

An East Asian Single Market? Lessons from the European Union

Simon HIX · Hae-Won JUN

Korea Institute for International Economic Policy



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**KOREA INSTITUTE FOR
INTERNATIONAL ECONOMIC POLICY (KIEP)**

300-4 Yomgok-Dong, Seocho-Gu, Seoul 137-747, Korea

Tel: (822) 3460-1178 Fax: (822) 3460-1144

URL: <http://www.kiep.go.kr>

Kyung Tae Lee, *President*

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Executive Summary

Regional economic integration has been one of the most significant developments in the global political economy in the last twenty years. However, East Asia is an exception where institutionalized economic integration has progressed slowly. What we do in this paper is to consider the possibility of economic integration in East Asia from the perspective of the single market in Europe. The European experience demonstrates that creating a single market is primarily an exercise in market regulation, and that creating a single market requires a convergence of socio-economic preferences and sufficiently independent courts and the rule of law. However, these starting conditions are necessary but not sufficient. What is also required is the delegation of significant agenda-setting and enforcement powers to independent regulatory agents. If designed carefully, a single market in East Asia would lead to further trade integration between the members, industrial consolidation in certain sectors, and higher growth rates and more jobs. An East Asian single market organization might also produce significant political benefits, such as an arena for promoting political integration and resolving disputes, and the spread of democratic government and free markets in the region.

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Dr. Simon Hix is a professor at London School of Economics and Political Science. He received his Ph. D. in Political and Social Science from European University Institute. His areas of interest are political economy, European Union, etc. His recent articles include "Europeanised Politics? European Integration and National Political Systems", (London: Frank Cass. Co-edited with Klaus Goetz, 2001), "The Political System of the European Union", (Basingstoke: Macmillan/Palgrave, 1999), "Neither a Preference-Outlier nor a Unitary Actor: Institutional Reform Preferences of the European Parliament", (*Comparative European Politics* 3, 2005), "Understanding Public Support for British Membership of the Single Currency", (*Political Studies* 53(1) 65-81. With Matthew Gabel, 2005). E-mail: s.hix@lse.ac.uk

Dr. Hae-Won Jun is a Teaching fellow at Yonsei University. He received his Ph. D. in Politics from St. Antony's College, University of Oxford. His areas of interest are European politics, International Cooperation, etc. His recent articles include "Catching the runaway bureaucracy in Brussels. Euro-parliamentarians in budgetary politics", (*European Union Politics* 4 (4), 2003), "Parliamentary Scrutiny in the European Union", Thesis, St. Antony's College, University of Oxford, 2005. E-mail: hae-won.jun@yonsei.ac.kr

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An East Asian Single Market?

Lessons from the European Union

Simon HIX, Hae-Won JUN

I. Introduction

Regional economic integration has been one of the most significant developments in the global political economy in the last twenty years. The European Union (EU) remains the leading case of this phenomenon, which now incorporates twenty-five states in Western and Eastern Europe in a highly-integrated economic, political and security union (cf. Hix 2005). No other region has, so far, undertaken such an ambitious level of economic and political integration as in the EU. Nevertheless, regional free trade, customs unions and monetary cooperation arrangements have emerged in several regions of the world, such as the North Atlantic Free Trade Area (NAFTA), the Southern American Common Market (Mercosur), the Central American Common Market, the Caribbean Community (CARICOM), the Gulf Co-operation Council (GCC), the Economic Community of West African States (ECOWAS), and the Common Market for Eastern and Southern Africa (COMESA) (cf. Mattli 1999). In comparison, economic integration in East Asia is underdeveloped. A variety of reasons are often cited to explain the lack of integration in East Asia, such as the large variance in population size, economic size and prosperity, national rivalries, the division of Asia in the Cold War, the legacy of past conflicts, the regional economic dominance of Japan, and the diversity of religious and cultural values (e.g. Akaha 1999; Rozman 2004).

Nevertheless, towards the end of the millennium things began to change. In 1992, the members of the Association of South East Asian Nations (ASEAN), which had been established in 1967 as mainly a political organization, agreed to create a free trade area amongst themselves by 2008. In 1989, led by Australia,

Japan and the United States, the Asia-Pacific Economic Cooperation (APEC) was established as a bridge between ASEAN, Northeast Asia (China, Japan, South Korea and Russia) and North and South America. Then, in 1994, APEC agreed to promote 'free and open trade and investment in the Asia-Pacific by 2010 for industrialized economies and 2020 for developing economies'.¹⁾ In 2001, in the wake of the Asian financial crisis, the ten ASEAN countries launched the Chiang Mai Initiative with China, Japan and South Korea (the so-called ASEAN+3), which committed these states to monetary cooperation, financial liberalization, and monitoring each others' economic and financial situations. And, bilateral free trade agreements are in the process of being negotiated between one or more members of ASEAN and Japan, Korea, China, Hong Kong, Australia, New Zealand, Canada, the United States, Mexico, Chile and several other countries in the Asia-Pacific region.

Some commentators remain sceptical that these developments will amount to much (e.g. Lincoln 2004; Tsunekawa 2005). However, others are more optimistic that genuine market and financial integration may develop between the ASEAN+3 states or some other combination of 'economies' on the Western Pacific (e.g. Pempel 2005).²⁾

This paper assesses the prospects of economic integration in East Asia from the perspective of the formation of a single market in Europe. Our starting assumption is that any regional community that aims to do more than create a free trade area can, and should, learn from the experience of the European Union. In our opinion, most existing research and discussion about economic integration in East Asia has alluded to this fact, but has not followed though the logic of this perspective (perhaps because most specialists on East Asia are understandably less knowledgeable on economic integration in Europe or the institutional design of the EU). We should say at the outset, however, that although we are experts on the European Union we are not experts on East Asia or East Asian integration. We

1) Quote from the APEC website:

http://www.apecsec.org.sg/apec/about_apec.html, 27 March 2005.

2) We use the word 'economies' rather than 'states', as this is the formulation used within APEC to allow for China and Chinese Taipei to be a part of the same organization.

come at this question as outsiders, and our ideas should be read with this in mind.

The rest of this paper is organized as follows. Section two sets out some general theoretical issues related to the construction of a single market in a supranational context, focusing on the fact that creating a single market is primarily an exercise in market regulation. Section three then looks at the model of the European Union, and particularly the institutional design of regulatory policy-making in Europe. Section four sets out a possible East Asian single market organization, and justifies why we feel such an organization might be feasible. We consider a scenario with thirteen economies (Australia, Chinese Taipei, Hong Kong, Indonesia, Japan, Malaysia, New Zealand, Papua New Guinea, the Philippines, Singapore, South Korea, and Thailand) as well as the possibility of including China. Finally, section five contains a brief conclusion.

II. How to Construct a Supranational Single Market

1. Two Methods: Harmonization and Mutual Recognition

A free trade area involves the removal of barriers to trade in a particular set of goods or services, via the reduction or abolition of import tariffs and quotas. All free trade agreements exclude particular sectors of the economy. A 'single market', in contrast, involves the complete free trade in goods, services, capital and labor. Put simply, in a genuine single market, separate national markets cease to exist. Creating a single market involves the removal of three types of barriers to the movement of goods, services, capital and labour: *physical barriers*, such as customs controls at national borders and airports; *technical barriers*, such as import quotas, different product standards, and discrimination on the grounds of nationality in public procurement contracts or in labour contracts; and *fiscal barriers*, such import duties and capital controls.

Two methods can be used to remove these controls. The first method is *harmonization*, which involves the replacement of existing national rules with commons rules on the production, distribution, and exchange of goods and services, and on the movement of capital and labor. Harmonization consequently involves passing a large amount of new legislation. For example, the European Commission's White Paper on *Completing the Internal Market* set out approximately 280 pieces of legislation that would be necessary to complete a single market in Europe (European Commission 1985).

The second method is *mutual recognition*, which involves the establishment of the principle that any good or service that can legally be sold in one member of the single market can legally be sold in any other member. In this method, the main motors of market integration are private citizens and firms, who take cases to courts to enforce mutual recognition rights.

In practice, these two methods are mutually reinforcing, as different methods are used for integrating different economic sectors. The result, in practice, is a continuum of methods. At one end, highly technical sectors (such as financial services) require a large amount of harmonization beyond which mutual recognition can apply. At the other end, in sectors that are relatively straight forward to integrate (such as consumer electronics), mutual recognition can be applied once some basic safety and quality standards have been harmonized.

2. The Result: A Mix of Deregulation and Reregulation

The result of creating a single market is a mix of *deregulation* as well as *reregulation* (esp. Dehousse 1992; Majone 1996). On the deregulatory side, mutual recognition and harmonization lead to the removal of huge amounts of national regulatory 'red tape'. Most obvious, governments are forced to abolish capital controls, import tariffs, quotas and customs duties. Less obvious are the indirect effects of a single market on public procurement and working conditions. A single market may require the establishment of the principle of 'non-discrimination' on the grounds of nationality in the awarding of public procurement contracts (where the free movement of goods and services are concerned) or in the award of working contracts and the treatment of workers (if the free movement of persons is included). Such rules would consequently force the liberalization of large sectors of national economies as well as industrial relations and workers' rights. Furthermore, a single market should include rules governing state aids to industry, to create a 'level playing field' across all member states. Such rules would lead to the privatization of nationalized industries and the opening up of 'national champions' to competition from international firms.

On the reregulatory side, harmonization involves the establishment of new regulations for all members of the single market. To enable goods and services to circulate, common 'product regulations' need to be adopted, such as product safety standards, consumer health standards, product labelling rules, and environmental packaging and waste disposal standards. In addition, some 'process standards' would need to be adopted to avoid a 'race to the bottom' in social and environmental standards, as states compete to cut the costs for their own industries or to attract

foreign direct investment. At a bare minimum, these process standards would include rules on health and safety at work and controls on environmental pollution in the production process. Process standards might also be adopted to cover workers rights, such as working conditions, working hours, parental leave, and workers' consultation rights (Scharpf 1996).

How far a single market would change the domestic policy mix of a state depends on the specific mix of deregulation and reregulation in the single market program as well as how liberal or highly regulated a national economy is before joining a single market. For example, the EU single market program is a 'social market' model that combines the liberalization of almost all national economic sectors with a comparatively high set of common environmental standards (such as car recycling standards) and social rights (such as non-discrimination on the grounds of nationality, gender, race, religion, disability, age, and sexuality). Nevertheless, this policy mix affected the members of the EU very differently. States with high social standards, such as France and Germany, were able to keep many of their existing social rules, but were forced to open up their economies to competition from firms from other EU member states. On the other side, states with more liberal economies, such as the United Kingdom and Ireland, did not need to privatize new industries, but were forced to accept new regulations in the area of social rights and environmental protection. Depending on the existing domestic policy status quo, then, a single market can either be seen as a 'neo-liberal plot' (as the French left claims) or 'socialism through the back door' (as Margaret Thatcher famously claimed).

3. The Normative Theory of Regulation: Delegation to Independent Regulators

If creating a single market involves making new regulations, two questions immediately arise. First, what should be regulated? Second, how should these regulations be made? The two main theoretical perspectives in the study of regulatory policy lead to different answers to these questions.

According to the 'normative theory of regulation', the aim of regulation should

be to promote the ‘public interest’ (e.g. Mitnick 1980; Sunstein 1990). In neo-classical economic theory, free markets are naturally pareto-efficient, but in the real world there are numerous ‘market failures’. Regulation should hence be used to correct these failures:

- *technical standards and consumer protection standards* enable consumers to gain information about the quality of products that would otherwise not be publicly available;
- *health, safety, and environmental standards* reduce the adverse effects (‘negative externalities’) of market transactions on individuals not participating in the transactions;
- *competition policies* prevent monopolistic markets from emerging, market distortions (through state subsidies), and anti-competitive practices (such as price collusion); and
- *industry regulators* through such instruments as price controls, ensure that ‘natural monopolies’ operate according to market practices.

If economic policies are made through traditional democratic (‘majoritarian’) institutions, such as parliaments or governments, they will tend to be ‘redistributive’ rather than pareto-efficient. Political parties, who will try to achieve policy outputs that benefit their supporters, control parliaments and governments. Democratic government consequently tends to lead to policies that redistribute resources from the losing minority to the winning majority in a particular electoral contest (Majone 1998). For example, where expenditure policies are concerned, governments on the left usually increase taxes on the wealthiest members of society and increase public spending on social benefits, whereas governments on the right tend to reduce taxes and cut benefits. If democratic majorities are allowed to govern regulatory policies, similar redistributive outcomes would result: for example, the left would use regulation to increase the rights of workers and protect the environment, imposing costs on business, and the right would do the opposite. Consequently, a central argument in the normative theory of regulation is that if regulatory policies are meant only to correct market failures, with pareto-efficient and not redistributive outcomes, these policies should be made by independent institutions.

This normative perspective also has specific implications for supranational regulatory regimes (Moravcsik 1993, 1999; Pollack 1997, 2003). Making regulatory policy in a supranational context involves two sorts of strategic dilemmas. First, deciding which set of regulatory standards to adopt is a 'coordination game' (for example between states with existing high regulatory standards and states with existing low regulatory standards), where several equilibria are possible. To resolve this problem, agenda-setting should be delegated to an independent actor (like the European Commission) to come up with legislative proposals that are globally optimal. Second, enforcing agreements once adopted is a 'prisoners' dilemma game', where the optimal strategy for member states is not to open up their markets to competition while waiting for others to implement the rules. To resolve this problem, enforcement of the agreement needs to be delegated to a judicial body, such as a court, or a quasi-judicial body, such as a disputes panel.

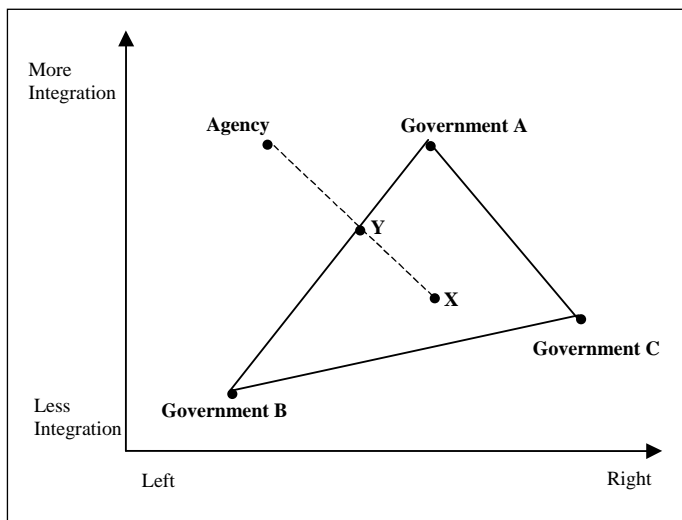
In other words, from a normative perspective, creating a supranational single market requires the delegation of substantial powers to initiate and enforce agreements to independent agencies. Any agreement to create a single market is simply not credible without such delegation because either policy are unlikely to be adopted and enforced or the regulations that are adopted are not guaranteed to be in the general interests of the community.

4. The Positive Theory of Regulation: Institutional Design to Limit Policy Drift

Against this normative theory, the 'positive' theory of regulation seeks to explain policy outcomes through deductive reasoning. The first positive approach to regulation was Stigler's (1971) so-called 'economic theory of regulation', in which regulation is 'demanded' by private interests and 'supplied' by politicians. On the demand side, applying Olson's (1965) theory of interest group organization, certain interests groups (such as large firms with concentrated interests) are more able to influence regulators than others (such as consumers or taxpayers). On the supply side, using Downs's (1957) theory of electoral politics, Stigler assumed that politicians recognise that regulations impose costs on some voters

and benefits for others, and that groups that are the subject of regulation tend to have more resources available to finance politicians' campaigns. Stigler (p. 94) consequently concludes that 'as a rule, regulation is acquired by the industry and is designed and operated primarily for its benefit'. Furthermore, regulatory agencies have interests and policy preferences of their own. For example, agencies can try to increase their influence in the policy process. They can also seek larger budgets or to maximize their independence from political control. Either way, this leads to a different set of conclusions from the normative approach about how regulation should be made. In the positive view, independent regulators are likely to try to change policy in a particular direction that will lead to winners and losers rather than a pareto-efficient outcome.

The result is 'policy drift', as illustrated in Figure 1. In the figure there is a two-dimensional policy space in which there are three governments with 'ideal policy preference' at points A, B, and C. The regulatory agency, meanwhile, prefers a high level of regulation and the promotion of faster market integration, and is hence located in the top-left of the figure. The governments and the agency each try to secure a policy as close as possible to their ideal points. The governments agree on a piece of legislation at position X and delegate responsibility to the agency to implement the legislation. Through the implementation process, the agency is able to shape the final policy outcome, and in fact can move the final policy as far as position Y. Governments A and B prefer this policy to the original deal because Y is closer to their ideal preferences than X, and hence have no incentive to introduce new legislation to overrule the agency. However, governments A and B will block any moves further towards the agency's ideal point, as any policy in this direction would be less attractive to these two governments than position Y. The result, however, is that the agency has discretion to change the original policy outcome, within the constraints of the preference structure of the legislators.

Figure 1. Technical and Allocative Efficiencies

Source: Hix(2005)

Nevertheless, this sort of policy drift can be limited by institutional design (cf. McCubbins and Schwartz 1984). For example, the structure of representation in a regulatory agency can be designed to minimise the gap between the preferences of the ‘principals’ and the ‘agent’, for example by giving each of the principals a seat on the executive board of the agency. Similarly, the procedure for appointing the head of the agency could be designed to maximize the consensus on the candidate, through an oversized majority procedure or through approval by multiple institutions. Principals can also gather information on the performance of the agent, and force the agent to disclose information in public hearings (known as a ‘police patrol’ oversight procedure). Alternatively, principals can use private interest groups to do the monitoring for them by providing judicial review of the agent’s actions and easy access to the courts for individuals or firms who are affected by regulations (known as a ‘fire alarm’ oversight procedure). The result of these controls is a restriction of the ability of an agent to move from the original policy intention.

In sum, constructing a supranational single market is primarily an exercise in

market regulation. The main policy aim of such regulation should be the creation of a level playing field for economic competition and the correction of potential market failures. These goals are best secured through a particular institutional design: where agenda-setting and enforcement are delegated to an independent agent (such as the Commission), and the discretion of this agent is minimized through the structure of representation in the agency, the procedure for appointing the head of the agency, and the judicial review of the agency's actions.

III. The European Union Model

The only successful example of a supranational single market is the European Union. The roots of the EU single market go as far back as the Treaty of Rome, which was implemented in 1958 and aimed to create a 'common market' amongst the then six member states. The goal of the free movement of goods, services, capital and labor was already a central feature of the Treaty of Rome. However, it was not until the 're-launch' of European economic and political integration in the mid 1980s that the necessary institutional design was created to establish a genuine single-market. Specifically, the Single European Act, which was signed in 1986 and implemented in 1987, included three key institutional changes: (1) the delegation of significant agenda-setting powers to the Commission (to propose almost 300 pieces of legislation for the creation of a single market by 31 December 1992); (2) the creation of an efficient yet legitimate legislative procedure to pass these measures (where legislation would be passed by a 'qualified-majority' in the EU's Council of Ministers as well as a simple majority in the European Parliament); and (3) the establishment of a series of 'side payments' to potential losers from a single market (such as an increase in regional subsidies to the poorer member states).

All subsequent EU institutional reforms have followed directly from the Single European Act and the logical consequences of the single market. For example, the 1992 Maastricht Treaty, which formerly established the European Union, launched the timetable and procedures for creating the single currency (the Euro), which was an essential component of an integrated single market. Similarly, the 1997 Amsterdam Treaty reformed the rules in the area of justice and home affairs to enable the governments to tackle the security and immigration consequences of the genuine free movement of persons across Europe.

Perhaps the clearest indicator of the success of the EU single market project has been the continued enlargement of the EU. In 1995 Austria, Finland and Sweden joined the original twelve (Belgium, Denmark, France, Germany, Greece,

Ireland, Italy, Luxembourg, the Netherlands, Spain, Portugal, and the United Kingdom). Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, and Slovenia then joined in 2004. And, over the next decade the EU will expand further to include Bulgaria, Romania and Croatia and potentially Turkey, Norway, Switzerland and the Ukraine.

1. Why a Single Market in the 1980s?

There are several reasons why the decision to create a single market in Western Europe came in the 1980s. First, for the first time, there was a convergence in the basic socio-economic preferences of all the EU member states (esp. Moravcsik 1998). There was now a consensus in favor of a single market that included every major political party and political leader in Europe. On the right, the British Conservative government, led by Prime Minister Margaret Thatcher, realized that the impact of British privatization and deregulation would be much greater if these policies could be spread to the Continent. On the left, following the failure of radical socialist economic policies in the early 1980s, the French Socialist government, led by President François Mitterrand, turned in the mid 1980s to the creation of a European-wide market as a way of promoting the rationalization of European industry and the emergence of European industrial champions.

Second, this political consensus was supported by a broad consensus amongst professional and academic economists. By the mid 1980s, most economists agreed that Keynesian policies had been a failure, as they had not enabled Europe to recover from the economic recession of the 1970s and early 1980s as quickly as the United States and Japan had done. The solution, so most felt, was the creation of a European-wide market that would force national governments to liberalize their economies and produce enormous economies of scale. For example, a group of economists produced a famous report on *The Cost of Non-Europe*, which claimed that a single market would add 4.5 percent to the Gross Domestic Product of the EU member states, reduce prices by 6 percent, and create 1.8 billion new jobs (Cecchini *et al* 1988).

Third, multi-national corporations across Europe mobilized to lobby their

governments to integrate and liberalize their national markets. The primary vehicle for this action was the Round Table of Industrialists, which brought together the chief executives of many hi-tech and industrial giants from both inside and outside the member countries of the EU, such as Unilever, Solvay, Volvo, Olivetti, Siemens, Philips, Volkswagen, Bayer, Royal Dutch Shell, and Thomson.

Fourth, the Commission was lead by an activist President, Jacques Delors. Jacques Delors became Commission President in 1985 after a series of relatively low-key Presidents. As the French Finance Minister in the early 1980s he had played a major role in orchestrating Mitterrand's economic policy u-turn from a strongly Keynesian economic management program to a more liberal and free market program. Delors was also ideologically committed to European integration, a brilliant administrator, and did not fear confronting any government leader who opposed his ideas. The fact that the single market and several key flanking policies (such as reform of the EU budget and Economic and Monetary Union) were successfully prepared, proposed and negotiated in the late 1980s and early 1990s is at least in part due to Delors' leadership and entrepreneurial skills as head of the Commission for nine years.

Fifth, after the so-called 'Eurosclerosis' years of the 1970s, by the mid-1990s there was widespread public enthusiasm in most countries for a renewed effort to integrate Europe. This was partly driven by optimistic expectations about the positive economic benefits of European integration. But, the new ideological commitment to European integration was also driven in the mid 1980s by growing antipathy in many European countries to the Reagan administration in Washington.

In other words, a particular, and potentially unique, set of factors came together in the mid 1980s in Western Europe to create the environment for Europe's political leaders to embark on an ambitious program of market integration.

2. Institutional Design: Credible, Efficient, and Legitimate

This environment may have been a necessary condition for creating a single

market. However, it was not sufficient. What was also needed was a particular set of institutions. As it happens, whether by good fortune or by the genius of the 'founding fathers' in the 1950s and the reformers in the 1980s, the European Union already possessed an ideal set of institutions that with some moderate reform could be used to create and implement a single market.

First, the Treaty of Rome and the Single European Act established a highly-stable hierarchical division of competences between the EU and national levels of government. Public policies in the EU are separated into four categories. *Exclusive EU competences* include the construction and regulation of the single market, agricultural subsidies, external trade negotiations (such as EU representation in the World Trade Organization), and monetary policy (for the members of Economic and Monetary Union). *Shared competences between the EU and the member states* include environmental and social standards, although most environmental regulations are now 'made in Brussels'. *Coordination competences*, where the member states agree to monitor and coordinate each others' policies, including macro-economic policy, justice and home affairs policies, and foreign and security policies. Finally, *exclusive member state competences* include all the main areas of public spending, such as healthcare and public education provision.

Essentially, the European level of government is responsible for creating and regulating the continent-wide market, while the national level of government is responsible for providing public spending goods. The two levels work together to coordinate policies where there are high externalities for national governments from the construction of a single market, such as macroeconomic management and controls on the movement of persons. This basic constitutional structure is highly stable, and has not changed substantially since it was established informally by the Single European Act and the Maastricht Treaty. It is also the basic structure that was formalized in the proposed EU Constitutional Treaty, which the governments signed in 2004.

Second, the Treaty of Rome and the Single European Act created an institutional design with a careful set of checks-and-balances. The EU possesses a 'dual executive,' half of which are the national governments. The European Council, which brings together the heads of government of the EU member states

every three months, sets the medium-term policy agenda of the EU (by unanimity), delegates to the Commission through treaty reforms and other instruments (usually by unanimity), and nominates the Commission President (by a qualified-majority). The individual governments of the member states also appoint the individual members of the Commission and the judges in the European Court of Justice (ECJ). The other half is the Commission, which has a monopoly on legislative initiative and is responsible for monitoring the execution of legislation, bringing cases to the ECJ to enforce EU laws, and exercise some direct executive powers (for example in the area of merger control).

Table 1. Trends in IQFS and KAO

| Member state | Population (mil.) | Votes in Council under QMV | Commissioners | MEPs |
|----------------|----------------------|-------------------------------|---------------|------|
| Germany | 81.8 | 10 | 2 | 99 |
| United Kingdom | 58.7 | 10 | 2 | 87 |
| France | 58.3 | 10 | 2 | 87 |
| Italy | 57.3 | 10 | 2 | 87 |
| Spain | 39.2 | 8 | 1 | 64 |
| Netherlands | 15.5 | 5 | 1 | 31 |
| Greece | 10.5 | 5 | 1 | 25 |
| Belgium | 10.1 | 5 | 1 | 25 |
| Portugal | 9.9 | 5 | 1 | 25 |
| Sweden | 8.8 | 4 | 1 | 22 |
| Austria | 8.1 | 4 | 1 | 21 |
| Denmark | 5.3 | 3 | 1 | 16 |
| Finland | 5.1 | 3 | 1 | 16 |
| Ireland | 3.6 | 3 | 1 | 15 |
| Luxembourg | 0.4 | 2 | 1 | 6 |

The EU has a bi-cameral legislature. The main legislative chamber is the Council of Ministers, where government ministers from each member state meet by policy area – such as the Economic and Finance Council (EcoFin), the Agriculture Council, the Internal Market Council, and so on. When making legislation governing the single market, the Council of Ministers usually decides by a ‘qualified-majority’, where each member state has a particular number of votes in proportion to its population size and an oversized majority of votes (of approximately 70 percent) is required for legislation to be passed (unanimity is kept in some sensitive areas, such as tax and social security harmonization). Table 1 shows the voting weights in the EU Council, and the design of representation in the Commission and European Parliament.

The other legislative chamber is the European Parliament, which meets in Strasbourg and Brussels. The European Parliament had 626 members after the enlargement of the EU in 1995, and after the enlargement in 2004, it now has 732 members. The European Parliament has been directly elected every five years since 1979, and the last European elections were held in June 2004. The Members of the European Parliament sit in transnational party groups rather as national delegations, and the two largest groups in the current Parliament are the European People’s Party (EPP) on the centre-right and the Party of European Socialists (PES) on the centre-left, who together hold almost 70 percent of the seats in the chamber.

The main procedure for adopting single market legislation is the so-called ‘codecision procedure’, which was established by the Maastricht Treaty and reformed by the Amsterdam Treaty. Under the codecision procedure, legislation cannot be passed without approval by a qualified-majority in the Council and a simple majority in the European Parliament. If after two readings in each chamber, the texts adopted by the two institutions are not identical, a ‘conciliation committee’ is convened to try to reach a compromise before an agreed text is put to both institutions in a final reading. The Council and the European Parliament are also jointly responsible for appointing the Commission President and the Commission as a whole, and together monitor the behaviour of the Commission - although the European Parliament has the sole power to censure the Commission

(by a special majority).

The judiciary of the EU incorporates the European Court of Justice and the national courts. The European Court of Justice, which has one judge per member state, rules on cases brought to it by the other EU institutions or by the national courts. The national courts are responsible for enforcing EU law, and are able to make references to the ECJ by the so-called 'preliminary reference procedure'. This procedure empowers the national courts to increase their own authority in their domestic systems. Two key legal principals that have been developed by the ECJ and the national courts underpin the EU legal system: the 'direct effect' of EU law, which means that EU law is the 'law of the land' throughout the EU and in contrast to international law impose direct rights and obligations in individual citizens as well as states; and the 'supremacy' of EU law, which means that when there is conflict between a national law and an EU law, EU law is supreme. Although these two principles are crucial in the operation of the single market, they were established by the ECJ in the 1960s.

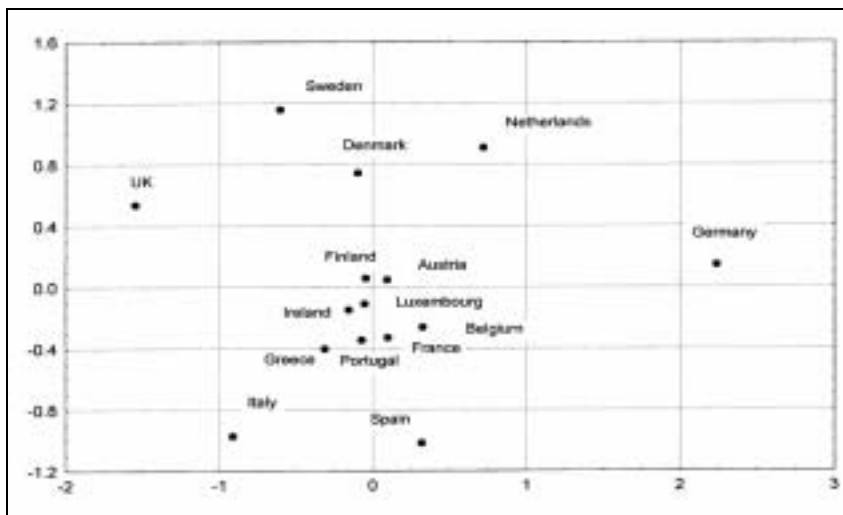
This particular design of institutions is ideal for the creation of an effective single market. The combination of a continental regulatory regime and national spending policies creates a balanced and centrist policy regime, and prevents governments from either pursuing radical deregulatory policies or radical 'borrow and spend' programs. Although the design of executive authority maximizes the credibility of regulatory policy-making as the Commission's independence is guaranteed, the policy-drift by the Commission is limited by the structure of representation in the Commission, the Commission appointment procedure, scrutiny by the Council and the European Parliament, and judicial review by the ECJ. The design of the legislative procedure ensures a careful combination of efficiency, since legislation only requires a qualified-majority to pass in the Council, and legitimacy, since the majority in the Council is balanced by a majority amongst the transnational political parties in the European Parliament. The design of the EU's main legislative procedure virtually guarantees 'centrist' policy outcomes and that no major political or economic interest is on the losing side. Finally, the enforcement of EU single market is ensured by the ECJ in cooperation with national courts, who apply EU law as part of the national rule of law.

3. Functioning of the EU Institutions

How the making of policy governing the EU single market works in practice can be seen in the day-to-day functioning of the EU institutions. For example, the governments in the Council overwhelmingly decide by consensus, even when they are allowed to rule by a qualified-majority (e.g. Mattila and Lane 2001). Nevertheless, when votes do split along left-right lines, they split in predictable and transparent ways, with those governments most in favor of market liberalization on one side and those most opposed to market liberalization on the other side. This is illustrated in Figure 2, which is a multi-dimensional-scaling plot of votes in the Council between 1994 and 1998. The figure illustrates that there are only a few outliers in voting in the Council, such as the United Kingdom and Germany. However, the fact that these outliers are in different places in the figure demonstrates that splits in the Council vary. Basically, the EU Council works because, first, governments are rarely on the losing side and, second, if they are on the losing side on one issue they are more than likely to be on the winning side on a lot of other issues.

A different picture emerges from voting in the European Parliament (Hix *et al.* 2005a, 2005b). Figure 3 shows the location of individual MEPs derived from applying the NOMINATE scaling method to all the roll-call votes in the first half of the fifth directly elected Parliament (1999 to 2001). The positions of the parties in the figure suggest that the first dimension of voting in the Parliament is the left-right and the second dimension is pro- and anti-Europe. Also, the tightness of the clusters reveals that the transnational party groups in the European Parliament are surprisingly cohesive.

Figure 2. Voting in the EU Council

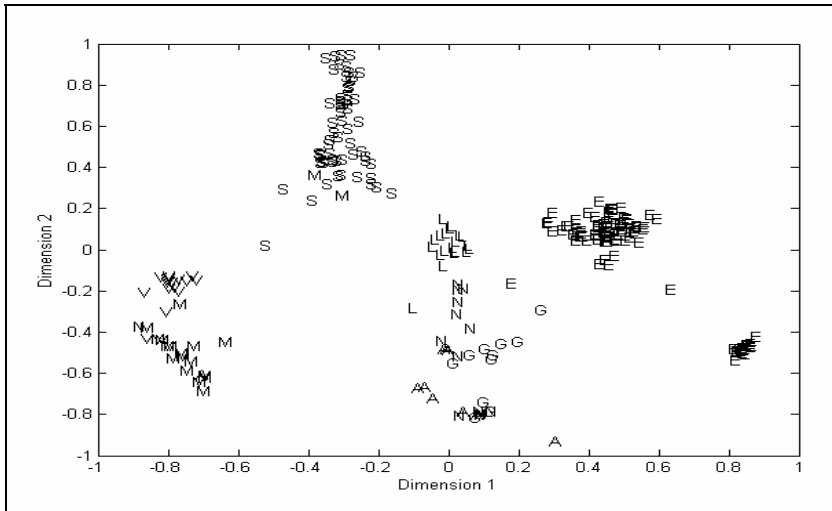


Note: This is a 'multi-dimensional-scaling' plot of all roll call votes in the Council between 1994 and 1998.

Source: Mattila and Lane (2001)

And, the relative positions of the party groups, where the European People's Party is slightly off-set to the right and the Party of European Socialists is slightly off-set to the left, with the Liberal group between these two, reveals that votes in the European Parliament split along left-right lines, but coalitions on this dimension shift from vote to vote, with a centre-left majority winning on some issues (such as environmental regulation) and a centre-right majority winning on other issues (such as the liberalization of financial services). Hence, voting in the Parliament, where Europe's historical ideological traditions are articulated, complements voting in the Council, where votes are split along national lines.

Figure 3. Voting in the European Parliament



Notes: This is a NOMINATE plot of all roll call votes in the European Parliament between 1999 and 2001.

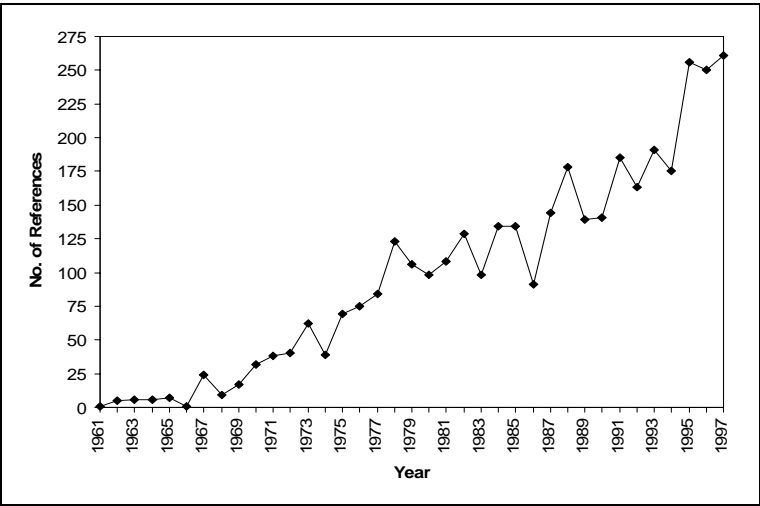
Key to party abbreviations:

- A Group for a Europe of Democracies and Diversities (Anti-European)
- E European People's Party-European Democrats (Conservatives & Christian Democrats)
- G Union for a Europe of Nations (Nationalist Conservatives)
- L European Liberal, Democrat and Reform Party (Liberals)
- M European United Left/Nordic Green Left (Radical Left)
- N non-attached MEPs
- S Party of European Socialists (Social Democrats)
- V Greens/European Free Alliance (Greens & Regionalists)

Source: Hix, Noury and Roland (2005)

Regarding the operation of the EU judicial institutions and the enforcement of EU law, Figure 4 shows the annual number of referrals to the ECJ by national courts between 1961 and 1997. There was a steady increase in the use of the preliminary reference procedure until the mid 1980s, and then a dramatic increase until the end of the 1990s. Essentially, national courts have been the main motors of legal integration in the EU. They have been eager to apply and extend EU law as a way of asserting their own powers against national executives and legislatures.

Figure 4. Number of Referrals by National Courts to the ECJ



Source: Calculated from the Stone Sweet and Brunell (1999) dataset.

Nevertheless, the single market was not finished on 31 December 1992. Completing the single market is an ongoing project. Several areas of the single market remain incomplete, such as the free movement of services (particularly financial services), the free movement of persons (particularly for third country nationals), and the liberalization of labour markets. Also, as Table 2 shows, some member states are more efficient and effective in transposing EU single market law into domestic law.

Table 2. The Single Market Scoreboard

| | % of single market legislation not transposed into national law(as at 15 April 2003) | Open infringement proceedings (as at 15 April 2003) |
|---------|--|---|
| Denmark | 0.6 | 36 |
| Finland | 1.0 | 47 |
| Sweden | 1.0 | 32 |

Table 2. Continued

| | | |
|-------------------------|------------|-------------|
| Spain | 1.2 | 153 |
| United Kingdom | 1.5 | 121 |
| Belgium | 1.8 | 138 |
| Netherlands | 2.0 | 68 |
| Germany | 3.0 | 136 |
| Luxembourg | 3.2 | 34 |
| Greece | 3.3 | 144 |
| France | 3.3 | 220 |
| Austria | 3.4 | 79 |
| Ireland | 3.5 | 132 |
| Portugal | 3.7 | 57 |
| Italy | 3.9 | 200 |
| EU average/total | 2.4 | 1597 |

Note: The average percent of single market legislation not transposed per member state is reported for the second column, and the total number of open proceedings is reported for the last column.

Source: European Commission (2003)

Overall, the EU single market has been a great success. On the economic side, the single market has been the main motor behind the liberalization of the European economy, the integration of trade, and the restructuring and consolidation of numerous industrial sectors. This has had the effect of promoting economic growth and employment, and stabilizing currencies. Also, by strengthening the European economy, the single market has enabled Europe to maintain rather than abandon its particular 'social model', of a liberal market economy with a relative generous welfare state.

On the political side, the single market has increased the political and social freedoms of European citizens, in terms of their ability to move freely throughout the continent and to consume products from many countries more cheaply than before. The single market has also promoted further political integration, such as the Economic and Monetary Union, cooperation in the field of justice and home

affairs, and the Common Foreign and Security Policy. Furthermore, with the single market, the EU has a more powerful voice in the world in multilateral trade negotiations, and in using the 'soft power' of economic sanctions and access to the EU single market to secure collective European economic, political and security priorities (such as the current policy towards Iran). Finally, and perhaps most significantly, the 'carrot' of membership of the EU single market has been one of the most powerful geo-political weapons of the past half-century, and this in turn is fostering and consolidating economic and political reform throughout Central and Eastern Europe and now Turkey.

IV. A Possible East Asian Single Market

Table 3 shows all the 'economies' that are either in ASEAN or on the Western Pacific side of APEC, plus the Macau Special Administrative Region. These are the cases we shall consider for membership of an East Asian Single Market. Other countries, such as India and Bangladesh, are often discussed as potential regional economic partners. However, as we discussed in the introduction, current debates about East Asian economic integration usually start with ASEAN, ASEAN+3, or the Asian members of APEC.

1. Basic Assumptions: Preference Convergence, Democracy, and Trade Integration

Given our discussion of the theory of how to create a supranational single market and the example of the European Union, we believe a single market is only feasible between states/economies that meet all of the following three conditions:

- 1) They have a reasonable degree of convergent socio-economic preferences, such as a preference for a 'social market' model of capitalism;
- 2) They have significantly independent judicial institutions and a sufficiently established rule of law to enable the enforcement of the rights and obligations of a single market;
- 3) They have a relatively high level of trade integration relative to trade with other countries or parts of the world.

Table 3. East Asian Countries

| | Population (mil., 2005) | GDP (\$bn, 2003) | GNI/head (ppp, 2003) | Date joined ASEAN | Date joined APEC |
|-------------------|----------------------------|---------------------|-------------------------|----------------------|---------------------|
| China | 1315.8 | 1409.9 | 4,990 | -- | 1991 |
| Indonesia | 222.8 | 208.3 | 3,210 | 1967 | 1989 |
| Russia | 143.2 | 433.5 | 8,920 | -- | 1998 |
| Japan | 128.1 | 4326.4 | 28,620 | -- | 1989 |
| Vietnam | 84.2 | 39.2 | 2,490 | 1995 | 1998 |
| Philippines | 83.1 | 77.6 | 4,640 | 1967 | 1989 |
| Thailand | 64.2 | 143.2 | 7,480 | 1967 | 1989 |
| Myanmar | 50.5 | 74.5 | -- | 1997 | -- |
| South Korea | 47.8 | 605.3 | 17,930 | -- | 1989 |
| Malaysia | 25.3 | 103.2 | 8,940 | 1967 | 1989 |
| Chinese Taipei | 22.8 | 528.6 | -- | -- | 1991 |
| Australia | 20.2 | 518.4 | 28,290 | -- | 1989 |
| Cambodia | 14.1 | 4.3 | 2,060 | 1999 | -- |
| Hong Kong SAR | 7.0 | 158.6 | 28,810 | -- | 1991 |
| Papua New Guinea | 5.9 | 3.4 | 2,240 | -- | 1993 |
| Laos | 5.9 | 2.0 | 1,730 | 1997 | -- |
| Singapore | 4.3 | 91.3 | 24,180 | 1967 | 1989 |
| New Zealand | 4.0 | 72.4 | 21,120 | -- | 1989 |
| Macao SAR | 0.5 | 6.8 | 21,920 | -- | -- |
| Brunei Darussalam | 0.4 | 6.5 | -- | 1984 | 1989 |

Note: These are all the countries in the Association of South East Asian Nations (ASEAN), the members of the Asia-Pacific Economic Cooperation (APEC) on the west side of the Pacific Ocean, plus the Macao Special Administrative Region. The other five members of APEC (and the year they joined) are Canada (1989), Chile (1994), Mexico (1993), Peru (1998), and the United States (1989).

Sources: Population: United Nations (<http://esa.un.org/unpp>); CIA World Fact Book (for Chinese Taipei) (<http://www.cia.gov/cia/publications/factbook>); Gross Domestic Produce: World Bank (<http://www.worldbank.org/data/databytopic/GDP.pdf>), and CIA World Fact Book (for Brunei and Myanmar); Gross National Income/Head, at Purchasing Power Standard: World Bank (<http://www.worldbank.org/data/databytopic/GNIPC.pdf>).

We shall tackle each of these issues in turn.

Starting with the degree of preference-convergence in East Asia, Table 4 shows the responses to a variety of questions in the 1995-97 wave of the World Values Survey for all the states in our set covered by in the World Values Survey plus, for comparison, a sample of states elsewhere in Asia, North and South America, Europe, and Africa. The responses illustrate a relatively high degree of divergence in values across Asia. This is particularly striking when compared to the similar value-profile of Germany and Sweden in Europe. Nevertheless, the citizens of Japan, South Korea, Australia, and Chinese Taipei share many values in common, and are clearly distinct from India or the United States on some issues (such as religiosity) (editor's note: according to the dictionary, religiosity means affected piety, which doesn't make sense. Religion would be a better choice.) and China and Russia on others (such as democracy). With the enlargement of the EU to include countries in Central and Eastern Europe, the variance in socio-economic preferences in the EU has increased, as is shown by the difference in values in Poland compared to Germany and Sweden.

Another reasonable proxy for socio-economic preferences is the level of public spending as a percent of Gross Domestic Product (GDP). The level of public spending in a society is highly correlated with the level of GDP per head, with richer societies generally spending more as a percent of GDP through the government than poorer countries (Scharpf 1997). Nevertheless, at any given level of public spending, a society that is trying to build a welfare state will choose a larger government budget than a society that is aiming for a more liberal macroeconomic model.

Table 4. Asian Values?

| | Do more to cut poverty | Environment or growth? (% environ.) | Pro Democracy | Freedom or order? (% freedom) | Anti immigrants | Religious |
|----------------|------------------------------|---|------------------|-------------------------------------|--------------------|-----------|
| Australia | 51 | 63 | 87 | 48 | 5 | 48 |
| China | 41 | 68 | -- | -- | 20 | -- |
| Chinese Taipei | 64 | 73 | 93 | 10 | 25 | 47 |
| Japan | 60 | 53 | 87 | 22 | 18 | 23 |
| Philippines | 36 | 69 | 84 | 54 | 20 | 98 |
| Russia | 94 | 59 | 58 | 55 | 12 | 40 |
| South Korea | 72 | 77 | 85 | -- | 40 | 51 |
| Bangladesh | 61 | 48 | 98 | 11 | 30 | 98 |
| India | 57 | 31 | 91 | 26 | 33 | 78 |
| Argentina | 82 | 52 | 93 | 60 | 5 | 69 |
| Brazil | 65 | 51 | 85 | 51 | 4 | 89 |
| USA | 40 | 56 | 91 | 51 | 10 | 83 |
| Germany | 67 | 52 | 96 | 50 | 12 | 38 |
| Poland | -- | 51 | -- | 23 | 21 | 83 |
| Sweden | 66 | 69 | 96 | 53 | 5 | 29 |
| Nigeria | 83 | 41 | 93 | 28 | 22 | 98 |
| South Africa | 62 | 30 | 89 | 28 | 19 | 90 |

Notes: The questions in the World Values Survey were as follows:

Do more to cut poverty – Do you think that what the government is doing for people in poverty in this country is about the right amount, too much, or too little? 1. Too much 2. About the right amount 3. Too little. (table shows percent who chose 3).

Environment or growth? – Here are two statements people sometimes make when discussing the environment and economic growth. Which of them comes closer to your own point of view? 1. Protecting the environment should be given priority, even if it causes slower economic growth and some loss of jobs; 2. Economic growth and creating jobs should be the top priority, even if the environment suffers to some extent (table shows the percent who chose 1).

Pro democracy – I'm going to read off some things that people sometimes say about a democratic political system. Could you please tell me if you agree strongly agree, agree, disagree or disagree strongly, after I read each one of them?

Table 4. Continued

Agree Disagree: Democracy may have problems but it's better than any other form of government (table shows the percent who chose 'Agree strongly' or 'Agree').

Freedom or order? – If you had to choose, which would you say is the most important responsibility of government: 1. To maintain order in society; OR: 2. To respect freedom of the individual. (table shows the percent who chose 2).

Anti immigrants – I'd like to ask you about some groups that some people feel are threatening to the social and political order in this society. Would you please select from the following list the one group or organization that you like least? (Table shows percent who selected 'immigrants' from a list of possible answers).

Religious – Independent of whether you go to church or not, would you say you are: 1. A religious person; 2. Not a religious person; or 3. A convinced atheist? (Table shows percent who chose 1).

Source: World Values Survey dataset, Third Wave (1995-1997).

Consequently, Table 5 shows the levels of public spending and Gross National Income per head for the East Asian countries where the data is available, compared to Europe and North America. Again, there is considerable variance in public spending across East Asia. However, different levels of income, except for Singapore, which has a very low level of public spending given its economic wealth, mainly explain this variance. This suggests that if economic wealth converges, as it has done in the EU as a result of the European single market, the levels of public spending will also converge. Moreover, there is a twenty percent difference in the level of government expenditure in Ireland and France, despite similar levels of wealth. In other words, Ireland is Europe's Singapore.

Table 5. Preferences for Government Spending

| | GNI/head (ppp, 2003) | Public spending as percent of GDP (2004) |
|------------------|-------------------------|---|
| Australia | 28,290 | 45.3 |
| Japan | 28,620 | 38.1 |
| New Zealand | 21,120 | 35.3 |
| Papua New Guinea | 2,240 | 33.0 |
| South Korea | 17,930 | 28.9 |
| Malaysia | 8,940 | 24.7 |
| Indonesia | 3,210 | 23.3 |
| Singapore | 24,180 | 22.1 |
| Thailand | 7,480 | 22.0 |
| Philippines | 4,640 | 21.0 |
| France | 27,460 | 54.1 |
| Germany | 27,460 | 48.6 |
| UK | 27,650 | 43.0 |
| Ireland | 30,450 | 35.1 |
| EU15 | -- | 48.0 |
| USA | 37,500 | 35.7 |
| Canada | 29,740 | 40.1 |

Source: Eurostat (<http://epp.eurostat.ec.eu.int>); Organization for Economic Cooperation and Development (<http://www.oecd.org/statsportal>); and United Nations Committee of Experts on Public Administration (http://www.unpan.org/statistical_database-publicsector.asp).

Concerning the degree of independent judicial institutions and the rule of law, what is required is a sufficient level of institutional development and independence of courts and judges, to a level that would enable a court to apply the rights and obligations of the single market against conflicting domestic laws. For example, a court should be allowed to strike down an existing domestic law if it conflicts with a primary provision of a single market treaty or a secondary legislative instrument.

Table 6. Civil Liberties and Political Rights in 2004

| | Civil Liberties | Political Rights |
|---------------------|-----------------|------------------|
| Australia | 1 | 1 |
| New Zealand | 1 | 1 |
| Chinese Taipei | 1 | 2 |
| Japan | 2 | 1 |
| South Korea | 2 | 1 |
| China-Hong Kong SAR | 2 | 5 |
| China-Macao SAR | 2 | 5 |
| Philippines | 3 | 2 |
| Thailand | 3 | 2 |
| Papua New Guinea | 3 | 3 |
| Indonesia | 4 | 3 |
| Malaysia | 4 | 4 |
| Singapore | 4 | 5 |
| Brunei Darrusalam | 5 | 6 |
| Russia | 5 | 6 |
| Cambodia | 5 | 6 |
| Vietnam | 6 | 7 |
| China | 6 | 7 |
| Laos | 6 | 7 |
| Myanmar | 7 | 7 |

Note: Freedom House ratings are based on a checklist of 10 political rights questions and 15 civil liberties questions. The political rights questions mainly cover to what extent the system offers voters the opportunity to choose freely from among candidates and to what extent the candidates are chosen independently of the state, and the civil liberties questions cover both laws and actual practices. Raw points are awarded on each question on a scale of 0 to 4, where 0 points represents the smallest degree and 4 points the greatest degree of rights or liberties. The total points are then normalized on a 1-7 scale, where 1 represents the highest and 7 the lowest level of political rights or civil liberties.

Source: Freedom House (<http://www.freedomhouse.org/research/survey2005.htm>).

Although not a perfect proxy for independent courts, a strong indicator of this is the level of civil liberties and political freedoms. Table 6 shows the Freedom House scores in 2004 for civil liberties and political rights for all our cases, where 1 represents the highest level of rights and freedoms and 7 represents the most restricted rights and freedoms. Freedom House classifies states that score 1 or 2 as 'free' and states that score '3 or 4' as 'partly free'. By this yardstick, only Australia, New Zealand, Japan, South Korea and Chinese Taipei have the highest levels of civil liberties and political rights. Nevertheless, Hong Kong, Macao, the Philippines, Thailand, Papua New Guinea, Indonesia, Malaysia, and Singapore may have a sufficient level of civil liberties protection to enable them to adhere to the necessary legal and judicial requirements of a single market. Meanwhile, it is highly doubtful that Brunei, Russia, Cambodia, Vietnam, China, Laos, or Myanmar would be able to provide sufficient legal protection and judicial independence for a single market to be implemented in these states.

Finally, regarding the level of trade integration in East Asia, Table 7 shows the volume and share of global exports and imports in goods and services from and to East Asia as well as the share of this trade that is intra-Asia. Despite a relative decline in Japan's trade dominance in the region in the 1990s, it remains the leading exporter and importer of goods. However, Japan's dominance is being strongly challenged by China (especially if combined with Hong Kong and Macao). However, it will be some time before China overtakes Japan as the major importer of services in the region. These global trade figures also reveal that all the countries in the region are major traders, relative to the size of their GDP. For example, the value of exports from the Philippines is about the same as the value of exports from Denmark, which has almost twice the GDP of the Philippines and a much higher GDP per head. Hence, all East Asian countries have benefited from the general liberalization of global trade.

Table 7. Trade and Trade Integration

| | Goods | | | | Services | | | | Exports | | Imports | |
|----------------|-----------------|-------|-----------------|-------|-----------------|-------|-----------------|-------|-------------------|----------------------|-------------------|---------------------|
| | Exports | | Imports | | Exports | | Imports | | Goods (% Asia) | Services (% Asia) | Goods (% Asia) | Services (%Asia) |
| | Total (\$bn) | Share | Total (\$bn) | Share | Total (\$bn) | Share | Total (\$bn) | Share | | | | |
| Australia | 56.1 | 1.3 | 69.1 | 1.5 | 17.2 | 1.3 | 17.9 | 1.3 | 76.5 | 23.5 | 78.6 | 21.4 |
| China | 195.2 | 4.6 | 165.8 | 3.7 | 23.7 | 1.8 | 30.7 | 2.3 | 89.2 | 10.8 | 83.8 | 16.2 |
| Chinese Taipei | 121.6 | 2.9 | 110.7 | 2.5 | 14.5 | 1.1 | 23.5 | 1.7 | 89.3 | 10.7 | 81.8 | 18.2 |
| Hong Kong SAR | 174.4 | 4.1 | 180.7 | 4.0 | 31.4 | 2.6 | 24.5 | 1.8 | 83.4 | 16.6 | 87.9 | 12.1 |
| Indonesia | 48.7 | 1.1 | 24.0 | 0.5 | -- | -- | 11.3 | 0.8 | 91.3 | 8.7 | 72.5 | 27.5 |
| Japan | 419.4 | 9.9 | 311.3 | 6.9 | 60.3 | 4.5 | 114.2 | 8.5 | 87.0 | 13.0 | 71.1 | 28.9 |
| Malaysia | 84.5 | 2.0 | 65.0 | 1.4 | 12.0 | 0.9 | 14.3 | 1.1 | 87.5 | 12.5 | 81.1 | 18.9 |
| New Zealand | 12.5 | 0.3 | 14.3 | 0.3 | -- | -- | -- | -- | 74.8 | 25.2 | 74.3 | 25.7 |
| Philippines | 36.7 | 0.9 | 32.5 | 0.7 | 4.8 | 0.4 | 7.5 | 0.6 | 87.7 | 12.3 | 79.6 | 20.4 |
| Singapore | 114.7 | 2.7 | 111.1 | 2.5 | 23.6 | 1.7 | 18.8 | 1.4 | 83.0 | 17.0 | 84.8 | 15.2 |
| South Korea | 144.7 | 3.4 | 110.8 | 2.7 | 24.8 | 1.8 | 26.1 | 1.9 | 85.4 | 14.6 | 81.7 | 18.3 |
| Thailand | 58.4 | 1.4 | 50.3 | 1.1 | 14.1 | 1.0 | 14.0 | 1.0 | 80.0 | 20.0 | 75.6 | 24.4 |
| Vietnam | 11.5 | 0.3 | 11.6 | 0.3 | -- | -- | -- | -- | 0.3 | 11.6 | -- | -- |

Source: World Trade Organization (http://www.wto.org/english/res_e/statis_e/stats2000_e.pdf).

Which countries would benefit most from deeper regional economic integration, in terms of increased trade, is harder to assess. Table 7 also shows WTO data on the proportion of goods and services from each country that are exported and imported to the rest of what the WTO defines as the Asian region (which includes Australia and New Zealand). Hence, these figures include other Asian countries, such as India, although the overwhelming proportion of this trade is between the other potential members of an East Asian single market. Put simply, this data shows that trade integration is already very high in the region. All countries would benefit from further liberalization of trade in goods in the region. Perhaps more interesting are the figures on trade in services, which is not as

uniformly integrated and is much less integrated than the current trade in goods. This suggests that a genuine single market in services in the region would lead to a step-change in the level of trade integration in this sector. Assuming that the countries that currently have the highest proportion of service trade with the rest of the region would benefit most from a single market in services, then Thailand, Australia and New Zealand would gain the most from growth in the export of services. These three countries plus Indonesia, the Philippines and Japan would gain the most from the reduction of the cost of importing services from the rest of the region that would result from a single market.

In sum, we believe that the necessary starting conditions exist for the creation of an East Asian single market. There is some divergence in socio-economic preferences, but these differences are no greater than the variance in preferences that exist in the EU of twenty-five states. And this divergence is likely to decline as the levels of economic and political development converge in the region. Most countries in the region also have sufficiently developed civil liberties to enable them to allow for the necessary delegation of the protection of property rights and the implementation of a single market treaty and secondary legislation to independent agencies and courts. Nevertheless, several of the members of the current ASEAN do not meet this basic necessary condition, and would hence find it difficult to implement a single market program. Finally, the level of trade in goods in the region is already high and is likely to grow with further economic integration, and a single market should boost trade in services across East Asia.

2. Possible Members and Some Justifications

Given these findings, an East Asian single market is perhaps most feasible between the following thirteen 'economies': Indonesia, Malaysia, Thailand, the Philippines, and Singapore from ASEAN; Japan and South Korea from ASEAN+3; Australia, Chinese Taipei, Hong Kong, New Zealand, Papua New Guinea from APEC; and Macao. This would consequently exclude five of the existing members of ASEAN (Brunei, Cambodia, Laos, Myanmar, and Vietnam) as well as China and Russia.

These thirteen economies would have a total population of almost 640 million (about 10 percent of global population), a total GDP of almost 7 billion dollars (about 4 percent of global GDP), and would command about 30 percent of world export trade (including intra-East Asian traded but excluding intra-EU trade). In comparison, the EU of twenty-five states has a population of 450 million, a total GDP of approximately 10 billion dollars, and approximately 20 percent of global trade if one excludes intra-EU trade and 40 percent of global trade if one includes intra-EU trade.

This list of potential members of an East Asian single market is different to some current thinking. First, this proposal is not based around ASEAN. The main reason for this is the lack of a sufficient level of democratic development in many ASEAN states. For example, the tendency to authoritarianism in several ASEAN states is the main reason why this organization operates through informal procedures. But, a certain level of institutionalization, legalization, and judicial authority is essential for a single market to be credible.

A possible compromise, however, would be to allow for the inclusion of Indonesia and Malaysia, despite some concerns about the level of democratic development and stability in these two states. Another compromise would be to allow some 'variable geometry' in the design of the single market, for example by enabling the development of an ASEAN Free Trade Area to continue in parallel to the creation of an East Asian single market. This is similar to the European Economic Area, which is essentially a free trade area between the EU and Norway, Iceland and Liechtenstein. Also, as with the case in the EU, we would expect that the creation of a single market in the East Asian region which only allows states to join (or stay as members) if they have a specific level of political, democratic and judicial development would solidify political reform in Indonesia and Malaysia and encourage reform in the currently non-democratic members of ASEAN.

Second, this list does not include China, which is often included in discussions of regional integration, particularly amongst the states of Northeast Asia (e.g. Rozman 2004). Including China in an East Asian single market at its current stage of political development would severely undermine the credibility of the project. The main problem is that without sufficient independent judicial institutions, it is

very unlikely that a Chinese court would be allowed to invoke a single market law to strike down an existing Chinese law that restricts the free movement of a particular good or service. Another problem with including China is the size of China's population. China is more than six times larger than the second largest country in the region (Indonesia). As a result, it is difficult to design of system of representation in the central institutions of an East Asian single market that would allow for fair Chinese representation without also allowing China to dominate decision-making.

However, China would almost certainly oppose the creation of an East Asian single market that includes Chinese Taipei but does not include the Chinese mainland. The other states in the region would more likely to listen to China, as they all accept a 'one China' policy, and hence do not recognize Taiwan as a sovereign state. China might even demand that Chinese Taipei is excluded, although both China and Chinese Taipei are members of APEC and now the WTO.

Hence, it would be important to all countries in East Asia to find a way to incorporate China in any East Asian single market arrangement. At a bare minimum, Chinese Taipei could only be included as an 'economy' and not a state, following the legal formulation used by APEC and the WTO. A 'special relationship' could also be established with China, for example with an 'association agreement' between China and the East Asian single market organization which aims to create a free trade area with China. China could even be granted 'consultation' rights at summit meetings and in the other institutions of the organization.

Third, the inclusion of Australia, New Zealand and Papua New Guinea might seem strange to some Asian countries, particularly in Northeast Asia due to there geographical distance. Although Australia seems much closer from Southeast Asia, where Jakarta is in fact closer to Canberra than to Tokyo. One common objection to including Australia and New Zealand is that they are not really 'Asian'. This objection takes two forms: these countries do not share so-called 'Asian values', and they are not ethnically Asian. Regarding the first objection, if Asian values mean a more benign model of 'social capitalism' than the United States, then Australia and New Zealand are in fact closer to the other democracies in the region

than they are to the United States. They both have welfare states and high levels of social and environmental protection. The second objection, meanwhile, is dangerously close to racism. The European Union is already an ethnically diverse community and would become even more diverse with the inclusion of Turkey. Also, the size of the ethnically Asian population in Australia and New Zealand has grown dramatically in the past decade, and is likely to continue to grow if current immigration trends persist. As a result, ethnically Asian communities in these countries will become increasingly economically and politically powerful in the coming years. In other words, Australia and New Zealand are perhaps more 'Asian' than many people in Northeast Asia realize.

Furthermore, Australia and New Zealand have a lot to contribute to an East Asian single market. They already have experience of how to construct economic integration, in the Australia-New Zealand Closer Economic Relations (CER) trade agreement. They also have powerful independent judicial institutions and a rule of law. And, Australia was instrumental in the creation of APEC in the 1980s, and was originally in favour of restricting this organization to countries on the Western side of the Pacific, and so is likely to be in favor of the creation of a broad-based East Asian single market.

Perhaps most importantly, including Australia and New Zealand in an East Asian single market would appease likely concerns in the United States that such an organization would threaten the U.S.'s strategic interests in the region by demonstrating that the organization is a form of 'open regionalism'. Heading-off potential opposition in Washington would be important for many states in East Asia who have close economic, political and security ties to the United States. Including Australia and New Zealand would be a small price to pay if it guarantee's United States' support for an East Asian single market.

3. Institutional Design of an East Asian Single Market Organization

The lesson from the European Union is that the right economic and political conditions for the creation of single market are not sufficient by themselves. The other crucial factor is a particular institutional design. Borrowing from the

European Union set-up, the institutions of an East Asian single market organization could be designed as follows.

First, the highest authority in the single market organization could be a *Council* that brings together the heads of government (or the equivalent) from the member countries (in other words, modelled on the European Council). This organization could meet on a quarterly basis, and the 'presidency' of the organization could rotate every six months. The country holding the presidency would be responsible for setting the agenda of the meetings. The Council would be responsible for deciding on the allocation of policy competences, setting the medium- and long-term agendas, and delegating agenda-setting and enforcement to the main regulatory agency (see below). All decisions in the Council should be made by unanimously to ensure that no national interest is threatened on any key decision of the organization.

Second, the main executive body of the single market organization could be a *Commission*, modelled on the European Commission. This body would have a monopoly on the initiation of secondary legislation, and would be responsible for monitoring the enforcement of treaty commitments and secondary legislation (via 'opinions' on the position of the single market in each state and bringing cases before the court). The *Commission* would also have some direct regulatory powers (for example, in the area of competition policy). The president of the Commission could be nominated by the Council (by unanimous vote) and ratified by the Assembly (see below). The Commission could also be 'censured' by a particular majority in both the Council and the Assembly.

Third, the legislature should be bicameral and designed to balance state interests and transnational socio-economic preferences. One chamber could be a *Senate*, modelled on the EU Council of Ministers. This would bring together ministers from member countries as well as possess a permanent secretariat. The presidency of the Senate could rotate with the presidency of the Council. The Senate should reach a majority of decision by a qualified-majority (see below). The second chamber could be an *Assembly*, modelled on the European Parliament. Members of the assembly could be appointed by national parliaments, and perhaps with a rule specifying that the make-up of each national delegation in the

Assembly should be directly proportional to the make-up of a country's national parliament. This would ensure a close connection between the vote-choices of citizens in national elections and the proceedings of the Assembly, and would probably ensure that the Assembly would naturally organize along partisan rather than national lines – which is important for allowing the Assembly to articulate transnational interests and preferences as a balance against the articulation of national preferences in the Senate. The Assembly should decide by a simple majority.

Finally, there should be a judicial body, such as a *Court* or *Disputes Panel*, modelled on the European Court of Justice. There should be one judge per member country and the members should be appointed by the national governments. The Court should hear cases brought to it by any of the other institutions of the organization as well as cases referred to it by national courts. National courts, meanwhile, should be responsible for directly applying the provisions of the single market treaty and the secondary instruments as part of the corpus of domestic law in each country. National courts and the single market Court should have the power to impose fines on any member country that fails to abide by the rules.

Table 8 shows a possible structure of representation in a Commission, Senate and Assembly for the thirteen economies we have identified. The weighting of votes in each of the institutions should be designed to balance 'one-state-one-vote' and population size. For example, each member could have one seat in the Commission as well as one seat in the Council. The weighting of votes in the Senate and Assembly, meanwhile, could be decided by Penrose's 'square-root law' – which states that the most equitable trade-off between the rights of states and the rights of individual citizens is to design a system of representation based on the square-root of a country's population divided by some number (Penrose 1946; Felsenthal and Machover 2001). The higher the divisor the closer the system of representation is to one-state-one-vote, and the lower the divisor the closer the system of representation is to population size. In the example in Table 8, the number of votes in the Senate is determined by dividing the square-root of population by 1400 and the number of seats in the Assembly is determined by

dividing the square-root of population by 400. (In the current European Union of 25 states, representation in the EU Council is approximately based on the square-root of population divided by 2200, and the number of seats each member state has in the European Parliament is approximately based on the square-root of population divided by 400).

Table 8. Possible Representation in the Institutions of an East Asian Single Market

| | Population (mil. 2005) | Square-root of population divided by 1400 | Square-root of population divided by 400 | Commissioners | Votes in Senate (under QMV) | Seats in Assembly |
|---------------------|---------------------------|--|---|---------------|--------------------------------------|----------------------|
| Indonesia | 222.8 | 10.7 | 37.3 | 1 | 10 | 37 |
| Japan | 128.1 | 8.1 | 28.3 | 1 | 8 | 28 |
| Philippines | 83.1 | 6.5 | 22.8 | 1 | 6 | 23 |
| Thailand | 64.2 | 5.7 | 20.0 | 1 | 6 | 20 |
| South Korea | 47.8 | 4.9 | 17.3 | 1 | 5 | 17 |
| Malaysia | 25.3 | 3.6 | 12.6 | 1 | 4 | 13 |
| Chinese Taipei | 22.8 | 3.4 | 11.9 | 1 | 3 | 12 |
| Australia | 20.2 | 3.2 | 11.2 | 1 | 3 | 11 |
| Hong Kong SAR | 7.0 | 1.9 | 6.6 | 1 | 2 | 7 |
| Papua New Guinea | 5.9 | 1.7 | 6.1 | 1 | 2 | 6 |
| Singapore | 4.3 | 1.5 | 5.2 | 1 | 2 | 5 |
| New Zealand | 4.0 | 1.4 | 5.0 | 1 | 2 | 5 |
| Macao SAR | 0.5 | 0.5 | 1.8 | 1 | 1 | 2 |

Note: A Qualified-Majority in the Senate = 37 votes out of 54 (approximately 69 percent).

As regards to the appropriate ‘threshold’ for passing legislation in the Senate, the threshold needs to be set at a level that would prevent a coalition of big states dictating to the small states while also preventing any one state from blocking the will of a large majority. For example, with 54 votes in the Senate the threshold could be set at 37 (which is approximately 69 percent of the votes), which would mean that 17 votes would constitute a ‘blocking minority’. This would mean that a blocking-minority could be composed of a coalition between Indonesia and Japan or by an alliance between Indonesia and two other states from the Philippines, Thailand, South Korea and Malaysia.

Table 9 sets out a possible design of representation in a single market organization that would include China. The aim, here, is to illustrate that it is not impossible to design a structure that would allow for the inclusion of China, despite its size. However, this would only work if there were some deviation from the square-root rule where China is concerned – for example, by giving China only two more votes than Indonesia in the Senate and only five more seats than Indonesia in the Assembly. Also, the decision-making threshold would need to be set at a level that would prevent China from blocking a decision of all the other members – for example, with the allocation of voting weights in Table 9, the threshold could be set at 28 votes out of 47 (which is approximately 60 percent of total votes).

Table 9. A Possible Design that Includes China

| | Population (mil. 2005) | Square-root of population divided by 2000 | Square-root of population divided by 800 | Commissioners | Votes in Senate (under QMV) | Seats in Assembly |
|-------------|---------------------------|--|---|---------------|--------------------------------------|----------------------|
| China | 1,315.8 | 18.1 | 45.3 | 1 | 10 | 24 |
| Indonesia | 222.8 | 7.5 | 18.7 | 1 | 8 | 19 |
| Japan | 128.1 | 5.7 | 14.1 | 1 | 6 | 14 |
| Philippines | 83.1 | 4.6 | 11.4 | 1 | 5 | 11 |

Table 9. Continued

| | | | | | | |
|------------------|------|-----|------|---|---|----|
| Thailand | 64.2 | 4.0 | 10.0 | 1 | 4 | 10 |
| South Korea | 47.8 | 3.5 | 8.6 | 1 | 4 | 9 |
| Malaysia | 25.3 | 2.5 | 6.3 | 1 | 3 | 6 |
| Chinese Taipei | 22.8 | 2.4 | 6.0 | 1 | 2 | 6 |
| Australia | 20.2 | 2.2 | 5.6 | 1 | 2 | 6 |
| Papua New Guinea | 5.9 | 1.2 | 3.0 | 1 | 1 | 3 |
| Singapore | 4.3 | 1.0 | 2.6 | 1 | 1 | 3 |
| New Zealand | 4.0 | 1.0 | 2.5 | 1 | 1 | 3 |

Note: A Qualified-Majority in the Senate = 28 votes out of 47 (approximately 60 percent).

4. Against 'ASEAN Principles'?

Finally, one potential criticism is that this proposed institutional design for an East Asian single market organization is against the so-called 'ASEAN principles', of consensus (unanimity), national sovereignty, and informality. Although there would need to be some compromise on each of these principles for a formal single market organization to be successful, if designed carefully each of these principals could play a central role in the operation of the organization.

Consensus could remain the basic principle of the organization, just as it remains the basic principle of the European Union. This could be operationalized in two ways. First, no decision could be made in the Council (the summit meetings) without unanimous approval of all the participants. This way, no initial delegation to the executive, legislative and judicial agents could be made without the prior approval of all members of the organization. Second, the legislative procedure could be designed so that it is very unlikely that anything would pass without overwhelming support, as we have suggested.

National sovereignty, meanwhile, could be preserved in those areas that are highly politically sensitive or threaten particular powerful domestic constituencies. For example, particular economic sectors, such as agriculture, could be excluded from the initial set-up. Similarly, the free movement of persons could be excluded altogether, or introduced in several phases with careful checks along the way. Unanimous voting in the legislative process could also be kept in some sensitive policy areas, as has been the case in the EU. Also following the EU model, some form of 'variable geometry' could be allowed, whereby sub-groups of countries integrate further in some areas, for example in the creation of a common currency or the removal of barriers to the free movement of persons (as is already the case between Australia and New Zealand). And, 'side payments' could be used to appease specific states, such as budgetary transfers to states that are reluctant to participate in a particular policy area, as was the case in the EU with the increase in regional aid to Italy, Spain, Portugal, Greece and Ireland as part of the package deal that allowed for the single market program to go ahead.

Informality, on the other hand, may be more difficult to maintain, as the creation of a single market requires a certain degree of formal institutionalization and legalization. One of the reasons why informality has remained a central principal in the working of ASEAN is that this principle is necessary for non-democratic states to participate in such an international organization. Hence, if non-democratic states were excluded from a single market organization, there would be less need to maintain a norm of informality.

V. Conclusion

The creation of a supranational single market is predominantly an exercise in market deregulation and regulation. Such policies should create a level playing field for economic competition and aim to correct potential market failures. These goals are best secured through the delegation of significant agenda-setting and enforcement powers to independent agents, and a set of procedures that limit the discretion of these agents. Such a design would create a 'credible commitment' to the project and enable regulators, courts, and private citizens to get on with the business of integrating the market.

This is exactly what happened in the European Union. The necessary political commitment to create a single market—in terms of the convergence of socio-economic preferences—did not exist in Europe until the mid 1980s. However, Europe's leaders were fortunate enough to have inherited an ideal set of institutions for creating a single market from the Treaty of Rome. The Treaty of Rome had established a powerful independent executive (the Commission) and a set of judicial institutions that enabled private citizens to invoke European-level rights and obligations in national courts. All that was then required in the Single European Act was to invite the Commission to initiate the necessary legislation and to reform the legislative procedures to ensure that this legislation could be passed and would be accepted by Europe's citizens. Hence, unanimity voting in the EU Council was replaced by a combination of a qualified-majority in the EU Council and a simple majority in the European Parliament.

Learning from the European experience, an East Asian single market is also feasible if the necessary starting conditions exist and if the institutions are designed appropriately. The key starting conditions are the convergence of basic socio-economic preferences, a high existing level of trade integration, and sufficiently independent courts and the rule of law. The first two conditions exist in almost all states in the region. However, the last condition only exists for some. We consequently propose that an East Asian single market is most feasible, at least

initially, between a subset of the ASEAN states, plus Japan, Korea and the other democratic states in APEC. We also discussed a possible institution design, to illustrate how delegation and decision-making could work in such an organization.

The likely economic benefits of an East Asian single market are hard to assess. The current status quo is not so terrible for most countries in the region. As a result of the gradual liberalization of world trade, the level of trade integration in East Asia is already high. Also, with the rapid opening and expansion of the Chinese market and the development of bilateral free trade agreements across the region, it is not obvious that a single market would add much. This is in marked contrast to the situation in Western Europe in the mid 1980s, when Europe had not yet recovered from the recessions of the 1970s, a global trade organization had not yet been established and world trade remained highly regulated, and it was the height of Cold War tensions between Washington and Moscow. Put simply, the economic costs of not having a single market are almost certainly not as large for East Asia now as they were for Europe in the 1980s.

Nevertheless, a single market in East Asia would lead to even greater trade integration between the members, particularly in the service sector. A single market would also promote economies of scale, facilitate industrial rationalization and consolidation in certain sectors, and ultimately lead to higher growth rates and more jobs, as it has done in Europe.

Also, the potential political benefits of a single market in East Asia may be less tangible than the economic benefits, but may in fact be more significant. Once a single market is created, there will be pressure for further economic and political integration as states are forced to coordinate their responses to the policy externalities of a supranational single market. For example, some form of monetary policy coordination would almost certainly follow the creation of a single market. Also, an East Asian single market would significantly strengthen the influence of the region in the global political economy, for example by providing the region with a powerful tool for the exercise of 'soft power', by threatening to refuse a state access to the single market. Furthermore, a single market organization, with regular summits of all the key actors in the region, would be a vehicle for promoting growing political integration and for resolving long-standing

political differences. Finally, a single market in East Asia would be a 'magnet' of political and economic stability, which would solidify democratic government and free markets in the members of the organization as well as spread democracy and the market economy to other states in the region – just as the EU has done in Southern and Eastern Europe and is now doing in the Eastern Mediterranean.

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An East Asian Single Market? Lessons from the European Union

Simon HIX · Hae-Won JUN

This paper considers the possibility of economic integration in East Asia from the perspective of the single market in Europe. A single market in East Asia would lead to further trade integration between the members, industrial consolidation in certain sectors, and higher growth rates and more jobs. An East Asian single market organization might also produce significant political benefits, such as an arena for promoting political integration and resolving disputes, and the spread of democratic government and free markets in the region.



Korea Institute for International
Economic Policy

300-4 Yomgok-dong, Seocho-gu, Seoul 137-747, Korea
P.O.Box 235, Seocho, Seoul 137-602, Korea
Tel 02-3460-1001, 1114 / Fax 02-3460-1122, 1199
[Http://www.kiep.go.kr](http://www.kiep.go.kr)



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