

Hamanaka, Shintaro

Working Paper

Regionalism Cycle in Asia (-Pacific): A Game Theory Approach to the Rise and Fall of Asian Regional Institutions

ADB Working Paper Series on Regional Economic Integration, No. 42

Provided in Cooperation with:

Asian Development Bank (ADB), Manila

Suggested Citation: Hamanaka, Shintaro (2010) : Regionalism Cycle in Asia (-Pacific): A Game Theory Approach to the Rise and Fall of Asian Regional Institutions, ADB Working Paper Series on Regional Economic Integration, No. 42, Asian Development Bank (ADB), Manila, <https://hdl.handle.net/11540/1962>

This Version is available at:

<https://hdl.handle.net/10419/109558>

Standard-Nutzungsbedingungen:

Die Dokumente auf EconStor dürfen zu eigenen wissenschaftlichen Zwecken und zum Privatgebrauch gespeichert und kopiert werden.

Sie dürfen die Dokumente nicht für öffentliche oder kommerzielle Zwecke vervielfältigen, öffentlich ausstellen, öffentlich zugänglich machen, vertreiben oder anderweitig nutzen.

Sofern die Verfasser die Dokumente unter Open-Content-Lizenzen (insbesondere CC-Lizenzen) zur Verfügung gestellt haben sollten, gelten abweichend von diesen Nutzungsbedingungen die in der dort genannten Lizenz gewährten Nutzungsrechte.

Terms of use:

Documents in EconStor may be saved and copied for your personal and scholarly purposes.

You are not to copy documents for public or commercial purposes, to exhibit the documents publicly, to make them publicly available on the internet, or to distribute or otherwise use the documents in public.

If the documents have been made available under an Open Content Licence (especially Creative Commons Licences), you may exercise further usage rights as specified in the indicated licence.



<http://creativecommons.org/licenses/by/3.0/igo>

ADB Working Paper Series on Regional Economic Integration



Regionalism Cycle in Asia (-Pacific): A Game Theory Approach to the Rise and Fall of Asian Regional Institutions

Shintaro Hamanaka

No. 42 | February 2010



ADB Working Paper Series on Regional Economic Integration

Regionalism Cycle in Asia (-Pacific): A Game Theory Approach to the Rise and Fall of Asian Regional Institutions

Shintaro Hamanaka*

No. 42 | February 2010

*Shintaro Hamanaka is an Economist in the Office of Regional Economic Integration, Asian Development Bank, 6 ADB Avenue, Mandaluyong City, 1550 Metro Manila, Philippines. Tel +63 2 632 5844, Fax +63 2 636 2342, shamanaka@adb.org

Asian Development Bank

The ADB Working Paper Series on Regional Economic Integration focuses on topics relating to regional cooperation and integration in the areas of infrastructure and software, trade and investment, money and finance, and regional public goods. The Series is a quick-disseminating, informal publication that seeks to provide information, generate discussion, and elicit comments. Working papers published under this Series may subsequently be published elsewhere.

Disclaimer:

The views expressed in this paper are those of the author(s) and do not necessarily reflect the views and policies of the Asian Development Bank or its Board of Governors or the governments they represent.

The Asian Development Bank does not guarantee the accuracy of the data included in this publication and accepts no responsibility for any consequence of their use.

By making any designation of or reference to a particular territory or geographic area, or by using the term "country" in this document, the Asian Development Bank does not intend to make any judgments as to the legal or other status of any territory or area.

Contents

Abstract	iv
1. Introduction	1
2. Hypothesis: Regionalism Cycle	1
2.1 Cost and Benefit of Various Regional Frameworks	1
2.2 Game Pay-off Matrix	4
2.3 Regionalism Cycle	5
3. Examination of the Regionalism Cycle	7
3.1 The Cycle of Regional Financial Cooperation Meetings	8
3.2 The Cycle of Regional Summit Meetings	12
4. Conclusion	15
References	16
ADB Working Paper Series on Regional Economic Integration	18
Tables	
1. Leader's Cost and Benefit	2
2. Cost–Benefit Structure	3
3. Pay-Off Matrix	5
Figures	
1. Change in Choices	5
2. Model Cycle of Asian Regionalism	7
3. Regionalism Cycle of Financial Cooperation	9
4. Regionalism Cycle of Regional Summit	13

Abstract

Despite a commonplace view that Asian regionalism lacks institutions, Asia, in fact, is full of regional institutions and frameworks in various forms. The rise and fall of regional institutions in Asia is an extremely dynamic process. Using a game theory approach, this paper hypothesizes that the dynamic nature of Asian regionalism can be explained by a "regionalism cycle." The institutional outcome of regionalism in Asia has been cyclical because the game played by Japan and the United States does not have a stable equilibrium. This paper tests the hypothesized regionalism cycle using actual cases of regional institutions in the field of financial cooperation and regional summit meetings.

Keywords: regionalism, Regionalism cycle, Asian Monetary Fund (AMF), East Asia Summit (EAS), Game Theory

JEL Classification: F15, F36

1. Introduction

Despite the commonplace view that Asian regionalism lacks institutions¹, Asia, in fact, is full of regional institutions and frameworks in various forms. There are a considerable number of regional frameworks with different sets of membership that cover different issue areas. The rise and fall of various institutions in Asia is an extremely dynamic process. In addition to a number of existing institutions and those that no longer exist, there have also been many proposed institutions in Asia that were once considered but never established. Therefore, the most pertinent questions regarding institutions of Asian regionalism are: Why is the rise and fall of regional frameworks remarkable? Why have there been so many frameworks? And finally, why do the activities of a certain regional framework become insignificant after a certain period?

This paper argues that there is a "regionalism cycle" in Asia. The cycle exists in terms of the membership of institutions, which is one of the most critical aspects of institutions (Koremenos et al., 2001). Various countries' reactions to a number of regionalist projects have clear patterns, with the critical determining factor being the membership of each regional framework. As a result of such patterns, the institutional evolution of Asian regionalism has become cyclical with respect to institutional development and the eventual waning and/or abolishment of such institutions since changes in membership lead to changes in the effectiveness of institutions.

The structure of this paper is two-fold. First, it presents a hypothesis on regionalism cycle using game theory. The rise and fall of various regional institutions is the result of states' rational choices in terms of their membership preferences. Since the pay-off matrix among concerned parties (especially Japan and the United States [US]) in this game does not have a stable equilibrium, there is no stable institutional equilibrium. Hence, the institutional outcome is cyclical. The second half of the paper analyzes the actual development of Asian regionalist projects in light of the proposed regionalism cycle. The rise and fall of various regional financial cooperation meetings and regional summits are examined. In particular, sequences of various regionalist projects proposed by a number of countries are closely analyzed. Only when various projects are analyzed together can we find that Asian regional cooperation has a cyclical feature.

2. Hypothesis: Regionalism Cycle

2.1 Cost and Benefit of Various Regional Frameworks

Sponsoring a regional framework entails both costs and benefits. The cost-benefit structure of sponsoring a regional framework varies depending on issue areas covered by an institution. While a regional framework covering a particular issue brings a specific cost-benefit structure to each member, generalization is possible to a certain degree. In such instances, sponsoring international frameworks or institutions is considered to be supplying an international public good (Kindleberger, 1973). Sponsoring a (regional) framework or institution for cooperation among states entails coordination costs (e.g., monitoring, enforcement, policy coordination, and

¹ ADB (2008) and Hu (2009).

side-payment) (Mattli, 1999) and various economic costs (e.g., providing finance and opening domestic markets).² It also entails benefits such as a gain in prestige and the diffusion of favorable rules, as well as an increase in influence and the imposition of taxes on other members (Kindleberger, 1973).

The costs and benefits that member countries incur and enjoy in sponsoring a regional framework depend on their relative position in the group (Table 1). It may be safe to consider that the lead state (number 1 state) gains relatively large benefits, while at the same time incurring relatively large costs as well. The long-lasting question on whether sponsoring a framework or institution is beneficial or costly to the leader, which is known as the benevolent versus predatory hegemon debate (Kindleberger, 1973; Snidal, 1985; Conybeare, 1987), rests on which side is emphasized. As has been argued by Lake (1993) and Russett (1985), we should recognize that the leading position entails the both, rather than developing a decisive argument. The role of the number 2 state in a regional framework has a critical impact on the lead state's costs and benefits. The leader may expect the number 2 state to behave as its junior partner by sharing the burden of sponsoring the framework, but without giving comparable benefit to the number 2 state. The rational choice of the leader is to request only the number 2 state to share the burden with it rather than requesting all participating members to equally shoulder the burden, which could increase the unpopularity of the leader among other members.

Table 1: Leader's Cost and Benefit

	Number 1 state (Leader)	Number 2 state
Benefit	Large (this becomes larger when the number 1 state considers prestige to be critical)	Small
Cost	Large (this can be reduced by requesting the number 2 state to share the burden)	Small (this can be increased if the number 2 state is required to share the burden)

Source: Author's original.

Based on the analysis above, we can then consider the cost and benefit of sponsoring regional frameworks with various combinations of membership from the Japanese and US perspective (Table 2). Basically, the cost–benefit structure of Japan and the US follows Table 1, but a minor modification is necessary to reflect their actual capacities and preferences. When there is no framework, there are no associated costs and benefits that Japan or the US incur or enjoy. Therefore, the net benefit of having no institution is zero for both Japan and the US since both the cost and benefit are zero. Other than this scenario (no framework), the magnitude of the costs and benefits that Japan and the US incur or enjoy are different. Moreover, these costs and benefits for Japan and the US are often contrasting as is explained below. The base line for the cost–benefit analysis of other scenarios is the “no framework” scenario.

² Providing long-term finance for investment and short-term liquidity in the case of financial crisis is the important role of the hegemon (Kindleberger, 1973). In addition, providing official development assistance (ODA) is another important responsibility of the hegemon.

Table 2: Cost–Benefit Structure³

Japan

	No Framework	Asia-Only Framework	Asia–Pacific Framework	
			Japan's Active Participation	Japan's Inactive Participation
Benefit	None	Extremely Large	Small	Small
Cost	None	Large	Large	Medium
Net Benefit	None (0)	Positive (2)	Negative (–2)	Slightly Negative (–1)

Source: Author's original.

United States

	No Framework	Asia-Only Framework	Asia–Pacific Framework	
			Japan's Active Participation	Japan's Inactive Participation
Benefit	None	Negative	Medium	Medium
Cost	None	None	Very small	Large
Net Benefit	None (0)	Negative (–2)	Positive (2)	Slightly Negative (–1)

Source: Author's original.

Sponsoring an Asia-only framework in which Japan is able to hold the leading position brings an extremely large benefit to Japan. The benefit of being the leader in a regional institution is especially large for Japan partly because the country considers prestige as critically important (Yasutomo, 1983). In contrast, the benefit of having membership in an Asia–Pacific framework where the US holds the leading position is small to Japan. Being a leader in an Asia-only framework certainly comes with large costs for Japan, but these can be offset by extremely large benefits. The cost that Japan incurs in the US-sponsored Asia–Pacific framework depends on how actively it participates in such a framework. If Japan is obliged to participate actively and contribute financially to the framework's projects as a junior partner of the US, then the cost becomes relatively large. However, the cost becomes smaller if inactive participation (virtual non-participation) is possible.

From the US perspective, the establishment of an Asia-only regional framework from which it is excluded would be a negative as US influence on Asian countries would be diminished by the establishment of such a framework. Compared with this scenario, participating in a regional framework such as an Asia–Pacific framework is a better

³ Actual figures in the net-benefit column are very rough estimates based on a qualitative analysis. Qualitative assessment of benefit and cost are categorized into the following: "very small" as 1, "small" as 2, "medium" as 3, "large" as 4, "very large" as 5 and "extremely large as 6". The net benefit is the difference between benefit and cost. For example, Japan gains an extremely large benefit (6) while it incurs a large cost (4) in an Asia-only framework; therefore Japan's net benefit becomes 2.

option for the US in terms of benefits, which would be medium-sized.⁴ The establishment of an Asia-only framework does not require any specific cost to the US just because it is not a member, while the net cost–benefit of this scenario is negative. Meanwhile, the cost that the US incurs in an Asia–Pacific framework is small when Japan resigns itself to play the role of junior partner to the US, while the cost becomes larger if Japan refuses to do so.

2.2 Game Pay-off Matrix

A game pay-off matrix for Japan and the US can be deduced based on the cost–benefit structure for each of the two countries explained above. The choice for Japan and the US is whether to participate or not in a regional framework. Non-participation would result in either non-member status or virtual non-participation (inactive participation) in which no substantial contribution to the framework is made by the member (e.g., attendance at meetings only).

The four combinations of choices available to Japan and the US in the matrix are equivalent to the four types of regional frameworks explained in the previous section. First, when neither Japan nor the US participates in a regional framework, such a situation is equivalent to there being no framework. This includes both the actual and virtual nonexistence of a regional framework—also known as a dysfunctional regional framework—or a situation where both Japan and the US do not seriously engage in the framework. Second, when only Japan participates but the US does not participate in a regional framework, such a regional framework is considered an Asia-only framework. Third, when both Japan and the US participate substantially, such a situation is equivalent to an Asia–Pacific framework that includes active Japanese participation. Finally, when the US participates and Japan does not actively participate, such a situation can be described as an Asia–Pacific framework with inactive Japanese participation. As will be explained later in more detail, this situation usually happens after the establishment of an Asia–Pacific framework in which the form of Japanese non-participation is basically inactive participation (virtual non-participation), rather than non-membership status since withdrawing from a framework is difficult in practice.

At this stage, we can produce a pay-off matrix following the cost–benefit structure of Japan and the US as explained above (Table 3). When neither Japan nor the US participates (no framework), both Japan and the US gain zero (0). When Japan participates and the US does not participate in a regional framework (Asia-only framework), Japan gains two (2) and the US loses two (–2). If both Japan and the US participate in a regional framework (Asia–Pacific framework), Japan loses two (–2) and the US gains two (2). However, in a situation where Japan decides not to actively participate in an Asia–Pacific framework, both Japan and the US lose one (–1).

⁴ The benefit that the US gains by holding the leading position in a regional framework is small when compared with Japan in a similar leading role. This is because the US is a hegemon that is able to pursue its agenda through global institutions. Therefore, there is no need for the US to be a leader in a regional framework. In contrast, Japan is keen to be a leader in a regional institution to pursue its agenda.

Table 3: Pay-Off Matrix

Japan \ US	Participation	Non-Participation
Participation	(-2,2)	(2,-2)
Non-participation	(-1,-1)	(0,0)

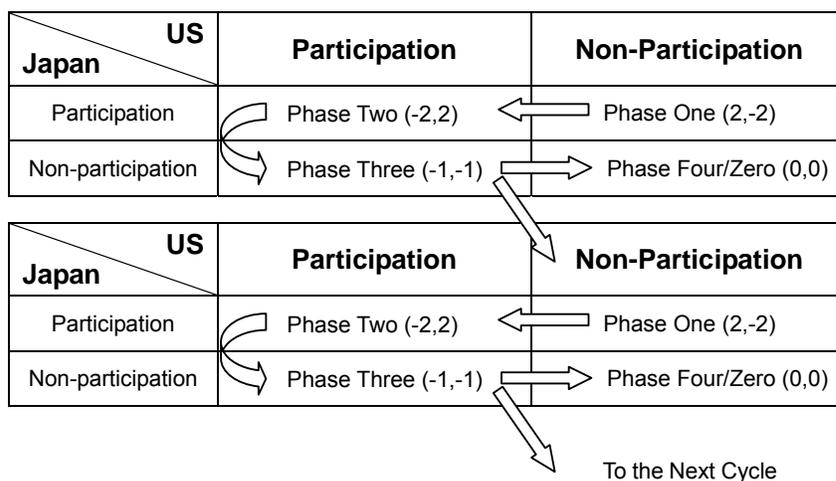
Note: (X, Y), X: Japan's pay-off; Y: US' pay-off.
 Source: Author's original.

What is noteworthy about the pay-off matrix is that this game does not have a stable equilibrium. There is no dominant strategy for both Japan and the US. Either country can increase its gain by changing its choice to maximize its interest once the other country has made a choice. For example, if Japan attempts to establish an Asia-only regional framework that the US was either unaware of or unable to participate in, this combination of Japanese participation and US non-participation would provide Japan with the highest pay-off (2). However, under this situation, the US could potentially increase its pay-off from -2 to 2 by moving from non-participation to participation. This change in US behavior would, in effect, reduce Japan's pay-off from 2 to -2. Then, Japan could decide to reduce its involvement in the transformed Asia-Pacific framework because inactive participation would be less costly (-1) than sharing the costs of maintaining the US-sponsored framework (-2). Since it is costly for the US to support a framework without Japanese participation (-1), the US might disengage from activities under the transformed framework. Since there is no stable equilibrium situation in this game matrix, the institutional outcome becomes cyclical.

2.3 Regionalism Cycle

Based on the game pay-off matrix explained above, the cycle of regionalism, which focuses on membership development, can be deduced (Figure 1). The cycle has four phases.

Figure 1: Change in Choices



Source: Author's original

Phase One: Japan proposes and attempts to establish a regional framework that includes Asian countries only. The exclusion of the US is successful when the framework is established as the US is unaware of it.

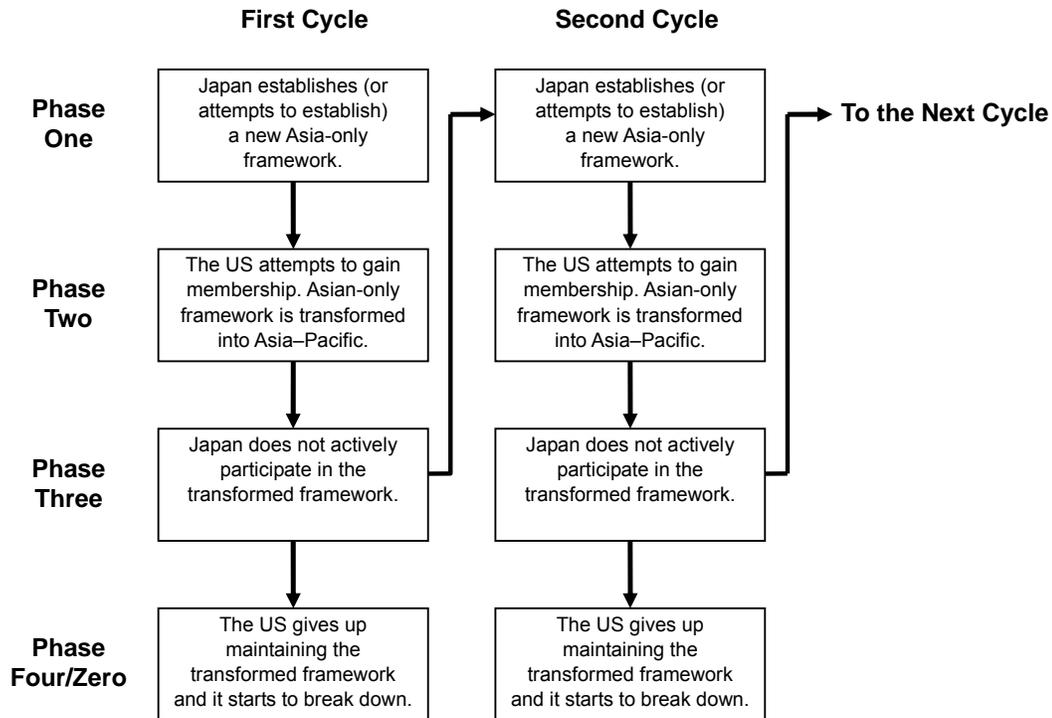
Phase Two: When the US becomes aware of the existence of a new regional framework that it is not a member of, the US attempts to gain membership. If the US successfully obtains membership, the framework becomes an Asia–Pacific framework, and is no longer an Asia-only framework. The alternative scenario of Phase Two is that if the US were to have difficulty gaining membership to the Asia-only framework, a new Asia–Pacific framework would be sponsored by the US to compete with the existing Japan-sponsored Asia-only framework.

Phase Three: As a result of the extension of membership to the US, Japan loses an interest in the transformed regional framework in which the US now plays a dominant role. Or if a new US-sponsored Asia–Pacific framework were created to compete with the Japanese-sponsored Asia-only framework, Japan would not actively participate in the new framework.

Phase Four/Zero: Since it is costly for the US to support the transformed framework, which would now be an Asia–Pacific framework, by itself, the US also begins to disengage from the transformed framework's activities, which results in the breakdown of the framework. Alternatively, both a Japan-sponsored Asia-only framework and the US-sponsored Asia–Pacific framework would become dysfunctional due to competition and duplication between the two.

An important point of this cyclical process is that eventually Japan will explore the establishment of a new Asia-only framework if (i) the previous framework is transformed into an Asia–Pacific framework through US participation or (ii) the old Asia-only framework declines in the face of competition from a new Asia–Pacific framework. Therefore, after the cycle reaches Phase Three and before reaching Phase Four/Zero, Phase One of a subsequent cycle begins anew. An illustration of the cyclical regionalism model is present in Figure 2 below.

Figure 2: Model Cycle of Asian Regionalism



Source: Author's original.

There is one caveat with this analysis of the regionalism cycle, namely, the limits placed on the predictive power of the model by major powers' membership preferences. The major powers' incentives to establish a new regional group and/or abolish an old group are a central question of research. The focus of this paper is the major powers' desire to supply a favorable institution with a preferred membership. In addition to the supply side, the demand side, which is determined by whether or not minor powers support the proposed institutions, is also critical to understanding the final institutional equilibrium (Snidal, 1994). This paper emphasizes the supply side of regional frameworks in order to clarify that the struggle for leadership, not the absence of leadership, has been the fundamental reason why the rise and fall of regional institutions and frameworks is significant in Asia. The proliferation of regional frameworks can best be explained by the over-supply of institutions.

3. Examination of the Regionalism Cycle

This section examines the actual development of regionalism in light of the regionalism cycle detailed in the previous section. Regional frameworks in the field of finance and through summity are analyzed in turn. Trade regionalism is not covered in this paper because most trade regionalism, such as free trade arrangements/areas

(FTAs), are basically perpetual in nature.⁵ Since the wane and/or fall of FTAs is a rare occurrence, FTAs seldom follow a cyclical process. Since the rise and fall of regional institutions became significant in Asia only after the end of the Cold War, the main analysis focuses on institutions in the 1990s.

3.1 The Cycle of Regional Financial Cooperation Meetings

First cycle. The first attempt at creating a regional meeting among financial officials was made by the Japanese Ministry of Finance (MOF) soon after the end of the Cold War.⁶ Then Vice Finance Minister, Tadao Chino, considered the establishment of a regional meeting on financial matters as being critical for Asian countries to have their own voice in setting the financial and economic agenda at global-level meetings rather than simply following the lead of the US and Europe.⁷ He proposed to establish the Four Markets Group comprising countries that have major financial markets in the region. The first Four Markets Group meeting took place in Hong Kong, China in May 1992 with the participation of Japan; Australia; Singapore; and Hong Kong, China. At meetings held twice a year, the Four Markets Group aimed to strengthen the relationship among regional financial authorities and exchange market information, particularly on foreign exchange markets. The participants in these meetings were at the level of director general within their respective institutions (i.e., the third-ranking ranking official).

In March 1997, the Four Markets Group expanded to become the Six Markets Group with the inclusion of the People's Republic of China (PRC) and the US. At the same time, the US pushed for the level of the participants from each financial institution to be raised from director general to vice minister (i.e., the second ranking official) (Ostry, 1997). Then Japanese Vice Finance Minister for International Finance, Katō Toshihiko, who chaired the first Six Markets Group meeting, once recalled how the US sought to join the Four Markets Group only after first learning of its existence (Katō et al., 2002). At the time, the US did not consider the group to be particularly useful, given the existence of multilateral fora such as the World Trade Organization (WTO) and the Asia–Pacific Economic Cooperation (APEC), both of which it considered to be more important. However, the US decided to join the new group for the simple reason that it was determined not to be excluded from a regional financial cooperation forum.⁸ Because the Four Markets Group did not use a geographic label, the inclusion of the US did not lead existing members to question whether the US was considered to be a part of the region or not. In the end, the US (and the PRC) joined the group, which subsequently changed its name to the Six Markets Group.

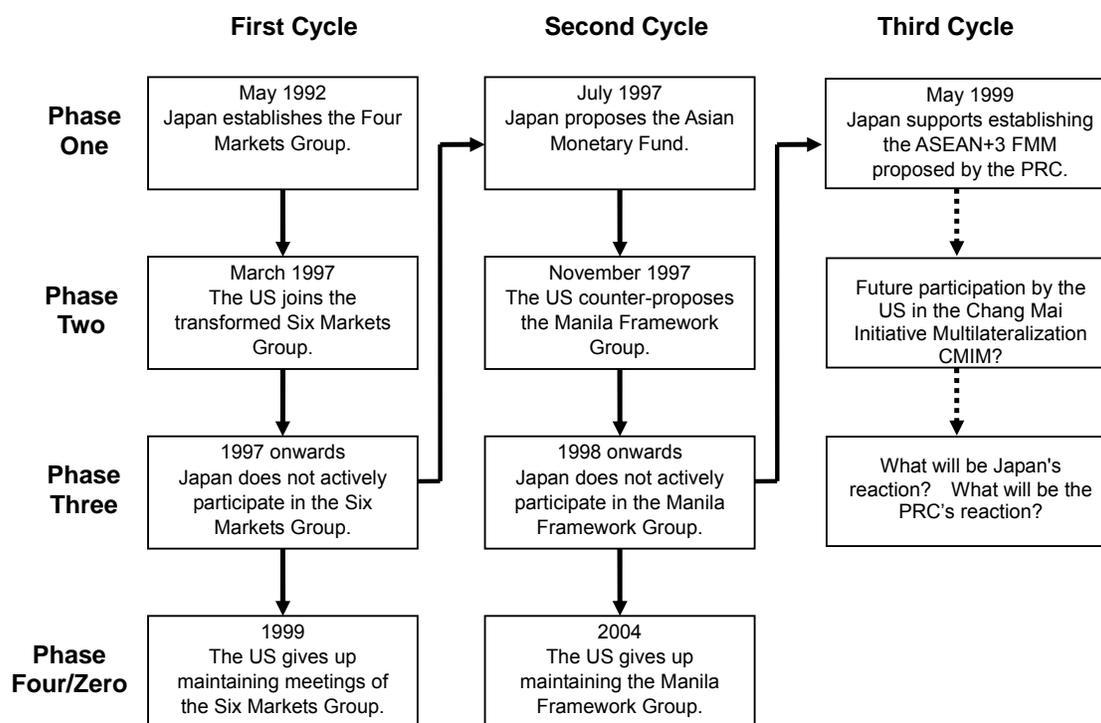
⁵ Trade forums such as Asia–Pacific Economic Cooperation (APEC) can decline. Therefore, theoretically speaking, there is also a possibility that trade forums form a cyclical process. However, trade forums are not included in the analysis because the number of cases is too low.

⁶ Before the Four Markets Meeting, a central bank forum called the Executives' Meeting of East Asia and Pacific Central Banks (EMEAP) was established in 1991 under the initiative of the Bank of Japan. But central bank forums such as EMEAP is not included in the analysis of this paper. For central bank forums, see Hamanaka (2009) and Haas (1989).

⁷ *Australian Financial Review* (February 1997).

⁸ As reported in *Korean Economic Review* (13 March 1997).

Figure 3: Regionalism Cycle of Financial Cooperation



Source: Author's original.

This regional financial meeting among six key Asia–Pacific economies attracted considerable attention. While APEC had expanded its membership significantly by 1997 and grown somewhat dysfunctional in the process, the smaller Six Markets Group, which included three major countries(the PRC, Japan, and the US), was viewed as an optimal forum for substantial discussion. Many observers were expecting it to upgrade to a minister-level gathering and possibly evolve into an Asian version of the G6 or G7.⁹

However, the group lost centripetal force soon after the upgrade. It was decided at the first meeting in Tokyo that the expanded Six Markets Group would hold meetings only on an annual basis, unlike its predecessor, the Four Markets Group, which had met twice a year.¹⁰ It soon became apparent that an annual event was ineffective for economic surveillance purposes. As a consequence of this, no meetings have been held since February 1999 under the framework of the Six Markets Group. Moreover, Japan's MOF expressed interest in reviving the Four Markets Group, rather than utilizing the Six Markets Group, to promote regional financial cooperation.¹¹ In fact, in

⁹ As reported in *New Strait Times* (4 March 1997) and *Yomiuri Shimbun* (6 March 1997).

¹⁰ In the first meeting organized by MOF in March 1997, it agreed to organize the second meeting of the group in the *second half* of 1998.

¹¹ *Nikkei Shimbun* (22 August 1999).

September 1999, the Four Markets Group meeting was re-organized in Tokyo without the participation of the PRC and US. The Four Markets Group has since held meetings twice a year, while the Six Markets Group has stopped holding meetings.¹²

Second cycle. Immediately after the Four Markets Group was transformed into the Six Markets Group in March 1997, Japan's MOF launched an initiative known as the Asian Monetary Fund (AMF). One should note that this is before the onset of the 1997/98 Asian financial crisis. After an internal study jointly conducted with the Institute for International Monetary Affairs (IIMA), MOF planned to propose the AMF during an Asian Development Bank (ADB) annual meeting held at Fukuoka in May 1997 under the name Gyōten Initiative (Lipsy, 2003). MOF, however, eventually decided to postpone its proposal because it judged that the plan was unlikely to win support from several of the region's economies. In particular, the Republic of Korea (Korea) and Taipei, China were suspicious of Japan's regionalist policy, partly because it had not invited them to the meeting of the Six Markets Group held a few months before, nor were they supportive of the overall plan (Lipsy, 2003).

The 1997/98 Asian financial crisis increased the momentum for establishing the AMF. For example, the contributors to the Thai rescue package sensed the "unity of Asian countries" in the face of the crisis.¹³ Under this favorable situation for Japan, Vice Minister Sakakibara Eisuke decided that the time was right to realize Japan's goal of establishing the AMF immediately. The prospective members were to include Australia; the PRC; Hong Kong, China; Indonesia; Korea; Malaysia; the Philippines; Singapore; and Thailand. Japan sent an unofficial paper outlining the proposed AMF to prospective members in August. The US was not included among the recipients of this proposal.

However, Japan's attempt to establish the AMF while at the same time keeping the US unaware was not successful. One of the recipients of the outline proposal must have alerted the US because on 14 September, US Assistant Treasury Secretary Lawrence Summers called Sakakibara in the middle of the night and complained about the Japanese project, reportedly saying: "I thought you were my friend."¹⁴ On 17 September, the US sent out a letter to all APEC finance ministers that was signed by Treasury Secretary Robert Rubin and Federal Reserve Board Chairman Alan Greenspan. The letter implied that the US was interested in the formation of an Asia-Pacific cooperative framework to tackle crisis resolution issues. However, the letter emphasized the need to link such a framework with the International Monetary Fund (IMF). At a meeting held on September 21 in Hong Kong, China and attended by prospective AMF members as well as the US, it was agreed that the AMF would not be created. It is important to note that the US specifically opposed the creation of the AMF, rather than the creation of a regional monetary fund in general. Fred Bergsten, a close aide to the Clinton administration and Head of Institute for International Economics (IIE) in Washington, argued at the time that an Asia-Pacific Monetary Fund, which included the US, would be useful (Bergsten, 1998).

Even after the AMF meeting in Hong Kong, China in September 1998, the US felt that Asian countries were not convinced of the capacity of the IMF to resolve the ongoing

¹² However, the activities of the revived Four Markets Group did not develop into anything substantial.

¹³ The US did not contribute to the Thai rescue package (Sakakibara, 2000).

¹⁴ Ibid.

crisis and it feared the possibility that Asians were still exploring regional financial arrangements. According to Blustein (2001), the US Treasury's Assistant Secretary for International Affairs, Timothy Geithner, produced a report on 30 September 1997 arguing that "the approach outlined in the Rubin–Summers letter was likely to prove insufficiently compelling to avoid some regional financing mechanism. Our best case outcome would probably be an *ad hoc* arrangement for mobilizing bilateral resources alongside IMF programs (underline supplied)." Accordingly, in November, concerned parties had a meeting in Manila to finalize discussions on regional financial cooperation. The participants of the Manila meeting were: Japan; the PRC; Hong Kong, China; Korea; Indonesia; Malaysia; Singapore; Brunei Darussalam; the Philippines; Thailand; Australia; New Zealand; the US; and Canada. Three international institutions—the IMF, ADB, and World Bank—also attended. At this meeting, the participants agreed to establish the Manila Framework Group as a new semi-annual regional surveillance mechanism to complement the IMF.

Japan did not actively utilize the Manila Framework Group. A common view of the Manila Framework Group among Japanese MOF officials was that the US had established the group with the intention of blocking the formation of the AMF.¹⁵ At one point, MOF released a critical press statement arguing that Manila Framework Group members (implicitly naming the US) should make financial contributions to regional financial arrangements if they were really serious about the crisis resolution rather than the prevention of future crises.¹⁶

The US also started to disengage from activities under the dysfunctional Manila Framework Group. In 2000, the group stopped releasing a joint statement at the conclusion of its semi-annual meetings. Moreover, the group has not held a meeting since 2004. The nearly co-equal voices of the US and Japan in the Manila Framework Group seem to have resulted in dysfunction. The Manila Framework Group was unique because it mixed US-style surveillance with Asian-style peer pressure (Higgott, 1998), but such a new model did not function well in practice.

Third cycle. Soon after the failure of the AMF proposal, another opportunity to establish a regional financial meeting among Asian countries was created by the PRC. At the second ASEAN+3 Summit held in December 1998 in Hanoi, the PRC proposed establishing the ASEAN+3 Finance Ministers Deputies Meeting (FMDM).¹⁷ Japan strongly supported the PRC's idea. Subsequently, the first ASEAN+3 FMDM was held in March 1999 and the first ASEAN+3 Finance Ministers Meeting (FMM) was held the following month, back-to-back with the ADB annual meeting in Manila.¹⁸ At the third ASEAN+3 Summit held in November 1999 in Manila, the PRC insisted on the significance of strengthening the ASEAN+3 financial process. The PRC's proposal was supported by other participants (especially Japan) who collectively agreed to formalize the ASEAN+3 FMM (Kikuchi, 2001). One year later, in May 2000, the ASEAN+3 FMM agreed upon the Chiang Mai Initiative (CMI). The implementation of activities under the ASEAN+3 FMM were led by the Japanese MOF. At the time, the general view of CMI among Japanese MOF officials was that it was being led by the Japanese MOF. As one former MOF official said: "it would have been possible to use

¹⁵ For example, see Kuroda, 2004

¹⁶ See: <http://www.mof.go.jp/jouhou/kokkin/frame.html>

¹⁷ *Asahi Shimbun* (17 December 1998).

¹⁸ *Asahi Shimbun* (19 March 1999); *Sankei Shimbun* (1 May 1999).

a name that clearly associated [CMI] with the Japanese initiative, but Japan played down its leadership and decided to give credit to the host country and city, namely Thailand and Chiang Mai."¹⁹

The current situation of Asian financial cooperation can be described as phase one of the third cycle. An Asia-only financial meeting—the ASEAN+3 financial process—is the dominant cooperative framework and in 2009 the Chiang Mai Initiative Multilateralization (CMIM) was established under this framework. Notably, Japan and the PRC agreed to each make financial contributions to the CMIM fund equivalent to 32% of the total. So far, the US has not officially attempted to participate in the CMIM nor made a counterproposal on an Asia–Pacific financial cooperative framework.

3.2 The Cycle of Regional Summit Meetings

First cycle. Japan has been interested in regional summits since the 1970s.²⁰ In early 1976, soon after Prime Minister Miki Takeo had attended the Rambouillet Summit, he proposed an Asian Summit. However, he failed to win widespread support. When ASEAN members first held a summit meeting in August 1976, Japan attempted to participate but was stopped mainly due to opposition from Indonesia. Nevertheless, Japan successfully demonstrated its special relationship with ASEAN by sending messages from the Prime Minister and Foreign Minister to ASEAN leaders expressing Japan's desire to strengthen relations with ASEAN. The US State Department also planned to send a similar message to the ASEAN Summit and held consultations on doing so with the Japanese Ministry of Foreign Affairs (MOFA). The State Department was, however, dissuaded from sending a similar message to ASEAN leaders.²¹ Sudo (1992) considered this political maneuver by Japan as giving the impression of an exclusive role for Japan in the region.

Japan's attempt to get involved in the ASEAN Summit was successful in the following year when the Fukuda Administration declared an equal partnership between Japan and ASEAN, which became known as the Fukuda Doctrine. The understanding of the Japanese MOFA was that Japan would participate in the ASEAN Summit with observer status, rather than participate in an ASEAN–Japan Summit held back-to-back with the ASEAN Summit.²² When ASEAN held its third summit in 1987, Japan again successfully participated as an observer.

Meanwhile, the US sought to upgrade APEC from a meeting at the foreign and trade ministers-level to a regional summit attended by leaders of each member country. While APEC was established in the late 1980s as a trade forum under a Japanese and Australian initiative, its diplomatic inclination became more significant through the US-led upgrade. Australian Prime Minister Paul Keating was the first to propose that leaders attend the annual APEC meeting. He consulted with US President George H.W. Bush about the idea in early 1992. Although President Bush showed interest in Keating's proposal, he was unable to host an APEC Summit with leaders in

¹⁹ Kuroda (2004).

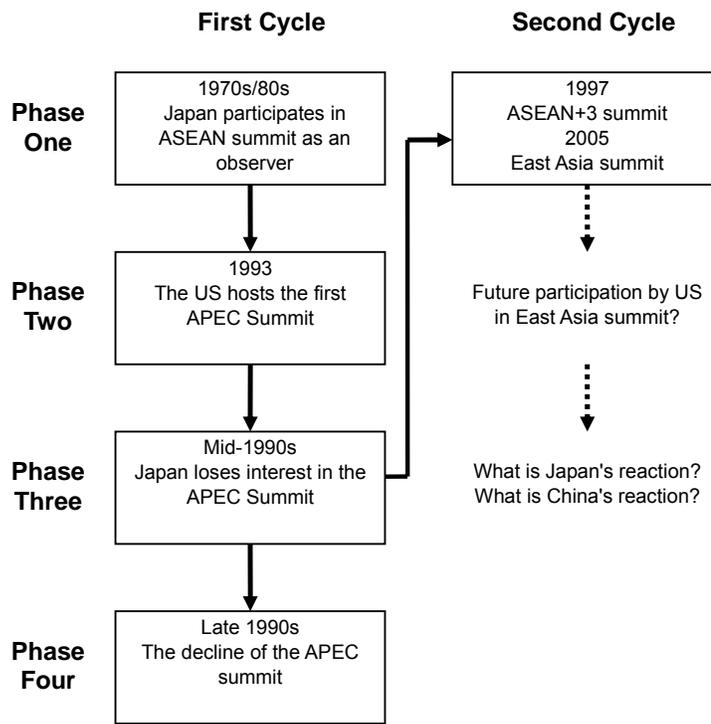
²⁰ The first regional summit in Asia was the Bungdong meeting in 1955. This meeting was actually a pan Asia–Africa summit and was a one-off event.

²¹ Yano (1978).

²² See: <http://www.mofa.go.jp/mofaj/area/asean/initiative.html>

attendance due to being voted out of office in November 1992. However, US President Bill Clinton, who was inaugurated in January 1993, actively pursued the idea of an APEC Summit (Funabashi, 1995). President Clinton officially proposed to host the first APEC Summit in a speech made in San Francisco in July 1993 before his first Asian tour. The first APEC Summit would eventually be held in November of that same year in Seattle.

Figure 4: Regionalism Cycle of Regional Summit



Source: Author's original.

Japan was indifferent to the idea of holding an APEC summit from the beginning. Australian Prime Minister Keating sent out a letter in April 1992 in which the idea of an APEC summit was explained to the leaders of key APEC members, including the US, Japan, Korea, Singapore, and Indonesia. Although Keating received positive responses from the others, Japan was said to have been reticent about the proposal. Moreover, although Keating urged Japanese Prime Minister Miyazawa Kiichi to support the proposed APEC Summit when he visited Japan in May 1993, Japan did not finally approve it until July 1993 once the establishment of the APEC Summit had become unavoidable. A senior US official recalled that Japan was reluctant to accept the APEC Summit even when the US initiated the project of upgrading APEC (Funabashi, 1995).

Takanaka Kimio, a former senior official at the Japan External Trade Organization (JETRO), a government-linked think tank, straightforwardly criticized the Clinton administration for upgrading APEC from minister-level to leader-level by misusing the position of the APEC chairmanship (Takanaka, 2001). Since APEC was elevated to the summit level in 1993, Funabashi (1995) wrote: “Japan has not taken a leadership role.” Although Japan maintained some interest in the APEC Summit until 1995 when it held the chairmanship, its attitude hardened toward in the late 1990s. For example, in 1998, the Diplomatic Blue Book of Japan abolished a subsection on APEC.

The US engagement with the APEC Summit in particular and APEC in general also weakened substantially in the second half of the 1990s. President Clinton was absent from the APEC Summit in 1995 and 1998, which is one of the main reasons for APEC’s drift at the time (Ravenhill, 2001). US President George W. Bush attempted to utilize the Shanghai APEC Summit in 2001 for the nontraditional purpose of national security. However, this attempt led to further indifference toward APEC’s activities among other members (Pempel, 2008).

Second cycle. When the APEC Summit became a dominant summit in the region, Japan attempted to organize a smaller regional summit for Asian countries only. In January 1997, Prime Minister Hashimoto visited Southeast Asia and proposed to hold the Japan–ASEAN Summit on an annual basis. However, ASEAN feared a situation in which the summit would be dominated by Japan and therefore made the counter-proposal of an ASEAN+3 Summit. The first ASEAN+3 Summit was held in Kuala Lumpur in December 1997. Since 2005, an East Asia Summit has been held with the participation of ASEAN+3 members plus Australia, New Zealand, and India. Only signatories to the Treaty of Amity and Cooperation in Southeast Asia (TAC) are eligible to attend this summit. The US did not sign the TAC until 2009.

The current situation of the summit process is similar to phase one of the second regionalism cycle. However, given that the US became a signatory to the TAC in 2009, it is possible to regard that the US will be able to participate in the East Asia Summit in the near future. In fact, some Asian countries have shown interest in US participation. Notably, Japan has expressed the view that US involvement in the East Asia Summit would be desirable (Bōno, 2005). Japanese Foreign Minister Machimura Nobutaka insisted during a previous ASEAN+3 meeting that the US should participate in the East Asia Summit as an observer (full participation would have been impossible at the time due to the TAC issue.)²³ In contrast, the PRC has been reluctant to involve the US in the East Asia Summit.²⁴

Japan's interest in involving the US in the East Asia Summit would appear inconsistent with the hypothesis presented in this paper that Japan seeks to exclude the US from a regional framework. However, Japan is in the process of being replaced by the PRC as the most dominant power in Asia and it is now the PRC, and not Japan, that would hold the leading position in an Asia-only regional framework. This means that the new seeker of an exclusionary regionalism policy in the field of summitry is the PRC. Therefore, the PRC now has an incentive to establish an Asia-only regional summit, just like Japan did so in the past.

²³ *Asahi Shimbun* (7 May 2005); *Sankei Shimbun* (7 May 2005).

²⁴ For details of the PRC's and Japan's preferences with regard to East Asia Summit membership, see Hamanaka (2008).

4. Conclusion

This paper develops a hypothesis of a regionalism cycle using a game theory approach and examines its explanatory power based on actual cases of regional institutions in Asia. Since the pay-off matrix for this game does not have a stable equilibrium, meaning that there is no dominant strategy for both Japan and the US, either the US or Japan can increase its gain by changing its choice in reaction to the other's choice. As a result of this, the institutional outcome of Asian regional cooperation becomes cyclical.

This hypothesis fits very well with empirical evidence on the rise and fall of regional financial institutions. Japan has traditionally sought to establish an Asia-only regional framework, with the US subsequently attempting to gain membership. Japan would then abandon an old framework once it had included the US and attempt to establish a new Asia-only regional framework. The hypothesis also explains the development of regional summitry to a degree. Japan's attempts to hold a regional summit among Asian countries only and the US attempts to establish a summit for the Asia-Pacific region were competing efforts.

Interestingly, Japan is currently being replaced by the PRC as the state holding the leading position in an Asia-only framework and which therefore attempts to establish such regional frameworks. So long as the US is excluded, the PRC will hold the leading position in an Asia-only framework, just as Japan did in the past. The PRC's newfound dominance is evident in the diplomatic field. Therefore, it is not surprising if the PRC, not Japan, becomes the hunter of an exclusionary regional summit. As Fareed Zakaria puts it: "Beijing thought up the East Asia Summit as a regular meeting and one where, with the United States absent, the PRC would be the star."²⁵ In the case of finance, however, the power balance between Japan and the PRC is still nearly equal as the example of their co-equal CMIM contributions suggests. However, the PRC eventually may pursue an exclusionary Asia-only financial cooperation framework once its financial power overwhelms that of Japan.

Despite the commonplace view that Asian regionalism lacks institutions, a considerable number of regional frameworks have been established and subsequently abolished in Asia. The struggle for leadership, not the absence of leadership, has been the fundamental reason for the dynamic rise and fall of many Asian regional frameworks.

²⁵ *Newsweek* (12 December 2005).

References

- ADB. 2008. *Emerging Asian Regionalism: A Partnership for Shared Prosperity*. Manila: Asian Development Bank.
- C. Fred Bergsten. 1997. Open Regionalism. *Institute for International Economics Working Paper*.
- N. Bono. 2005. Higashi Ajia Samitto [East Asia Summit]. Available at: <http://www.jjia.or.jp/keyword/200512/07-bounoseihiroshi.html>.
- J.A.C. Conybeare. 1987. *Trade Wars: The Theory and Practice of International Commercial Rivalry*. New York: Columbia University Press.
- Y. Funabashi. 1995. *Asia Pacific Fusion: Japan's Role in APEC*. Washington, DC: Institute for International Economics.
- M. Haas. 1989. *The Asian Way to Peace: A Story of Regional Cooperation*. New York: Praeger.
- S. Hamanaka. 2008. Comparing summitry, financial and trade regionalism in East Asia: from the Japanese perspective. In Christopher Dent (ed.) *China, Japan and Regional Leadership in East Asia*.
- S. Hamanaka. 2009. *Asian Regionalism and Japan: The Politics of Membership in Regional Diplomatic, Financial and Trade Groups*. London: Routledge.
- R. Higgott. 1998. The Asian Economic Crisis: A Study in the Politics of Resentment. *New Political Economy*. 3(3). pp. 333–56.
- R.W. Hu. 2009. Building Asia Pacific Regional Architecture: The Challenge of Hybrid Regionalism. *The Brookings Institution Working Paper*. Washington, DC: Brookings Institution.
- T. Katō *et al.* 2002. *Dai-7-kai Genron NPO Ajia Senryaku Kaigi [Round Table of Asian Strategy at Genron NPO]*.
- T. Kikuchi. 2001. Higashi Ajia Chiiki-shugi no Kanou-sei [The Potential of East Asian Regionalism]. *Kokusai Mondai [International Affairs]*. 494. pp. 16–33.
- C. Kindleberger. 1973. *The World in Depression*. pp. 1929–1939. London: Allen Lane.
- H. Kuroda. 2004. *Gen Kiriage [Re-peg of the Chinese Yuan]*. Tokyo: Nikkei BP.
- D. Lake. 1993. Leadership, Hegemony, and the International Economy: Naked Emperor or Tattered Monarch with Potential? *International Studies Quarterly*. 37(4). pp. 459–89.
- P. Lipsky. 2003. Japan's Asian Monetary Fund Proposal. *Stanford Journal of East Asian Affairs*. Vol. 3.
- W. Mattli. 1999. *Logic of Regional Integration*. Cambridge: Cambridge University Press

- 17 | Regionalism Cycle in Asia (-Pacific): A Game Theory Approach to the Rise and Fall of Asian Regional Institutions
- S. Ostry. 1997. Canada and the Year of Asia-Pacific: Trade and Investment. Paper Presented at the Canadian Institute of International Affairs Foreign Policy Conference.
- T.J. Pempel. 2008. How Bush bungled Asia: militarism, economic indifference and unilateralism have weakened the United States across Asia. *The Pacific Review*. 21 (5). pp. 547–581
- J. Ravenhill. 2001. *APEC and the Construction of Pacific Rim Regionalism*. Cambridge: Cambridge University Press.
- B. Russett. 1985. The Mysterious Case of Vanishing Hegemony; or, Is Mark Twain Really Dead? *International Organization*. 39 (2). pp. 207–31.
- D. Snidal. 1985. Limits of Hegemonic Stability Theory. *International Organization*. 39(4). pp. 579–614.
- D. Snidal. 1994. The Politics of Scope: Endogenous Actors, Heterogeneity and Institutions. *Journal of Theoretical Politics*. 6(4). pp. 449–72.
- S. Sudo. 1992. *The Fukuda Doctrine and ASEAN: New Dimensions in Japanese Foreign Policy*. Singapore: Institute of Southeast Asian Studies.
- K. Takanaka. 2001. *Keizai Tōgō no Power Game [Power Game of Economic Integration]*. Tokyo: Bunshun Shinsho.
- D.T. Yasutomo. 1983. *Japan and the Asian Development Bank*. New York: Praeger.

ADB Working Paper Series on Regional Economic Integration *

1. "The ASEAN Economic Community and the European Experience" by Michael G. Plummer
2. "Economic Integration in East Asia: Trends, Prospects, and a Possible Roadmap" by Pradumna B. Rana
3. "Central Asia after Fifteen Years of Transition: Growth, Regional Cooperation, and Policy Choices" by Malcolm Dowling and Ganeshan Wignaraja
4. "Global Imbalances and the Asian Economies: Implications for Regional Cooperation" by Barry Eichengreen
5. "Toward Win-Win Regionalism in Asia: Issues and Challenges in Forming Efficient Trade Agreements" by Michael G. Plummer
6. "Liberalizing Cross-Border Capital Flows: How Effective Are Institutional Arrangements against Crisis in Southeast Asia" by Alfred Steinherr, Alessandro Cisotta, Erik Klär, and Kenan Šehović
7. "Managing the Noodle Bowl: The Fragility of East Asian Regionalism" by Richard E. Baldwin
8. "Measuring Regional Market Integration in Developing Asia: a Dynamic Factor Error Correction Model (DF-ECM) Approach" by Duo Qin, Marie Anne Cagas, Geoffrey Ducanes, Nedelyn Magtibay-Ramos, and Pilipinas F. Quising
9. "The Post-Crisis Sequencing of Economic Integration in Asia: Trade as a Complement to a Monetary Future" by Michael G. Plummer and Ganeshan Wignaraja
10. "Trade Intensity and Business Cycle Synchronization: The Case of East Asia" by Pradumna B. Rana
11. "Inequality and Growth Revisited" by Robert J. Barro
12. "Securitization in East Asia" by Paul Lejot, Douglas Arner, and Lotte Schou-Zibell
13. "Patterns and Determinants of Cross-border Financial Asset Holdings in East Asia" by Jong-Wha Lee
14. "Regionalism as an Engine of Multilateralism: A Case for a Single East Asian FTA" by Masahiro Kawai and Ganeshan Wignaraja
15. "The Impact of Capital Inflows on Emerging East Asian Economies: Is Too Much Money Chasing Too Little Good?" by Soyoung Kim and Doo Yong Yang
16. "Emerging East Asian Banking Systems Ten Years after the 1997/98 Crisis" by Charles Adams

17. "Real and Financial Integration in East Asia" by Soyoung Kim and Jong-Wha Lee
18. "Global Financial Turmoil: Impact and Challenges for Asia's Financial Systems" by Jong-Wha Lee and Cyn-Young Park
19. "Cambodia's Persistent Dollarization: Causes and Policy Options" by Jayant Menon
20. "Welfare Implications of International Financial Integration" by Jong-Wha Lee and Kwanho Shin
21. "Is the ASEAN-Korea Free Trade Area (AKFTA) an Optimal Free Trade Area?" by Donghyun Park, Innwon Park, and Gemma Esther B. Estrada
22. "India's Bond Market—Developments and Challenges Ahead" by Stephen Wells and Lotte Schou- Zibell
23. "Commodity Prices and Monetary Policy in Emerging East Asia" by Hsiao Chink Tang
24. "Does Trade Integration Contribute to Peace?" by Jong-Wha Lee and Ju Hyun Pyun
25. "Aging in Asia: Trends, Impacts, and Responses" by Jayant Menon and Anna Melendez-Nakamura
26. "Re-considering Asian Financial Regionalism in the 1990s" by Shintaro Hamanaka
27. "Managing Success in Viet Nam: Macroeconomic Consequences of Large Capital Inflows with Limited Policy Tools" by Jayant Menon
28. "The Building Block versus Stumbling Block Debate of Regionalism: From the Perspective of Service Trade Liberalization in Asia" by Shintaro Hamanaka
29. "East Asian and European Economic Integration: A Comparative Analysis" by Giovanni Capannelli and Carlo Filippini
30. "Promoting Trade and Investment in India's Northeastern Region" by M. Govinda Rao
31. "Emerging Asia: Decoupling or Recoupling" by Soyoung Kim, Jong-Wha Lee, and Cyn-Young Park
32. "India's Role in South Asia Trade and Investment Integration" by Rajiv Kumar and Manjeeta Singh
33. "Developing Indicators for Regional Economic Integration and Cooperation" by Giovanni Capannelli, Jong-Wha Lee, and Peter Petri
34. "Beyond the Crisis: Financial Regulatory Reform in Emerging Asia" by Chee Sung Lee and Cyn-Young Park

35. "Regional Economic Impacts of Cross-Border Infrastructure: A General Equilibrium Application to Thailand and Lao PDR" by Peter Warr, Jayant Menon, and Arief Anshory Yusuf
36. "Exchange Rate Regimes in the Asia-Pacific Region and the Global Financial Crisis" by Warwick J. McKibbin and Waranya Pim Chanthapun
37. "Roads for Asian Integration: Measuring ADB's Contribution to the Asian Highway Network" by Srinivasa Madhur, Ganeshan Wignaraja, and Peter Darjes
38. "The Financial Crisis and Money Markets in Emerging Asia" by Robert Rigg and Lotte Schou-Zibell
39. "Complements or Substitutes? Preferential and Multilateral Trade Liberalization at the Sectoral Level" by Mitsuyo Ando, Antoni Esteveordal, and Christian Volpe Martincus
40. "Regulatory Reforms for Improving the Business Environment in Selected Asian Economies—How Monitoring and Comparative Benchmarking can Provide Incentive for Reform" by Lotte Schou-Zibell and Srinivasa Madhur
41. "Global Production Sharing, Trade Patterns, and Determinants of Trade Flows in East Asia" by Prema-Chandra Athukorala and Jayant Menon

* These papers can be downloaded from: (ARIC) <http://aric.adb.org/reipapers/> or (ADB) www.adb.org/publications/category.asp?id=2805

Regionalism Cycle in Asia (-Pacific): A Game Theory Approach to the Rise and Fall of Asian Regional Institutions

Despite a commonplace view that Asian regionalism lacks institutions, the rise and fall of Asian regional institutions is in fact an extremely dynamic process. This paper argues that there is a “regionalism cycle” in Asia that helps to explain the dynamic nature of Asian regionalism.

About the Asian Development Bank

ADB's vision is an Asia and Pacific region free of poverty. Its mission is to help its developing member countries substantially reduce poverty and improve the quality of life of their people. Despite the region's many successes, it remains home to two-thirds of the world's poor: 1.8 billion people who live on less than \$2 a day, with 903 million struggling on less than \$1.25 a day. ADB is committed to reducing poverty through inclusive economic growth, environmentally sustainable growth, and regional integration.

Based in Manila, ADB is owned by 67 members, including 48 from the region. Its main instruments for helping its developing member countries are policy dialogue, loans, equity investments, guarantees, grants, and technical assistance.