

## The Domestic Political Impact of Rapid Economic Change in the Indo-Pacific Region

By Ellen L. Frost

Structural changes in the external economic environment have a profound and complex impact on the distribution of power and wealth among and within national societies. They mobilize new actors, influence the content of domestic and foreign economic policies, and ultimately contribute to—or erode—the legitimacy of national governments.

Nowhere in the world are these impacts more visible and more dynamic than in the nations of the Indo-Pacific, many of which will hold elections within the next year. These challenges are not new, but they have intensified. Beginning in the 1980s, the revolution in communications technology and the advent of large-scale container shipping swept across East and Southeast Asia, connecting people and markets as never before. In the 1990s, burgeoning production networks linked the more competitive and investment-friendly developing economies—such as Singapore, Thailand, Malaysia, South Korea, and Taiwan—with world markets, leaving more closed economies such as Laos, Myanmar, and India lagging behind. Market-opening in China fueled spectacular rates of growth, lifted millions out of poverty, and enabled the country to become not only an assembly nexus and production hub but also an assertive regional power.

Regional economic integration has become a dominant feature of today's Indo-Pacific. All governments are committed to promoting closer economic ties with each other, whether half-heartedly or not. Integration is inching along, gingerly encouraged by governments but driven more powerfully by pressure from the private sector and from ocean-facing local governments. Trade-liberalizing agreements, though imperfect and limited, are the new norm. Negotiations spearheaded by the Association of South East Asian Nations (ASEAN) have made some progress. Despite the Asian financial crisis of 1997-98 and the U.S.-origin global recession of 2008-09, no government in the Indo-Pacific region has rejected the rules embodied in the World Trade Organization (WTO) or retreated from its slow and uneven march toward more open markets.

Indo-Pacific governments that signed on to the high-standard Trans-Pacific Partnership (TPP) agreement—Brunei, Singapore, Malaysia, Vietnam, Australia, and New Zealand—remain committed to improving the protection of intellectual property and tackling other behind-the-border measures that impede trade and investment, with or without the United States. Promoting the transition to a digital economy is likely to gain more prominence next year, when Thailand takes over the chairmanship of ASEAN. Meanwhile, negotiations on a less demanding, ASEAN-sponsored Regional Comprehensive Economic Partnership (RCEP), which includes India as well as Australia, and New Zealand, continue to inch along.

Even India has embraced closer integration, as emphasized most recently by Prime Minister Modi at the June 2018 Shangri-La Dialogue. India's economic reform is lagging, but its high growth rate, relatively low level of public debt, and youthful population have attracted an upsurge in foreign investment. The Modi government's outward-looking strategic awakening is gradually improving relations with nations bordering the Bay of Bengal and the Indian Ocean littoral, thus facilitating closer integration. But the combination of India's federal system, local politics, corruption, and remnants of the "license raj" has thus far thwarted wide-ranging economic liberalization.

### Domestic Aspects of Regional Integration

The upsurge in Indo-Pacific economic integration has spawned a rising middle class whose members have embraced the choices available in the regional (and global) marketplace. Urban dwellers in particular have become used to higher standards of living, more consumer choice, and a wide spectrum of social media. Thousands of Asians have found employment in foreign firms or joint ventures, while others have lost their jobs. What Karl Marx and others called the "comprador bourgeoisie"—local agents or managers working for foreign entities—has emerged as an educated political class with a major stake in regional integration.

### Ellen L. Frost

Senior Advisor and Fellow at the East-West Center in Washington, explains that "A key question is whether the strategies employed by current Indo-Pacific governments are working well enough to be both competitive in the new regional economic environment and responsive to legitimate grievances at home."

Many provincial and urban authorities have developed close ties to their nearby counterparts across borders, particularly in mainland Southeast Asian countries bordering on or close to China (Myanmar, Laos, Vietnam, and Thailand). Small- and medium-size companies and local enterprises account for a growing share of China's overseas investment. All of these groups have acquired a stronger political voice.

### **China**

Overshadowing all this activity is the sheer weight of China. China's economic growth and central role in production networks have made it the number-one or number-two trading partner of virtually all countries in the East and Southeast Asia regions. Some smaller nations have found a niche in China-centered manufacturing networks, while others have boosted their sale of commodities and raw materials. China's Belt and Road Initiative and the China-sponsored Asian Infrastructure Investment Bank will spur badly needed development of Indo-Pacific infrastructure and connectivity. Local interest groups have sprung up accordingly. For all of these reasons, most Indo-Pacific governments feel compelled to maintain friendly relations with China.

Dependence on China comes at a price, however. Huge loans for infrastructure projects can feed large-scale corruption and saddle poorer countries with unsustainable debt. To enforce its geopolitical agenda, Beijing is increasingly resorting to coercive economic statecraft ("sharp power"), including surprise "inspections" and delayed approvals, selective boycotts, and limits on tourism. Chinese companies investing in Indo-Pacific countries typically import large groups of Chinese workers to perform jobs that might otherwise go to local laborers. The militarization of islands claimed or created in the South China Sea has gone unchecked, spurring criticism in rival claimants.

### **Challenges Facing Indo-Pacific Governments**

A number of major threats to integration, growth, and political stability in the Indo-Pacific region are beyond national governments' control. They include financial volatility, cyber crime, terrorist attacks, refugee flows, fluctuating commodity prices, rising sea levels, severe storms, and other natural disasters. Grievances and conspiracy theories proliferate via social media. Manufacturing breakthroughs such as 3-D printing may localize or otherwise shrink the regional supply chains in which many Asians have found a profitable niche. Growing income inequality is also a threat; when those left behind come from a neglected or persecuted ethnic or religious group, the result can be highly destabilizing.

The latest threat to Indo-Pacific prosperity—and indirectly to regional integration—is the outbreak of protectionism and populist nationalism in the United States. The Trump administration's "America First" campaign may well divert investment away from the Indo-Pacific and into the United States. Indeed, that is an explicit U.S. policy goal. As regional integration stalls, domestic interest groups with a stake in the expanding regional economy and others with previously high expectations may turn against established governments.

### **Electoral Prospects: Finding a Balance**

Upcoming elections in Bangladesh, Bhutan, Cambodia, the Philippines, Indonesia, Thailand and India (including Indian states), scheduled for 2018 or 2019, will put the leaders of these countries to the test. Governments not facing challenges from the ballot box will feel pressure from their citizens as well. Some of the likely issues will be linked to or exacerbated by the evolving external economic environment, such as large-scale corruption in the infrastructure sector, widening income gaps, unwelcome Chinese activities, and worker layoffs in non-competitive sectors.

A key question is whether the strategies employed by existing Indo-Pacific governments are working well enough to be both competitive in the new regional economic environment and responsive to legitimate grievances at home. Governments that fail to reform the structure of their economies risk falling even further behind in the regional marketplace, but those who neglect their most vulnerable citizens may be voted out of office—or overthrown.

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