The Trans-Pacific Partnership Negotiation

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The Trans-Pacific Partnership

Looking Ahead to Next Steps

Deborah Kay Elms, Director, Asian Trade Centre in Singapore

THE UNFINISHED BUSINESS IN THE END GAME

After more than four years of negotiations, officials have been scrambling to conclude the Trans-Pacific Partnership (TPP) among the current 12 participating members: Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States, and Vietnam. After dozens of rounds of very complex bargaining across an expanding set of members, negotiators are down to the final political decisions on how deep, wide, and ambitious the TPP agreement will ultimately become.

Most of the final sticking points could have been (and were) predicted at the outset of the negotiations. Rather than rehash specific problem areas, such as sugar, dairy, rice, intellectual property rights, or the environmental chapter (Elms 2013a, Schott et al. 2013), the focus here is on some of the broader issues that remain in the negotiations.[1] This chapter discusses the context of the negotiations, the concept of a "living agreement," and the importance of creating a TPP Secretariat, and it engages in a discussion of future admission procedures for new members.[2]

These broader issues are likely to be critical to the future success of the TPP. Many of these ideas were discussed at length at the very outset of negotiations, starting in March 2010 in Melbourne. However, once officials began getting serious about the technical issues, most of the deeper concerns fell by the wayside. As officials limp toward the finish line, the urgency in finding creative solutions to these far-reaching aspects of the agreement has only increased.

THE CLUSTER APPROACH

One of the biggest challenges in getting the TPP to reach the highest aspirational goals of the "twenty-first century, high quality" agreement set forth from the beginning has been prodding trade officials to think as broadly as possible about the implications of their actions. Since the TPP-12 has been so active in negotiating free trade agreements (FTAs) in the past, many of the officials involved view the TPP as just another trade agreement, albeit one that is bigger and harder to negotiate than many of the others.

In the initial round of negotiations in Melbourne, officials wanted to think creatively. Rather than split themselves into traditional "chapters" for discussions (goods, services, investment, intellectual property, etc.), they tried dividing themselves into clusters. These clusters were supposed to consider overarching themes that ran across multiple issue areas and that might better conform to the "real world" of business than past FTA practices. However, the cluster idea quickly broke down once the discussions started moved into substantive areas. Officials reached for the familiar settings of traditional chapters, and the whole "cluster" approach was rapidly abandoned.

The only exception was the "horizontal" chapter, where nearly everything new and innovative about the TPP was tossed. This included ideas such as fostering small- and medium-sized enterprises, encouraging supply chains, bringing about regulatory coherence, and all things related to development and cooperation.

A moment's reflection, however, will suggest that this approach was also going to be problematic. Placing all these diverse issue areas into

one basket left a handful of officials grappling with a wide range of topics and concerns. To compound the difficulties, these were all issues that had never before been addressed in a trade agreement—mostly because they were extremely tough to tackle. Now they were all bundled together and handed to one team.[3] It is therefore not particularly surprising that the results from the horizontal chapter will be deeply disappointing to many.

The efforts to assist small- and medium-sized enterprises quickly devolved into a website.[4] Much of the "meat" of the supply chain/business connectivity issues got pulled out and placed elsewhere in the agreement. This is fine, except that many in the supply chain industry, particularly those in logistics, have argued for years that the primary problem for supply chain operators is precisely that their issues fall in between ministries and, therefore, are never appropriately managed by anyone. The TPP was supposed to represent a rare opportunity to pull together a host of issues into one place and keep governments focused on this critical web of interlocking elements for business in the twenty-first century. By pulling these items out of their own special "chapter" and placing them back into various substantive chapters, such as goods or services, some of the synergies that were supposed to be unlocked by bundling them together will have been lost.

The regulatory coherence agenda may be the most disappointing of all. Whenever officials in the TPP have been asked about the twenty-first century components of the agreement, they cite regulatory coherence. The idea was that all the economies would try to harmonize standards in food, agriculture, and other areas if such a thing were possible. If not, they would at least try to accept as small a set as possible of compatible, multiple standards. As an example, if Economy A permitted a certain type of food safety inspection for apples, Economy B would be willing to accept this certification, even if their own apple inspection might be different. They would not be forced to harmonize standards to the same degree (which was seen as *too* ambitious), but they would go beyond what is typically found in an FTA—especially one with multiple parties.

The November 12, 2011, the Trans-Pacific Partnership Leaders' Statement highlighted regulatory coherence in particular, noting that members pledged to "work to improve regulatory practices, eliminate

unnecessary barriers, reduce regional divergence in standards, promote transparency, conduct our regulatory processes in a more trade-facilitative manner, eliminate redundancies in testing and certification, and promote cooperation on specific regulatory issues."

Such high ambition proved problematic to implement. It was especially difficult to get regulators from different ministries and agencies to cooperate with trade officials in the TPP around a broad agenda of increasing market access for members. In the end, the TPP chapter on regulatory coherence will be about the institutional framework for coherence. It will contain information on inquiry points and procedures for obtaining information and promoting transparency. It will not really discuss standards at all. Some of this material got put into the specific chapters on sanitary and phytosanitary standards (SPS) or technical barriers to trade (TBT). But in general, it proved too difficult to get regulators to cooperate in the TPP.[5] The final result will be much less ambitious and twenty-first century than the early rhetoric would have suggested.

A LIVING AGREEMENT

All is not yet lost. One of the best ideas of the TPP from the beginning was to create the TPP as a "living agreement." The idea gained momentum after officials observed problems in the World Trade Organization's (WTO) Information Technology Agreement (ITA), which was being renegotiated at the same time that the TPP was getting underway. In the ITA, the electronics sector was liberalized and unleashed tremendous growth, especially in Asia. However, officials soon came to recognize that it had a serious flaw—given the method of negotiations (a positive list), technology was only liberalized if it was included on the list (c.f., Beltz 1997, Lee-Makiyama 2011, Lin 2011). This meant that as new technology was developed, it was not automatically included for market opening. Over time, and in a rapidly evolving industry, the ITA became less and less relevant as fewer and fewer traded products were covered. Record players might be eligible, but not smart phones, for example. Getting economies to sit down and reopen negotiations also proved extremely difficult and tedious.

It is true that FTAs usually have a clause for regular reviews. However, in practice, such reviews are frequently not held or are largely superficial. Even when economies take the review process seriously, the revisions undertaken generally consist of changes to the legal language of the document to bring sections into conformity with one another, or to try to bring different FTA provisions into compliance with one another. But periodic reviews have not, so far, been used for major renegotiations of an FTA.

Officials are not oblivious to these problems in other agreements. There are generally two different approaches taken to avoid creating obsolete commitments in "modern" FTAs. First, officials try to negotiate on the basis of a "negative" list. This approach means that new sectors are automatically opened for partner preferences, unless members specifically meet and declare reservations to opening the sector. The TPP uses a negative list for both services and investment, partly as a mechanism for remaining relevant in the future without the need for complex revisions to the agreement. It ensures that new industries and sectors are automatically opened for investment or foreign competition.

Second, most next-generation FTAs have complex committee structures built into their agreements from the beginning. The parties may agree to create a general trade committee that meets every year or every two years. This is supplemented with specific committees on goods, services, investment, government procurement, and so forth. These subcommittees or working groups are also scheduled to meet regularly—often every two years.

However, while these committees have made arrangements to meet, the actual practice of holding consistent, productive meetings has yet to be seen. In many of the latest generation of FTAs, it is frankly too soon to tell how well these committee structures will work because many have only just been completed and no reviews have been held. If there is an obvious flaw in the agreement, the committees will allow the parties to correct the problem. But modifications or improvements to the agreement to make it work better overall are less likely to happen. In most cases, committee meetings will probably be short affairs attended by junior staff.

Recall the promiscuity of many TPP members, as they signed multiple FTA agreements. Chile has agreements with 60 economies. By the

time it joined the TPP, Mexico had 12 FTAs linking 44 economies. By 2013, Singapore had 20 agreements, with another 5 under negotiation. Many of these deals come with complex committee structures for management. In most of the TPP economies, some portion of their trade ministry officials could spend their whole careers just preparing for one FTA committee review after another.

Because of this, TPP officials suggested a slightly different approach early on in the talks. This FTA would become a "living agreement." This meant that it would not just be opened for annual reviews. Instead, it would be up for regular and ongoing discussions and revisions going forward. In this way, the TPP would never be out of date.

From an institutional perspective, a benefit of a living agreement is that TPP member economies would dedicate specific individuals to oversee and monitor their TPP commitments. The TPP would not just be examined in the every-two-years committee period.

A living agreement could, for example, take the rather limited framework for regulatory coherence in the original TPP document and, over time, turn it into something much more substantial.[6] Regulators from across the TPP economies could engage in ongoing meetings and become accustomed to coordinating their regulations with one another before proceeding with changes that might impact the membership. New elements like sub-federal–level entities or states could be added to the government procurement commitments relatively easily under a living agreement provision. Reservations in specific service sectors or subsectors could be removed over time without requiring a wholesale renegotiation of the agreement.

The idea of the living agreement was discussed at length early on in the TPP negotiations. It was then largely dropped from conversations for most of the next three years while officials moved on to more substantive conversations about specific chapters. At the time of the endgame negotiations in 2014, it is not clear whether the idea will survive at all, or whether it will simply be a puffed up or enhanced version of the regular FTA review mechanisms.

A TPP SECRETARIAT

If it is to survive and be meaningful, a living agreement cannot be managed without a robust secretariat dedicated to supervising the TPP agreement. The intention of the TPP is to continue to expand in the future—at least in terms of membership. If the living agreement idea gains traction, the issue areas and coverage of the agreement will also increase over time.

Even if it does not expand any further, the TPP includes nearly 30 chapters and 12 member economies. Many of the rules go well beyond anything promised in the WTO or other FTAs. Commitments will be phased in over the implementation period(s), with different start dates likely for many members. This will add to the complexity of administering the agreement.

The TPP will require a dedicated staff to monitor implementation and reach out to the business community in each of the member economies. Otherwise, the provisions negotiated at great cost and difficulty through so many years are likely to be underutilized.

For example, many of the commitments in the agreement go well beyond obligations made in the WTO. This will make it impossible to use WTO dispute settlement for many issues in the TPP. Like most FTAs, the TPP has its own dispute settlement mechanism (DSM). However, unlike most FTAs, the TPP DSM has been designed to be actively used. Managing dispute cases will require an institutional structure. If the DSM picks up momentum over time, the case load could increase. It might even be possible to imagine a scenario under which the TPP develops a standing dispute system (more similar to the WTO).

Even leaving dispute settlement aside, such a complicated agreement cannot be managed by trade officials in the Asia desk, as in many other bilateral FTAs. Existing regional FTAs do not extend nearly as far, nor do they include such deep, behind-the-border commitments. The fact that these FTAs have worked without a secretariat is not a convincing argument for managing the TPP in the future. As it stands, many TPP officials have already complained about the difficulties of coordination in the negotiation stage.

Some have suggested that the APEC Secretariat could be used as the TPP Secretariat. After all, the TPP is officially one of the four possible pathways to the Free Trade Area of the Asia-Pacific (FTAAP) for APEC.[7] So far, all TPP members are also APEC members. The accession clause for the TPP privileges APEC members as well.[8] Leaving aside the issue of whether or not the TPP might eventually become the FTAAP, let us focus instead on whether or not the APEC Secretariat could do double-duty as the TPP Secretariat as well.

There are at least three reasons why using APEC is problematic. First, APEC's own statement of purpose is to "serve as an incubator of ideas." This function would be lost if the secretariat were to become somehow divided between staff responsible for monitoring the TPP, and staff incubating ideas in a nonbinding manner. APEC already has a very complex organizational structure of its own, and an extremely small secretariat staff to manage hundreds of meetings and thousands of participants in a rotating set of locations.

Second, not all of the APEC members are also members of the TPP. It is highly likely that the non-TPP members of APEC would find the suggestion to convert APEC into the TPP Secretariat quite objectionable. Even if only a portion of the APEC Secretariat was kept busy with TPP tasks, it would run the risk of diluting the non-TPP portion of the agenda.

Third, two of the possible pathways to the FTAAP are currently in play—the TPP and the Regional Comprehensive Economic Partnership (RCEP). The RCEP involves 16 parties in Asia, and may also need a secretariat at some point in the future, depending on if this agreement also progresses to become a kind of deep integration effort similar to the TPP. But this would mean that the APEC Secretariat would effectively be split into three different elements—a nonbinding ideas hub in APEC, the deeply ambitious TPP, and the (slightly?) less ambitious RCEP.

It is possible to argue that, in the long run, these functions might merge again in the FTAAP. In the meantime, the costs involved in setting up the institutional structure of a TPP Secretariat could be significant. However, even if the TPP eventually evolves into the FTAAP, such an outcome is likely to be well over a decade (and more likely two decades) away. In the interim period, businesses could

substantially benefit from a strong institutional structure to effectively implement the complicated TPP agreement.

In short, using the APEC Secretariat as the TPP Secretariat is a poor idea. The two ought to coordinate, but they must remain separate to provide the best service to both institutions. The TPP needs its own dedicated secretariat to manage this complex, binding agreement.

ACCESSION OF NEW TPP MEMBERS

In addition to the institutional issues around a secretariat, another broader, long-term issue that must be sorted out prior to closure of the TPP agreement is the procedures for accession of new members. Under the current "rules," new members have been admitted after first applying to the current members. Each prospective member must then engage in a series of bilateral meetings to discuss possible irritants in the relationship that may prove problematic for the group as a whole. These issues may require resolution or progress toward resolution prior to entry to avoid having them interfere negatively on negotiations with others. Finally, the whole TPP membership has to collectively approve the new member for admission. New members must then wait for final domestic procedures to be completed before they are allowed to see the negotiating texts and formally sit down with other members at the table.[9]

A further informal provision introduced when Canada and Mexico joined in late 2012 prevented new members from "reopening" any closed chapters or provisions that had already been agreed upon by the existing members. Outstanding issues (those remaining in square brackets, which is how negotiators signal disagreements over specific points in a text) could be discussed and new issues tabled, but anything resolved could not be taken up again.

Taken as a package, these accession procedures suggest that, going forward, the next tranche of TPP members will have no room for negotiating on the TPP rules. New members will engage in bargaining over their own market access commitments in goods, services, investment, government procurement, and so forth, but they will have no input into the rest of the document.

From the perspective of those who have just spent more than four years negotiating over every comma, clause, and paragraph in the existing agreement, such provisions make a great deal of sense. They do not see any need for new members to be able to reopen any portion of the document that was finally nailed down. After all, many probably feel that the agreement was open to new members (particularly from APEC economies) at any point starting in 2008. If any new economy had wanted to enter at the negotiating stage, they could simply have put their hand up, gotten in, and negotiated for whatever priorities they might have wanted.

However, a lack of flexibility collides with one important political reality. The TPP would be substantially strengthened if China—currently with world's second-largest economy—enters. After all, one of the most important factors driving this mega-regional is the opportunity to knit together global value chains in a seamless trade agreement that contains not just tariff reductions but also substantial behind-the-border provisions. Since many of the presumptive second tranche of members, such as China, South Korea, Hong Kong, and Chinese Taipei, are deeply enmeshed in value chains across the Asia-Pacific region, getting them into the TPP would provide significant economic benefits (Wignaraja 2013; Baldwin and Kawai 2013; Petri, Plummer, and Zhai 2012).

For China, in particular, joining the existing TPP with no opportunity at all for discussing any of the existing provisions may present political difficulties at the domestic level. This suggests that current TPP members would be wise to think carefully about a mechanism that would apply specifically to the first batch of new entrants in the next tranche of negotiations. To write into the agreement that accession terms are to be negotiated later with each new entrant will be unacceptable to many. Some sort of clarity, therefore, is needed on what sort of accession provisions will be required of new aspirants.

One suggestion is that officials think creatively now about a clause that gives certain measures of flexibility to the first set of members entering the TPP. Such a clause will not allow a wholesale rewriting of the agreement, but might allow for some modest changes, or perhaps participation in writing new rules or new chapters. Done carefully, it would

satisfy the demands for new members to put their collective stamp on the agreement, while not prolonging new negotiations.

Such a mechanism would also encourage any economy considering membership to declare its interest. This would have the added benefit of getting all potential new members into the deal at the same time. The alternative could be to add new members on an ongoing and regular basis, which would be deeply problematic.

Some sort of clause in the agreement that privileges entrants in the first wave of new applicants could be extremely helpful in pushing TPP expansion in the near term. The clause does not need to allow wholesale changes to the existing text, but some ability to show flexibility may be necessary to encourage new entrants. Otherwise, entry becomes a "take it or leave it" proposition and increases the risk that prospective members may opt to "leave it."

CIRCLING BACK TO THE LIVING AGREEMENT

Managing revisions is tricky, of course. It also comes with one final caveat for officials. Although there are some strong incentives to create a living agreement overall that allows for general flexibility and improvements to the document going forward, there is at least one challenge to be addressed. For economies that require a ratification procedure for approval of the TPP, there is, presumably, some threshold level of change than cannot be exceeded in the document before it triggers a new ratification process. In other words, it remains to be worked out how much change can take place within the TPP in terms of revisions to the text, rules, schedules, commitments, new members, and so forth without going back to member-state domestic procedures for ratification. These conditions should be specified as clearly as possible in advance of closing the agreement so that members know what to expect from one another in the future.

CONCLUSIONS

Pressure has been building for closure of the TPP. Getting the deal done is important. The economic benefits from this 12-party agreement are likely to be substantial. But the TPP is not just another FTA. It represents the chance to set a trade agenda for the future across a wide range of topics for economies throughout the Asia-Pacific region. This means that the agreement should not be settled in haste. More importantly, it also means that key decisions need to be reached about broader issues related to the institutional structure of the TPP. These decisions must be made now, before the deal is closed, on issues such as creating the TPP as a living agreement, setting up a TPP Secretariat, and clarifying entry conditions for future members. These choices must be made deliberately and carefully, even while officials are struggling to get closure on the most highly sensitive issues remaining in settling the agreement. It will not be easy, but wise decisions are necessary now to ensure the long-term success of the TPP.

NOTES

1. To show how deep and enduring the sticking points have been in these talks, the book by Lim, Elms, and Low (2012) is likely to have highlighted nearly every problem area still contested in October 2013, although the book was completed by the team of authors very early in 2012.

2. See also a longer version in "The Trans-Pacific Partnership Agreement: Looking Ahead to the Next Steps," Asian Development Bank Institute Working Paper Series, No. 443, December 2013.

3. Of course, officials will quickly argue that they had other individuals they could engage as resources whenever and wherever needed. But I believe that history will show that most of the teams on the horizontal chapter managed the bulk of the details on their own.

4. And, I would argue, this is even worse than it sounds—unless the TPP creates a meaningful secretariat, such a website will rapidly collapse since no one will be responsible for maintaining it.

5. If the living agreement idea takes off, this may not be a fatal blow, as regulators would meet regularly to discuss changes and, perhaps, move toward harmonization.

6. Other than the European Union, perhaps the closest trade agreement to a "living" agreement idea is the Australia–New Zealand Closer Economic Relations (Leslie and Elijah 2012). Another potential model might be APEC itself, where commitments made by member states evolve over time. The difference, of course, with APEC is that APEC is not binding.

7. The others are what is now called the Regional Comprehensive Economic Partnership (RCEP) or ASEAN-Plus-Six, consisting of the 10 members of ASEAN plus China, Japan, South Korea, India, Australia, and New Zealand; ASEAN-Plus-Three; and "other."

8. The relevant clause is drawn from the original P4 agreement and reads, "The Agreement is open to any APEC economy or any other State (Article 20.6), subject to terms to be agreed among the Parties."

9. In practice, this basically means that if a new member did not have clearance from the US Congress in the form of existing coverage under trade promotion authority (TPA), the new member had to wait for the Office of the US Trade Representative (USTR) to inform Congress of the intention to begin negotiations. New members then wait 90 days for comments inside the United States before US domestic procedures were considered concluded. For the existing members, Malaysia already "had" approval under a stalled bilateral negotiation and could join the talks almost immediately, but Japan, Mexico, and Canada did not and had to wait 90 days before entry. This was true even though TPA technically was expired, since the USTR was acting "as if" TPA rules were in place for TPP negotiations. For details on what is now called TPA, see Destler 2005, Fergusson et. al., 2013.

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2

Japan's Approach to the TPP

Masahiro Kawai, Project Professor, Graduate School of Public Policy, University of Tokyo

INTRODUCTION

Japan joined the Trans-Pacific Partnership (TPP) negotiations in July 2013 despite strong opposition from the domestic agricultural lobbies. Since then, it has been negotiating on trade and investment rules with other member economies multilaterally, and on trade liberalization measures with other members, particularly the United States, bilaterally. The TPP is expected to be a comprehensive, high-quality, twenty-first century free trade agreement (FTA), which covers 21 areas—market access, rules of origin, services, investment, intellectual property rights, competition policy, government procurement, the environment, labor, and other areas. These are truly twenty-first century issues needed to support supply chains developed in the Asia-Pacific region.

The TPP is important for Japan, and will help to achieve economic recovery after two decades of stagnation and to restore sustained growth. It is part of the "Abenomics" growth strategy. In addition, pursuing the TPP is consistent with Japan's economic partnership agreement (EPA) policies toward East Asia through the Regional Comprehensive Economic Partnership (RCEP), and toward the EU through the Japan-EU EPA. The TPP and the economic partnership agreements attempt to

further connect Japan with the major centers of the world economy and, thus, to generate significant economic benefits for Japan.

This paper attempts to answer several key questions: What is the progress so far from the Japanese perspective? What are important challenges for Japan to successfully complete a TPP agreement? What is next after the TPP?

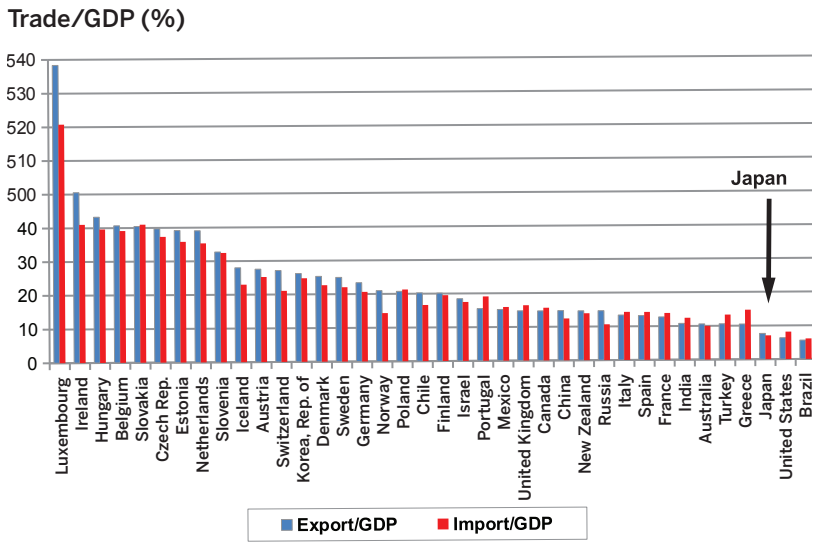
JAPAN'S ECONOMIC CHALLENGES AND TRADE POLICY STRATEGY

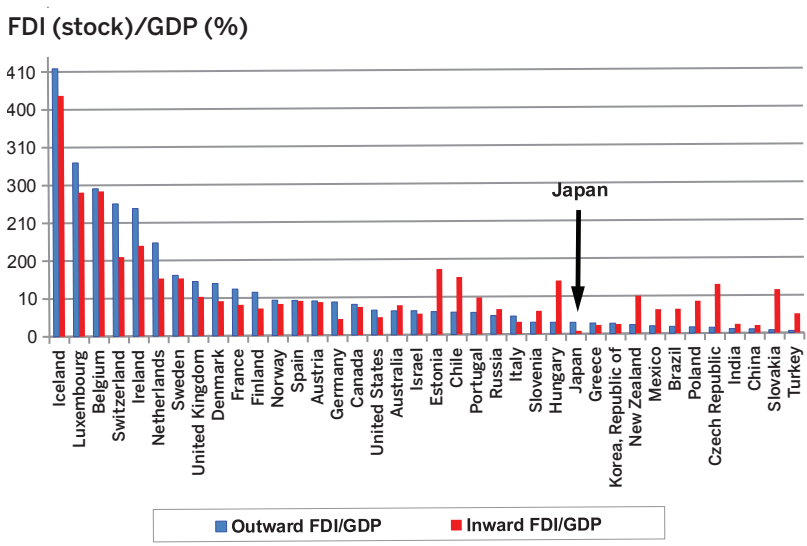
The Japanese government considers it vital for the economy to recover from two decades of economic stagnation. Without growth, Japan cannot solve various important problems, such as securing and expanding employment, maintaining a reliable social security system in an aging society, and reducing public debt to a sustainable level.

From international comparative perspectives, the Japanese economy has been relatively closed in terms of trade and foreign direct investment (FDI). Figure 1 demonstrates that Japan's trade (both exports and imports) and FDI stock (both outward and inward), measured as a ratio of GDP, are low. This suggests that Japan can further open its economy and integrate itself with the global market and to enhance its growth potential.

Traditionally, Japan has been trading with and investing in the United States and Europe. But in recent years, its trade and FDI relations with emerging economies in Asia have deepened. Japanese multinational corporations (MNCs) were the first that developed extensive production networks and supply chains throughout emerging Asia, helping to create "factory Asia" through advanced technological capabilities. Figure 2 shows that Japan's trade dependence on China has been rising rapidly, as have fears of overdependence on China and the perceived "China risk."

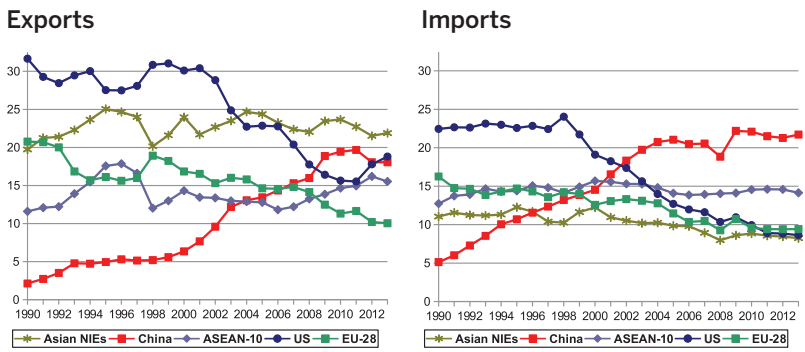
As a result of heavy investment in Asia's emerging economies, Japanese firms have accumulated sizable FDI stocks in emerging Asia, which have exceeded those in the United States and Europe (see Figure 3A). Figure 3B demonstrates that the computed rate of return on FDI is higher in emerging Asia—with the exception of those years immediately following the Asian financial crisis—than in the rest of the world.





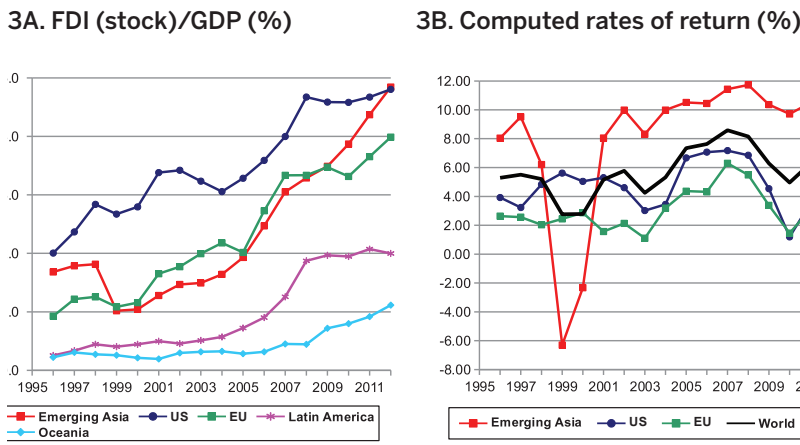
Source: International Monetary Fund, International Financial Statistics; United Nations Conference on Trade and Development.

FIGURE 1 *Japan's Trade/GDP and FDI (Stock)/GDP Compared Globally*



Source: International Monetary Fund, Direction of Trade Statistics.

FIGURE 2 *Geographical Distribution of Trading Partners for Japan's Trade (%)*



Note: Computed rates of return on FDI are obtained from the stock of FDI and investment income flows reported in the balance of payments.
Source: Bank of Japan.

FIGURE 3 *Global Comparison of Japan's FDI (Stock)/GDP and Computed Rate of Return*

This suggests the continued importance of emerging Asia for Japanese businesses.

Given that mature markets in the United States and the EU remain important for Japanese MNCs, and that emerging Asia has been

growing rapidly, it is natural for Japan to focus its trade and FDI policies on strengthening economic ties with the United States, the EU, and emerging Asia.

Japan's Trade Strategy

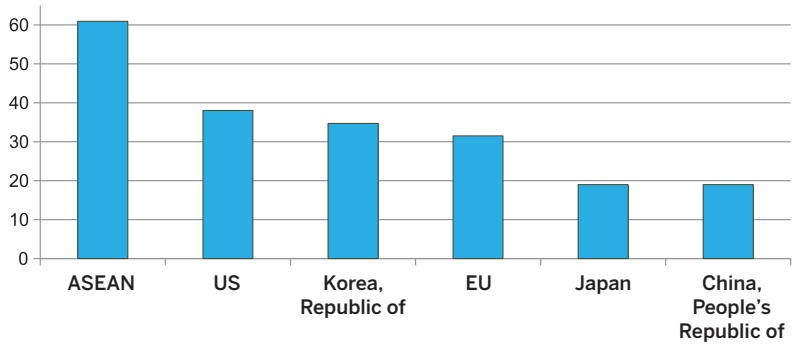
Japan had long taken a policy of liberalizing trade through the GATT/WTO. In about 2000, however, Japan shifted from a WTO-only approach to a multi-track approach that uses both the WTO process and economic partnership agreement (EPA) policies.

So far, Japan has implemented 13 EPAs with 1 region (ASEAN) and 12 economies (7 ASEAN economies, Mexico, Chile, Switzerland, India, and Peru). Japan has just concluded an EPA with Australia and is now under official negotiations with Canada, Colombia, the EU, the GCC, and Mongolia, as well as with other ASEAN-Plus-Six economies (for a RCEP), China and South Korea (for a trilateral EPA), and 11 Asia-Pacific economies (for the TPP).

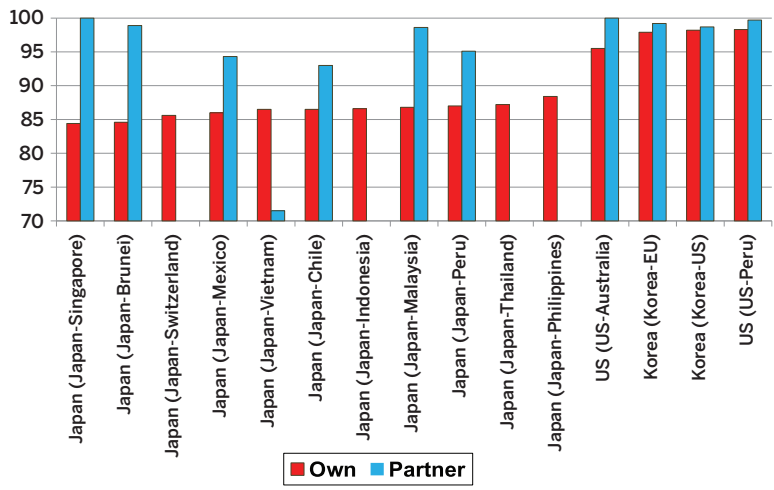
Until recently, several problems have stymied Japan's EPA approach. One problem has been the low trade coverage of its EPA partners, which at only 19 percent is lower than other developed economies (see Figure 4A). This reflected the fact that Japan had never forged EPAs with its major trade and FDI partners—the United States, the EU, and China. Recent efforts to start negotiations on the TPP, the Japan-EU EPA, the China-Japan-Korea FTA (CJK FTA), and the Regional Comprehensive Economic Partnership (RCEP) are potential solutions for addressing this problem. Indeed, these EPAs provide excellent opportunities for Japan to further connect with the United States and the Pacific side of Latin America, the EU, and China. They will also help Japan in achieving greater openness in its economy and greater diversification of its trade and FDI relationships.

Another problem has been that Japan's FTA/EPA liberalization ratio has been low, in the range of 84 percent to 88 percent (see Figure 4B). This is in sharp contrast with the liberalization ratios of most of its trading partners. For example, the United States, the EU, South Korea, Malaysia, and a few others have consistently achieved liberalization ratios of more than 95 percent. The low liberalization ratio in Japan is a result of protecting too many products, mainly in the agricultural sector.

4A. FTA/EPA trade coverage ratio (%)



4B. FTA/EPA liberalization ratio (%)



Note: The FTA/EPA trade coverage ratio is trade with FTA/EPA partners as a ratio of total trade. ASEAN data include intra-ASEAN trade, while EU data exclude intra-EU trade (if intra-EU trade was included, the ratio would be 76%). The FTA/EPA liberalization ratio is the number of tariff lines to become zero in ten years as the ratio of total number of tariff lines. Source: Calculated from International Monetary Fund, Direction of Trade Statistics; Cabinet Office, Government of Japan.

FIGURE 4 *Characteristics of Japan's EPAs: International Comparisons*

The elimination of tariffs has been hampered by policy considerations toward the agricultural sector, which has been regarded as internationally noncompetitive and in need of tariff protection. An important challenge for Japan is how to strengthen productivity and competitiveness of its agricultural sector so that it could withstand pressures from greater market opening and see eventual elimination of tariffs.

HIGHLIGHTS OF THE TPP

The TPP is often characterized as a comprehensive, high-quality, twenty-first century free trade agreement (FTA). This means that it aims to eliminate all tariffs in principle, and includes trade and investment rules that strongly support international supply chains. Twelve APEC economies are currently negotiating on the TPP, and South Korea, the Philippines, and Thailand may join in the near future. The negotiations cover 21 areas (with 29 chapters), including market access to goods (tariff elimination), rules of origin, services, investment, and so forth.[1]

One of the distinct features of the TPP is the diversity of its negotiating members, which include developed and developing economies, as well as agricultural exporting and importing economies.[2] Reaching a meaningful, high-quality agreement among them has been a difficult task, though some progress has been made. The most contentious issues have been market access, intellectual property rights (IPR), competition policy (particularly state-owned enterprise [SOE] reform), government procurement, investment (particularly the investor-state dispute settlement [ISDS] system), the environment, and labor. Table 1 provides a summary of the issues and different views among the negotiating members.

Market access issues are negotiated bilaterally between a pair of economies under the TPP framework.[3] The most serious bilateral negotiations have been taking place between the United States and Japan. Japan has been aggressive about opening US markets for manufactured products, particularly automobiles and home electric appliances, while it is defensive about protecting its own agricultural product markets. As another example, Vietnam has been aggressive about opening US markets for textiles, while the United States has been defensive.

TABLE 1 *Contentious Issues in TPP Negotiations as of June 2014*

Areas	Economies most involved	Issues
Market access	US vs. JPN	The US claims that Japan's tariffs on agricultural products should be substantially reduced. Japan claims that auto tariffs in the US should be eliminated.
Intellectual property rights	US (JPN) vs. MAS & VIE	The US claims that data for pharmaceutical products and copyrights (for novels, movies, music, etc.) should be protected for a long period, while Malaysia and others claim that such protection should be for a short period.
Competition policy	US (AUS, JPN) vs. MAS, VIE, BRU	The US claims that policies that favor SOEs (such as subsidies) should be abolished to establish a level playing field against private firms, while Malaysia and others argue against such a claim.
Government procurement	SIN (US, JPN) vs. MAS, VIE, BRU	Singapore and others argue that government procurement should be opened to foreign firms, while Malaysia and others are reluctant.
Investment	US (JPN) vs. AUS (NZL, MAS)	The US and others argue that an investor-state dispute settlement (ISDS) system should be introduced, while Australia and others are against it.
Environment	US (CAN, JPN) vs. VIE, MAS	The US and others argue that environmental standards for firm activity should be improved, while Vietnam and others are reluctant.

Note: AUS=Australia, BRU=Brunei, JPN=Japan, MAS=Malaysia, NZL=New Zealand, SIN=Singapore, US=United States, VIE=Vietnam.
Source: Compiled by the author from various sources.

Trade and investment rules are negotiated multilaterally among all economies. On IPR issues, the United States currently protects data for new pharmaceutical products for five years (as do Malaysia, Vietnam, Australia, and New Zealand) in principle, but insists that the protection period should be lengthened to 10 years. On copyright protection for novels, movies, and entertainment products, the United States argues for the protection period to last for 70 years (as done in the US, Singapore, Australia, Chile, and Peru), while Mexico protects for 100 years

and other economies (Japan, Malaysia, Vietnam, New Zealand, Brunei, and Canada) offer 50 years of protection.

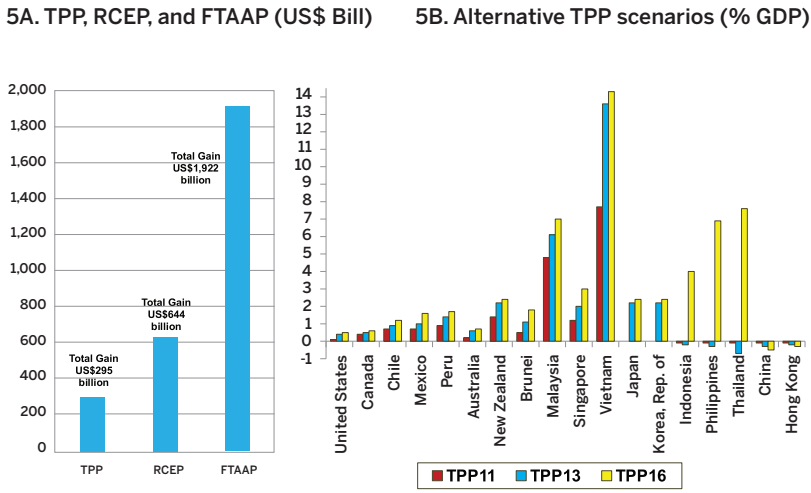
Ensuring a level playing field in markets where state-owned enterprises (SOEs) have significant presence is also a contentious issue. Malaysia and Vietnam are vehemently resisting US demands that SOEs should stop receiving favorable treatment from the government. The Malaysian government claims that such reforms would force it to reconsider its long-standing policy of promoting indigenous Malays and, thus, could change the foundation of the society.

Government procurement is another sensitive area. Economies that have opened procurement processes in their central governments and, at least partially, in their local governments include Japan, the United States, Australia, Canada, and Peru. Economies that have opened their central government procurement to foreign firms are Mexico, Chile, New Zealand, Singapore, and Brunei.[4] For those economies that have not opened any procurement—namely, Malaysia and Vietnam—the challenges are significant.

Developing-economy members may need somewhat different treatments in most of these areas. For example, the protection period for data of some pharmaceutical products (to combat contagious diseases, for example) may have to be shorter in developing economies than in developed ones, as the former need low-cost generics. A sufficiently long period should be allowed for SOE reforms in developing economies. It is noted that Malaysia and Vietnam represent the interests of many developing and emerging economies, a role that China would play if it were a negotiating member of the TPP.

Income Gains under Alternative TPP Scenarios

A study by Petri, Plummer, and Zhai (2012) has examined the impact of the TPP and other scenarios on incomes of TPP member economies, as well as others. Figure 5A demonstrates that the TPP has a positive impact on world income, measured by the percentage change in 2025 from baseline scenarios, but that this impact is less than that of the RCEP and much less than that of a Free Trade Area of the Asia-Pacific (FTAAP). Thus, the study suggests that once the TPP has been agreed upon, APEC members should combine the TPP with the RCEP to forge an



Note: Effects of various FTA scenarios (TPP, RCEP, and FTAAP in Figure 5A; TPP-11, TPP-13, and TPP-16 in Figure 5B) on world income (5A) and on individual economies (5B) in 2025 in terms of percentage changes from baseline scenarios. TPP-11 excludes Japan, TPP-13 includes South Korea, and TPP-16 further includes Indonesia, the Philippines, and Thailand.
Source: Petri, Plummer, and Zhai (2012).

FIGURE 5 *Income Gains under Alternative Scenarios*

FTAAP, as this would generate higher income from a world perspective. Figure 5B shows that Malaysia and Vietnam, which are engaged in many contentious negotiations with the developed economies, will actually be big winners as a result of the TPP. They are advised to conclude the TPP by pursuing domestic reforms, which would lead to agreement on contentious trade and investment rules. In addition, the study shows that as membership grows, income gains for each member will also rise.

OPPORTUNITIES AND RISKS OF TPP FOR JAPAN

Japan decided to join TPP negotiations in July 2013 in the midst of extensive domestic debate. The business sector strongly supported partici-

pation in TPP negotiations, while the agricultural lobbies were strongly opposed to such a move. A central feature of Prime Minister Shinzo Abe's growth strategy, announced in June 2013, included economic partnerships such as the TPP.

Opportunities for Japan

As a key pillar of the growth strategy, the TPP can (1) stimulate foreign firms' investment in Japan; (2) increase Japanese producers' access to goods and services markets in member economies with whom Japan has not had EPAs, particularly the United States; and (3) provide more confidence for Japanese multinational corporations investing in member economies through more equal treatment of foreign investment and IPR protection in host countries. It also provides opportunities for Japanese small- and medium-sized enterprises to conduct business through simpler trade procedures and movements of business people.

But the largest intangible benefit for Japan would be that it could participate in designing trade and investment rules for the twenty-first century Asia-Pacific region. As the TPP is potentially a step toward an FTAAP, the rules under the TPP will likely form the basis for future common rules in the Asia-Pacific region.

The TPP can have other benefits as well. It can strengthen Japan-US political relationships and allow diversification of Japan's trade, given the fear of overdependence on China and the perceived China risk. It also rectifies Japanese firms' disadvantageous positions in the US markets relative to South Korean firms, which enjoy preferential tariffs. The TPP negotiations can induce China to be more firmly committed to RCEP negotiations, as well as push the EU to accelerate official negotiations on a Japan-EU economic partnership agreement. Finally, the TPP provides an opportunity to reform and strengthen Japan's agricultural sector in a fundamental way.

The advantageous position given to South Korean firms is worthy of further explanation. With the implementation of the South Korea-US (KORUS) FTA in January 2012, Japanese firms have become less competitive in the US market relative to South Korean manufacturers. South Korean firms now enjoy preferential tariffs in the United States (and in the EU with the implementation of the South Korea–EU FTA in July

2011), while Japanese firms do not. For example, Japanese car producers face a 2.5 percent tariff on automobiles and a 25 percent tariff on trucks, while South Korean producers face zero tariffs. Tariffs are levied on Japanese producers of bearings (9 percent), polyethylene and polyester (6.5 percent), and color televisions (5 percent), while their South Korean counterparts can export tariff-free. The TPP can correct this imbalance.

Initial Concerns about the TPP

While Japan's government decided to join TPP negotiations, various concerns were expressed by the public about possible negative consequences of the TPP.

First, the TPP would require the immediate tariff elimination on all products, thereby exposing domestic noncompetitive sectors—such as the agricultural sector—to fierce competition from abroad and resulting in the collapse of these sectors. If the agricultural sector is severely affected, food self-sufficiency would also be further reduced and food security threatened.

Second, the TPP would weaken the Japanese social security system, particularly its universal health and medical insurance system, because it would allow private firms to enter the medical industry (such as hospital management). In addition, higher protections of pharmaceutical IPR would lead to higher costs of medical drugs (such as generics). Critics argued that a private sector–driven health and medical system could create a huge divide between the haves and the have-nots, and reduce the quality of services to low-income people. According to them, this would not be consistent with the idea of a universal healthcare system. Compounding the problem, less-qualified medical professionals might immigrate from abroad, reducing the overall quality of medical services in Japan.

Third, insurance services provided by Japan Post Insurance (JPI) and cooperative credit institutions would be prohibited from receiving favorable treatment from the government, and would be required to behave as if they were private entities. The reason is that JPI, as a government-owned insurance provider, enjoys a number of statutory, regulatory, and other governmental privileges. Cooperatives offering insurance also enjoy business, tax, and regulatory advantages over foreign insurance providers, which would distort market competition with the private sector.[5]

The fear is that once these insurance providers stop receiving favorable treatments, people in local or remote areas might lose access to such services as a result of their transformation into private-like entities.

Fourth, the TPP would open local government procurement to foreign firms, shifting business opportunities away from domestic firms. It would allow foreign investors' legal disputes against the state to expand and might undermine national sovereignty. In addition, the TPP might also allow more imports of unsafe food because of relaxed food safety standards.

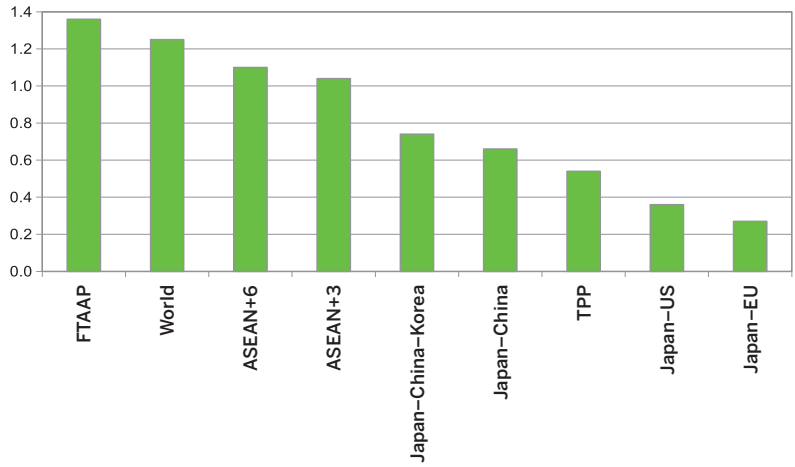
Most of these initial concerns were based on misinformation and/or misunderstanding of the TPP. As information on the bilateral negotiations between the United States and Japan has been revealed, most of these concerns have dissipated. However, concerns over the negative impact of the TPP on agriculture have persisted, and they deserve further attention.

Economic Impacts of the TPP on Japan

Government reports about the impact of the TPP on agriculture have been contradictory. The Ministry of Agriculture, Forestry, and Fishery (MAFF) emphasized serious negative impacts, while the Cabinet Office and the Ministry of Economy, Trade, and Industry (METI) reported positive impacts.

MAFF estimated that the TPP would cause significant damage to both Japan's agriculture and the overall economy. Under the assumption that all tariffs on agricultural imports were eliminated, the report found that agricultural production would decline by 4.1 trillion yen, the value of multifunctional agriculture would drop by 3.7 trillion yen, employment opportunities would be lost in the amount of 3.4 million jobs, and GDP would decline by 7.9 trillion yen. The food self-sufficiency rate would decline substantially, from 40 percent to 14 percent.

A Cabinet Office report (2010 supported by Kawasaki 2011) concluded that Japan's participation in the TPP, and its elimination of tariffs, would raise real GDP by 0.48 percent to 0.65 percent (see Figure 6).[6] It also found that Japan's nonparticipation in the TPP (while South Korea implemented FTAs with the United States, the EU, and China) would cause a decline of Japan's real GDP by 0.13 percent. The reason for this



Source: Kawasaki (2011).

FIGURE 6 *Benefits of Various FTA Scenarios for Japan (% of GDP)*

is that Japan's exports and production of automobiles, electric and electronic products, machinery, and other manufacturing goods will decline, as firms in these sectors lose market shares in the United States, the EU, and China due to competition from South Korean firms. These negative impacts on the manufacturing sector would be large if Japan did not participate in the TPP.

An analysis conducted by METI showed that Japan's failure to participate in the TPP and conclude EPAs with the EU and China (while South Korea implemented FTAs with China in addition to the United States and the EU) would reduce Japan's real GDP by 1.53 percent in 2020, relative to the benchmark case. There would be a loss of 812,000 jobs. Japan's exports, production, and GDP would all decline.

An additional finding was that Japan's participation in the TPP would make a notable difference to some Asian members, particularly Vietnam and Malaysia. The reason for this is that the economic size of Japan is large enough to create additional benefits to smaller developing economies. Thus, Japan's participation in the TPP benefits not only Japan, but also developing member economies in Asia.

PROGRESS ON THE TPP NEGOTIATIONS

The most difficult issue for Japan in its bilateral negotiations with the United States has been the tariff reduction of agricultural products, particularly pork and beef. The second difficult issue is the auto market in both Japan and the United States. The results of bilateral negotiations between the United States and Japan are important for the TPP negotiations as a whole, given that the combined GDP of the two economies accounts for more than 80 percent of the total GDP of all negotiating members.

Tariff Reductions on Agricultural Products

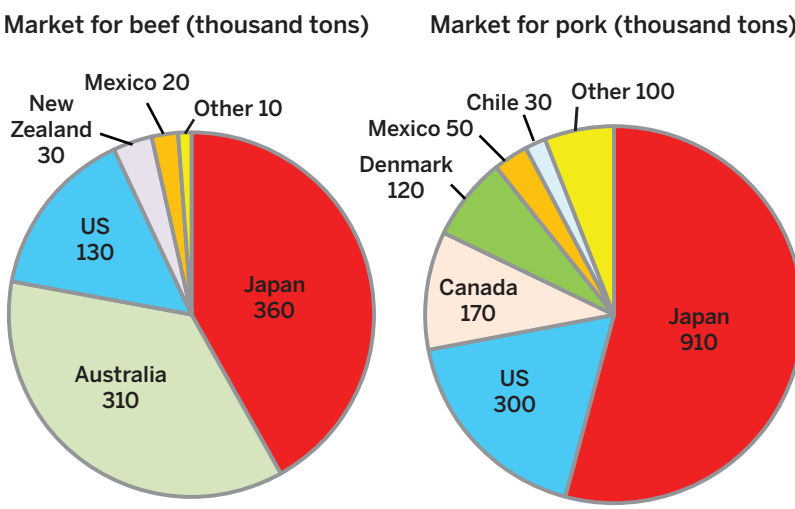
The Japanese government identified five critical product categories to be protected from tariff elimination. These were rice, wheat, beef and pork, dairy products, and sugar. The five categories include 586 tariff line products. Table 2 shows that there are altogether 9,018 tariff line products in Japan. Of these, 8,089 tariff line products have been subject to tariff elimination (with the maximum potential liberalization rate of 89.7 percent) and the remaining 929 tariff line products—including the five critical product categories (586 tariff line products) and other sensitive products (343 tariff line products)—have never been subject to tariff elimination.

The bilateral negotiations have revealed that the United States is not particularly interested in opening the Japanese rice market. Rather, it is interested in opening the pork and beef markets and, to a lesser extent, the dairy product market. The United States is the largest producer of beef in the world, and the second-largest producer of pork (following China). It exports about US$7 billion worth of beef and US$6 billion worth of pork. Japan is the largest importer of US pork. Figure 7 shows that in the Japanese beef market, Japanese producers are the largest supplier (accounting for 42 percent), followed by Australian (36 percent) and US (15 percent) producers. In the Japanese pork market, Japanese producers account for 55 percent of total supply, and the United States is the largest foreign supplier of pork, accounting for 18 percent of the market. For US producers of pork and beef, Japan is indeed one of the most attractive markets in the world.

TABLE 2 *Classification of Japan's Import Products*

Products that have never been subject to tariff elimination (929 tariff lines, 10.3%)	Five critical product categories (586 tariff lines, 6.5%)	Rice (58) Wheat (109) Beef (51) and pork (49) Dairy products (188) Sugar (131)	
	Other sensitive product categories (343 tariff lines, 3.8%)	Agricultural, forestry, and fishery products (248)	Fishery (91) Beans (16) Konjak (3) Prepared food (30) Plywood (34)
		Manufactured products (95)	
Products that have been subject to tariff elimination (8,089 tariff lines, 89.7%)			
Total number of Japanese imports (9,018 tariff lines)			

Source: Compiled by the author from various sources.



Source: Ministry of Agriculture, Forestry, and Fishery.

FIGURE 7 *Japanese Markets for Beef and Pork: Major Supplier Countries , 2012*

The United States and Japan have been negotiating intensively on the extent of tariff reductions, the time frame for tariff reductions, conditions for triggering safeguard measures, and use of low- or zero-tariff import quotas. Japan would like to protect their beef and pork producers by maintaining high tariffs, pursuing gradual reductions over long time periods (more than 10 years), and adopting easily usable safeguard measures.[7] In contrast, the United States would like to open the Japanese beef and pork markets by reducing tariffs as deeply and quickly as possible, and by constraining implementation of safeguard measures. It appears that it would not insist that tariffs be completely eliminated on the five critical agricultural categories, as long as US producers can meaningfully increase exports of their products.

In the case of rice and wheat, it is likely that the current high tariffs will remain, while Japan will introduce special tariff-free import quotas for US rice and wheat under private trading. For dairy products, Japan is considering setting up low- or zero-tariff import quotas on cheese. Sugar has not been discussed.

Thus, tariff reductions are expected for beef and pork, but tariff elimination is unlikely to occur. This poses a problem with regard to the liberalization ratio for Japan. To achieve a high liberalization rate, such as 95 percent or higher, tariffs need to be eliminated among the five critical product categories and other sensitive categories that have never been subject to tariff elimination. It turns out that of the five critical product categories (586 tariff line products), 181 tariff line products have not been imported over the 2008–2012 period, and can potentially be subject to tariff elimination. If the Japanese government can further identify 269 tariff line products for tariff elimination from these critical and sensitive categories, the liberalization ratio could reach 95 percent.

Japanese and US Automobile Market Issues

The United States has been insisting that the Japanese automobile market is closed. Figure 8 shows that Japanese automobiles account for 95.5 percent of the Japanese market, and foreign automobiles account for only 4.5 percent. In contrast, US automobiles account for 47 percent of the US market and Japanese automobiles account for 35 percent of the US market. The United States interprets these figures as an indica-

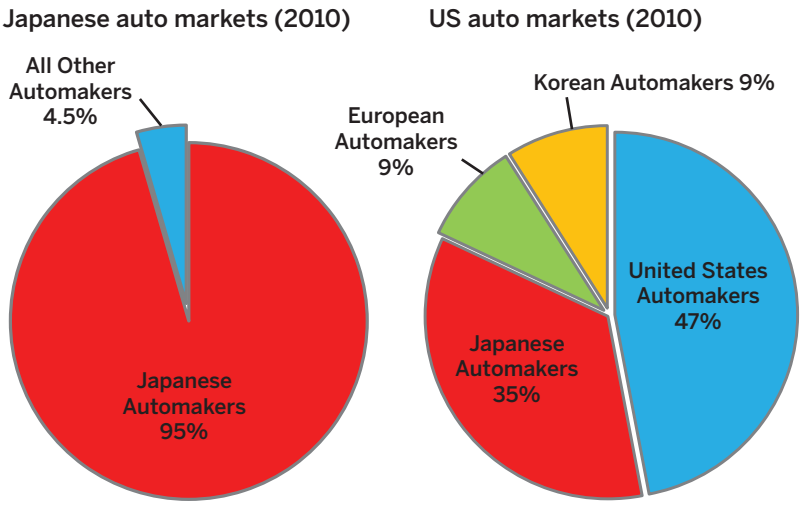
tion that Japan's automobile market is closed, while the US market is open. As Japan's tariff on auto imports is zero, the United States argues that nontariff barriers to trade are responsible. That is, Japan's automotive regulations—such as safety standards—make it hard for US autos to be imported. They argue that auto sector rules and regulations in Japan are often developed in a nontransparent manner without consultation with foreign producers. In addition, Japan provides preferential treatment to a specific car segment, the tiny kei (light) car, which is manufactured only in Japan. Japanese automakers, on the other hand, believe that the Japanese market is fully open, and wonder what the United States really wants. Although it seems to want Japanese safety standards to be relaxed and the preferential treatment of light cars to be dismantled, it is not clear whether US auto sales in Japan would expand even with these changes.

Japanese automakers would like to see auto tariffs in the United States (2.5 percent for automobiles and 25 percent for trucks) eliminated. The United States seems to be agreeable, but tariff elimination could take place over the longest possible time frame allowed under the TPP, such as 20 years. This is not an acceptable proposition for Japan.

CONCLUSIONS

Japan needs to further open its economy and integrate with the global economy, particularly the United States, the EU, and emerging Asia. The TPP, now led by the United States, aims to achieve high levels of openness among like-minded economies and is a key step toward an FTAAP, together with a RCEP. Japan can benefit from joining the TPP because it affords greater market access, protection of its investment abroad, enforcement of IPR rules, and attraction of foreign investment.

The bilateral negotiations between the United States and Japan have revealed that the TPP would not require immediate elimination of tariffs on all products, but that many exceptions could be allowed. Japan's rice tariffs will most likely remain untouched. The US auto market will likely achieve zero tariffs on Japanese autos, but over a long time period. These developments run counter to initial expectations of the TPP. Nonetheless, the progress that has been made should be valued highly.



Source: Japan Automobile Manufacturers Association for Japan's data; Automotive News Database 2010 sales for US data.

FIGURE 8 *Auto Markets in Japan and the US*

A major challenge for Japan to successfully complete the TPP is to improve the productivity and competitiveness of the agricultural sector, particularly beef and pork producers, through comprehensive reforms. Japanese authorities may consider changing the mode of protection away from border measures (such as tariffs and quotas) to domestic measures (such as income transfers) if agricultural protection is to continue long term. It is important for Japan to open the beef and pork markets to the maximum extent for the benefit of domestic consumers, and to see tariff elimination on autos in the United States within the shortest possible time frame. Another challenge is to remove or reduce behind-the-border regulations, which would also be required for a Japan-EU EPA.

The US negotiators must obtain trade promotion authority (TPA) to make sure that the TPP will be ratified without major problems and delays. Otherwise, other negotiating members might not be able to make maximum possible concessions as the US Congress could force renegotiation without the TPA.

Once the TPP is implemented, the Asia-Pacific economies need to connect the TPP with the RCEP to forge a greater FTAAP. This is likely

to take the form of an increasing number of RCEP members joining the TPP. In this sense, the TPP has the role of setting a benchmark that other developing and emerging economies, such as China, India, and Indonesia, will eventually accept.

The next step would be for member economies of the TPP and TTIP to work together to further connect the two mega-regionals, starting with the adoption of common trade and investment rules, particularly rules of origin. This would be a bottom-up approach to global integration that counterbalances the WTO's top-down, often poorly functioning approach. Hopefully, this process will put pressure on the WTO to restore its function of promoting global integration without discrimination.

NOTES

1. There is a discussion in the US as to whether the TPP should include a currency manipulation clause. Currency manipulation is said to be present when foreign exchange market intervention prevents currency appreciation in the presence of a large current account surplus.

2. In the case of the US-EU FTA, called the Transatlantic Trade and Investment Partnership (TTIP), negotiating members are all developed economies and relatively homogeneous. In this sense, given the diversity of WTO members, the TPP could be a model for future multilateral trade and investment liberalization. This model might be pursued by a future WTO, if the organization could be significantly reactivated and remodeled.

3. This means that any one country's agreed on tariff tables will not be common vis-à-vis TPP partner members. The US, Canada, and Mexico have taken the approach that each economy's tariff tables can be different depending on bilateral partners, which was essentially the approach adopted by NAFTA. Australia, New Zealand, and Singapore, on the other hand, take the view that each economy should establish common tariff tables vis-à-vis all TPP bilateral partners. The former approach can easily accommodate exceptional treatments vis-à-vis particular partners, while the latter approach tends to limit such treatments. Japan appears to prefer the former approach for agricultural products, and the latter for manufactured products.

4. Japan, the United States, Canada, and Singapore are signatories of the WTO Agreement on Government Procurement (GPA) of April 1994 (signed by 15 parties, including Hong Kong, South Korea, and Chinese Taipei in Asia).

5. As a result, the United States wants JPI not to provide new or modified products, such as cancer insurance, until level playing fields have been established between JPI and US insurance suppliers (like Aflac). JPI seems ready not to introduce new insurance products.

6. The Cabinet Office report also estimated the benefit of forming an ASEAN-Plus-Three FTA to be 1.04% of real GDP, the benefit of ASEAN-Plus-Six FTA to be 1.10% of real GDP, and the benefit of forming an FTAPP to be 1.36% of GDP. These are typically smaller than the Petri-Plummer-Zhai estimates.

7. When imports of a certain product surge in value within a short period of time, the importing country's government can invoke safeguard measures by applying high tariffs on the product.

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3

Canada and the TPP

Short-Term Tactics and Long-Term Strategy

Hugh Stephens, Vice Chair, Canadian National Committee on Pacific Economic Cooperation

There are valid questions about whether it will be possible to bring the Trans-Pacific Partnership (TPP) to a successful conclusion within a reasonable time frame, but Canada is firmly committed to—and needs—a successful outcome, despite its early ambivalence toward the agreement. There are still a number of difficult issues to be dealt with in the negotiations, made more complex by the addition of new participants such as Japan and the narrow room for maneuver of US negotiators, given the administration's lack of trade promotion authority (TPA) from Congress, and considerable congressional opposition to granting such authority. Given all these concerns, one might well ask: why was Canada so keen to join the TPP, and why is it so committed to the TPP now?

THE STAKES FOR CANADA

For Canada, the TPP is both an end in itself (that is, a vehicle for trade liberalization and job growth), and a means to an end, which is to reestablish Canada's economic credentials in the Asia-Pacific region

generally. The TPP is rightly seen as one of the vehicles that could become the foundation for a Free Trade Area of the Asia-Pacific (FTAAP). The other, at the moment, is the Regional Comprehensive Economic Partnership (RCEP) process, an ASEAN-centered plurilateral negotiation that includes all 10 ASEAN states, plus China, South Korea, Japan, India, Australia, and New Zealand. Canada and the United States are excluded. The Pacific Economic Cooperation Council (PECC) has estimated—based on economic modeling work done by Peter Petri and Michael Plummer—that a 12-economy TPP (including Japan) will lead to economic gains of US$295 billion by 2025. The RCEP will lead to gains of almost double that amount, totaling US$500 billion, owing in part to higher existing barriers in the RCEP economies that will be removed. The real payoff, however, comes with a combined TPP and RCEP in the form of the FTAAP, which will bring gains of US$1.9 trillion in 2025.

In addition to being a potential pathway to the holy grail of the FTAAP, the TPP has a very real significance for Canada beyond protecting its access to the US market. A key player for Canada is Japan. Japan's (and potentially South Korea's) entry into the TPP was a significant factor in Canada's decision to seek participation. Japan is Canada's fourth-largest export market, but much of Canada's exports to Japan compete directly with the United States. While Canada and Japan have launched bilateral negotiations, there is no guarantee that this process will be successful. It is important, therefore, for Canada to be at the TPP table with Japan, along with the United States, engaged in a process where the removal of trade barriers to the Japanese market is being discussed.

With a population of only 35 million, Canada learned a bitter lesson from its experience with South Korea, which lost interest in concluding a deal with Canada once the South Korea–US and South Korea–EU deals were completed. Canada, as a smaller economy, does not have the same negotiating leverage as the United States, yet obtaining access to the South Korean market for those Canadian products, such as pork and beef, that compete directly with similar or identical US products was an essential negotiating objective for Canadian officials. Canada's unwillingness to settle for second-best, combined with South Korea's lack of interest and opposition from some auto manufacturers based in Canada,

led to the current impasse. (Since the original date of writing, Canada and South Korea have successfully concluded their bilateral FTA, with agreement reached on March 11, 2014). Canada needs to avoid a similar outcome in its negotiations with Japan, where the attraction of the US market for Japan may trump interest in doing a bilateral deal with Canada. Recent indications of South Korea's willingness to join the TPP provided an added lever that Canada apparently used as a way to break the South Korea–Canada logjam.

CANADA'S DELAYED PARTICIPATION

When Canada was officially invited to join the negotiations in Los Cabos, Mexico, in June 2012, it marked (for Canada) an important milestone on what had become a long and tortuous road to participation. Canada's invitation came a day after the invitation was extended to Mexico, and the hitch in what was supposed to have been a simultaneous invitation demonstrated the difficulty that Canada faced in convincing the US administration—and some other TPP economies—that its presence would be a positive element toward a successful outcome. At the same time, it seemed to reflect the reality of Canadian ambivalence toward the TPP process.

The fact that Canada was not openly welcomed is somewhat surprising given its economic heft (by most counts, it is the world's tenth- or eleventh-largest economy) and its massive trading relationship with the United States. In fact, in his letter to Congress seeking approval for the administration's invitation to Canada to join the TPP negotiations, then US Trade Representative Ron Kirk noted that US exports to Canada totaled US$337 billion in 2011, the largest export market for US goods. He went on to say, "We have conducted in-depth discussions with Canada about the standards and objectives that the TPP countries are seeking, particularly in those areas where the standards and objectives are higher than those that exist in the North American Free Trade Agreement (NAFTA). Canada has assured us of its willingness to negotiate on these issues and its preparedness to achieve these high standards together with other TPP countries."[1]

But Canada was a latecomer, and had to work overtime to push its way into the negotiations. Its Asia credentials had lapsed. Although Canada has had a long history of engagement with Asia—going back to the days of the Colombo Plan in the 1950s, becoming an ASEAN dialogue partner in 1977, being a founding member of the Pacific Economic Cooperation Council (PECC) in 1980, and being a founding member of APEC in 1989—in recent years, it has neglected to maintain its previous level of engagement with Asia. Part of the reason can be blamed on a series of minority governments from 2004 through 2011, which resulted in a degree of political uncertainty and relative lack of interest in foreign policy and trade issues on the part of Canadian political leaders—other than in the war in Afghanistan, which became a significant political liability as Canadian casualties mounted. Even though Canada launched FTA negotiations with Singapore in 2001 and with South Korea in 2004, these negotiations did not make progress. When Canada was offered a chance in 2005 to join the then Pacific 4 (P4), the precursor to the TPP, it wasn't interested. Even after the United States breathed new life into what became the TPP, Canada's attention was elsewhere.

ROLE OF THE UNITED STATES

For Canada, the overriding policy issue has always been access to the US market. This was the driving motivation for the Canada-US FTA in 1989 that developed into NAFTA. Instead of focusing on the TPP negotiations, it was all too easy for Canadians to focus on the huge US market just next door. In addition, there were concerns in Canada that "sensitive" issues, such as supply management in dairy, would have to be addressed if it entered into talks with economies like Australia and New Zealand. Moreover, the United States had—and still has—ongoing concerns in Canada regarding a number of trade issues, such as its cultural exception, and Canada was concerned that these might be reopened. As a result, during the early phases of the TPP, Canada showed no interest. The 2008 global financial crisis changed Canadian attitudes, as it changed much else.

The slowdown in the US economy in the wake of the financial crisis, combined with the growing economic clout of Asia, became a wake-up call impossible to ignore. The business community was calling for bold moves to get Canada back in the game in Asia. The Conservative government of Stephen Harper had positioned itself as the party of economic growth and jobs, and—after a series of minority governments—it finally won a majority in 2011. Part of Prime Minister Harper's economic platform was to push for trade liberalization across the board. In May 2009, negotiations were launched with the EU on a Canada-EU Trade Agreement (CETA). Other initiatives followed: a bilateral framework was established with the United States to discuss border issues that impeded trade, and a full-court press was mounted to get Canada into the TPP. But despite Canada dropping broad hints that it would be open to an invitation to join the talks, the welcome mat was not rolled out. Apart from New Zealand's well-known antipathy to Canada's supply-managed dairy policies, the US response was guarded—and distinctly cool.

Several reasons have been advanced for the lack of enthusiasm on the part of the United States for Canadian participation. Despite their NAFTA partnership and the fact that the vast majority of Canada-US trade crosses the border without problems, there have been a number of bilateral disagreements. The United States may have felt that these issues would not be helpful additions to the TPP negotiating agenda. In the eyes of some in Washington, DC, Canada would be more of a hindrance than a help. One of the principal areas of concern was intellectual property (IP) rights protection, where US copyright industries were unhappy with Canada's weak copyright regime, as well as issues regarding the length of protection for pharmaceutical patents. There was no doubt concern that Canadian insistence on protecting its "cultural industries" could potentially contaminate negotiations with some of the other TPP economies in ways that would not be helpful to the United States. Finally, adding a new and potentially "difficult" partner part way through the negotiations would do nothing to speed up what was already becoming a protracted process. Canada was reluctant to openly profess interest lest it be publicly rebuffed. Finally, at the Honolulu APEC Summit in November 2011, Prime Minister Harper took the plunge (presumably after getting the signal that the United States would not oppose Canada's and

Mexico's TPP applications)[2] and declared the TPP to be a process "that Canada was interested in moving forward on." Canada's International Trade Minister Ed Fast was dispatched on a trans-Pacific odyssey of epic proportions, visiting all TPP capitals in the space of a few months. In each, he secured either supportive or benign statements regarding Canadian participation. This admirable demonstration of determination did not go unnoticed, and the effort to "surround" the United States by getting other partners on board was partially responsible—along with heavy Canadian lobbying of both government and business groups in Washington, DC—for securing the full support of the Obama administration and in successfully navigating the congressional approval process. Many US businesses with operations in Canada (and Mexico) were becoming concerned that the exclusion of their Canadian operations from TPP preferences could complicate supply chains. There was additionally the opportunity to update and complete some of the unfinished business of NAFTA. Canada could even be helpful in some areas, such as the controversial investor-state provision, given its experience with such a regime in NAFTA.

OPPOSITION IN CANADA

After the announcement that Canada would be joining the negotiations (once the necessary consultation with Congress had been completed), a vocal and active anti-TPP chorus emerged in Canada. This was fueled largely by those with a mistrust of trade liberalization generally (such as anti-WTO groups), but also because of the terms on which Canada was admitted—the so-called "take it or leave it" provisions. The "anti-just-about-everything" nature of the opposition was perhaps best summed up by a quote from the advocacy group the Council of Canadians. The TPP, said the group, "could lead to the dismantling of Canada's important supply management regimes for dairy, poultry, and egg production; the race-to-the-bottom potential in a proposed regulatory harmonization chapter; extreme intellectual property protections for big drug companies that would limit access to life-saving medicines; investor-state provisions that would allow companies to sue governments over rules

to protect the environment; government procurement restrictions, and copyright rules that undermine Internet freedom."[3] These same voices are now busy denouncing the Canada-EU Trade Agreement (CETA), on which agreement in principle was announced on October 18, 2013. That agreement maintained Canada's supply management system, but allowed for a doubling of European quotas for cheese; opened subnational government procurement to European companies; and extended the patent protection period for pharmaceutical drugs to partially cover the lengthy patent approval process.[4] The offset, of course, is improved market access for 35 million Canadians to a market of 500 million, including better access in the areas of automotive products, beef and pork, and financial services. The outcome of CETA offers some indications of where Canada may be prepared to make concessions in the TPP negotiating process, but these will necessarily be part of larger trade-offs.

TPP OUTCOMES

It seems clear that despite the high-blown rhetoric about TPP negotiating partners having to put everything "on the table," and talk of a "gold standard, twenty-first century" agreement, the reality will be somewhat different. Everything may in theory be on the table, but some things will fall off as part of the negotiating process. Don't expect US sugar quotas to go away, or Canada's supply management system to be dismantled, or Australia to sign on to investor-state provisions, or Vietnam to put its state-owned enterprises (SOEs) under full market discipline. Don't expect all the TPP economies to meet the sort of IP standards the United States would like, or US trade remedy laws to be made subordinate to a TPP dispute settlement mechanism. There is now talk in the US Congress of a "currency manipulation" provision being added to the agreement, a move that would surely be a deal breaker given the vagueness of definitions in this area, and the potential for misuse of such a clause.[5] On the other hand, if the TPP can achieve progress in a substantial number of areas by rationalizing the conflicting rules of origin that exist across the region and simplifying supply chains, strengthening investor protection generally and improving respect for intellectual property laws,

addressing e-commerce issues and opening services markets, it will have made a significant contribution to trade liberalization in the region.

The biggest gains will come from dismantling the import barriers that exist in the Japanese market. Their removal will benefit Japan significantly,[6] and will also bring important benefits to Japan's trading partners. Given the nature of the TPP negotiations, the bilateral US-Japan talks within the TPP framework will be critical to achieving the fullest possible economic gains for all members. Despite Japan's predictable reluctance to make any significant movement on key agricultural commodities, and ongoing US concerns over the balance in auto trade with Japan (concerns that are linked to the so-called "currency manipulation" clause favored by many members of Congress), the importance of achieving even a partial breakthrough in the US-Japan bilateral talks is critical if the US administration is to win trade promotion authority from Congress, and both the Obama and Abe administrations are acutely aware of this. The rest of the TPP partners are watching and waiting to see how and when the United States and Japan can resolve their differences, so that their own negotiations with Japan can be finalized. At that point, there is a reasonable prospect that the agreement will be able to proceed to its final phase.

The gains that Canada can expect to achieve from the agreement are dependent in large part on successfully opening the Japanese market, as well as the productivity gains that will accrue from opening its own market. Indeed, the Canadian Council of Chief Executives has published a study arguing the benefits of "unilateral disarmament" (i.e., unilateral removal of tariffs) for Canada, which it claims could generate CA$20 billion in economic gains, approximately five times the value of the CA$4 billion a year that Canada currently collects in customs revenues.[7] These gains would more than double the estimated gains to Canada from the TPP, using Petri and Plummer's calculations. Realistically, neither Canada nor any other TPP partner is going to unilaterally open its market, so gains will have to be based on the mutual concessions achieved within the TPP. The TPP started with a high level of ambition with regard to tariff removal, and the gains to be achieved will be significant as long as economies follow through on commitments to comprehensive coverage. Additionally, Petri and Plummer have pointed out that as much as 20

percent of additional gains will be brought about by investment liberalization through the increase of foreign direct investment (FDI) flows. Individual investment liberalization agreements, such as the one Canada has reached (but not implemented) with China,[8] have the potential to bring about positive investment results. However, as the Canada-China bilateral has shown, such bilateral agreements can fall hostage to other unrelated issues, and are not a substitute for a regional investment liberalization regime. To achieve the benefits that will come with a successful TPP, and potentially an FTAAP in the future, Canada recognizes that it needs to be part of the process, and the TPP at the moment is the only negotiating forum where it has a seat at the table.

CONCLUSIONS

The success of the TPP is still an open question. The TPP may not be concluded, and if it is, the results may be less than originally hoped for. Ratification will be politically difficult, not only for the United States, but also for some of the other TPP partners. There will be vocal opposition on the part of a number of special interest groups. Despite these challenges, for Canada—not part of the RCEP or any ASEAN-Plus agreement, and not part of the East Asia Summit—the TPP is the best available forum on offer. It cannot afford to squander this opportunity. Now that it has proven the skeptics wrong and found enough common ground with the EU to initial an agreement, Canada will be pushing hard to conclude the TPP as early as possible. Through its EU agreement, Canada has already signaled where it may have some negotiating flexibility, and Canadian trade negotiators will work hard to ensure that Canada stays in the game and comes home with positive gains that it can sell to the provinces and business community, particularly with reference to Japan. Beyond any specific improvements in market access to TPP economies, Canada will use its reasserted Asia-Pacific presence through the TPP to push for a broader role generally and to reach beyond the TPP to China, South Korea, Indonesia, India, and others. That is the ultimate end game for Canada, and it is why the TPP has strategic significance well beyond its immediate economic impact.

NOTES

1. Ambassador Ron Kirk to Speaker John Boehner and Senator Daniel Inouye, July 10, 2012.

2. "The United States welcomes the interest of Canada and Mexico, our neighbors and largest export markets, in seeking to join the Trans-Pacific Partnership talks," said Ambassador Kirk. "We look forward to initiating consultations with them, and with Congress and our domestic stakeholders, and to discussing the TPP's high standards for liberalizing trade and specific issues of concern to the United States. These will include stronger protection of intellectual property rights, additional specific opportunities for US goods, services, and investment, and the elimination of various nontariff barriers." From the website of the Office of the US Trade Representative, "Statement by US Trade Representative Ron Kirk on Announcements from Mexico and Canada Regarding the Trans-Pacific Partnership," November 13, 2011.

3. The Council of Canadians website, www.canadians.org, accessed November 25, 2012.

4. See http://www.theglobeandmail.com/news/politics/eu-harper/article14924915/.

5. See http://www.theglobeandmail.com/report-on-business/economy/leave-currency-manipulation-out-of-trade-talks-ed-fast-urges/article14563787/.

6. Peter A. Petri and Michael G. Plummer, "The Trans-Pacific Partnership and Asia-Pacific Integration: Policy Implications," Policy Brief No. PB 12–16, Peterson Institute for International Economics, June 2012, Table 1.

7. See http://www.theglobeandmail.com/report-on-business/economy/study-recommends-canada-remove-all-trade-tariffs/article18598773/; http://www.ceocouncil.ca/wp-content/uploads/2014/05/Should-Canada-unilaterally-adopt-free-trade-Ciuriak-and-Xiao-May-20141.pdf.

8. See http://www.international.gc.ca/trade-agreements-accords-commerciaux/agr-acc/fipa-apie/index.aspx?lang=eng.

4

Chile and the TPP

Waiting for Outcomes

Rodrigo Contreras, Chile's former lead TPP negotiator

The project of establishing a free trade zone around the Asia-Pacific region is an ambitious and important undertaking. Indeed, in 2004, the president of Chile proposed the idea of making a large FTA within the framework of APEC. Chile then initiated negotiations with the P4 economies (Chile, Brunei, New Zealand, and Singapore), developing a very comfortable agreement for all participants. A distinctive characteristic of these agreements was the potential for growth in the future.

SIGNIFICANCE OF THE TPP

In terms of its macroeconomic dimensions, the TPP is a very attractive area. It produces 38 percent of total worldwide GDP, and about 73 percent of Asia-Pacific GDP, and it has a population of 800 million people. For Chile, the TPP represents around 40 percent of total exports, while TPP economies account for 33 percent of investments into Chile and 16 percent of Chilean investments abroad.

After the stagnation of negotiations under the World Trade Organization (WTO), plus the lack of binding commitments in the APEC framework and the poor trading policies of the United States, the TPP initiative

appears very promising. It would be an ambitious alternative to the WTO and move the US agenda forward, and it could serve as the seed for a future FTA among the APEC economies. Expectations, then, are very high.

In one scenario of success, the TPP could link the interests of South Korea, Chinese Taipei, and at least three more ASEAN economies, as well as several Latin America economies, starting with Colombia. The goal is to reach 19 economies of the Asia-Pacific region, which will create a very prominent future for this project.

OBJECTIVES AND CONTENTS OF THE TPP

When the negotiations began, the participating economies of the TPP did not yet have enough clarity about the contents of the future agreement. All the participants recognized where they wanted to go, but they didn't know how to best craft the contents to get to that point.

The distinctive characteristic of these negotiations was to create a next-generation agreement. Although at the beginning no one could explain what this affirmation implied, now that details of the contents are being hammered out, the agreement provides concrete direction.

The main guideline of the TPP is to alleviate trade problems, which all concern the inconveniences or barriers that affect trade, investment, and services flows among the economies. In relation to this, it is important to consider that most trade problems evolve over time. If past barriers were mainly related to tariffs, today's problems will be related to quotas, import licenses, distribution channels, and behind-the-border barriers, among others. Each economy's problems and solutions depend on its degree of openness and development, which vary widely.

There are very open and nonaligned countries, such as Chile, Singapore, New Zealand, or Peru; large, liberal economies with strong internal policies, such as Mexico, the United States, Japan, or Australia; and, finally, highly planned and directed economies, such as Vietnam, Malaysia, or Brunei.

In formulating the benchmarks, it should be taken into account that each economy will weigh numerous possibilities to address their objectives. While objectives in negotiations can be legitimate, if the costs for the other parties are too high, it doesn't make sense to push so hard.

OBJECTIVES AND BALANCE OF POWER OF EACH ECONOMY IN THE NEGOTIATIONS

In the real world, even having apparently common objectives is not enough to reach agreement. Differences in power among negotiators can change the way those objectives are actually addressed. In terms of how power in the room is balanced and how consensus is reached, plurilateral negotiations can resemble bilateral negotiations more than multilateral negotiations. This failure in the system harms small countries far more than powerful countries.

The lack of natural consensus in plurilateral discussions can also damage the multilateral system. Plurilateral negotiations can promote specific disciplines to global agreements, despite the fact that these provisions would fail to achieve consensus in multilateral discussions, and do not even represent consensus in a small group.

In any group of economies there are subgroups with particular objectives and interests in negotiations. In the TPP, we can define three groups of economies: one is seeking market access, another has systemic interests, and a third group wants to develop new trade rules.

In the group of economies seeking to gain market access through negotiations, we could put New Zealand, Vietnam, Malaysia, Japan, Mexico, Canada, and Australia. The first four do not have free trade agreements with the United States, which is a significant objective for them, and the rest are looking to improve access for their products through new or existing agreements.

In the second group of economies, we can put Chile, Brunei, Peru, and Singapore. All of them have traditionally or recently opted for openness, several have trade agreements with their main trade partners, and all consider this agreement to be a good way to improve their individual agreements, as well as to reduce the impact of the "spaghetti bowl" and contribute to a better multilateral system.

The third group is integrated primarily by the United States, and even if they are seeking market access for their products in Asia (as are all the rest), they are mainly looking to develop new rules that will address the trade problems they are facing and improve their competitiveness.

Directly related with the expectations of reaching each of these objectives is the disposition of the participants to compromise in order to achieve a successful agreement.

We must keep in mind the difference in power of each participant, in part based on the different backgrounds they bring to trade agreements, but mainly based on the size of each economy. We can't dismiss the fact that the United States is three times larger than the second-largest economy in the group, Japan. In theory, all economies in the negotiations have the same weight, but at the end of the day, that is not the reality.

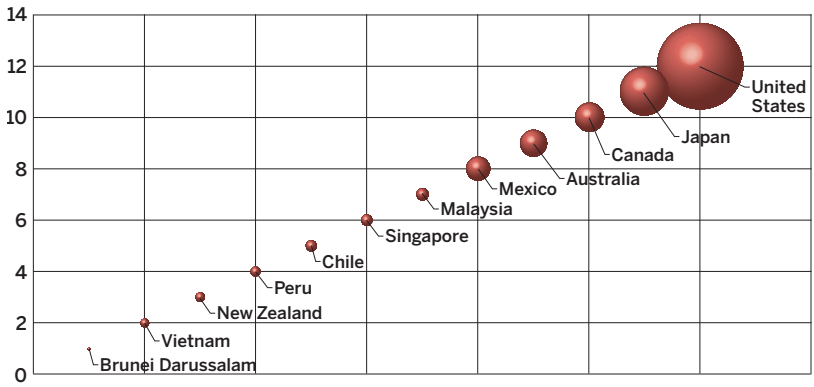

FIGURE 1 *Relative Dimension Based on the GDP*

When groups of economies with different objectives/interests are crossed with power players in the negotiation process, certain results are likely to occur. The most powerful economies, as well as the more determined, will impose the agenda and the terms of the final negotiations.

THE TPP'S MAIN CONTENTS AND POSSIBLE OUTCOMES

A free trade agreement represents a huge assemblage of chapters on a multitude of different matters relating to the trade in goods, the trade in services, investment, intellectual property, labor, the environment, and legal issues, among others. Thus, it is very difficult to make a detailed analysis in a few words, especially considering that there is no public

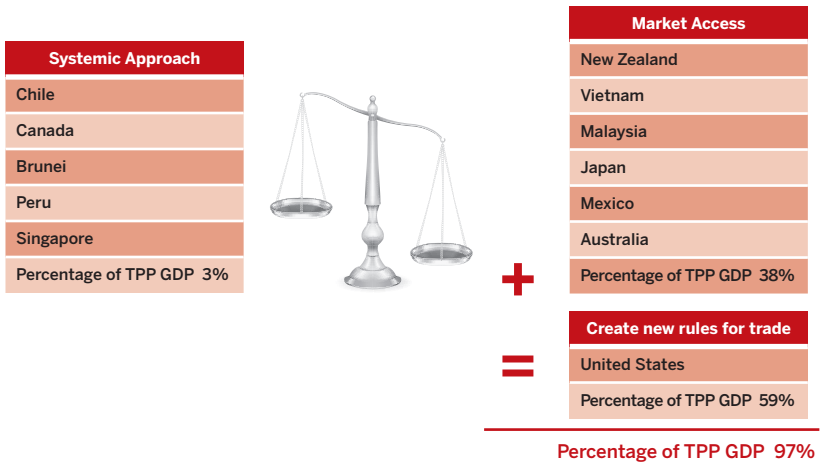

FIGURE 2 *Percentage of TPP GDP*

information released about the agreement's contents. For that reason, the following comments are based on the available information.

Trade in Goods

Trade in goods is an issue that has at least two main areas. The first is related to the disciplines for trade, mainly nontariff barriers to trade, such as export subsidies, distribution channels, or any export or import restriction. The second big area is related to the reduction of tariffs between economies. Even if, in principle, all the economies have a common objective, the sensitive sectors (products) of each can create bottlenecks in the negotiations.

In terms of disciplines, progress is being made in the first important area, which is related to restrictions and discriminatory treatments to imports inside each economy.

In respect to distribution channels and government presence in trade areas, discussions veer toward eliminating any interference in order to avoid discrimination of private imports once the product has been introduced in each economy. If this goal is reached, it would be a step forward in trade liberalization.

The requirements for licensing are usually used as a trade policy measure and as a way to control trade flows. Under the TPP, as with the WTO, it is very important to use licensing, and especially to add components of transparency for its use. Without transparency, any tariff concessions could be lost by export prohibitions.

Export subsidies are, in general, terms that are considered negative for trade agreements, and we could expect a compromise concerning the nonapplication of subsidies in the free trade area. Certainly one of the most powerful agreements that could be reached would be the control of internal supports, but acceptance seems to be very difficult to achieve in all the TPP economies.

Tariff elimination is a primary interest of all the participants; represents a clear concession that is reflected in reductions of trade barriers, which bring immediate gains; and has a positive impact on the competitiveness of the economies. While tariff elimination is the most visible result in any trade agreement, and would be good news for most of the economies involved, that would not be the case for Chile, which has FTAs with all the participants.

A basic requirement to be part of the TPP was to be committed to liberalizing the tariffs for all products. But we have heard repeatedly about the difficulty some economies have to committing to full liberalization, including the economies of Japan, the United States, Canada, Vietnam, and others. As a result, we can expect that exceptions in tariff liberalization will become a reality.

Rules of Origin

Rules of origin are very technical issues, and constitute one of the key chapters of this agreement. Considering that the main objective is to bring order to the "spaghetti bowl" of FTAs, to help construct global chains of production in the region, and to create a free trade zone, the rules of origin must operate in an open way in order to ensure the flexibility required today. To think that they have to be applied with the restricted vision developed 20 years ago is a big mistake that would severely and permanently damage this agreement.

The section of the chapter that relates to the framework for the application of rules by product seems to be nearing an end. But the section

related to specific rules by products, and the way they are materializing and accumulating, seems to be reaching a breaking point. Controversial sectors such as automotive and textile products are seen from both a defensive point of view, in the case of the Americas, and from an offensive point of view in the case of Asia.

Sanitary and Phytosanitary Issues and Barriers to Trade

Expectations in these two areas were very high, but the application of norms as a trade policy instrument is, unfortunately, rarely used. Advancements in transparency and the development of common criteria for decisions would be satisfactory results from the negotiations, but those seem unlikely to happen because of a lack of consensus among the participating economies.

In the case of sanitary and phytosanitary measures (SPS), gains could be made by improving transparency concerning the procedures, and by including a dispute settlement mechanism for solving plurilateral problems inside the group.

The case of trade barriers, on the other hand, is a little different because of expectations to include particular agreements about good practices for certain industries, which could impact SPS.

Investment

In terms of investment clauses, they should follow the same direction as the North American Free Trade Agreement–Plus (NAFTA-Plus) design.

While there is a general concern, mainly from the Asian economies, about assuring a wide framework of protection for foreign investors, it is helpful to realize that investment and services disciplines are uncommon in Asian trade agreements. Additionally, there appear in the public discussion at least two areas of concern: the free flow of capitals and, a big concern for Australia, clauses about investor-state dispute settlements.

Trade Facilitation

Every economy shares the objective of trade facilitation, which is why it appears on WTO, APEC, and, of course, the TPP forums. There are

practical problems that affect exports and imports in their day-to-day movements. The difficulty this issue poses is clarifying the scope and extent of commitments, which is not clear even under the WTO's technical barriers to trade. It is difficult to evaluate the possible results of other negotiations because previous standards have been very low.

Intellectual Property

The intellectual property chapter covers copyrights, patents, trademarks, geographical indications, and mechanisms for implementation, including Internet environments.

The background in all these matters is the desire to create protections for creators, and to improve compliance by users, especially in Internet environments. This chapter models itself on World Property Intellectual Organization–Plus (WIPO-Plus) agreements, and aims to not only comply with multilateral compromises, but also to improve upon them.

The big question is whether there is a consensus about the level of desired protection. A legitimate question to ask is whether the economies understood what improvement would actually look like, and if they were interested in making the same advancements. As an example, there seems to be asymmetrical interests in favor of patents and copyrights in relation to geographical indications.

A horizontal area is intellectual property applied to Internet environments. The Internet Age has been as transformative as the Industrial Revolution. It has changed communications (from expensive and limited to free and integrated), compressed financial transactions (from weeks to fragments of seconds), increased trade of products by previously unimaginable magnitudes (the world's products, culture, and knowledge at your fingertips). The latter, in fact, may be the most powerful and democratic consequence of the Internet. For small- and medium-sized enterprises and entrepreneurs, it serves as an inexhaustible information resource and a way to provide services to nearly everyone, in any place on the planet.

The effort to rule this media becomes an enormous and onerous challenge, one that Chile did not anticipate when negotiations began. Past experiences have been disastrous, with the Anti-Counterfeiting Trade

Agreement (ACTA) being a prime example. To try to interfere in the creation, education, and trade patterns generated by the Internet is a daunting challenge and heavy responsibility.

An argument to increase protection is that it would increase innovation. But it is impossible to raise the level of innovation in the developing economies without appropriate policies and incentives. Moreover, extending the rights of creators without providing previous incentives would block any possibility to develop knowledge.

New Matters

The main characteristic of the TPP agreement is that it would address matters of actual trade, such us trade facilitation, small- and medium-sized enterprises, regulatory coherence, and more. While this objective is very positive, the final evaluation would depend on the degree of commitments achieved on each chapter.

Other Issues

Some other issues have also been mentioned, such as the possibility of having disciplines to rule the participation of state-owned enterprises on the market, systems of reimbursement of medicines, or supervision of the currency exchange systems. All of these matters, again, are positive objectives, but it is difficult to advance any because participants' interests are, in some cases, contradictory.

CHILE IN THE TPP

Chile is a small country that made the decision to have a free market economy more than 30 years ago. While this decision created initial difficulties for some production sectors, many industries—including the fruit, wine, and salmon industries—launched into a process of evolving competitiveness.

Chile is not a big player in the international economy, with just 0.36 percent[1] of global GDP, a population of 0.25 percent of world inhabitants, and exports of 0.38 percent in relation to population. To synthesize these figures, Chile is only the thirty-sixth economy in the world. As a

small economy in the international context, Chile is unable to impose rules on all of the other economies.

Consistent with being a liberal economy, Chile fosters the external sector and promotes exports (68 percent openness today[2]), with a high composition of raw materials and semi-elaborated products, and around 53 percent of exports composed of copper and related minerals. It is a country that does not impose barriers to imports, and rarely uses trade defense tools.

With a small geographical area and a very exposed economy, Chile needs trade rules that assure a minimum of governance and stability to its model. That is the reason that Chile plays an active role in the WTO and maintains a consistent unilateral policy with very low, even nonexistent, trade barriers. The main component of its trade policy has been the negotiation of bilateral trade agreements.

In bilateral trade policy, Chile has an outstanding record. It has 23 trade agreements in force with 60 countries, having started in the early 1990s with a set of agreements within the region, and continuing to negotiate agreements with economies throughout North America, Europe, and Asia. Today, Chile has access to 62 percent of the global population, representing 86 percent[3] of world GDP. This opens up the possibility of sending 93 percent of Chilean exports under preferential agreements. Based on those figures, we can infer that Chile has established a successful process.

In terms of public policy, it is very difficult for a developing economy to consider the perspective of one that has reached state-of-the-art levels in trade. The main problem is that bilateral options have been maintained for so long, it has created great disparity in the contents between agreements. Even focusing on the same matters illuminates differences among the agreements, and generates what is often known as the "spaghetti bowl." But what is worse, this phenomenon of market segmentation occurs as a consequence of the application of restrictive bilateral rules of origin.

The above-mentioned issues suggest that there are many things to improve in terms of trade policy. The actual system, even if it has driven good results in increasing trade flows, is far from what economic theory indicates should be achieved, or what a multilateral system should strive to be.

The way to level the field in terms of coverage among Chile's free trade agreements—and transition from the restrictive characteristics of the bilateral agreements to the optimum characteristics of the multilateral system—is to take the plurilateral path. That is why Chile and other economies that have exhausted their bilateral policies are working on projects such as the Pacific Alliance and the Trans-Pacific Partnership (TPP) agreement.

The P4 agreement, along with the APEC experience, represents a solid rock to build an ambitious initiative like the TPP. But it is important to keep in mind that in the real world, many good ideas are dismissed because of practical problems. There are basically two threats that are generating instability in the TPP process: the first is the assumption that everyone has agreed upon the initial contents, and the second is the assumption that all the economies possess the same negotiating power in a plurilateral system. Given that neither assumption is true, the attractive TPP project faces difficult moments and searching questions.

The most important gains for Chile are not in the tariff-elimination process, as it has agreements with all the economies involved. The gains, rather, are in relation to the harmonization of disciplines and trade facilitation, which are very difficult to calculate.

The main concerns are the development of more ambitions rules (than the multilateral standard) in areas such as intellectual property, as well as the loss of tools such as prudential measures for capital flow controls or commitments in areas like the environment, both of which could slow down the actual dynamics of local economies.

Today, Chile is waiting for the final package because, as was stated earlier, the TPP is considered a worthy project but with unknown results, especially considering the lack of US trade promotion authority.

NOTES

1. World Bank statistics.
2. (Exports + Imports) / GDP.
3. General Directorate of Economic Relations, Ministry of Foreign Affairs, Chile.

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How Far Away Is China from the TPP?

Zhang Jianping, Director, Institute for International Economic Research at the National Development and Reform Commission

INTRODUCTION

China's attitude toward the TPP has undergone a fundamental change since 2013, but despite the "seven misunderstandings" of the TPP before 2013 or the "get involved immediately" theory that followed, both attempts failed to be objective and realistic. There is still a great distance between China and the TPP. Big differences exist on issues such as rules of trade in goods, service market access, and investment rules, while behind-the-border issues—standards and certification, environmental protection, intellectual property rights, labor standards, and government procurement—constitute severe challenges to China's current management systems and mechanisms. In the short term, China is not qualified to enter the TPP negotiations. However, there might be practical ways for China to integrate the TPP pathway with the RCEP pathway in the future, which could push China to seek reform and adjustment when the time is right. It should be emphasized that transparent mechanisms play a significant role in the Asia-Pacific integration strategy, and that they are promoted by China, the United States, and other TPP members. It is strongly recommended that TPP negotiation

members consider a more transparent information communication mechanism in their FTA negotiations.

The United States is pushing its "one body with two wings" FTA strategy globally, with NAFTA as the body and the TPP and TTIP as the wings. Simultaneously, the EU-Japan FTA negotiations are beginning to accelerate. The developed economies are in the process of formulating systems of new international trade and investment rules. Since the end of 2011, when TPP negotiations suddenly accelerated, until now, the TPP has not been just an ordinary FTA, but has embodied an early form of new, twenty-first century international trade and investment rules. As such, the TPP has aroused extensive attention and close follow-up studies among China's top officials and academic circles. There is still no clear consensus on whether China should join the TPP negotiations and, if so, when to join. However, starting in 2013, China changed course and deepened its understanding of the TPP, and it is gradually developing a relatively objective and realistic picture, together with making its own choices about strategy and policy toward the TPP.

CHINA'S ATTITUDE TOWARD THE TPP HAS CHANGED FUNDAMENTALLY SINCE 2013

At the 2011 APEC annual meeting held in Honolulu, Hawai'i, China began to pay more attention and conduct more relevant studies due to the TPP's rapid expansion and the acceleration of the negotiation progress. But with regard to its understanding of the TPP, different views and perspectives prevailed among China's academics, government officials, and the media. Prior to June 2013, China's academics mostly criticized the TPP. Their arguments can be categorized as six objections, including the conspiracy theory, pessimism theory, standby theory, spoiler theory, rival theory, and the US-dominate theory.[1] Two further objections were added soon afterward: the exclusive theory and the "get involved immediately" theory. The scholars who hold the exclusive theory maintain that the developed economies, led by the United States, took advantage of the TPP to exclude China on purpose, a position that does not tally with the fact that government and academic

circles in the United States, Japan, and other states maintain a positive attitude about the TPP.[2]

With the declaration by the Chinese Ministry of Foreign Affairs that the "TPP, ASEAN-Plus-Three, and ASEAN-Plus-Six are all possible paths for Asia-Pacific regional integration" in June 2013, and the public comment by the spokesperson of China's Ministry of Commerce that "China will study the TPP's influence on China's economy and the possibility of China's entry into TPP positively," many scholars in China decided that it should enter TPP negotiations immediately. This sharp turn of perspective, which can be called the "get involved immediately" theory, has made many Asia-Pacific economies, especially the United States and Japan, puzzled. This shift in perspective is totally unacceptable because it ignores the gap between China and the TPP standards, and it does not consider practical ways to ease China's entry into the TPP. What China needs to do now is to strengthen its follow-up studies on the TPP. China needs to carry out a new round of reforms and open up in many fields in order to bridge the gap between its own rules and the TPP rules. In a word, it is not realistic to enter TPP negotiations now. China's current policy of pushing forward the China–South Korea FTA and the China-Japan-Korea FTA (CJK FTA) negotiations, accelerating the process of the RCEP, and constructing the integration of East Asia's economy should be priorities.

HOW FAR AWAY IS CHINA FROM THE TPP?

Already, 19 rounds of TPP negotiations have been actively carried out. According to the consensus reached by members of the ministerial-level conferences and leaders' conferences during APEC, the economies negotiating the TPP hoped to conclude in 2013. The negotiations involve 21 fields, and the framework agreements have been expanded from 26 chapters to 29 chapters. Until now, consensus has been reached on half of the chapters; however, for issues such as market access, intellectual property protection, state-owned enterprises, and environmental protection and labor standards, no consensus has been reached yet. Even if preliminary agreements can be reached before the end of 2013, which

would probably constitute partial or early-stage agreements, the overall liberalization levels and requirements for high standards would not satisfy US expectations.

If China declares its intention to enter the TPP now, issues from a variety of fields need to be taken into consideration, including lowering tariff and nontariff barriers, and solving both on-the-border issues and behind-the-border issues. Given that China has signed regional trade agreements (RTAs) with many economies, China has accumulated abundant experience that enables it to solve on-the-border issues. For behind-the-border issues, however, China faces tough challenges.

ON-THE-BORDER ISSUES

Trade in Goods: China Is Mainly Faced with the Challenge of Rules

The TPP will promote 100 percent zero tariffs for trade in goods, and 10–15 years of transitional period for those sensitive products, without exception. For Japan, immunity was won for a few agriculture products, such as rice, corn, beef, cane sugar, and dairy products, which can retain tariffs to a certain degree. Given the FTA that China signed, there is still a significant gap between China and the developed economies on the liberalization level of trade in goods. For the middle- and high-end manufacturing industry, China might be somewhat impacted by the United States, Canada, Australia, Japan, and South Korea, while for the rules of trade in goods, the challenge is more severe. For example, for the textile and clothing industry, the TPP sets a strict rule of origin, which means that the Vietnam textile industry can enjoy tariff-free status only if the fabric originates in Vietnam. As such, that tariff-free status could be jeopardized in the future due to the fact that 50 percent of its fabric now comes from China. Some textile enterprises are moving from China to Vietnam, which will lead to the investment division effect.

Trade in Service: Market Access Is the Challenge

In service trade, the TPP has set higher-standard rules than the WTO. In terms of commitment, the TPP requires an overall opening of service

sectors and the carrying out of the "negative list." With regard to the service provision models, the "Mode 3" (commercial presence) and rules of trade in service are established separately. This means that both commercial presence and trade in service will be affected by the constraint of investment rules. In the financial and telecommunications sectors, the United States strongly requires that the two sectors be set up in independent chapters, and that each fully eliminate ration requirements of stock shares. In addition, operators must be allowed to choose service providers independently. The United States has also asked Japan to reform their postal and social insurance systems, so as not to slow things down in TPP negotiations. For China, its commitment to open up levels of trade in service when entering the WTO is the minimal requirement of the TPP as well, However, that opening process has not been completed, and there are still restrictions on the proportion of shares in a number of service subsectors. Moreover, China has just joined the negotiations of the Trade in Services Agreement (TISA), so it lacks experience in opening up trade in service. Given the high entry threshold and powerful groups of vested interests in China's service industries, such as finance and telecommunications, expanding the level of openness in trade in service is proving to be very difficult.

Investment: The Issue of National Treatment Before Market Access and the "Negative List" Barrier

Since 2000, China has signed 34 bilateral investment treaties (BIT). However, for the establishment, acquisition, and expansion of foreign direct investment (FDI) enterprises, national treatment before market access and negative list management have not been committed. It remains to be seen whether the TPP or ASEAN's agreements with Japan, South Korea, Australia, Singapore, and India will carry out national treatment before market access and negative list management, which will directly challenge China's current FDI management system and mode.

China is currently negotiating a BIT with the United States. Previously, the two economies had exchanged notes on investment agreements, which included eight terms that established US investment interests in China. US bilateral investment treaties are based on the US national security bill, whose template is very complex; on the minimum standard of national treatment

issues; and on its requirements for justice, equity, and comprehensive safety measures. Because China and the United States have no established BIT in terms of investment, the United States has conducted a sweeping security censorship of Chinese investors, and many Chinese enterprises felt the obvious discrimination, including the China Investment Corporation and Huawei. National treatment before market access and negative list management have brought challenges for China as it attempts to reform and open up its domestic investment management system, along with the government's economic management. This is caused because the management mode of foreign enterprises should be applied to the domestic investors, which forces China to reform its domestic investment system in turn. Reform is also highly relevant to China's industrial restructuring, as well as foreign exchange management reform and financial reform. The Shanghai FTA is making an effort in this regard. But from the Shanghai FTA negative list that was released, very limited breakthroughs have happened in comparison with the positive list. The negative list is currently under study. How to promote reforms in this field will be a daunting task for China, which will require time to accomplish them.

BEHIND-THE-BORDER ISSUES

A series of behind-the-border issues constitute an even bigger challenge for China, including the unification of standards, the governance of state-owned enterprises, environmental protection, labor standards, government procurement, and intellectual property protection. All of these issues are independent chapters in the TPP agreement, and all require intensive consideration and arrangement.[3]

The Unification of Standards

There is a huge gap between China and the United States on the understanding of standards, together with the formulating and implementing mechanisms for these standards. For the United States, the position is that the standards should be formulated by the enterprises or the organizations within the industry, and the government should not be involved. For China, the position is that national standards should be

formulated by the National Standardization Administration, based on the "Standardization Law," and certificated by the National Certification and Accreditation Administration. However, the fact is that the US government–backed Energy Star program has greatly impacted China's products. The establishment of new US rules on food safety has also led to stricter regulations on food that emphasize the producers' responsibilities and obligations, and that require a process of certification from agriculture product to dining table and whole chain regulation. This certification is required to be carried out by third-party checking and certification authorities. But in China, the third-party certification process is rather weak. Given the above facts, Chinese enterprises need to adjust their quality management systems, which would lead to a cost increase of more than 20 percent.

Environmental Protection

Drawn from its experience with NAFTA, the United States spares no effort in promoting environmental standards and labor standards, and it requires that any FTA signed by United States cover these fields. Until now, it has successfully promoted these standards to Chile, Peru, and other economies. In addition, the United States exerts influence on developing economies like China. For example, when Chile and Peru negotiated FTAs with China, they also required negotiations on environmental and labor issues. The TPP now has a special environment chapter requiring that environmental protection should take priority in foreign investment decisions. The areas of biodiversity conservation and marine fishing also require high transparency and administrative and judicial procedures. In China's FTA with Switzerland, the environmental protection chapter is provided. Among all the FTAs signed by China and another economy, this is the first time the environmental issue has become an independent chapter. But in the formulation and implementation of environmental protection standards, environmental data monitoring and transparency, and the participation of nongovernmental organizations, there is a still a long way to go before meeting the requirements of the TPP and the United States. This gap is due to weak institutional mechanisms, which cannot be solved in the short term.

Labor Standard Protection

The TPP is trying to fulfill the International Labour Organization's (ILO) fundamental commitment to basic rights, including freedom of association, prohibition of forced labor, elimination of child labor, gender discrimination, and so on. However, of the ILO's eight core conventions, a few have not been approved by China, including the freedom of association and collective bargaining of wages. These rules are very sensitive in China's existing system, which struggles to achieve systematic transformation. China cannot make external promises that it cannot keep in the short term.

State-owned Enterprises Governance

The TPP is promoting new rules for the governance of relevant state-owned enterprises. These rules specify that the share of government capital in state-owned enterprises should be below 20 percent. State-owned enterprises should not give preferential treatment and favorable financing to each other. Affiliated enterprises should not carry out affiliate transactions. State-owned enterprises should not pursue unfair competition. Subsidies and financing should be no different from nonstate enterprises, etc. China's state-owned enterprises have carried out joint-stock system reform. However, as most of their state-owned shares are rather high, these shares have surpassed 50 percent—even 80 percent in many cases—which far exceeds the TPP requirements, but cannot be changed immediately.

Government Procurement

The TPP's standard for government procurement is supposed to be higher than the WTO's Agreement on Government Procurement (GPA) and build-operate-transfer agreements (BOTs). China is currently carrying out a bilateral procurement agreement with the EU, but there has been no marked improvement in four or five rounds of negotiations in a past few years. China has domestically formulated its government procurement laws and carried out procurement processes, including the detailed environmental list. But there is still a huge gap between opening up to foreign enterprises, transparency, and third-party monitoring of China's government procurement and the normative and transparent

international conventions. Issues such as high costs, tedious procedures, and inadequate supervision continue to exist.

Intellectual Property Protection

In the TPP negotiations on intellectual property, the United States strongly promotes TRIPS-Plus. This aligns with its national interest, given that the United States holds two-thirds of the world's core patents. Although Australia and New Zealand consider TRIPS to be enough, US domestic law is multilateralized and rises to international conventions. In addition, the United States proposes to expand the range of intellectual protection and extend the protection period, such as extending the terms of copyright protection to 70 years. For China, the term is 50 years. The US pharmaceutical industry advocates that if the contracting parties get generic drugs, the intellectual property rights should be extended for longer periods. For China, the pharmaceutical industry will be heavily reliant on generic drugs if TRIPS-Plus is accepted. China's pharmaceutical industry and social and medical security systems will be impacted seriously.[4]

E-commerce and Internet Freedom

The TPP agreement promotes the free flow of data across borders and Internet freedom with no restrictive measures, as well as no restrictions on outside messages. Digital products should enjoy nondiscriminatory treatment, tariffs must not be imposed on online music, legitimate free downloads are promoted, and so on. China is currently experiencing economic and social transition, where various social contradictions have become increasingly apparent and social instability has increased. In order to maintain a stable environment for development, China needs to take necessary restrictive measures on new media like the Internet. The revelations contained in Edward Snowden's leaks and examples of wiretapping make it more difficult for China to accept Internet freedom in the short term.

TIME WINDOW AND COOPERATION FOR CHINA'S ENTRY INTO THE TPP

Given the above arguments, even if China decides to participate in TPP negotiations during the bilateral pre-negotiation process with the 13 member economies, it will be confronted with the preconditions and commitments that developed economies such as the United States and Japan have put forward. Putting aside the intense issues of national treatment before investment access, the negative list, and expanding market access of service industries, other issues will create new challenges for China's existing management systems. These challenges include behind-the-border issues, government procurement, state-owned enterprises, environmental protection, labor standards, intellectual property protection, and product standards.

Considering the congressional procedures of the United States and Japan, even if China pursues pre-negotiations in 2014, it would only be part of the negotiations after two or three years. Moreover, in China, every reform of behind-the-border issues needs to be solved in medium- and long-term frameworks, instead of only in the short term. Thus, China is not yet qualified to be a party of the TPP negotiations. In the future, China can positively participate and promote the RCEP negotiations, and seek the integration of the RCEP pathway and the TPP pathway, which may be a practicable course for China. In this way, China can seek to make reforms and adjustments at the right time.[5]

At the same time, China is extremely worried that it will lose the right to help formulate the trade and investment rules of the twenty-first century if it is excluded from the TPP negotiations. For Japan and South Korea, the economic benefits of entering TPP negotiations are rather limited, but entering allows them to be involved in the formulation of new rules. At the same time, involvement in the TPP helps them promote domestic reforms. For these economies, the "rules effect" is more pronounced than the "market effect." China is pushing forward a new round of reforms and is in the process of opening up. Although China cannot be a party to the TPP negotiations in the short term, it can be a key positive force for global and Asian trade and investment liberalization and facilitation. China should conduct a close follow-up

study on the TPP's development and direction, identifying the realistic gap between China and the TPP's new rules, and ultimately seeking a possible way to integrate with the TPP member economies in the future.

Currently, the TPP's transparency is very limited, which is also one of the primary reasons that China misunderstands the TPP. In fact, transparent mechanisms for communication would be very beneficial for China, the United States, and other TPP members, as well as being very important for promoting the Asia-Pacific integration strategy. Therefore, I strongly recommend that TPP negotiation members consider a more transparent communication mechanism, one which would further help the Asia-Pacific economies become a larger Asia-Pacific economic community.

Finally, the TPP's applicability for developing economies remains to be seen, even if it represents the direction that international economic development and social progress is taking. Using Malaysia as an example, the TPP will impact the health care system and rights of indigenous people, but the protection of indigenous people's rights have been enshrined in the constitution of Malaysia. The question becomes, is it necessary for Malaysia to revise its constitution for the TPP? For Vietnam, there are issues such as government procurement, state-owned enterprise reform, labor issues, environmental protection, etc. Given the conditions, the question of how to build systems and mechanisms that meet the TPP requirements in the near future looms for Vietnam. China will be paying close attention to how these issues are tackled. China's current preference is, undoubtedly, to build an East Asia mechanism, with the integration of the China–South Korea FTA, the CJK FTA, and the RCEP.[6]

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6

The TPP, China, and FTAAP

The Case for Convergence

Peter A. Petri, Professor of International Finance,
Brandeis International Business School

Michael G. Plummer, Eni Professor of International Economics,
The Johns Hopkins University, SAIS

Fan Zhai, Managing Director and Head of the Asset Allocation and
Strategic Research Department, China Investment Corporation

Asia-Pacific trade negotiations are evolving more fitfully than expected a few years ago. The Trans-Pacific Partnership (TPP) negotiations are nearing the endgame, but divisions remain and political opposition is intense. The Regional Comprehensive Economic Partnership (RCEP) negotiations are at an earlier stage, but progress also appears to be slow due to the region's diversity and geopolitical strains. Further impeding progress, macroeconomic conditions—turning less favorable now in East Asia and not yet sufficiently improved in the Americas and Europe—are not especially conducive to new agreements. None of these factors is likely to prove fatal to large trade initiatives, but each adds uncertainty on what can be accomplished and when.

These challenges have a silver lining: slow negotiations offer an opportunity to reexamine fundamental, long-term goals, including region-wide

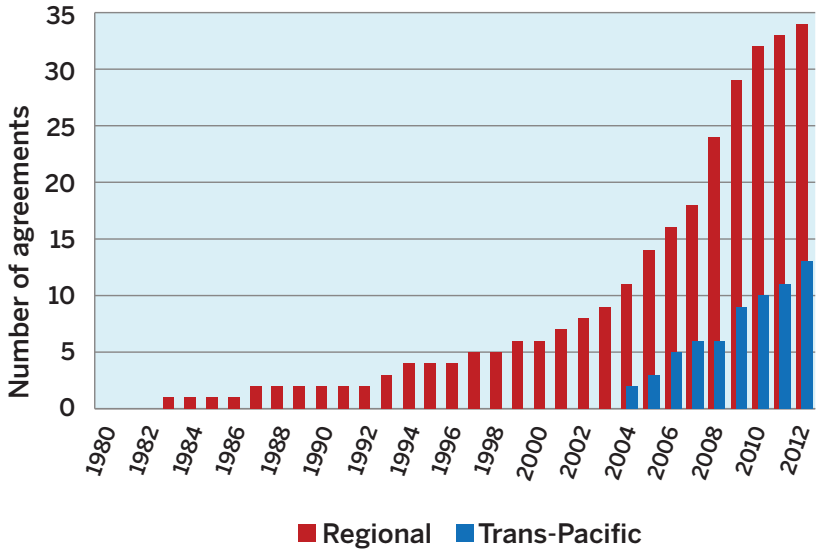
free trade through a Free Trade Area of the Asia-Pacific (FTAAP). Work on these goals in the Asia-Pacific Economic Cooperation (APEC) forum and related venues has been episodic; it moved quickly with the Bogor Declaration, and later with the negotiation of the P4 trade agreement among Brunei, Chile, New Zealand, and Singapore, but forward movement has also stagnated at times. Institutions have lagged behind in facilitating market-led integration. This suggests that innovations such as an FTAAP have to be debated and nurtured well in advance of when they become feasible. This paper explores several such options, among them the expansion of the TPP to include China.[1]

WHY THE ASIA PACIFIC?

Asia-Pacific trade is a logical setting for new agreements due to its scale and dynamism. First, the region's trade is immense. Of the world's US$14 trillion in trade in 2010, US$9 trillion involve APEC economies—a useful, though synthetic definition of the region—as either an exporter or importer or both. Within the APEC region, trade in the Americas amounted to US$1 trillion, in Asia and Oceania US$2 trillion, and across the Pacific also US$2 trillion. The region comprises not only the world's "factory floor," but also its most important sources of services, technology, investment, and final goods markets.

Second, Asia-Pacific trade is dynamic—it has changed the pattern of international economic relations through innovations such as modern supply chains. The region's diverse resource endowments and development levels give rise to varied specialization advantages. These are connected by dense transport and communication links for exchanging products, people, and resources cheaply.

Third, the region's interest in formal linkages is clearly rising, spurred in part by the challenges of global negotiations. Before 2000, there were only four major trade agreements among APEC economies—the ASEAN Free Trade Area, the Canada-US Free Trade Area, the North American Free Trade Agreement, and the Australia–New Zealand Closer Economic Relations accord—while today they number in the thirties, with others in the works (Figure 1). An especially strong



Note: Among APEC members.
Source: United Nations ESCAP database.

FIGURE 1 *Trends in Asia-Pacific Trade Agreements*

uptick is now evident in agreements that connect the Pacific's eastern and western subregions.

UNEVEN PROGRESS

Despite the importance of the Asia-Pacific trading system, the task of building regional institutions has been arduous. An Asian track for drafting new rules has proceeded slowly because the region's economies have widely differing interests, and some of its members have tense political relations. The Association of Southeast Asian Nations (ASEAN), the convener of the negotiations, is itself often divided on trade issues. Thus, even if a RCEP agreement is achieved in 2015, it may not go much beyond the bilateral deals that already crisscross the region.

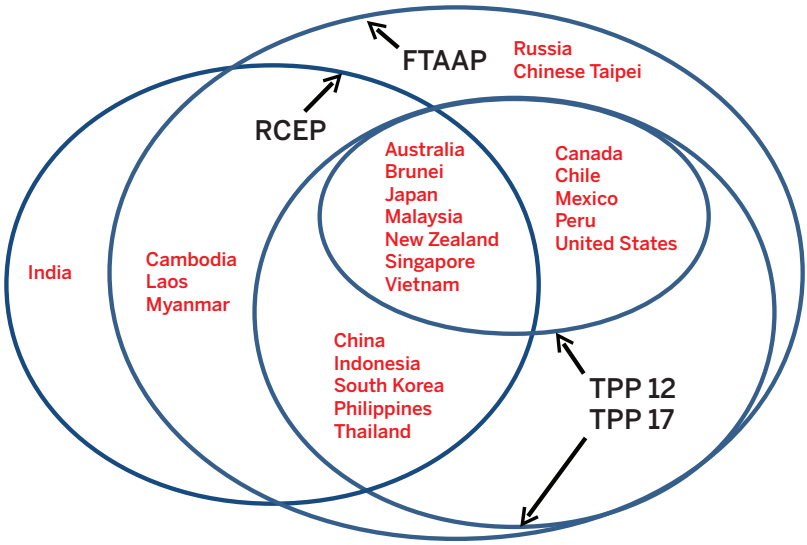
Meanwhile, a trans-Pacific track has laid out an ambitious agenda of negotiations since the United States made the TPP a priority in 2009.

The group of negotiating partners has expanded from four in the initial P4 agreement to now 12. These partners are in principle "like-minded," but their negotiations have been contentious. In addition, the leadership expected from the United States has been undermined by its domestic politics. In the run-up to the US elections, special interests from directly affected sectors in business, labor, and civil society have assumed disproportionate voices in the trade debate. These disagreements feed into much suspicion of globalization in the United States, and some public interest groups portray trade agreements as serving only corporate interests. As a recent Pew-Bertelsmann trade policy poll noted, there is a double deficit: "lack of understanding and a lack of trust" (Pew Research Center and Bertelsmann Foundation 2014). Hopes for an agreement in 2014 have faded.

None of this makes region-wide trade rules less urgent. The backlog of issues accumulated since the Uruguay Round was completed 20 years ago continues to expand, and the growth of world trade is slowing. The mega-regional negotiations offer potential answers to these issues, but they will need to be supported by strong arguments from leaders, as well as policies that ensure that the benefits are widely shared. Given improvements in macroeconomic conditions and reduced geopolitical tensions, the logic of region-wide trade rules should reemerge. In the meantime, there is good reason to search for pathways to full regional integration. China's year as the host of APEC creates excellent opportunities for this work.

BENEFITS FROM THE TPP AND ITS ENLARGEMENT

The gains from Asia-Pacific free trade agreements cannot be predicted with precision—for one thing, their terms are in flux. In recent studies, we nevertheless applied an advanced general equilibrium model to estimate rough benefits for several potential agreements, including the 12-member TPP, the 16-member RCEP, and the 21-member FTAAP. These studies found, as reported below, that the greatest economic benefits were associated with agreements that spanned China and the United States.



Source: Authors.

FIGURE 2 *Schematic View of Asian and Trans-Pacific Tracks*

In this paper, we add a new variant to previous simulations, an enlargement of the TPP to include China. Specifically, we hypothesize that the TPP will be eventually expanded to 17 members to include China, Indonesia, South Korea, the Philippines, and Thailand (see Figure 2). All five have expressed some interest in such an expansion and, as we shall see, the results suggest compelling benefits for them.

The modeling approach is explained in Petri, Plummer, and Zhai (2012) and on the website asiapacifictrade.org. We use a novel computable general equilibrium (CGE) framework developed by Zhai (2008) that incorporates firm-level differences in productivity. The version we use has 24 regions and 18 sectors, and also includes special detail on trade agreements and trade policy provisions in the Asia-Pacific region.

We assume that future agreements will be based on templates similar to those of past agreements. Thus, the TPP's template is assumed to be similar to the Korea-US (KORUS) free trade agreement (FTA), and the RCEP's template to those of agreements recently concluded by ASEAN. The TPP and RCEP templates differ on issues such as government

procurement, intellectual property rights, investment, and competition, as well as the depth of liberalization of tariff and nontariff barriers. These differences are not accidental; US agreements seek market access for leading sectors such as services and intellectual property, while Asian agreements focus on goods, consistent with their comparative advantages. We assume an FTAAP that would bridge these objectives with an intermediate template. Pairs of economies covered by more than one agreement are assumed to use—and benefit from—the one with the strongest provisions.

The results of these simulations are summarized in Table 1. These results should be viewed as mainly qualitative (they indicate relative gains), rather than precisely quantitative (since they are subject to many uncertainties and errors). In particular, three main conclusions of the comparisons remain reasonably robust in the face of alternative formulations and estimates.

First, the benefits of Asia-Pacific integration are large; for the most comprehensive agreements, income gains could approach US$2 trillion, or nearly 2 percent of world GDP in 2025. But even the current negotiations on the TPP-12 and the RCEP would generate substantial gains. The RCEP shows larger benefits than the TPP, mainly due to our optimistic assumption that it will liberalize economic relations among China, India, Japan, and South Korea.

Second, the results suggest divergences among the interests of economies. The TPP-12 favors economies that do not yet have an FTA with the United States, such as Vietnam and Japan. The RCEP favors China, India, Japan, and South Korea, assuming that trade among them would be effectively covered by an FTA. ASEAN economies, however, would gain modestly from the RCEP, assuming that the agreement does not substantially improve the FTAs that already cover all of the region's trade flows. Finally, the TPP-17 would offer large benefits to China, the United States, and others that gain access to *both* TPP and RCEP preferences.

Third, potential gains increase sharply with the scale of integration. For example, expanding the TPP from 12 to 17 members would triple global benefits from US$285 billion to US$893 billion in 2025. Since that expansion would include most large economies in the FTAAP, overall gains would be similar.[2] Moreover, gains will depend on the

TABLE 1 *Income Gains Under Alternative Scenarios*

	GDP 2025 ($2007 bill)	Income gain ($2007 bill)				% Baseline GDP2013			
		TPP-12	TPP-17	RCEP	FTAAP	TPP-12	TPP-17	RCEP	FTAAP
Template quality		**High**	**High**	**Moderate**	**Intermediate**	**High**	**High**	**Moderate**	**Intermediate**
Americas	24,867	101.7	468.0	2.5	373.3	0.4	1.9	0.0	1.5
Canada	1,978	8.7	33.2	-0.1	26.2	0.4	1.7	0.0	1.3
Chile	292	2.5	7.8	0.0	6.5	0.9	2.7	0.0	2.2
Mexico	2,004	9.9	91.1	2.8	67.7	0.5	4.5	0.1	3.4
Peru	320	3.9	8.4	0.0	6.3	1.2	2.6	0.0	2.0
United States	20,273	76.6	327.6	-0.1	266.5	0.4	1.6	0.0	1.3
Asia	34,901	125.2	1442.1	627.0	1354.3	0.4	4.1	1.8	3.88
Brunei	20	0.2	1.7	1.2	1.1	0.9	8.4	5.8	5.5
China	17,249	-34.8	808.6	249.7	678.1	-0.2	4.7	1.4	3.9
Hong Kong	406	-0.5	-1.9	46.8	84.9	-0.1	-0.5	11.5	20.9
India	5,233	-2.7	-29.3	91.3	-29.5	-0.1	-0.6	1.7	-0.6
Indonesia	1,549	-2.2	82.0	17.7	38.0	-0.1	5.3	1.1	2.5
Japan	5,338	104.6	237.3	95.8	228.1	2.0	4.4	1.8	4.3
South Korea	2,117	-2.8	136.3	82.0	129.3	-0.1	6.4	3.9	6.1
Malaysia	431	24.2	45.4	14.2	38.4	5.6	10.5	3.3	8.9
Philippines	322	-0.8	30.6	7.6	15.9	-0.2	9.5	2.3	5.0

Singapore	415	7.9	27.1	2.4	13.6	1.9	6.5	0.6	3.3
Chinese Taipei	840	-1.0	-31.5	-16.1	53.0	-0.1	-3.8	-1.9	6.3
Thailand	558	-2.4	64.9	15.5	27.4	-0.4	11.6	2.8	4.9
Vietnam	340	35.7	71.9	17.3	72.9	10.5	21.2	5.1	21.5
Other ASEAN	83	-0.4	-1.1	1.6	3.1	-0.4	-1.3	1.9	3.74
Oceania	1,634	10.7	41.3	21.7	32.1	0.7	2.5	1.3	2.0
Australia	1,433	6.6	34.1	19.8	26.4	0.5	2.4	1.4	1.8
New Zealand	201	4.1	7.2	1.9	5.8	2.0	3.6	0.9	2.9
Others	41,820	-14.1	-43.4	-6.8	162.0	0.0	-0.1	0.0	0.4
Europe	22,714	-3.7	0.9	5.1	-32.6	0.0	0.0	0.0	-0.1
Russia	2,865	-1.4	-8.8	-5.3	265.9	0.0	-0.3	-0.2	9.3
ROW	16,241	-9.0	-35.5	-6.6	-71.4	-0.1	-0.2	0.0	-0.4
WORLD	103,223	223.4	1908.0	644.4	1921.7	0.2	1.8	0.6	1.9
Memorandum									
TPP-12	33,045	285.0	892.8	155.1	759.5	0.9	2.7	0.5	2.3
RCEP	36,535	137.4	1516.8	617.9	1248.5	0.4	4.3	1.8	3.5
APEC	58,951	239.2	1973.0	553.0	2052.0	0.4	3.3	0.9	3.5

Notes: From scenarios reported on asiapacifictrade.org. The template used to represent the TPP-17 is more rigorous than the one used to simulate the FTAAP agreement. Thus, the difference between the two scenarios is partly explained by differences in membership and partly by the more extensive liberalization assumed under the TPP process. For further explanation, see endnote 2.

quality of the template; in other work, we show that global FTAAP benefits would be US$2.4 trillion with a TPP-style template versus US$1.9 trillion with the intermediate template of Table 1. The vast majority of gains in all cases would reflect trade creation, rather than the diversion of benefits from excluded economies.

POSSIBLE PATHWAYS

Regardless of the potential gains, large agreements that include both China and the United States face formidable challenges in terms of negotiations, as well as politics. They will not emerge quickly and will require ample preparation through reforms, innovative cooperation, and greater mutual trust. It is therefore important to consider pathways that could lead to convergence in the longer term. Two broad alternatives are considered below.

First, either the TPP or the RCEP could emerge as a pathway to region-wide free trade. The TPP is at this time the most probable pathway. It might initially expand to 17 members, as discussed above. Such enlargement would yield very positive outcomes for old and new members. China and the United States would reap the largest benefits, providing incentives for their joint leadership. Of course, many difficulties would be involved; China would have to accept provisions that were not included in its previous FTAs, and the United States would face large domestic adjustments that require careful implementation and confident leadership. Nevertheless, this path offers major political and economic opportunities for both economies, and some high-level attention is already directed toward it.[3] Whether the RCEP will emerge as an alternative pathway is still open to question; much will depend on whether it achieves the high standards expected by advanced economies.

Second, the TPP and the RCEP could develop in parallel, with an eventual "umbrella agreement" built around them. That agreement, often envisioned as the FTAAP, would impose new requirements that are intermediate to those of the TPP and the RCEP. For example, it could specify intermediate tariff reductions, service commitments, and intellectual property rules. It would, in turn, offer benefits more modest

than those offered by the TPP. This approach would yield an initially multi-tiered system, with economies choosing whether to accept RCEP, FTAAP, or TPP standards, but with the expectation that each economy would eventually converge to high standards. This is most likely to happen by adding economies gradually to the TPP. Another possibility is that the FTAAP becomes a living agreement that is upgraded over time. Precedents for an evolutionary approach are offered by ASEAN's experience with combining "plus one" agreements and bilateral agreements with external partners, and with its upgrading of the ASEAN Free Trade Area and some ASEAN-Plus-One partnerships. Unfortunately, the US political process offers no similar precedents.

An effective multi-tiered system would require its several agreements to be reasonably compatible. There is some evidence that recent trade agreements by the United States and Asian economies are more similar than earlier ones, and that agreements increasingly borrow language from each other. The guidelines for the RCEP, for example, overlap with the structure of the TPP. In any case, the attitudes of China and the United States will be crucial. Much of the incremental gains from a region-wide agreement would accrue to these economies, and their cooperation and leadership will be essential for bridging the Asian and trans-Pacific tracks. More work is needed to analyze the details of these alternatives, but APEC provides an ideal venue for such dialogue.

CONCLUSIONS

Asian and trans-Pacific regional negotiations are moving forward, despite business cycles, elections, geopolitics, and political controversy. Estimates suggest that they could generate large economic benefits, especially if they ultimately encompass the entire region.

The gains from Asia-Pacific integration will depend on the quality and regional reach of the templates used. There is tension between these objectives. A rigorous template, as is emerging in the trans-Pacific negotiations, yields greater gains, but will also impede region-wide participation. But there are ways to bridge these alternatives, such as through the multi-track, multi-tiered process sketched above.

Detailed policy recommendations are well beyond the scope of this short paper, but three issues merit attention:

- APEC could use the current lull in negotiations to intensify work on region-wide integration, including the FTAAP. New policy dialogues and research efforts might be directed, for example, toward minimizing divergences between emerging agreements.
- The TPP and RCEP agreements could develop "mutual accession" clauses—that is, commitments to consider expeditiously applications from each other's members. They could also identify future windows for enlargement. These provisions need not guarantee accession, but making the timetables explicit would motivate planning.
- China and the United States could follow a "third track" of discussions through bilateral efforts; they have the most to gain from, and contribute to, regional integration. Their steps could range from concluding an early bilateral investment agreement to other policy changes required for joint participation in a region-wide free trade agreement.

Region-wide agreements could produce compelling economic benefits and a more cooperative political environment. Yet achieving such agreements is difficult. Lengthy and complex negotiations will be required, which—amplified by the Internet—invite opposition from numerous special interests. The case for Asia-Pacific integration will have to be made effectively by governments, especially in the largest economies, if its benefits are to be realized.

NOTES

1. This possibility has been raised in recent commentary by Ma and Shi (2013) and Gordon (2014), among others.

2. The TPP-17 and FTAAP simulations differ, both in terms of their template (the TPP-17 template is assumed to be more rigorous) and membership (the FTAAP has 21 members). These differences complicate direct comparisons of the results. For China, for example, the gains are greater under the high standards of the TPP-17 than under the wider coverage

of the FTAAP. The same is true for the United States. For Chinese Taipei, however, gains are greater under the FTAAP than the TPP-17 because it is not assumed to be part of the latter.

3. These possibilities were explicitly noted, for example, by Wang Shouwen, Assistant Commerce Minister, and Lin Yifu, Vice Chairman of the All-China Federation of Industry and Commerce, speaking at the Boao Forum on April 9, 2014 (originally http://www.bruneitimes.com.bn/business-asia/2014/04/10/china-says-it-watching-trans-pacific-trade-pact-great-interest but now at http://www.aastocks.com/en/stocks/analysis/china-hot-topic-content.aspx?id=200000331986&type=18&catg=3).

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