



**FACULTY OF ECONOMICS  
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**Thesis**

**“Economic Integration Among ASEAN Countries:  
Evidence From Gravity Model”**

**By:**

**DIAN DWI GUSTIANA**

**06151145**

The Student of Bachelor Degree of Economics Department

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University Alumnus  
Registration No:

**DIAN DWI  
GUSTIANA**

Faculty Alumnus  
Registration No:

Personal Identity

a) Date of Birth: Padang/ August 3<sup>rd</sup> 1988 b) Parents' Name: Arsal Aburdin, SE and Rahmada Lenny c) Faculty: Economics d) Department: Economic e) Student No : 06 151 145 f) Date of Examination: January, 27<sup>th</sup> 2011 g) Graduate Standard: Very Satisfaction h) GPA: 3.11 i) Length of Study Period: 4 years and 4 months j) Parents' Address: Grya Elok Residence Blok H1/14, Padang

**Economic Integration Among ASEAN Countries: Evidence from Gravity Model**

Thesis by: Dian Dwi Gustiana Thesis Advisor: Drs. Masrizal, M.Soc, Sc

ABSTRACT

This research is a study about Economic Integration Among ASEAN Countries: Evidence from Gravity Model. The thesis analyzes the impact by using GLS (Generalized Least Square) of cross-country data and regress it each year from 1997-2007. In this thesis the writer uses some variables; they are export in logarithmic form (lnExp) as a dependent variable and gross domestic product in exporting country of logarithmic form (lnGDPi), gross domestic product of importing country in logarithmic form (lnGDPj), sum of population of exporting country in logarithmic form (lnPopi), sum of population of importing country in logarithmic form (lnPopj) as independent variables and gravity model as the model. Based on empirical result, the writers suggest that all independent variables are significant and have positive positive relationship to dependent variable. That means, all variables used to provide a positive impact on economic integration.

Keywords: economic integration, AFTA, ASEAN, generalize least square, gravity model

This thesis has been presented before the examiners in the Thesis Examination and successfully passed the Thesis Examination on January 27<sup>th</sup> 2010.

The Abstract has been approved by the advisor and the examiners:

Signature			
Full Name	Drs. Masrizal, M.Soc, Sc	Prof.Dr.H. Syafruddin Karimi, SE, MA	M. Nazer, SE, MA

Approved by :

Head of Department: Prof.Dr.H.Firwan Tan.SE.M.Ec.DEA.Ing  
NIP. 130 812 952

Signature

The Alumnus has registered to the Faculty of Economy of Andalas University and has obtained the Alumnus Registration Number:

	The officer in charge of Faculty /Andalas University	
University Alumnus Registration No:	Name :	Signature:
Faculty Alumnus Registration No :	Name :	Signature:



# CHAPTER I

## INTRODUCTION

### 1.1 Background

Over the past few decades, efforts at regional integration have increasingly become the central focus of various groups of countries. Economic integration, in particular, can lead to trade creation and other benefits in the form of a more competitive trade environment from the removal of trade barriers and the possibility of realizing economies of scale and higher economic growth. In addition, forming economic groupings can also stimulate investment in the member countries from both internal and foreign sources. It has been argued that integration can stimulate investment by reducing risk and uncertainty due to the larger market that producers become open to. Furthermore, foreign investors may wish to invest in productive capacity in a member country to avoid being excluded by trade restrictions and a high common external tariff (Appleyard, 1995).

In line with this idea, the ASEAN regional grouping was formed on 8 August 1967 by five countries, namely, Indonesia, Malaysia, the Philippines, Singapore, and Thailand. Brunei Darussalam later joined in 1984, followed by Vietnam in 1995, Laos and Myanmar in 1997, and also Cambodia in 1999. Among the objectives of ASEAN are to enhance economic growth and other fields such as social, cultural, technical, and educational in the region through cooperation, and to promote regional peace and stability.

Although the initial concerns of ASEAN during its early period of establishment were issues related to political security in Southeast Asia, over time attempts at organized regional co-operation were established. It was not until 1976 that ASEAN members agreed to pursue coordinated investment projects to complement the economic structures among member countries. In 1977 the ASEAN preferential trading arrangements were established to promote greater intra-regional trade and to co-ordinate industrialization policies (Park, 1999). The ASEAN preferential trading arrangements sought to reduce tariff and non-tariff barriers to goods produced in member countries. However, the consensus from existing studies suggests that only negligible increases in trade in the region were achieved (Ariff, 1994; Garnaut & Drysdale, 1994; DeRosa, 1995). According to DeRosa (1995), this initiative was not fulfilled due to several reasons including the reliance on non-tariff barriers among member countries and opposition of national interests which is more concerned with the profitability of their local investments.

This scenario changed during the late 1980s and 1990s when the global market became more competitive with the formation of NAFTA and EU. It raised questions among the ASEAN heads of state on the accessibility of ASEAN exports to the North American and European markets. In addition, with the emergence of China as the main global economic player, ASEAN faced an intense competition to attract foreign direct investment into their countries. In response to the situation, in January 1992, the six member countries at that time (ASEAN-6) agreed to establish the ASEAN Free Trade Area (AFTA) which among others,



## CHAPTER VI

### CONCLUSION AND RECOMMENDATION

#### 6.1 Conclusion

From the discussion and estimation that was explained in the previous chapter concludes as follows:

1. ASEAN will continue to benefit from AFTA and further "deepening" measures through the effects on strengthening macroeconomic stability, encouraging investment flows, enhancing technology transfer, minimizing intra-regional transactions costs to conducting business, and fostering policy reform in the region. ASEAN regional integration will help ASEAN countries to prevail over periodic crises by, among others, incorporating regional economic reform and providing information sharing with regards to crisis management.
2.  $POP_j$  or population of importer country is the most influential variable for economic integration. Demand of importer countries will increase if the populations of importer countries increase also.
3. For  $POP_i$  or population of exporter country, increasing number of population in this developing countries have positive impact to total export.
4. Test composed result that high levels of income in export indicate high level of production, which increases the availability of goods for exports.
5. For  $GDP_j$  or GDP of importer country has positive relationship with export. The purchasing power to import product will increase if the income

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