Comparative Analysis of Convergence on Regional Economic Integration:
The Eurozone and ASEAN

There was a fundamental change in international relations after World War II; regionalization as a part of economic integration among neighboring countries has since become a trend, with the goal of improving the welfare of all citizens concurrently. Instilling deeper economic integration, according to Baldwin and Wyplosz (2006), will contribute to medium- and long-term economic performance. Generally speaking, economic integration will improve efficiency, increase GDP per worker, and provide more investment per worker. From this point, the capital per labor ratio starts to rise towards new, higher-equilibrium value and faster growth of output per worker. Long-term effects from economic integration are faster knowledge creation and absorption.

Since the economic crisis in 1997, ASEAN has shown interest in developing policies to set up greater regional exchange rate stability (Bayoumi, Eichengreen and Mauro, 2000) and the Eurozone was seen as the ideal example. The story of crisis however repeated in the area of most developed countries situated or Eurozone. A decade after the Euro, the crisis has erupted in the Eurozone, suggesting that common currency might be less attractive. Before being pulled into the crisis that exploded in 2007, the Eurozone demonstrated stability; however, fallout from the crisis made it clear that the euro had been unprepared for such severe conditions (Lapavitsas et al, 2010).

Based on Jovanovic’s (2006) degrees of integration, the Eurozone has achieved half of an economic union and has ASEAN almost reached a free-trade area. While the Eurozone has been implementing the European Monetary Union (EMU), ASEAN is still struggling to implement the ASEAN Economic Community (AEC) and has only started building the ASEAN Free Trade Area (AFTA).

Geographically, ASEAN is one of the most important crossroads of world trade. However, it is difficult to create ASEAN economic integration, because of differences in the size and development of member states, as well as social issues like language, history, religion, and culture (Jovanovic, 2005). AFTA, established in Southeast Asia in 1992, was one of the most important regional trade arrangements (RTA) in Asia, aiming to eliminate tariff barriers among member countries by agreement on the Common Effective Preferential Tariff (CEPT) scheme. Eliminating tariffs was expected to induce higher intra-regional trade among ASEAN members, and AFTA was expected to become a full free-trade area by the year 2008 (ASEAN Secretariat).
In 1999, the EU first introduced the euro with the Maastricht Treaty (MT) for guidance. Regardless pessimistic and doomed to failure (De Grauwe, 2005), it gained a reputation as a strong currency and a stable financial anchor. Some countries expressed interest in applying such monetary arrangements. with attraction of euro lies in its success demonstration than hollowing out hypothesis (Wyplosz, 2001). The primary objectives of creating a common currency, as explained by Eichengreen (1992), are to reduce transaction costs associated with the elimination of national currencies, increase the credibility of the participating governments, create price stability, achieve more efficient resource allocation through the elimination of exchange rate uncertainty, and promote market integration. The Maastricht Criteria (MC) was a policy designed to maximize benefit and reduce potential outlay, allowing countries joining a common currency to weigh the potential benefit of joining against the inevitable cost (Mico, Stein and Ordonez, 2003).

ASEAN, intending to implement a full AEC by 2015, as announced at the Cebu Summit in January 2007, should consider the relevant macroeconomic policy lessons offered by the Eurozone, including the implementation of MC there as a guidance policy for implementing a common currency. The analysis in this paper primarily uses macroeconomic policy variables associated with MC to compare the effectiveness for both regions. After ASEAN countries suffered the exchange-rate crisis in 1998, encouraging the region to improve regional exchange-rate stability.

In this regard, this dissertation takes various approaches to comparatively measure regional economic integration between a developed, economically integrated area (the Eurozone, in the 6th stage of economic integration) and a developing one (ASEAN, in the 3rd stage of economic integration).

The objectives of this dissertation are as follows:
To investigate the importance of Euro with MC as a guidance policy for crisis in the Eurozone.
To examine the nominal convergence in term of MC variables in both the Eurozone and ASEAN;
To examine the real convergence (income, productivity, and unemployment rate) and growth in both regions; and
To investigate the impact of different degrees of economic integration on trade;

The dissertation consists of eight chapters. Four of eight (Chapters 4, 5, 6, and 7) are the primary analytical studies.

Chapter 1 provides a general overview of regional economic integration and MC policy. This chapter also provides the objective, scope, and outline of this dissertation.

Chapter 2 describes the figures and the facts of the Eurozone and ASEAN. It presents basic facts about the integration process of both regions.

Chapter 3 first discusses regional integration theory, then convergence theory, optimum currency area theory (OCA), international trade theory, and financial crisis theory.

In Chapter 4, by considering the Asian crisis, we track the Eurozone crisis by investigating the significant of Euro with MC on peripheral Eurozone countries. The results of descriptive and difference-in-difference analyses show that the pure effect was positive. Unfortunately, sharing a common currency restrains high per-capita GDP growth, and can create a higher deficit trade balance. The euro was not the main culprit in the current Eurozone crisis, since the debt crisis mainly derived from budget deficits, the inability to meet MC, trade imbalances between core and peripheral countries, the lack of a fund-transfer mechanism, and the lack of an institution by which to control capital mobility.

Chapter 5 describes the first research question, an empirical analysis of whether ASEAN satisfies MC criteria with the Eurozone as the benchmark. The study also measures the degree of convergence of MC variables in both the Eurozone and ASEAN. It was determined that ASEAN has high convergence of interest rates, and most countries met the budget criteria. High nominal convergence, price stability, and the Euro’s
evolution to become an anchor currency were signs that the modeling policy by the MC is a step in the right direction.

Chapter 6 examines the role of macroeconomic MC policy variables, using various approaches to analyze whether macroeconomic policy coordination in the Eurozone has improved the region’s economic performance, compared to a region that does not have such a policy. Based on these results, convergence was found to be conditional rather than unconditional, except with respect to unemployment and productivity in the Eurozone. Imposing macroeconomic MC policy variables on convergence and growth in the Eurozone and ASEAN makes it possible to determine any significant influence.

Chapter 7 investigates the impact of different level of economic integration on bilateral trade. Applying an augmented gravity equation, the deepening impact on bilateral trade was positive if incorporates all Eurozone members. In ASEAN, AFTA generates positive results only among ASEAN-6 countries. A policy related to MC variables has a small influence on reciprocal trade in both regions. Horizontal integration improved in both regions, showing a positive coefficient for size and similarity. Intra-industry trade was a phenomenon in the Eurozone. For ASEAN, different factors determined higher bilateral trade when Cambodia, Laos, Myanmar, and Vietnam (CLMV) were included.

Finally, Chapter 8 reports the main findings in each analytical chapter. It provides further insight into which regional integration policies are most effective, followed by summaries and policy implications.