

Professor Zhang Yuyan's speech at Cambodia Outlook Conference 2008 on 28 February.

Thank you, Mr. Chairman, Distinguished participants, ladies and gentlemen, good morning,

First of all, I would like to extend my deep gratitude to the organizers of the 2008 Cambodia Outlook Conference for inviting me to join with you, and I believe this event will be very successful and fruitful. Also I feel quite happy to visit your beautiful country and to have the opportunity to share my views with you. The topic I'm going to talk about focuses on two issues: the source of economic growth and the reason why the economic cooperation in Asia should be further strengthened.

More than two hundred years ago, Adam Smith, the founder of economics and the writer of the book *Wealth of Nations*, argued that the long term economic growth was exclusively the result of improvement in productivity, the later was in large part generated by the division of labor and specialization, while both were brought about by the enlargement of market size. With the understanding of this basic logic of economic growth, Adam Smith is one of the most steadfast advocates of free trade, which is, in his view, the fundamental source of the gain from trade. His fellowman, David Ricardo enriched Smith's theory of free trade in depth and in width by introducing a far-reaching and innovative concept: comparative advantages. He argued that, with few exceptions, each country had its own comparative advantages and its gains from trade could be guaranteed if exchange of goods and services was made on voluntary basis. Nowadays we find what Smith and Ricardo tried to prove centuries ago have already become the pillars of international economics.

Theoretically speaking, every country can be a beneficiary of free trade by making full use of their comparative advantages in a market. However, we need to keep in mind all the time that no any gain from trade can be made without a well-functioned market, and that no any incremental gain from trade can be harvested without a continuously expanding market. In one word, the gain from trade can only be realized on the condition of a well-functioned and a continuously expanding market. A well functioned market here mainly means that any changes of products are substantially based on the strictly protected contracts and clearly defined property rights. Due to the existence of a well-functioned and continuously expanding market, the gain from trade eventually emerge, which not only benefit those who get involved in transaction of goods and services but also make economic growth come true.

As a mechanism characterized by contracts enforcement, market is composed of two parts: domestic market and international market. Therefore, the task to

expand the size of market becomes twofold: to augment both domestic as well as international market simultaneously. When people talk about the enlargement of market, one question emerges and needs to be answered immediately is: who or which institutions are most suitable to shoulder the responsibilities of doing it? We now have known that a well-functioned market plays a vital role in the long term economic growth. Meanwhile, we can hardly avoid a question: property rights, no matter being individually or collectively owned, are protected by whom or what institutions? Putting it another way, what is the most efficient and effective way in which property rights can be protected and voluntary contracts can be enforced?

The answer to the above two questions is government in a broad sense. The late Professor Mancur Olson, who taught economics at the University of Maryland and used to be my supervisor while I was a visiting scholar to the university sixteen years ago, wrote a book entitled *Power and Prosperity*. In this book, the author links growth with government and comes to a conclusion that a market-augmenting government is the key to an economic success. According to Professor Olson, the essential elements of a market-augmenting government include two related obligations: to promote law-based contracts and constrain itself from infringing upon property rights. In other words, market will be consequently enlarged so long as the government is able to confine itself to effectively undertaking those two tasks. Here the logic of Smith and Olson meets and overlaps, and the combination of them provides us with a more complete picture of a long term economic growth theory.

Now let me shift my discussion from logic to the real world. Regional economic cooperation in Asia, in this context, can be understood accurately in line with the logic I elaborated above. The establishment of framework or mechanism like ASEAN+1 or ASEAN+3, for example, follows exactly the same logic. By becoming a member of a regional economic organization, a country's market can be extended beyond its territory. Maybe more importantly, a gradually integrated market is conducive to give rise to standardization of the rules of games that the participants of the specific organization play. Standardization of the rule of games, together with policy-coordination among those game players, may naturally reduce the transaction cost so as to increase the gain from trade.

Asia is a late comer in regional integration. However, economic integration in Asia has been accelerating at multiple levels since the breaking out of financial crisis in 1997, with ASEAN being the central hub, and ASEAN+1 and ASEAN+3 being two major supporting pillars. Apart from those, there are some sub-regional cooperative activities including the Great Mekong Subregion and the Tumen River Area Development Program. FTA is also playing an increasingly important part in economic cooperation between countries in Asia.

China began to carry out its reform and opening-up policy 30 years ago. It is widely recognized that in the past 30 years China has made a remarkable achievements with annual growth rate at 9% or more. In term of GDP and foreign trade, China ranks the 3rd in the world in 2007, while GDP per capita is 10 times as high as that of 30 years ago. People usually attribute all of the achievements to China's reform and opening-up. That is true. However, when we want to look into the contents and objectives of the economic reform and opening-up in China, we can easily find that the creation of a well-functioned and continuously expanding market has been put on the top priority during the period of the past 30years. That is why China firmly welcomes any initiatives which help to build up closer ties among nations in this region.

As far as regional cooperation in Asia is concerned, there are several points need to be emphasized. Firstly, all countries are politically equal, no matter big or small. Secondly, lasting or sustainable cooperation is preconditioned by shared interests and mutual benefits. Thirdly, a close regionalism will probably undermine the ability of reaping the gains from trade. In other words, we should always look forward to an open inclusive economic architecture. Last but not least, we need to be patient enough while taking into account expediting the process of cooperation. Differing greatly from Europe and North America, Asia is a far more complex and diversified area. This reality requires that the roadmap to advance economic integration be a very Asian one and in an innovative way.

The cooperation among the countries in Asia is in the interest of Asian people and can be likened to a tree, whose seeds have already been planted for quite a long time. Whether it is able to grow up and how many fruits it will bear in the years to come, mainly depend upon the circumstances surrounding it. In my view, the conference we have today is exactly a sort of effort to facilitate the growth of the tree. I believe, the tree of cooperation in this region will continue to grow and eventually benefit everyone who has made or is making contributions to the growth of it. Here, making contributions means to water the tree, to fertilize the tree, to trim unnecessary branches of the tree, and to protect the tree from being damaged by harmful insects and plant diseases.

No country can be fully developed while its neighbor is not. To go forward is to go together.

Thank you for your attention.