ocean countries and territories", their small land masses and economies still define them as "small island states". Despite their maritime wealth, they often lack the capacity to fully exploit their ocean resources or enforce their jurisdictions.

Although geographically positioned at the heart of a dynamic region, PICs encounter the "tyranny of distance", leading to infrequent and costly air and sea connectivity. Their limited market size and high trade costs present hurdles to integrating into global supply chains. Yet, there are promising developments, particularly in telecommunications infrastructure, e-commerce, and institutionalised regional integration.

PICs are striving to enhance their ties with traditional partners like Australia, New Zealand, and the United States, along with emerging partners in Asia and even the broader Indo-Pacific. Indeed, there are even examples of increased engagement with the 'Indo' part of the Indo-Pacific, as India seeks to increase its footprint in the region and as PICs look for strategic cooperation with Indian Ocean small island states. However, PICs remain cautious about being drawn into geopolitical struggles and emphasise maintaining friendly relations with all major players. They continue to adopt a 'friends to all approach' and seek to engage with, and benefit from, strong relations with all key partners.

Managing these complex partnerships may become more challenging, as PICs have moved closer to China but deeper integration is hampered by the fact that some countries continue to provide diplomatic recognition to Taiwan. Moreover, the region remains wary, especially amongst the general population, that economic cooperation with China carries more benefits than risks. While PICs seek to maximise the benefits of their relationships, traditional partners are also increasing their commitments to the region, with potential for greater engagement from the United States. However, the future of these developments remains uncertain.

The Pacific Region

Understanding how the PICs engage with the world involves exploring their dynamics of regional integration. The Pacific Islands Forum (PIF) plays a pivotal role in regional integration and has been bringing PICs together for over five decades. The PIF's secretariat, headquartered in Suva, supports various functions, from organising leaders' meetings to coordinating multilateral negotiations and providing technical assistance to members.

The PIF comprises 18 member countries: 14 PICs across Melanesia, Micronesia, and Polynesia, along with developed nations Australia and New Zealand, and the French territories of New Caledonia and French Polynesia. As a regional political and economic community, the PIF is unique insofar as it brings together both developed and developing countries. For certain purposes, Australia and New Zealand are considered fully integrated members of the region, although they are also deeply integrated into other regional economic groupings such as Asia-Pacific Economic Cooperation (APEC), Association of Southeast Asian Nations (ASEAN)+ arrangements, and the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). They are also involved in the Quad (i.e. the Quadrilateral Security Dialogue, consisting of the US, Australia, India, and Japan); Australia, New Zealand, and US Security Treaty (ANZUS); and AUKUS. Depending on the context, references to the 'region' may include Australia and New Zealand, or it may have a narrower meaning focused only on the PICs.

However, the unique inclusion of developed and developing countries within the same regional body makes it distinctive. This presents challenges and sometimes makes it difficult to define the region's membership, including whether Australia and New Zealand should be included.

The membership complexity deepens with the involvement of states and territories that are not part of the PIF, playing significant roles in regional cooperation. Territories like American Samoa, Guam, Northern Mariana Islands, and Wallis and Futuna, despite not being PIF members due to their status, engage in customs cooperation within the Oceania Customs Organisation.

Timor-Leste, while not sharing the same culture and history as the PICs, is included in the region by external actors like the European Union and China. Their engagement and alignment with the PICs are notable examples of the region's shifting dynamics.

Despite commonalities, the PICs face a notable distinction between larger players and Smaller Island States (SIS). For instance, Papua New Guinea (PNG) boasts the largest economy and population, but Fiji plays a more significant role, particularly as a hub for transportation. To ensure that SIS voices are heard, mechanisms like annual meetings have been established, although SIS states may still feel marginalised in discussions.

The Blue Pacific narrative, adopted in 2017, signifies the PICs' desire to strengthen their regional identity and cooperate on issues concerning their vast maritime jurisdictions. The Framework for Pacific Regionalism and the 2050 Strategy for a Blue Pacific Continent further guide regional cooperation.

Sub-regional integration adds another layer of complexity within the region. The Melanesian Spearhead Group (MSG) established a free trade agreement involving Fiji and PNG, contributing to sub-regional integration. Additionally, Micronesia's divergence and disputes highlight regional tensions.

Diplomatic recognition for China and Taiwan is a divisive issue within the PIF. While some members recognise Taiwan, the Solomon Islands' 2019 switch to China resulted in ongoing frictions, further complicated by Malaita's rejection of the decision. The PIF remains divided on this matter, impacting the region's approach to engagement with China.

Divergences also arise due to different PICs' relationships with the rest of the world. The Compact countries pursue closer association with the US, while other PICs maintain deeper integration with Australia and New Zealand. For instance, Cook Islands and Niue have full residency and working rights in New Zealand.

PNG's unique land border with Indonesia brings benefits and challenges. PNG's border arguably integrates it with Southeast Asia, including its APEC membership. However, the border tension, especially concerning the Free Papua Movement, presents challenges.

Despite regional differences, the PICs have achieved collective diplomacy on the global stage. Their united efforts led to success in negotiations on oceanic territories and climate change. Regional security cooperation, as seen in the Regional Assistance Mission to Solomon Islands (RAMSI), involved contributions from all PICs. Furthermore, regional infrastructure and economic integration projects, including regional trading agreements, exemplify the PICs' cooperative endeavours.

The PIF operates based on diplomatic engagement, with political declarations and personal relationships rather than legally binding treaties driving decisions. Regional institutions facilitate coordination, with implementation occurring at the national level. While peer-review mechanisms exist, the focus is on soft enforcement.

Despite the complex regional dynamics and divergences, PICs engage in collective diplomacy, pooling their diplomatic resources and presenting a unified voice on the world stage. This collective approach enhances their influence in international negotiations and dialogue with partner nations.

How Do the Pacific Islands Fit into the Indo-Pacific Region?

The PICs face challenges in integrating into the Indo-Pacific region, given their limited integration in the Asia-Pacific. Despite their geographic location in the heart of the Asia-Pacific, the PICs struggle with poor air and sea connectivity and face obstacles in joining global value chains due to small economies and high transport costs.

While the PICs are not actively seeking a geostrategic realignment towards the Indo-Pacific, they recognise that changes are happening with or without their involvement. These changes bring both opportunities and risks for the region. On the positive side, there is growing interest from countries looking to engage with the PICs, including China, and increased attention from traditional partners like Australia, New Zealand, and the US. The PICs have also strengthened ties with APEC and Southeast Asia through the ASEAN Outlook on the Indo-Pacific.

The 'Indo' part of the Indo-Pacific offers opportunities, although geographic limitations exist. The PICs have formed strategic partnerships with Indian Ocean island states to advocate for common interests, particularly related to climate change and oceans. Additionally, historical and cultural links with India, such as Fiji's South Asian heritage, create a potential for collaboration through India's Indo-Pacific Oceans Initiative.

However, the heightened attention to the PICs also presents risks, as geopolitical developments may pressure them to choose sides between great powers, potentially challenging their 'friends to all' approach.

Growing Interest in and Attention on Pacific Islands

The PICs are experiencing a surge in attention due to increasing geostrategic competition in the Indo-Pacific. In the past, the region received limited interest from global powers, with Australia and New Zealand being the primary nations cultivating deep relationships with trade, investment, diplomacy, and large-scale aid programs.

However, a significant shift is occurring as both the US and China vie for influence in the Pacific. China has gained diplomatic recognition from some countries, and they have conducted charm offensives and entered into bilateral agreements. China aims to enhance its presence in the region, and while the exact impact of these agreements remains uncertain, they hold symbolic importance.

The US, after years of relative absence from Melanesia and Polynesia, is re-engaging due to China's increased involvement. The reopening of the US embassy in Solomon Islands and the announcement of new embassies in Tonga and Kiribati, amongst other initiatives, signal a shift in US policy towards the region. However, some longstanding issues with the US, such as the ratification of the protocols to the Treaty of Rarotonga and addressing the legacy of nuclear testing in the Republic of the Marshall Islands, remain unresolved.

Yet, the increased attention from powerful nations does not guarantee greater benefits for the PICs. They face challenges in managing multiple relationships and assessing associated risks, particularly given their limited bureaucratic capacity. Concerns about Chinese 'debt trap diplomacy' have arisen, with several countries at high risk of debt distress, including Kiribati, PNG, Tonga, and Tuvalu. China's substantial lending presence in the region raises concerns about the value and potential dual-use purposes of infrastructure projects.

While PIC leaders assert their diplomatic capabilities to leverage regional competition to their advantage, concerns persist about the potential for 'elite capture', whereby Chinese resources may undermine governance and democracy. The views of PIC governments and their populations may also diverge, with resistance to Chinese investment in the face of economic enticements. Opposition politicians have capitalised on this sentiment.

Despite the complexities of these dynamics, the PICs' 'friends to all approach' has reignited interest from traditional partners. Australia's shift on climate change has improved its relations in the region, and the change in government in Australia in 2022 has contributed to enhanced Australia–Pacific relations. Australia is now working to strengthen its ties with the region, taking measures to counterbalance China's influence.

Risks: Picking Sides

The 'friends to all approach' of the PICs may face increasing challenges amid concerns of global politics evolving into a new Cold War between the US and China. Unlike the original Cold War, where the PICs were relatively distant from major conflicts, today's scenario presents a dilemma. The PICs share strong historical, economic, and cultural ties with Western nations, particularly Australia and New Zealand, and benefit from the rules-based international order, which secures their maritime jurisdiction and resources. People-to-people connections, including sports, education, tourism, and religion, link them to the West.

Simultaneously, the PICs see advantages in engaging with non-traditional partners, especially China. China is a significant trade partner, investor, and provider of development assistance. Chinese firms are involved in major construction projects in the region. Although people-to-people links with China are generally weaker, some PICs have sizeable Chinese diasporas, contributing to economic development but also leading to ethnic tensions.

Maintaining warm relations with all partners, as exemplified by Fiji hosting China's foreign minister and its participation in the US Indo-Pacific Economic Framework for Prosperity, holds immense benefits. However, the sustainability of this balancing act may depend on global developments and whether the world is moving towards a new Cold War.

Trade and Aid

Economic integration in the PICs has primarily centred on regional integration efforts, like the Pacific Island Countries Trade Agreement (PICTA). However, PICTA faces challenges such as non-ratification and limited implementation, with low trade flows amongst the member countries.

Australia and New Zealand have played pivotal roles in the region's economic landscape and promoted the PACER Plus—an FTA aimed at securing wider regional participation. While many Pacific states have ratified PACER Plus, Fiji and PNG, the largest regional economies, have not joined, limiting the agreement's integration potential.

PACER Plus offers innovative labour mobility programs enabling Pacific Islanders to work in Australia and New Zealand, benefiting their economies and skill development. These programs, originally meant for seasonal work, now include long-term options. Some PICs, like Samoa and the Solomon Islands, actively manage these programs, driving economic growth.

Labour mobility was intended to incentivise Fiji and PNG to join PACER Plus, but Australia and New Zealand have extended access to these programs regardless of their PACER Plus participation. However, excluding these major PIC economies diminishes the agreement's potential for regional integration.

Beyond FTAs, the PIF facilitates trade integration through annual trade minister meetings, addressing issues like the World Trade Organization's fisheries subsidies and COVID-19's economic impact. The PIF Secretariat initiated projects like the Pacific Quality Infrastructure initiative and the Pacific Regional Infrastructure Facility for trade promotion and infrastructure coordination.

Despite PICs' engagement with partners like the EU, the UK, Australia, and New Zealand to deepen trading arrangements, trade flows do not always reflect these efforts. China's trade with the PICs has surged, particularly in imports, thus influencing trade patterns. However, factors like labour mobility, remittances, and tourism contribute significantly to economic development and integration, although these aspects are often not fully reflected in trade statistics.

Australia and New Zealand remain essential trade partners for the PICs due to strong ties and their ability to offer deeper integration through people-to-people links, such as education and employment opportunities. Other countries like Japan and China offer scholarships and opportunities but face language and cultural barriers, limiting their influence in the region.

Efforts to enhance economic integration in the Pacific continue through regional agreements, labour mobility programs, and closer ties with key trading partners, making it a dynamic and evolving landscape.

Priorities and the Enhanced Concept of Security

In the Pacific region, security cooperation has seen significant developments. The Biketawa Declaration, initiated in 2000, emphasises security within a broader framework encompassing democratic governance. The Regional Assistance Mission to Solomon Islands (RAMSI) exemplified successful security collaboration under the Biketawa Declaration.

The PICs have generally enjoyed the peace dividend from the liberal international order. With most lacking standing armies and those with armies mainly focusing on disaster response or peacekeeping abroad, conventional warfare concerns are limited within the region.

A new approach to regional security emerged in 2018, when PIF members collectively redefined their stance with the Boe Declaration, reinforced by an action plan in 2019. This approach emphasises an “expanded concept of security”, highlighting climate change as the region’s greatest threat, along with human security, humanitarian assistance, and environmental and resource security. While addressing trans-national crime and cybersecurity, traditional security issues are not top priorities, and the Boe Declaration fails to explicitly mention international norms like non-aggression or respect for territorial integrity.

However, concerns persist about conventional military threats, as the region hosts US military bases and could become a frontline if US-China tensions escalate into open warfare. Additionally, reports of China negotiating with regional countries to establish military bases raise security implications, but there are no regional mechanisms to constrain such actions, and individual governments’ sovereignty remains paramount. A regional agreement with hard commitments could address such concerns and offer benefits for all countries.

Pacific Values

Proximity and historical ties to Australia and New Zealand have led PICs to share Western values, including parliamentary democracies, freedom of speech, and trust in the rules-based international system. The Biketawa Declaration solidified the pursuit of these values in the region.

However, these values can sometimes clash with traditional structures like village chiefs, leading to quandaries for officials when upholding the rule of law conflicts with traditional obligations. Moreover, the adoption of certain liberal ideas like gender equality and LGBTQIA rights faces resistance due to traditional values.

This tension can undermine seemingly deep-rooted institutions, as seen in Samoa's recent constitutional crisis. Some leaders with autocratic tendencies admire China's model, and there are concerns about compromising press freedom and media independence when governments make concessions to prevent diplomatic frictions with China.

Consensus-based decision-making at the regional level is crucial for the PICs, and meaningful outcomes with the rest of the world require deep engagement. The lack of prior dialogue with the PICs about Australia and New Zealand's Indo-Pacific strategy caused tensions. While China has succeeded in bilateral deals, regional diplomacy demands patience and sustained engagement. The PICs may strengthen their negotiating position when dealing with China collectively, but it remains to be seen if China will continue regional engagement despite its costs.

PICs: Influencers in the Indo-Pacific Economic Architecture

The reimagining of geopolitics in terms of the Indo-Pacific region represents a significant development for PICs. While there is some scope for them to increase their engagement with the 'Indo' part of the new region, the reality is that their security and economic interests primarily lie in the Pacific theatre. On the economic front, the increased attention and resources coming to PICs have the scope to make a meaningful contribution to development, provided that those resources target critical human and societal needs instead of being captured by elites.

PICs are right to prioritise climate change and development as their most pressing needs, but they should also recognise that the rules-based system, which is increasingly coming under threat, is foundational to the achievement of their priorities as well as to the maintenance of peace and security in their region and the world. PICs have scope to influence economic and strategic decisions by those major powers who are increasingly interested in the Pacific. This influence, however, may be undermined by insufficient political will and regional unity, especially as the PICs seek to sidestep politically difficult questions to maintain an increasingly fragile 'friends to all approach'.

The Indo-Pacific Partnership and Digital Trade Rule Setting:

Policy Frameworks

The term 'Indo-Pacific' has traversed its geopolitical and security concept, gaining prominence as an economic cooperation framework through the launch of the Indo-Pacific Economic Framework for Prosperity (IPEF) in 2022. The IPEF, with its focus on trade, supply chains, clean energy, and anti-corruption, mirrors the geo-economic aspects of the Trans-Pacific Partnership (TPP), aligning with the goal of setting rules for the 21st century.

The IPEF-TPP Linkage and the Global Trends

The IPEF's roots in the TPP are evident as it mirrors the TPP's commitment to high-standard, inclusive, and fair trade. With nine IPEF participants being TPP founding members and others expressing interest post-negotiations, the IPEF is poised to inherit and refine the TPP's multilateral trade agenda. Both initiatives aim to address regulatory and competition issues, protection of investments, and standards for environmental protection and workers' rights, shaping the economic landscape of the 21st century.

The IPP was born from a global trend that has (re)oriented the centre of the world's economic gravity to the East.[5] The Quad and IPEF represent these geo-political and geo-economic components; behind the scenes is the rapidly expanding international production-sharing network and digital transformation that fuels Asia's rise and fosters the global shift. Indeed, the IPEF emphasises this global trend and states that "[i]n the long term, economic competitiveness will be largely defined by [the] ability to harness technology, promote innovation, [and] participate in the digital economy" (The White House 2022). Specifically, negotiations on the trade pillar will "seek to build high-standard, inclusive, free, and fair trade commitments and develop new and creative approaches in trade and technology policy", and IPEF partners will seek to cooperate in the digital economy (The White House 2022).

5 This pivot seems to indicate China, yet the rapidly expanding international production-sharing network fuels rising Asia and fosters the global shift (Chen, 2017).

The IPEF responds to the shifting centre of the world's economic gravity towards the East, fuelled by an expanding international production-sharing network and digital transformation. Emphasising the significance of technology and innovation, the IPEF aligns with the broader global trend where economic competitiveness is increasingly defined by the ability to harness technology and participate in the digital economy.

Digital Trade in 21st Century Global Value Chains (GVCs)

Digitalisation stands at the forefront of 21st-century Global Value Chains (GVCs), as depicted in Figure 4.1. The evolution of GVCs, influenced by technological progress and economic globalisation, has undergone three main unbundling episodes: the separation between production and consumption, international fragmentation of production, and further fragmentation within production tasks. The reduction in trade costs, facilitated by technological advancements, has reshaped international trade dynamics.

Figure 4.1: Technological Progress in Global Value Chain Evolution

	Pre-globalised world	The 1st unbundling	The 2nd unbundling	The 3rd unbundling
Costs of transportation Costs of communication Face-to-face costs	High High High	Lower High High	Lower Lower High	Lower Lower Lower
What to move	None	Goods	Production factors, know-how	Skills, Services Data and information
Int'l division of labor	Autarky	Industry-wise	Task-wise (production fragmentation)	Person-wise (task fragmentation)
Technology		Automation, Transport	CT& IT	SMACI

CT = communications technology, IT = information technology, SMACI = social media, mobile phone, artificial intelligence, cloud computing, and Internet of Things.

Sources: Baldwin (2016), Kimura (2018), Kimura and Chen (2016)

During the pre-globalisation era, high costs necessitated proximity between production and consumption. However, advancements in technology, such as steamships and railways, initiated the first unbundling, allowing for separation between production and consumption. The technological progress managed to promote industry-wise division of labour and made mass production and economy of scale feasible. As production and consumption could locate in difference countries and be linked via international trade, countries started to trade more with each other. Yet at this stage, international trade was dominated by trade in goods, and the main content was final goods or raw materials. The 20th-century Information Revolution marked the second unbundling, further lowering trade costs and the threshold for global production sharing, enabling smaller enterprises to participate. The third unbundling, characterised by digitalisation, has further interconnected the global economy by blurring boundaries between value chain links.

Digitalisation has reduced the costs of people-to-people connections, particularly through enhanced connectivity in cyberspace. This has expanded the boundaries of international fragmentation of production and unleashed the full potential of GVCs. The application of digital technologies in the services sector has made services more innovative and productive. Digital-empowered services links have improved GVC coordination, fostering an ecosystem that is better connected, smarter, and more efficient.

This section highlights the growing influence of the Indo-Pacific concept, manifested in the IPEF, on the global economic landscape. By aligning with the trends of digitalisation and international production sharing, the IPEF positions itself as a significant player in shaping the rules for the 21st-century economy. As the world undergoes the third unbundling with the rise of digital technologies, the IPEF's emphasis on technology, innovation, and digital trade governance is pivotal to fostering inclusive and fair economic development.

Balancing Innovation and Inclusion: A Rules-based Playing Field for Digital Trade

The escalating prominence of digital trade in the global economy necessitates the establishment of international rules to ensure a level playing field. These rules should encompass existing WTO provisions while addressing new challenges, referred to as WTO-plus or WTO-extra issues. The former are topics that call for the extension of member *déjà fait* commitments at the multilateral level, while the latter are new issues that have not yet been covered by the WTO. Striking a balance is crucial, as inadequate regulations may lead to market disorder, while overly restrictive policies can create barriers to digital trade.

Definitions of digital trade vary, with the US focusing on internet-based transactions, the European Commission on electronic commerce, and the OECD on digitally enabled transactions of goods and services. Three shared understandings emerge: digital trade encompasses both goods and services, involves the trade of final and intermediate products, and relies on cross-border data flows. The WTO has not yet provided a clear definition for digital trade, but based on its definition of e-commerce, digital trade could refer to international production, distribution, marketing, sale, or delivery of goods and services by electronic means.

Digital solutions, exemplified by Apple's iTunes, have expanded services' role in economic activities, offering new value-added dimensions. Digitalisation has catalysed the growth of data-driven business models like servicification, thus transforming the traditional producer-consumer interaction into an ongoing exchange. This evolution, exemplified by Rolls Royce's data-driven engine support, has lowered barriers for businesses to adopt servicification.

Digital trade extends beyond final products to include intermediate goods and services. International division of labour, facilitated by telecommunications tools, has given rise to GVCs. Rules on digital trade must govern the entirety of GVCs, considering the impact of new communication tools like social media, instant messaging, and videotelephony in expanding GVC coverage.

Cross-border data flows are integral to digital trade, enhancing various trade flows and transforming traditional interactions. Videotelephony supported online meetings during the COVID-19 pandemic, while 3D printing technology could revolutionise the exchange of tangible objects. Setting rules for digital trade requires careful consideration of these common understandings and must address both tariff and non-tariff measures.

NTMs, encompassing laws and regulations affecting trade beyond tariffs, require specific attention in the digital trade landscape. Ambiguities and deficiencies in the existing General Agreement on Trade in Services (GATS) underline the need for updated rules. The rules should address limitations such as insufficient commitments, positive lists, and the lack of adaptation to technological changes.

Digital trade's foundation in a borderless internet necessitates rules that prevent cyberspace fragmentation. Balancing goals of increasing trust, ensuring security, and facilitating online business, regulations must span both the physical world and cyberspace. The core principle of non-discrimination between local and foreign suppliers is essential for equitable digital trade rules.

Rules for digital trade must prioritise the free flow of data, emphasising barriers such as localisation requirements, cross-border data flow restrictions, and intellectual property rights infringement. Non-discrimination principles, applied to cross-border data flows, payments, investments, and labour movements related to the Internet of Things (IoT), are critical. Tariff barriers should be reduced, and international standards for electronic transmissions and *de minimis* practices on cross-border e-commerce should be promoted.

Given the potential international ramifications of national regulations on the digital economy, global collaboration is imperative. Policymakers must consider conflicting goals such as internet enabling, e-commerce competition, and data privacy in crafting rules. International agreements on digital trade norms should address both at-the-border and beyond-the-border actions, ensuring coherence in the rapidly evolving digital landscape.

Navigating Challenges in Indo-Pacific Partnership for Digital Trade Rules

The United States prioritises a free, open, rules-based global market in its foreign policy, extending this commitment to the cyberspace domain. The IPEF presents an opportunity for the US to deepen ties with Indo-Pacific members, yet challenges arise in aligning high-standard agreements with domestic constraints while providing substantial benefits to attract partners (Meltzer 2022).

The IPEF serves as a platform for advancing US interests in digital trade and leading the development of global rules on the digital economy. However, fundamental disagreements persist amongst major trading nations regarding the global regime for digital trade, reflecting divergent views on regulatory approaches. Bridging these gaps through negotiations is crucial for building trust, reducing market uncertainty, and facilitating international business.

Formalising an agreement on no customs duties for electronic transmissions and *de minimis* practices is essential. While concerns about potential tariff revenue losses exist, especially for developing countries like Thailand and India, the overall benefits of duty-free electronic transmissions outweigh these losses (OECD n.d.). Initiating agreements within smaller groups like the IPEF can provide a pragmatic approach, fostering trade facilitation and compensating for potential revenue losses.

Globally, the ability to generate, collect, and monetise data is outpacing considerations for its consequences. Restrictions on data flows, such as data localisation requirements, hinder economic efficiency and can be seen as hidden protectionism. The IPEF should prioritise setting a common floor for data security and privacy legislation, emphasising transparency, and defining different types of data to build trust amongst member nations.

The rise in cyber threats necessitates collaboration in enhancing cybersecurity measures. Limitations on data flows, like data localisation requirements, may not improve cybersecurity and can create vulnerabilities. IPEF cooperation should focus on establishing international security standards, cross-compliance recognition frameworks, and norms of behaviour in cyberspace. The objective is to create a resilient digital ecosystem in the Indo-Pacific, balancing concerns for data security, privacy, business interests, and national security.

Digitalisation intensifies the cross-border exchange of intellectual property, making robust IPR protection crucial. The IPEF must consider higher standards than those outlined in existing international agreements, with effective enforcement mechanisms. Recognising varying interests amongst member countries, negotiations on IPR protection should learn from precedents like the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and the Regional Comprehensive Economic Partnership (RCEP), which introduce provisions beyond multilateral commitments.

The IPEF offers a unique opportunity for Indo-Pacific nations to collaborate on digital trade rules. Overcoming divergent views, establishing agreements on customs duties, *de minimis* practices, data flow, cybersecurity, and IPR protection are vital steps. By addressing these challenges, the IPEF can foster an inclusive and innovation-friendly digital trade environment, contributing to the overall economic development of the participating nations.

Four Policy Areas: Fundamental to the Rules-Setting in Digital Economy

The sustained development of digitalisation needs a rules-based ecosystem to support market openness, innovation, and fair competition. As a guideline, the World Bank (2016) suggested five policy areas: (i) establishing a digital favourable and competitive business climate, (ii) developing strong human capital, (iii) ensuring good governance, (iv) improving digital infrastructure, and (v) raising digital literacy. These objectives can be universally applied to policymaking for the digital economy.

The US and Asia are highly interdependent, and economic digitalisation tends to deepen their ties. The IPP will strengthen the economic links amongst members and set the tone for market openness and rules-based competition and cooperation in the region. To the US, Asia represents a large market—therefore, a main source of job creation and economic growth. US firms believe that the IPP can strengthen their links with Asia by securing the GVCs of their businesses with better access to foreign markets and supply bases. Other advanced economies, such as Japan and Australia, have similar economic interests.

Developing countries in the region are motivated to prioritise their partnership with the US not only because of the advance of the US market, capital, and technology, but also due to their need for the US to be an external auditor in promoting domestic regulatory reforms. For instance, the global consensus on regulating digital trade will require more beyond-the-border measures (i.e. modification of domestic laws and regulations to meet international commitments). The consequent social and economic adjustment and policy intervention in response call for collaboration between administrative and legislative agencies as well as cooperation amongst different government branches, particularly between foreign affairs departments and those in charge of domestic market regulations.

The IPEF needs to ensure that members' commitments to high-standard trade rules will contribute to their digital transformation and facilitate their integration into the global economy. New global rules on free digital trade will be a policy priority, which covers the IPEF's four pillars: connected economy, resilient economy, clean economy, and fair economy.

The process of rules setting for digital trade will involve complementary and competing interests amongst stakeholders. Several issues have legislative and oversight implications

(Fefer, Akhtar, and Morrison, 2019). Above all, any fruitful IPEF talks on digital trade need members to have clear objectives, which can only be obtained based on a full understanding of the economic impact of digital trade, potential trade barriers and their consequences, and internationally standardised or inter-operatable methods of measuring digital trade.

Trust building is the priority for an open, resilient, development-friendly ecosystem for the global digital economy. It is important to consider privacy; cybersecurity and trade secrets; the trade-off amongst market openness, free flow of data, and policy with other socioeconomic goals (e.g. protecting privacy, supporting law enforcement, improving safety, and ensuring national security); and inclusion of different standards-setting practices that may have global reach. The different practices could be due to countries' various stages of development, legal frameworks, and political systems.

The four policy areas under discussion—trade liberalisation of electronic transmissions, free flow of data with trust, cybersecurity, and IPR protection—are fundamental to the regulatory system that the digital economy needs to support its long-term development; thus, they should be prioritised in the agenda of the upcoming IPEF talks.

Human Capital for Economic Growth and Resilience in the Indo-Pacific

Nurturing Human Capital for Sustainable Development in the Indo-Pacific

Human capital, increasingly recognised as the primary driver of economic growth, plays a pivotal role in shaping the future of the Indo-Pacific region. As the global economy undergoes a technological transformation, international cooperation in human capital development becomes crucial. The ability of individuals to contribute to economic activities, shaped by education, training, health, and job experience, is central to achieving the vision of poverty alleviation and improved living standards in the Indo-Pacific. For only when the majority of workers in the Indo-Pacific has the necessary skills can the region be stable, resilient, and integrated.

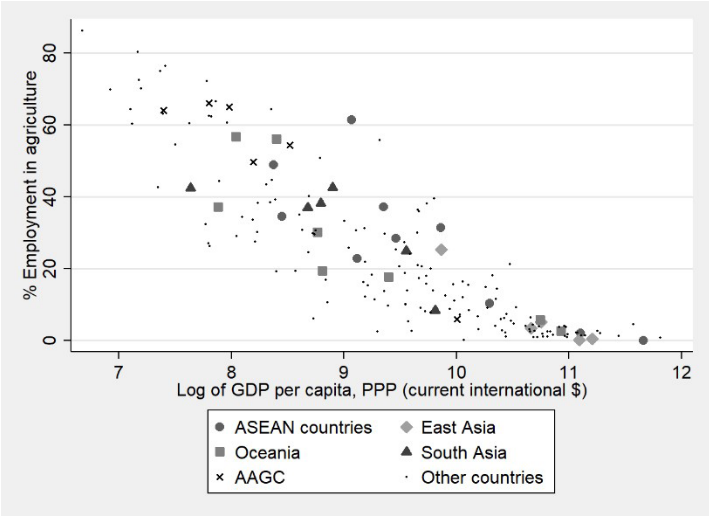
The Indo-Pacific vision, as outlined in the ASEAN Outlook on the Indo-Pacific, emphasises connectivity and infrastructure investments to foster integration and interconnection amongst nations. This cooperation is not only vital for economic development but also serves to prepare the workforce for the challenges posed by the Fourth Industrial Revolution. As the region pursues greater connectivity, attention to human capital development becomes imperative to mitigate disruptions caused by evolving economic activities and digitalisation.

Technological advancements, marked by lower production costs, increased efficiency, and enhanced market access, redefine economic activities in the Indo-Pacific. Automation and digitalisation, while creating new opportunities, pose threats to underprepared workers. The COVID-19 pandemic has accelerated these challenges, making skills development crucial for maximising the benefits of increased trade and investment flows in the region.

Workers' ability to harness digital technology determines their resilience in the face of technological change. The Asian Development Bank highlights the importance of technical, cognitive, and non-cognitive skills to benefit from technological advancements. Upgrading infrastructure for skills development, investing in education systems, providing training opportunities, reducing labour market rigidity, and enhancing social protection are essential components to address the skills gap.

As the demand for workers who complement digitalisation grows, their wages will also rise faster than those without such skills. In response, individuals will acquire the skills that are in high demand; this increasing supply will check the rise in wages while also enabling more people to benefit from digitalisation. Yet the ability of workers to respond to signals from the market will largely depend on their access to skills development systems. While some Indo-Pacific countries are well prepared to make this adjustment, others need financial and knowledge support to accelerate this human capital development. Figure 5.1 illustrates the high share of agricultural employment in many countries, emphasising the need for transitioning workers to modern sectors. Modern technology necessitates workers' abilities to excel in non-routine and cognitive jobs, which are less susceptible to automation.

Figure 5.1: Agricultural Employment Share and Gross Domestic Product per Capita in the Indo-Pacific (most recent year available)



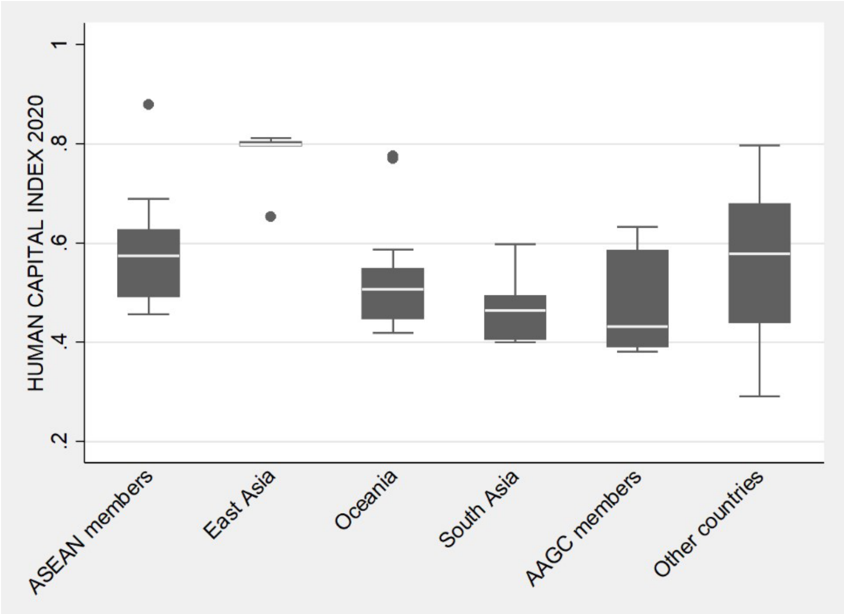
AAGC = Asia–Africa Growth Corridor, ASEAN = Association of Southeast Asian Nations, GDP = gross domestic product, PPP = power purchasing parity.

Source: Author's illustration from World Bank data. https://data.worldbank.org/indicator/SL.AGR.EMPL.ZS

State of Human Capital in the Indo-Pacific

The Indo-Pacific exhibits varying levels of human capital, with East Asia leading in general. Tertiary educational enrolment rates vary widely, reflecting diverse levels of readiness amongst Indo-Pacific countries to cope with technological disruptions. The average level of human capital in ASEAN is similar to rest of the world, but those in Oceania, South Asia, and Africa are below average.

Figure 5.2: Human Development Index, 2020



AAGC = Asia–Africa Growth Corridor, ASEAN = Association of Southeast Asian Nations.

Note: Some countries may not be included due to lack of data.

Source: Author's illustration from World Bank. Human Capital Project. https://www.worldbank.org/en/publication/human-capital

The COVID-19 pandemic led to significant school closures, impacting formal education systems and potentially resulting in learning losses. Addressing the long-term effects requires additional investment in education to facilitate catch-up learning and curriculum restructuring.

Youth unemployment increased from 15.4 percent to 17.9 percent between 2018 and 2021, with significant variation across Indo-Pacific countries. The pandemic exacerbated the situation, affecting young individuals' career opportunities and potentially leading to long-term repercussions. Unemployment can have a long-term impact due to depreciation of human capital and discouragement from participating in the labour force. It may also bring about other social problems such as crime and political instability.

The rise of remote work, accelerated by digitalisation and the pandemic, introduces opportunities and challenges. While it offers flexibility, concerns about digital equality arise, with the feasibility of remote work favouring certain industries and income groups. Widespread adoption of such work arrangements has increased flexibility but also raises issues of digital equality. The feasibility of remote work varies greatly across industries and mostly favours white-collar jobs. Even in a developed country like the United States, researchers estimated that only 37 percent of work can be done remotely. This proportion is much lower in developing countries. Moreover, jobs with remote work possibilities tend to cluster within a firm, which means that the proportion of businesses that can fully operate remotely is even smaller. Since cognitive tasks are more amenable to being performed remotely, educated and high-income workers benefit the most.

Increased remote work also has implications for labour flows across countries. Many countries are changing their policies to offer digital nomad visas. According to one report, as many as 46 countries have implemented or are planning to implement visas for individuals engaged in remote work (Stillman 2022). These open up new opportunities for workers to live and work in different countries, with mutual benefits for both countries.

Recommendations for Sustainable Human Capital Development

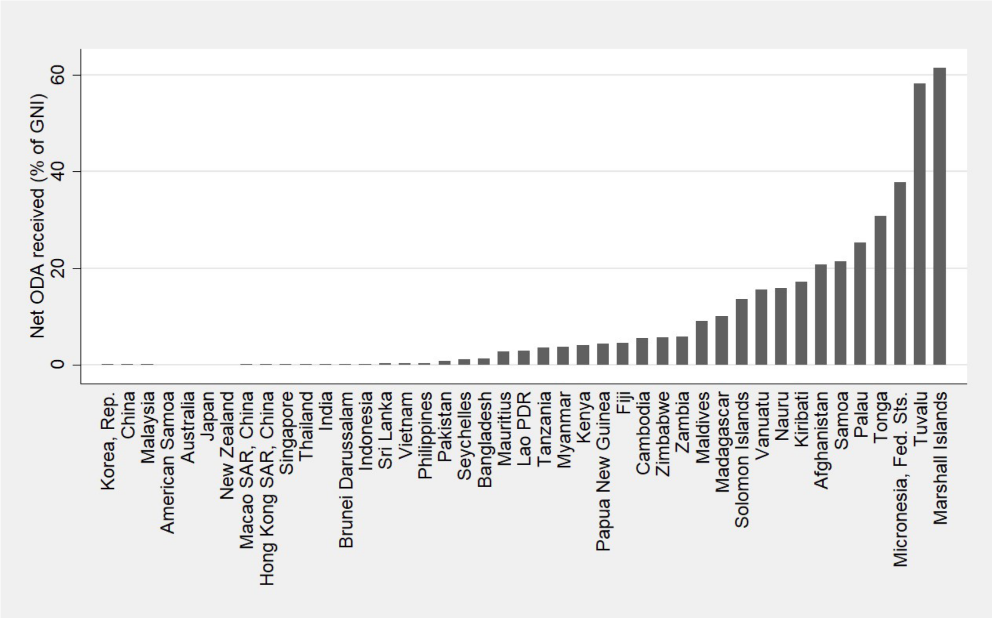
- Invest in Education Quality: Upgrade both the quantity and quality of education to ensure effective skills development.
- Address Learning Losses: Mitigate the impact of school closures by investing in catch-up learning programs and curriculum adjustments.
- Enhance Youth Employment Opportunities: Implement policies and programs to create gainful employment opportunities for young individuals, recognising the potential long-term consequences of youth unemployment.
- Promote Digital Equality: Develop strategies to address disparities in remote work opportunities, ensuring inclusive benefits across industries and income groups.

The Indo-Pacific's journey towards sustainable development hinges on effective human capital development. As the region navigates the challenges posed by technology, the Fourth Industrial Revolution, and the aftermath of the COVID-19 pandemic, prioritising education, training, and skills development is essential. By fostering a skilled and adaptable workforce, the Indo-Pacific can unlock its full potential, achieving stability, resilience, and integration across nations

Cooperation Areas and Mechanisms

International cooperation in the Indo-Pacific, especially concerning human capital development, is critical amid ongoing technological changes. While trade and investment agreements often include regulatory harmonisation and environmental issues, human capital cooperation remains underemphasised. Developing countries in the region, heavily dependent on international aid, must allocate substantial portions of their budgets to education, vocational training, and skills development. For many Indo-Pacific countries, aid still represents a substantial fraction of their national incomes (Figure 5.3). Building human capital in these countries will require investment of large fractions of their budgets in education, vocational training, skills development, and associated programs. While many bilateral and multilateral aid programs have focused on skills development, greater success may be achieved by pooling resources and coordinating programmes.

Figure 5.3: Aid Dependence in Indo-Pacific



Lao PDR = Lao People's Democratic Republic, ODA = official development assistance.

Note: For geographic delineation of Indo-Pacific, see Annex. Some countries may not be included due to lack of data.

Source: Authors' illustration from World Bank data. https://data.worldbank.org/indicator/DT.ODA.ODAT.CD

Movement of Workers

Facilitating the movement of workers can significantly benefit the Indo-Pacific. Advanced economies require young workers, while less developed countries seek capital for improved living standards. Cooperative mechanisms for human resource movement, such as the European Union's free movement and ASEAN's mutual recognition agreements, exist. Bilateral agreements between countries in the Indo-Pacific, handling the movement of low- and medium-skilled workers, are common. Enhancing labour mobility could not only address skills gaps but also promote 'brain gain' and 'brain circulation', encouraging skills development and efficiency gains.

The Indo-Pacific region already has some elements of labour mobility through bilateral agreements. In particular, the movement of low- and medium-skilled workers is usually handled through government–government agreements. It is not uncommon for countries in the region to sign bilateral labour agreements, which specify conditions under which one party to the agreement (i.e. 'source' country) sends temporary workers to the other party (i.e. 'host' country) (Chilton and Posner, 2018). These agreements often contain legal protections for migrants in the host country as well as obligations for the source country. The University of Chicago Law School catalogued as many as 582 bilateral labour agreements between 1945 and 2015, with over half ratified between 1990 and 2015.[6]

Table 5.1 presents the number of bilateral labour agreements amongst the various sub-regions comprising the Indo-Pacific. Within the Indo-Pacific, six bilateral labour agreements are found in which an East Asian country is the host country and an ASEAN Member is the source country. East Asian countries also have five bilateral labour agreements with South Asian countries. Oceania has as many as 26 bilateral labour agreements but with only three countries in East Asia as source countries.

Table 5.1: Bilateral Labour Agreements between Indo-Pacific Countries

		Source Country					
		ASEAN	East Asia	Oceania	South Asia	AAGC	Other Countries
Host Country	ASEAN	10	0	0	3	0	0
	East Asia	6	2	0	5	0	2
	Oceania	0	3	0	0	0	26
	South Asia	0	0	0	0	0	0
	AAGC	0	0	0	0	0	0
	Other Countries	25	9	1	19	1	175

AAGC = Asia–Africa Growth Corridor, ASEAN = Association of Southeast Asian Nations.

Source: Author's own

Making skills more transferable across the Indo-Pacific will lead to efficiency gains. The specificity of a worker's skills is an important concept within labour economics. Workers possess both general skills (i.e. those that can be easily transported across different firms) and specific skills (i.e. that are more efficiently utilised within a specific firm). With piece-meal labour agreements governing the movement of workers across countries, workers usually focus on specific skills. If it were possible, however, to transfer skills more widely across multiple countries, there would be a tendency to gain more general skills.

Educational opportunities in the Indo-Pacific vary, prompting individuals to seek better prospects in advanced countries. The flow of international students, facilitated by scholarships, reached over five million in 2017. Sustainable Development Goal 4 emphasises expanding scholarships for developing countries. Supporting each other, Indo-Pacific nations can enhance human capital by facilitating student flows through scholarships and reforming immigration laws in host countries.

Collaborative efforts in trade, investment, labour movement, and education are imperative for sustainable human capital development in the Indo-Pacific. By pooling resources, coordinating programs, and fostering mobility, the region can overcome challenges, reduce the skills gap, and unlock its full potential for shared prosperity and development.

Conclusion

Technology, especially digital technology, makes three things easier—access to information, connectivity or exchange of information, and computation or processing of large amounts of information—which improves productivity and economic growth. Digital technology offers the opportunity for countries to revitalise their traditional sectors like agriculture and manufacturing and to enhance productivity. It does require workers to be ready to adapt by increasing their skills, however. Indo-Pacific countries can collaborate on this important area by further increasing aid for skills development, fostering labour mobility amongst countries in the region, and increasing the flow of students.

The Indo-Pacific Seascape and ASEAN's Open and Convergent Economic Vision

The Indo-Pacific, a maritime counterpart to the Asia-Pacific landscape, offers natural advantages in the maritime sector. While the Asia-Pacific represents production networks in the context of global value chains (GVCs), the Indo-Pacific embodies maritime-based service networks and logistics, connecting regions through sea transport.

ASEAN member states straddle both the Indo-Pacific and Asia-Pacific, particularly in strategic locations like the Malacca Straits. This geographic position underscores ASEAN's pivotal role in the Indo-Pacific. ASEAN applies an "open regionalism principle" as it needs export-oriented foreign direct investment inflows from ASEAN non-member states. For regional economic integration purposes, ASEAN adopts economic convergence as a sufficient condition for open economic integration. The combination of open and convergence principles is reflected in the *ASEAN Community Vision 2025*.

Economic growth acceleration hinges on a country's competitiveness, reflected in net exports and long-term investment. The strength of the connection between FDI inflow and net exports signifies a country's role in global production networks, moving from forward to backward participation. ASEAN aims to transition from a raw material–dependent, forward participation stance to become a vital global production base, necessitating FDI inflows from outside its member states.

To achieve this export-oriented objective, ASEAN needs an open regionalism framework to attract FDI from non-member states. This shift will help transform ASEAN from raw material exports to intermediate input production.

ASEAN's regional economic cooperation efforts focus on fostering equitable economic growth through openness and convergence principles. The Indo-Pacific serves as a critical platform, enabling ASEAN's integration into global production networks and GVCs. This section explains the intricate relationship between ASEAN and the Indo-Pacific, emphasising ASEAN's centrality and its Indo-Pacific outlook.

The ASEAN Way: ASEAN Centrality and Outlook on the Indo-Pacific

A survey of 1,000 influential individuals in Southeast Asia revealed perspectives on the Indo-Pacific, where over 61 percent found the concept unclear and in need of further clarification, while 25 percent believed it was designed to contain China. The Free and Open Indo-Pacific campaign has gained traction in Southeast Asia, emphasising development and connectivity. It focuses on creating an environment for peace, stability, and prosperity, addressing global issues, and promoting economic diplomacy.

While Southeast Asia is becoming more confident in this approach, ASEAN sees growing geopolitical uncertainties in the Indo-Pacific. As each member state maintains dynamic relations with global powers like the US and China, ASEAN has crafted the ASEAN Outlook on the Indo-Pacific to absorb potential geopolitical shocks. ASEAN seeks to maintain its centrality, guided by the "ASEAN way" of non-interference, amid the rivalry between the US and China.

In the Indo-Pacific context, Southeast Asia aims to balance its engagement with both China and the US, adopting a strategy known as 'omni-enmeshment'. The ASEAN way employs consultation (*Musyawarah)* and consensus (*Mufakat*) in its decision-making process, unlike the EU's voting-based mechanism.

ASEAN's open regionalism principle aligns with various cooperation frameworks and the Regional Comprehensive Economic Partnership (RCEP) to enhance FDI inflows and export values. It emphasises inclusivity, requiring secure geopolitical conditions for economic stability.

From the Indo-Pacific perspective, ASEAN is aiming to preserve its market mechanism-led instead of government-led tenets. It is also applying inclusive principles that adopt non-discriminative actions towards every economic partner's domestic political system. This focus on inclusiveness will also be a path forward for the digital economic development of ASEAN and the Indo-Pacific.

ASEAN's view of the Indo-Pacific has two characteristics that differ from other conceptions. First, ASEAN recognises the Indo-Pacific as an aggregation of two existing regions of Asia —the Pacific and the Indian ocean regions — which have already regional or sub-regional mechanisms, rather than as an aggregation of the two oceans. Second, it puts the Asia-Pacific region first and the Indian Ocean region second, despite the Indo-Pacific word order. The ASEAN Outlook on the Indo-Pacific emphasises transparency, a rules-based framework, good governance, and respect for sovereignty, based on the Treaty of Amity and Cooperation in Southeast Asia.

ASEAN considers joining the Indian Ocean Rim Association (IORA), as a dialogue partner would enhance Indo-Pacific maritime congruence. The combination of open and convergence principles is reflected in the ASEAN Community Vision 2025, ensuring that all member states benefit from open regionalism by staying convergent in various platforms.

ASEAN Enlargement: East Asia Summit Role in the Indo-Pacific

The Asia-Pacific region holds immense potential, but it also faces conflicts, particularly territorial disputes, such as in the South China Sea, and tensions in US-China relations further complicate regional dynamics. Achieving a peaceful Indo-Pacific remains challenging, with different views on the evolving architecture of the region.

Indonesia, as the largest economy in Southeast Asia, plays a pivotal role in ASEAN's politics and economy, positioning itself as one of the Indo-Pacific's middle-power countries. Indonesia promotes cooperation over rivalry in the Indo-Pacific and emphasises maritime collaboration in the Pacific and Indian oceans.

Indonesia's economic relationships with China and the US highlight its role as a bridge between these two major powers. These countries are Indonesia's top export destinations, demonstrating their significant political and economic influence in ASEAN and the Indo-Pacific.

ASEAN, like Indonesia, must balance its relations with the US and China, fostering convergence in an open, transparent, inclusive, and rules-based regional architecture. ASEAN initiatives such as the RCEP align with the soft and open regionalism of the ASEAN way, acknowledging ASEAN's centrality.

Open, soft, inclusive, and free regionalism principles, combined with ASEAN centrality, enable ASEAN to cooperate securely with non-members and engage in mega-regional cooperation, enhancing FDI inflows while maintaining economic convergence.

ASEAN's strong regional value chains are vital to the ASEAN Economic Community (AEC), transforming economic cooperation toward intra-investment and positioning Southeast Asia as a key supply-side hub in the Indo-Pacific and Asia-Pacific. The AEC aligns with the Free Trade Area of Asia-Pacific (FTAAP) and strengthens regional economic networks.

However, the proliferation of regional free trade arrangements outside ASEAN can impact the region. It is essential for ASEAN to remain united and inclusive to ensure regional geopolitical stability and facilitate dialogue between global powers through ASEAN-led mechanisms.

In summary, the Asia-Pacific holds great potential, but cooperation and convergence, led by ASEAN and its members, are crucial for achieving a peaceful and prosperous Indo-Pacific.

The ASEAN Economic Network in the Indo-Pacific: Central Gravity

ASEAN's path to success involves enhancing both forward and backward participation in global value chains, especially through the manufacturing sector, to achieve economic convergence within the region. To foster a peaceful market mechanism in the Indo-Pacific, ASEAN should adhere to its open, soft, free, and inclusive principles, opting for security cooperation instead of military alliances in the Indo-Pacific. Additionally, ASEAN needs to embrace the digital economy, including fintech and e-commerce, for economic interconnection.

The Asia-Pacific is the landscape for global production networks, while the Indo-Pacific serves as the seascape for global services networks, like logistics and shipping services. Connecting to both the Asia-Pacific and Indo-Pacific is vital for ASEAN to establish resilient global linkages and become an innovative and competitive region. ASEAN aspires to be the central institutional platform in the Asia-Pacific and Indo-Pacific, but it faces challenges related to neutrality and maintaining cooperation across various political systems. Upholding the non-interference principle, multilateralism, and strategic independence are key to preserving ASEAN's centrality and relevance amidst major power competition in the region.

Governance Tools for the Indo-Pacific: ASEAN and Indonesia's Perspective

ASEAN's regionalism is characterised by openness and softness compared to the EU's closed and hard regionalism. It allows for the inclusion of non-member states through ASEAN Plus frameworks, promoting investment inflows from external sources. Soft regionalism involves non-binding consultation and consensus decision-making, fitting the ASEAN format. The region does not discriminate based on political systems and seeks inclusivity in its Free and Open Indo-Pacific approach, emphasising digital economic enhancement.

Economic convergence remains ASEAN's goal to prevent economic divergence damage in intra- and extra-regional cooperation. Indonesia plays a pivotal role in developing Indo-Pacific cooperation with ASEAN centrality as a primary focus, fostering an environment characterised by openness, transparency, inclusivity, and respect for international law.

Governance Rules for the Indo-Pacific: Trade and Investment Cooperation

Geopolitical stability and a practical approach to economic cooperation are simultaneous and mutually reinforcing conditions for ASEAN's regional prosperity. Ensuring rules and principles in agreements are binding and durable is crucial for soft regionalism. The US's Indo-Pacific Economic Framework can play a significant role in maintaining the region's economic standards and commitment. The EU's substantial global trade and investments align with the Indo-Pacific's rules-based international order, providing a level playing field for trade and investment. To address pressing regional issues, ASEAN must develop a policy framework, as external powers have taken the lead with initiatives like China's BRI and the US Indo-Pacific framework. ASEAN remains cautious about external interventions in domestic politics through the Free and Open Indo-Pacific initiative, emphasising the importance of contributing to this initiative while maintaining ASEAN's soft approach and promoting a rules-based order.

The Indo-Pacific must synergise integration while maintaining a free, open, inclusive, multilateral, and rules-based economic order. ASEAN's regional trading agreements can serve as building blocks for multilateral agreements. The RCEP should be prioritised over the CPTPP, as it includes all ASEAN member states and acknowledges ASEAN's centrality. Single-track RCEP implementation with sufficient investment capacity and higher industrial integration offers more substantial benefits, helping transition from preferential trade agreements to open regionalism. Open regionalism, through the RCEP, strengthens ASEAN's economic integration and benefits the Indo-Pacific economic network.

Enhancement of the ASEAN's Economic Institutions: Indo-Pacific's Stability and Prosperity

To ensure regional stability, ASEAN reaffirms its Zone of Peace, Freedom, and Neutrality (ZOPFAN), seeking to mitigate superpower rivalry and prevent a "new Cold War" in Asia. While the ZOPFAN is a step towards regional security, it requires more specific details. Neutrality principles and the non-interference spirit allow ASEAN to strengthen its central regional economic cooperation with 12 other Asia-Pacific nations, forming the world's largest trading bloc. China's recognition of the Indo-Pacific concept is a milestone for ASEAN, neutralising the discourse. ASEAN's pursuit of economic prosperity relies on a market-led mechanism and government intervention, emphasising the importance of government action at the regional level for economic convergence.

ASEAN is Central to a Stable Indo-Pacific Architecture

The Indo-Pacific is promoted as a free and open region, in line with open regionalism principles adopted by ASEAN and EAS. However, the notion of 'free' concerning domestic political systems does not align with ASEAN's non-interference principle. ASEAN's open and soft regionalism principles maintain flexibility, ensuring that all economic partners feel secure, promoting geopolitical stability. ASEAN's centrality as well as open, soft, free, and inclusive principles are vital for Southeast Asian regional economic integration, with economic convergence as the main objective. Stable geopolitics demand open, soft, free, and inclusive principles, while a prosperous regional economy requires economic convergence, creating interdependent relations in the Indo-Pacific.

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About the Editor

Anita Prakash is Senior Policy Advisor in the Office of the President at ERIA (Economic Research Institute for ASEAN and East Asia), Jakarta, Indonesia.

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20, Rouse Avenue Institutional Area,
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E-mail: contactus@orfonline.org
Website: www.orfonline.org

Economic Research Institute for
ASEAN and East Asia (ERIA)
Sentral Senayan II Building, 6th Floor
Jalan Asia Afrika Kav. 8
Jakarta Pusat-10270
Indonesia