



Regional Economic Integration Review and Outlook





The 27th Pacific Economic Community Seminar
 “Regional Economic Integration Review and Outlook”

Oct 4-5, 2012



Session I - (From Left) Mignon Chan, Ian Buchanan, Shujiro Urata,
 David Hong, Robert Scollay, Tan Khee Giap



Session II - (From Left) Linjun Wu, Stephen Cheung, Michael G. Plummer, Sheng Cheng Hu, Bo Chen, Shiro Armstrong



Concluding Session - (From Left) Hank Lim, Wook Chae, Don Campbell, Ippei Yamazawa, John Chen-Chung Deng



The 28th Pacific Economic Community Seminar: TPP and RCEP:
Emerging Dual-Track Pathways towards FTAAP

Nov 13-14, 2013



Session I - (From Left) Ian Buchanan, Bo Chen, Tan Khee Giap, Gary Hwake, Sheng Cheng Hu, Vipada M. Tuchinda



Session II - (From Left) Yose Rizal Damuri, Manfred Wilhelmy, Tan Khee Giap, David Hong, Kenichi Kawasaki, Chul Chung



Concluding Session - (From Left) Eugene Chen, Tan Khee Giap, Sheng Cheng Hu, Chul Chung, Ian Buchanan



Content

Policy Recommendations Concluded at the Seminars of Regional Economic Integration Review and Outlook

Session I : Overview of REI Development in Asia-Pacific and East Asia

Free Trade Agreements in East Asia:
Convergence toward a Region-wide FTA? **p.15**

Shujiro Urata

REI Development in Asia-Pacific and East Asia:
State of Play and Issues for TPP **p.41**

Robert Scollay

Session II : TPP vs. ASEAN plus N (or RCEP)

The Transpacific Partnership, Asian Track,
and Effects on Non-Partners **p.51**

Michael G. Plummer

Assessing the process and gains from the
economic integration in Asia Pacific Region **p.63**

Bo Chen

Session III : RCEP: Consolidating from Asia Track

RCEP: Consolidating from Asia Track **p.81**

Gary Hawke

China (Shanghai) Pilot Free Trade Zone:
A Solid Step towards Greater Liberalization **p.95**

Bo Chen

Session IV : TPP vs. RCEP: Building Blocks towards Greater Regional Economic Integration?

ASEAN-10 Competitiveness, Impact of
Global Growth Engines, Regional Economic
Integration through Free Trade Agreements **p.101**

Tan Khee Giap, Vu Minh Khuong

TPP vs RCEP: Competitor or Complements? **p.137**

Kenichi Kawasaki

Policy Suggestions

Concluded at the Seminars of Regional Economic Integration Review and Outlook

The seminars were hosted by CTPECC in 2012 and 2013. International experts from Australia; Chile; China; Hong Kong, China; Indonesia; Japan; Korea; New Zealand; Singapore; Thailand and; USA shared their views and exchanged ideas with Chinese Taipei tripartite participants.

It was proposed during the seminars that key findings and suggestions from the seminar should be delivered to the APEC Secretariat and other relevant parties for reference and consideration.

Key Findings and Suggestions

1. Research available to us reaffirms the value of further reducing tariff and non-tariff barriers to trade and investment not just in APEC but globally and therefore we strongly support efforts at the forthcoming 9th WTO Ministerial Conference in Bali to revitalise WTO and the *global* trading system. However in the interim TPP and RCEP should be regarded as important *complementary* dual tracks towards FTAAP, which is itself a path to the '*balanced, inclusive, sustainable, innovative, and secure growth*' as called for in the Yokohama vision and reaffirmed by the 2013 APEC Leaders Declaration.
2. The political and economic diversity within APEC means a '*One-size-fits-all*' approach to create new economic communities no longer applies and flexibility should be allowed for economies to join either RCEP or TPP.
3. While TPP and RCEP are complementary dual tracks towards FTAAP there is a risk that, as negotiations approach completion, if China dominates RCEP and the US dominates TPP this may bring unwelcome bi-polar division to the APEC region. The success of TPP or RCEP cannot depend on one single economy in either regional partnership or the political diplomacy of a particular period. To avoid this we believe PECC should work closely with APEC to establish coordinating mechanisms between the TPP and RCEP processes to facilitate alignment and convergence, which should ultimately lead to the emergence of one FTAAP.
4. APEC should clarify the schedule and timeframe to fulfill the goal of FTAAP in order that plans can be evolved to bridge TPP and RCEP into the FTAAP process. To fulfill the goal of FTAAP, all APEC members ought to be eligible to join the TPP and RCEP.
5. Public perception of both TPP and RCEP is that benefits may not justify the required sacrifices. PECC and APEC economists must work more closely with political leaders to provide independent and trusted analysis to the public and all key stakeholders.
6. TPP and RCEP will influence existing supply chains in our region. Members who have recently joined the TPP/RCEP need to be integrated into these and new supply chains. Economies that wish to join TPP/RCEP need to analyze the regional and domestic circumstances first and position themselves accordingly.

Chinese Taipei Pacific Economic Cooperation Committee (CTPECC)

The 27th Pacific Economic Community Seminar
Regional Economic Integration Review and Outlook
Date: 4-5 October, 2012
Venue: 1F, Noble House, Regent Hotel

Introduction

The global economy experienced somewhat slow to moderate growth during the 2011-2012 period. Uncertainties are still containing the improvement of business conditions of the world. However, the Asia-Pacific especially the East Asia region outperformed other regions by contributing more to the world economic growth. It is therefore very important to continue such a momentum and keep on the recovery process, since the world economy will be depending further on the economic potential and strength provided by this region.

The most recent global economic crisis had serious impacts on the world economy through the channel of international trade as well as financial linkage. European sovereign crisis, geopolitical factors and other uncertainties further block the path to recovery. In addition, protectionism in many forms seems revived at bad times, and transaction costs hindering the development of healthy business environment increased. The regional economic integration (REI) aiming at reducing or eliminating unnecessary economic barriers has been proposed, such as the initiative of Free Trade Area of Asia-Pacific (FTAAP), in-progress Trans-Pacific Partnership Agreement (TPP), and the unending idea of ASEAN plus Three or Six. We believe that economic integration with freer trade would help create a healthier business environment by eliminating protectionism in many possible ways. However, there still exist many political and economic challenges limiting the progress of REI. For that reason, we need to cope with challenges and explore potential opportunities.

Furthermore, it is also possible that the REI trend will create an entirely new business model that is much needed for the world economy to grow in a more adequate fashion. That means supply could better meet demand, whereas demand of the present and future generations ought to be clearly identified. In addition, how those integration processes can help create and execute a potential new economic format is also a crucial issue. For these reasons and to look for feasible solutions, the Chinese Taipei Pacific Economic Cooperation Committee (CTPECC) and Taiwan Institute of Economic Research (TIER) would like to cordially invite opinion leaders in our region to share their distinguished views and exchange ideas with representatives from business, government and academic circles in Chinese Taipei.



Day 1, October 4, 2012

Venue: Regent Taipei

08:20-08:55		Registration	Venue: Noble House, 1st Floor	
Opening Session				
Session Chair		Dr. David Hong		
		Chair, Chinese Taipei Pacific Economic Cooperation Committee (CTPECC)		
09:10-09:15		Welcome Remarks		
09:15-09:25		Opening Remarks		
		Amb. Don Campbell		
		Co-Chair, Pacific Economic Cooperation Council (PECC)		
09:25-09:40		Group Photo		
09:40-10:00		Coffee Break		
10:00-12:00		Session 1	Venue: Noble House, 1st Floor	
“Overview of REI Development in Asia-Pacific and East Asia”				
Session Chair				
		Dr. David Hong, Chair, Chinese Taipei Pacific Economic Cooperation Committee (CTPECC)		
Speakers (25 min each)				
		Prof. Shujiro Urata, Professor, Waseda University, Japan		
		Prof. Robert Scollay, Associate Professor, University of Auckland, New Zealand		
Discussants (15 min each)				
		Mr. Ian Buchanan, Chair, Australian Pacific Economic Cooperation Committee (AUSPECC)		
		Prof. Tan Khée Giap, Chair, Singapore National Committee for Pacific Economic Cooperation (SINCPEC)		
		Dr. Mignonne Chan, Executive Director, Chinese Taipei APEC Study Center		
Q & A (20 min)				
12:00-13:30		Lunch	Venue: Azie, 1st Floor	
13:30-15:30		Session 2	Venue: Noble House, 1st Floor	
“TPP vs. ASEAN plus N (or RCEP)”				
Session Chair				
		Dr. Sheng Cheng Hu, Academician, Academic Sinica, Chinese Taipei		
Speakers (25 min each)				
		Dr. Michael G. Plummer, ENI Chair, Johns Hopkins University, Bologna, Italy		
		Dr. Bo Chen, Associate Department Chair, Shanghai University of Finance & Economics		
Discussants (15 min each)				
		Prof. Stephen Cheung, Chair, Hong Kong Committee for Pacific Economic Cooperation (HKCPEC)		
		Dr. Shiro Armstrong, Research Fellow, Australian National University		
		Dr. Linjun Wu, Associate Research Fellow, Institute of International Relations, National Chengchi University		
Q & A (20 min)				
15:30-15:50		Coffee Break		
15:50-16:50		Concluding Session	Venue: Noble House, 1st Floor	
Session Chair				
		Amb. Don Campbell, Co-Chair, Pacific Economic Cooperation Council (PECC)		
Discussants (10 min each)				
		Dr. Wook Chae, Chair, Korea National Committee for Pacific Economic Cooperation (KOPEC)		
		Prof. Ippei Yamazawa, Professor Emeritus, Hitotsubashi University		
		Dr. Hank Lim, Senior Research Fellow, Singapore Institute of International Affairs		
		Mr. John Chen-Chung Deng, Deputy Secretary General, National Security Council		
Q & A (10 min)				

Chinese Taipei Pacific Economic Cooperation Committee (CTPECC)

The 28th Pacific Economic Community Seminar

TPP and RCEP: Emerging Dual-Track Pathways towards FTAAP

Date: 13-14 November, 2013

Venue: 1F, Noble House, Regent Hotel

Introduction

The regional economic integration (REI) has long been recognized as one of the most important issues for Asia-Pacific economies, as REI accelerates reducing trade barriers and creating a favorable business environment. In the region of Asia-Pacific, the Trans-Pacific Partnership (TPP) and the Regional Comprehensive Economic Partnership (RCEP) have been identified as two potential REI pathways to achieve the ultimate goal of the Free Trade Area of Asia-Pacific (FTAAP). At the emergence of the two pathways some key questions has been increasingly addressed. Are these two tracks in competition or complementation? How can TPP and RCEP converge to progress further? Are there potential impacts caused by the TPP and RCEP on members or non-members? How can members, possible members and non-members address the impacts?

To seek answers for those questions, the Chinese Taipei Pacific Economic Cooperation Committee (CTPECC) and Taiwan Institute of Economic Research (TIER) would like to cordially invite opinion leaders in our region to share their distinguished views and exchange ideas with representatives from business, government and academic circles in Chinese Taipei.



Day 1, November 13, 2013

Venue: Noble House, 1F, Regent Taipei

08:30-09:20 Registration

Opening Session

Session Chair

David Hong, Chair, CTPECC

Welcome Remarks

Group Photo

Guests, Speakers and Discussants

09:35-10:00 Coffee Break

10:00-12:00 Session 1: RCEP: Consolidating from Asia Track

Session Chair

Tan Khee Giap, Chair, SINCPEC

Speakers (25 min each)

Gary Hawke, Professor, New Zealand Institute of Economic Research

Bo Chen, Department Chair, Shanghai University of Finance & Economics

Discussants (10 min each)

Sheng Cheng Hu, Academician, Academic Sinica

Ian Buchanan, Chair, AUSPECC

Vipada M. Tuchinda, Assistant Director, Fiscal Policy Research Institute (FPRI)

Q & A (30 min)

12:00-13:30 Lunch

13:30-15:30 Session 2: TPP vs. RCEP: Building Blocks towards Greater Regional Economic Integration?

Session Chair

David Hong, Chair, CTPECC

Speakers (25 min each)

Tan Khee Giap, Chair, SINCPEC

Kenichi Kawasaki, Consulting Fellow, Research Institute of Economy, Trade & Industry, IAA (RIETI)

Discussants (10 min each)

Manfred Wilhelmy, Chair, CHILPEC

Chul Chung, Executive Director, KOPEC

Yose Rizal Damuri, Head of the Department of Economics, CSIS, Indonesia

15:30-15:50 Coffee Break

15:50-16:50 Concluding Session

Session Chair

Sheng Cheng Hu, Academician, Academic Sinica

Discussants (5 min each)

Tan Khee Giap, Chair, SINCPEC

Chul Chung, Executive Director, KOPEC

Ian Buchanan, Chair, AUSPECC

Eugene Chen, Managing Director, Grand Aspect Int'l Ltd.

Q & A (30 min)



Session I

Overview of REI Development in Asia-Pacific and East Asia





Free Trade Agreements in East Asia: Convergence toward a Region-wide FTA?

■ Shujiro URATA

I. Introduction

Asia joined other regions of the world in a free trade agreement (FTA) frenzy in the 21st century¹. Several regions in the world other than Asia began actively to look at FTAs as a means for promoting trade liberalization around 1990s, when the Uruguay round of multilateral trade negotiations under the auspices of the GATT (the General Agreement on Tariffs and Trade) was making little progress (Figure 1). A strong interest in FTAs has continued to exist and it has increased even more after the establishment of the WTO (World Trade Organization) in 1995, which succeeded the GATT with a more comprehensive coverage and stronger legal foundation, as the new multilateral trade negotiations (the Doha Development Agenda, DDA) under the WTO entered into the deadlock. Indeed, the number of FTAs reported to the GATT started to increase rapidly in the 1990s and then the pace has accelerated since the mid-1990s.

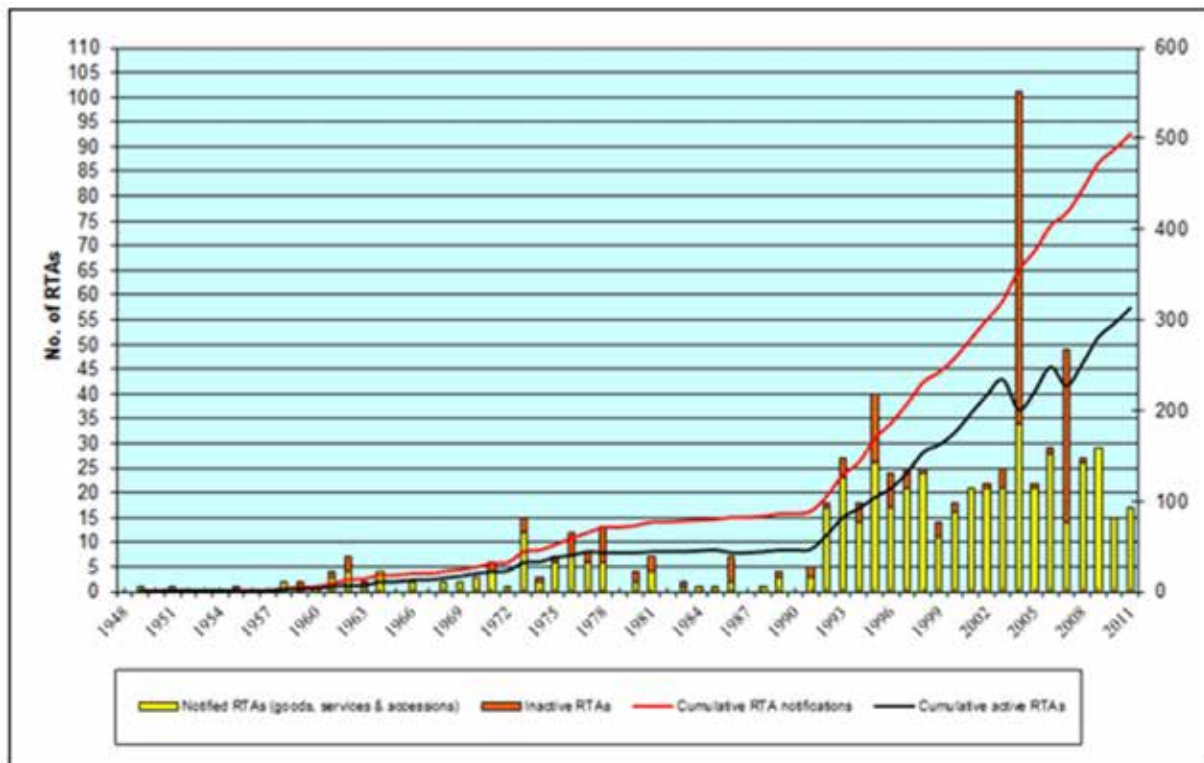
Around the turn of the century Asia began to negotiate FTAs with the economies in and outside of the region. The pace of starting FTA negotiations by Asian economies speeded up as the domino effect for signing FTAs was set off. Indeed, the number of FTAs in effect was only one in 1976 in Asia, but it increased rapidly to 92 by 2010². One of the concerns arisen from the proliferation of FTAs is possible increase in trade costs. A firm that is interested in enjoying the benefits of using FTAs has to satisfy certain conditions, which differ among the FTAs, leading to an increase in cost of using FTAs. Faced with the situation, countries in Asia began to examine the possibility of establishing a region-wide FTA, which would promote economic growth of the region by creating a large unified market. The realization of the need to establish a region-wide FTA in Asia on the part of policy makers and business people also comes from the fact that region-wide FTAs have been set up in North America and Western Europe making Asia the only region without a unified market among the three major regions in the world.

In light of these developments, this paper attempts to discuss the ways to construct a region-wide FTA in Asia. The structure of the paper is as follows. Section II reviews the FTA developments in Asia, while section III examines the factors, both economic and political factors, behind rapid expansion of FTAs. Section IV analyzes the utilization of FTAs and section V attempts to find the way to establish a region-wide FTA in Asia by examining the similarities and differences of existing major FTAs. Some concluding remarks are presented in section VI.

1 Unless otherwise indicated, Asia in this paper represents ASEAN+6 countries, that is, ten ASEAN countries, China, Japan, Korea, India, Australia, and New Zealand.

2 Asia Regional Integration Center, Asian Development Bank

Figure 1 FTAs (RTAs) in the World



Source: WTO website.

II. Proliferation of FTAs in Asia

Asia was not active in the formation of regional trade agreements (RTAs), which include FTA and customs union, until recently (Table 1)³. Indeed, the ASEAN Free Trade Area (AFTA), which was established in 1992, was the only major FTA until the 21st century, when the number of FTAs started to increase rapidly⁴. Many countries in Asia began to form FTAs with the countries not only in the region but also outside the region.

³ In the GATT/WTO, regional trade agreements (RTAs), which violate one of its basic principles of non-discrimination, are permitted under GATT Article XXIV with several conditions, which include liberalization of substantially all the trade of the members, not increasing trade barriers on non-members, and completing the RTA process within ten years. For developing members, more lenient conditions are applied under the enabling clause. An FTA is considered to be a shallow form of regional integration, because it only removes tariff and non-tariff barriers between and among the members, while a customs union is a deeper integration, as it adopts common external tariffs on non-members, in addition to the removal of tariff and non-tariff barriers on trade between and among the members. All the RTAs established so far in Asia are FTAs.

⁴ For discussions on FTAs in East Asia, see for example, Aggarwal and Urata (2006), Urata (2005), and Pangestu and Gooptu (2004), Soesastro (2006), Sally (2006), and Kawai and Wignaraja (2010).


Table 1 FTAs in Asia as of January 2012 (cumulative number)

	Framework Agreement					Total	Types of FTAs	
	Proposed	Signed/Under neg	Under Negotiation	Signed	In effect		Bilateral	Plurilateral
1989	1	0	0	1	3	5	3	2
1995	1	0	0	15	14	30	26	4
2000	3	0	6	19	25	53	46	7
2005	44	18	28	27	51	168	131	37
2010	57	17	48	27	92	240	179	61
2012	60	16	48	27	99	250	185	65

Note: Asia in this table include the Asian Development Bank members.

Source: Asian Development Bank, Asian Regional Integration Center website, accessed on October 1, 2012

Faced with increasing competitive pressure from emerging China and with a rising regionalism trend in Europe and other parts of the world, the members of the ASEAN started the ASEAN Free Trade Area (AFTA) process in 1992 to make ASEAN a competitive region for exports and for attracting FDI⁵. The 1992 agreement provided for the liberalization of tariff and non-tariff measures under the common effective preferential tariffs. The target year for achieving tariff and non-tariff liberalization was originally set for 2008, but was later moved forward to 2002. The AFTA has been in effect among the original six AFTA members—Brunei, Indonesia, Malaysia, Singapore, Thailand and the Philippines—since January 2002 when the tariff rates were reduced to 0-5 percent, though the exclusion list was long and individual country circumstances varied. The AFTA process was completed for the original members in January 2010, when all the tariffs for intra-ASEAN trade were removed with some exceptions. New AFTA members, Vietnam, Lao PDR, Myanmar and Cambodia have lowered tariff rates for their intra-ASEAN trade and they are expected to complete the tariff removal by 2015.

Compared to the tariff liberalization, non-tariff barriers including both border barriers such as import quotas and anti-dumping actions as well as behind-the-border measures such as technical, administrative, safety regulations are more difficult to be dealt with. In order to minimize trade costs arisen from these regulations, ASEAN countries have attempted to either harmonize or mutually recognize standards and other regulations. Although some progresses have been made in this area, substantial non-tariff barriers still remain.

ASEAN has pursued liberalization of trade in services under the 1995 ASEAN Framework Agreement on Services (AFAS). AFAS aims to go beyond commitments in the General Agreement on Trade in Services (GATS), in order to improve efficiency and competitiveness of ASEAN service providers. Services trade liberalization has proceeded through several rounds of negotiations, but there still remain substantial barriers to service trade. Among the four modes of supply of services trade, i.e.,

5 Chia (2011) gives a detailed account of ASEAN's programs for promoting its economic integration including those related to trade in goods and services and foreign direct investment.

(1) cross-border supply, (2) consumption abroad, (3) commercial presence, and (4) movement of natural persons, modes 3 and 4 are most sensitive. ASEAN adopted a flexible approach of “ASEAN minus X” to accommodate ASEAN member countries that are unable to move at the same pace.

FDI liberalization in ASEAN has been underway through the 1998 ASEAN Investment Area (AIA) and 2009 ASEAN Comprehensive Investment Area (ACIA), which provide coordinated investment cooperation and facilitation programs, market access, and national treatment of all industries. The AIA was criticized for its long exclusion lists, but there have been improvements. As with services liberalization, the “ASEAN minus X” formula has been introduced in AIA. Under the ACIA, in addition to the AIA provisions including investment liberalization and facilitation, investment protection, which has provisions on the investor-state dispute settlement mechanisms, transfer and repatriation of capital and others, was included.

In 2003 the ASEAN Leaders agreed to set the target year of 2020 for the establishment of an ASEAN Community, which is composed of the ASEAN Security Community, the ASEAN Economic Community (AEC) and the ASEAN Socio-Cultural Community. Under the ASEAN Economic Community free flow of goods, services, investment and capital is to be established. The target date for the establishment of an ASEAN Community was later moved forward to 2015. ASEAN countries introduced the AEC Blueprint in 2007 to achieve the AEC. The AEC Blueprint sets out the measures to be taken and the schedule for their implementation. In order to monitor the progress by the ASEAN members for the AEC Blueprint, ASEAN ministers and officials adopted a “scorecard” which is to assess the progress. According to the scorecard for 2008-2009, 82 percent of the goals have been achieved on the objective of a single market and production base⁶.

Besides AFTA, ASEAN as a group as well as its members individually have become active in FTA discussions with other countries in recent years. Indeed, ASEAN has enacted five ASEAN+1 FTAs (with China, Korea, Japan, India and CER, that is Australia-New Zealand), making ASEAN an FTA hub for East Asia. ASEAN and China enacted an FTA in goods trade in July 2005 and they completed liberalization process in January 2010. ASEAN and China enacted an FTA in services trade in July 2007 and they signed an ASEAN-China Investment Treaty in August 2009. ASEAN excluding Thailand enacted an FTA with Korea in August 2006 and tariff reduction began in June 2007. Thailand signed the ASEAN-Korea FTA in February 2009. ASEAN and Korea signed an FTA in services in November 2007 and an Investment Treaty in June 2009. ASEAN and Japan enacted an FTA in goods in December 2008. ASEAN enacted FTAs with India and Australia-New Zealand in January 2010. The ASEAN-Australia-New Zealand FTA includes trade in services and investment, while the ASEAN-India does not.

Many ASEAN members have become active in establishing bilateral FTAs (Table 2). Singapore enacted many FTAs with countries such as New Zealand, Japan, Australia, the USA, the EFTA, and

⁶ Chia (2011).



India and it is currently negotiating FTAs with many countries. It is important to note that Singapore established an FTA called P-4 (later changed to Trans-Pacific Strategic Partnership Agreement, or the TPP) with Brunei, New Zealand and Chile in 2006. Thailand has also become active in establishing FTAs, as it has implemented FTAs with Australia, New Zealand, and Japan and it is currently under negotiations with several countries. Malaysia enacted an FTA with Japan and it joined the negotiations of the expanded TPP. Indonesia, the Philippines and Vietnam each enacted an FTA with Japan.

Table 2 FTAs for Selected Asian Countries: (as of January 2012)

COUNTRY	Proposed	Under Negotiation		Conclusion		TOTAL
		A	B	Signed	In Effect	
ASEAN						
Brunei Darussalam	5	2	1	0	8	16
Cambodia	3	0	1	0	6	10
Indonesia	6	1	4	2	7	20
Lao PDR	3	0	1	0	8	12
Malaysia	8	1	5	2	10	26
Myanmar	3	1	1	0	6	11
Philippines	5	0	1	0	7	13
Singapore	5	1	9	3	18	36
Thailand	6	3	4	0	12	25
Viet Nam	7	1	1	1	7	17
Northeast Asia						
China, People's Republic of	7	2	4	0	12	25
Japan	8	0	2	1	12	23
Korea, Republic of	16	2	5	1	8	32
Hong Kong	1	0	0	1	2	4
Chinese Taipei	2	1	1	0	5	9
Mongolia	3	0	0	0	0	3
Australia-New Zealand						
Australia	3	2	8	0	8	21
New Zealand	4	1	5	0	9	19
South Asia						
Bangladesh	0	2	1	1	2	6
India	7	4	9	0	13	33
Pakistan	11	4	3	3	6	27
Sri Lanka	2	1	0	1	4	8

Note: A: Framework Agreement, B: FTA

Source: ADB, Asian Regional Integration Center, Free Trade Agreement Database for Asia, accessed on October 1, 2012

Compared to ASEAN countries in Southeast Asia, the economies in Northeast Asia including China, Japan, Korea, and Chinese Taipei had not been active in FTAs until the end of the 1990s. China, Japan and Korea have become very active in FTAs. China implemented 12 FTAs including those with ASEAN, Hong Kong, Macau, New Zealand, and Chinese Taipei, and it is negotiating FTAs with Korea and several other countries. Japan enacted twelve bilateral FTAs with Singapore, Mexico, Malaysia, Chile, Thailand, the Philippines, Indonesia, Brunei, Vietnam, Switzerland, India, and Peru, and one regional FTA with

ASEAN. It is currently in negotiations with Australia, the Gulf Cooperation Council (GCC), and Korea (suspended). Korea implemented eight FTAs including those with Chile, Singapore, India, EFTA, ASEAN, the EU and the US. Korea is actively pursuing FTA policies as it is currently negotiations with the countries including Canada, Mexico and China.

Chinese Taipei is very keen on having FTAs with many countries but political problems with China have precluded them from achieving this objective. The situation was expected to change as Chinese Taipei enacted an FTA with China in 2010, but so far it does not appear that the situation has changed. In addition to China, Chinese Taipei has enacted four FTAs with small countries in Central America including Nicaragua and El Salvador.

India enacted five FTAs with Sri Lanka, Singapore, ASEAN, Korea, South Asian Association for Regional Cooperation (SAARC), and Japan, and it finished negotiations and signed agreement with Malaysia. India is currently negotiating five FTAs including BIMSTEC (The Bay of Bengal Initiative for Multi-Sectoral Technical and Economic Cooperation)⁷, EU, GCC, Mauritius, and Thailand.

As a result of increasing FTAs in Asia, the share of trade that is covered by FTAs in overall trade (FTA coverage ratio) increased for Asian countries. Among the Asian countries, ASEAN registers the highest FTA coverage ratio amounting to 56.5 percent⁸. The FTA coverage ratios for China, Japan and Korea are much lower compared to those for ASEAN. Specifically, the values for China, Japan, and Korea are 21.9, 16.5, and 36.0 percent, respectively⁹. The values rise to 28.3, 36.5 and 61.1 percent, if the FTAs under negotiation are considered in the computation. These values indicate that there is room for further FTA expansion for Asian countries, especially for those in Northeast Asia. Confining the scope of analysis to ASEAN+6 countries, one finds that the FTA coverage ratio for intra-regional trade for ASEAN+6 is 54.3 percent. The limited FTA coverage ratio in East Asia is mainly due to the absence of an FTA covering China, Japan, and Korea.

Unlike Europe or North America, both of which have established region-wide FTAs, East Asia so far has established a number of bilateral and minilateral FTAs and not a region-wide FTA. Recognizing the economic benefits of region-wide FTAs such as a large unified market, two region-wide FTAs covering East Asia were proposed, ASEAN+3 (China, Japan, and Korea) FTA and ASEAN+6 (China, Japan, Korea, Australia, New Zealand, and India).

At the Leaders' summit meeting of ASEAN+3 in 1998 the leaders decided to set up the East Asia Vision Group to study long term vision for economic cooperation. The group has presented the leaders with recommendations including the establishment of East Asia FTA (EAFTA). The Expert Group, which was set up at the recommendation of ASEAN+3 Economic Ministers, presented recommendations to

⁷ BIMSTEC include Bangladesh, Bhutan, India, Myanmar, Nepal, Sri Lanka, and Thailand.

⁸ FTAs used for the computation of FTA coverage ratios include enacted and signed FTAs. FTA coverage ratios that are reported in the text are for 2009. The trade statistics used for the computation of the FTA coverage ratios are taken from IMF's Direction of Trade Statistics.

⁹ For comparison, the FTA coverage ratios for the US and the EU are 38 and 74.8 percent, respectively.



the Economic Ministers in 2006 to start the process in 2007 toward the establishment of an East Asia FTA. The recommendations by the Expert Group were not adopted and the Expert Group was asked to conduct further study. The Expert Group undertook a phase two of the project and recommended to start the process toward the establishment of an EAFTA in 2009. Responding to those recommendations, the Leaders ordered the government officials to set up four working groups (rules of origin (ROOs), tariff nomenclature, customs procedure, and economic cooperation) as steps toward achieving an EAFTA.

Japan proposed the CEPEA (Comprehensive Economic Partnership in East Asia), which is an Economic Partnership Agreement including an FTA covering ASEAN+3+3 (India, Australia, and New Zealand) or ASEAN+6, at ASEAN+6 Economic Ministers' meeting in 2006. ASEAN+6 were also then the members of the East Asian Summit, which was held for the first time in 2005. It has been argued that behind the CEPEA idea lies Japan's strategy of taking a leadership role in setting up regional institution in East Asia, as it was China that has taken an initiative in the EAFTA discussions. A similar course of events to those for EAFTA evolved for CEPEA. As also is the case for EAFTA, government officials are engaged in the discussions under the four working groups.

New developments emerged in August 2011, when China and Japan jointly proposed to ASEAN to set up three working groups, trade in goods, trade in services and investment, in EAFTA and CEPEA discussions. Behind this somewhat unexpected joint-proposition seemed to lie a bit of frustration on the part of China and Japan about slow progress achieved by ASEAN toward either EAFTA or CEPEA. Responding to the joint proposition, ASEAN decided to establish an ASEAN-led "Regional Comprehensive Economic Partnership (RCEP)" in November 2011 and then set up three working groups, which were proposed by China and Japan. The Leaders attending the East Asian Summit the same month welcomed the initiative by the ASEAN. At ASEAN Summit in April 2012, ASEAN Leaders agreed to begin the RCEP negotiations before the end of the year. It is expected that the Leaders from ASEAN and possible RCEP members agree to start negotiations in November 2012. RCEP members are likely to include ASEAN+6 countries, but it is up to +6 countries if they would or would not join the RCEP negotiations.

One big obstacle in establishing RCEP is the absence of China-Japan-Korea(CJK) FTA, as CJK account for a dominant economic position in East Asia. A feasibility study of a tripartite FTA by the "private sector" involving government related research institutes began in 2003. The study continued by changing the focuses of research topics over time. Through many years of feasibility study, the important topics were more or less examined and it was the political decision that needed to be made, in order to move forward. It was in 2010 that CJK decided to begin an official joint-study on CJK FTA involving government officials, academics, and business persons. The official joint-study was scheduled to finish by the end of 2012 and to present recommendations on a CJK FTA to the Leaders. The official joint-study was finished one year ahead of schedule in December 2011 and presented recommendation in February 2012 to start CJK FTA negotiations.

Responding to the recommendations by the joint-study, CJK Leaders were expected to launch the start of CJK FTA negotiations at the CJK Summit in May 2012. But Korean President Lee Myung Bak opposed to the idea and the Leaders agreed to start CJK FTA negotiations within 2012. While President Lee did not agree to start CJK FTA negotiations in May, he began FTA negotiations with China in May. Considering growing tensions between Japan on the one hand and China and Korea on the other hand regarding territorial issues, the chances of start of CJK FTA in 2012 are very slim.

It was somewhat surprising that CJK made substantial progress toward CJK FTA until recently, when tensions suddenly emerged. In addition to economic issues such as increased competition among CJK, non-economic issues such as historic and social problems made it difficult for discussing tripartite cooperation such as a CJK FTA. However, economic and non-economic environment surrounding the three countries have changed, as we discuss in the next section, and therefore, positive steps toward the establishment of a CJK FTA were adopted.

One FTA that has attracted an enormous attention recently is the Trans-Pacific Strategic Economic Partnership Agreement (TPP). TPP was originally established under the name of Pacific 4 (P4) by Brunei, Chile, New Zealand and Singapore in 2006. TPP started to draw attention because the United States along with Australia, Peru, and Vietnam joined the four countries in the expanded TPP negotiation in March 2010. Malaysia joined the negotiation in September 2010 and thus nine countries are in negotiation with a target of concluding the negotiation by the end of 2012, which is unlikely. Japan, Canada, and Mexico indicated a keen interest in joining the TPP negotiation in November 2011. Canada and Mexico have been accepted to join the negotiation but Japan has not because the US, Australia and New Zealand have not given an approval. These three countries have demanded firm commitment on the part of Japan to put all the products including agricultural products on the negotiating table for tariff liberalization before they accept Japan in the negotiation. China or Korea have not indicated its intention to join the TPP negotiations. It has been said that for China joining the TPP may not be easy as it requires China to accept not only high level of trade liberalization but also other requirements such as high labor and environment standard. For Korea, which has already enacted an FTA with the US, joining the TPP with the current membership may not give them much additional benefit.

TPP, ASEAN+3, and ASEAN+6 FTAs were recognized as pathways toward an FTAAP, or Free Trade Area of the Asia-Pacific, covering 21 APEC member economies, by APEC Leaders in their summit in 2010. It was the US that proposed an FTAAP in 2006. Behind the US proposal of an FTAAP is a concern that the US would be excluded from East Asia to result in the decline in its economic activities in East Asia. It should be noted that the differences in the members between ASEAN+6 and APEC give rise to important implications of the groupings. Chinese Taipei and Russia, important economic players, are included in an FTAAP, while India, a member of ASEAN+6, is excluded from it. Cambodia, Lao PDR and Myanmar are ASEAN members and thus included in ASEAN+3 and ASEAN+6, but they are not included



in APEC. Because of this, APEC and more significantly TPP are regarded as frameworks that may weaken ASEAN cohesiveness. Another important characteristic of TPP is its high liberalization requirement in that practically all the tariffs on intra-FTA members' trade are to be removed within ten years.

It may be important to point out that the US does not seem to be interested in promoting economic development of ASEAN countries as a group. Unlike China, Japan, Korea, Australia-New Zealand, and India, which enacted FTAs with ASEAN, and the EU, which is negotiating an FTA with ASEAN, the US has not discussed the possibility of the US-ASEAN FTA. Instead, the US enacted bilateral FTAs with Singapore and began discussions with selected ASEAN countries within the framework of TPP. This reflects the US view that the US is interested in high-level FTA with comprehensive coverage including labor, environment, competition policy, intellectual property right, and trade facilitation with a focus on supply-chain management. To the eyes of the US, some ASEAN countries are not ready to participate in such high-level FTA.

III. Characteristics and Motives of FTAs in East Asia

One notable characteristic of FTAs in East Asia is their comprehensiveness in coverage. As such, some of the FTAs established in East Asia are named as Economic Partnership Agreement (e.g. Japan-Singapore EPA, JSEPA), or Closer Economic Partnership Arrangement (e.g. China-Hong Kong CEPA), and others. These new types of FTAs typically include facilitation of foreign trade, liberalization and facilitation of foreign direct investment (FDI), and economic and technical cooperation, in addition to trade liberalization, which is included in traditional FTAs. It may be worth noting that the contents of these new types of FTAs are similar to those of Asia Pacific Economic Cooperation (APEC) forum, whose three pillars are (1) liberalization and (2) facilitation of foreign trade and foreign investment, and (3) economic and technical cooperation.

Among the three pillars, economic and technical cooperation is given a special attention in FTAs established in Asia because narrowing development gap between the high-income and low-income countries is considered very important for achieving economic prosperity and social and political stability of the region, which consist of the countries with very different levels of economic development. One of the cooperation programs that can be found in many FTAs in Asia is promotion of small and medium sized enterprises (SMEs), which would contribute not only to the construction of competitive and resilient economic structure but also to the improvement of livelihood of people. These objectives may be achieved because SMEs have important positions in many economies in terms of production and employment. It may be important to note that economic assistance has been used to gain support for FTAs from FTA partners by China and Japan, which are eager to play a leadership role in regional integration.

Having noted a common characteristic of comprehensiveness of FTAs in Asia, specific contents do differ among the FTAs, reflecting different motives of the countries concerned. Japan emphasizes the importance of liberalization and facilitation of investment and service trade, as such measures would provide free, transparent and stable business environment for Japanese firms, which have invested heavily in Asia. In particular, Japan is interested in setting up well functioning intellectual property right protection system. By contrast, developing countries such as ASEAN and China do not have equally strong interests in these measures. Indeed, ASEAN and China have adopted a gradual and sequential approach by dealing with trade in goods and services and investment separately with different timing, as liberalization in trade in goods is followed by liberalization in service trade and investment. India is interested in liberalization of services trade such as IT software, legal, financial, and medical services, while it is not keen on opening up goods' trade.

Another notable characteristic of FTAs in Asia in recent years is high degree of trade liberalization in goods. As noted earlier on the discussions of AFTA, the trade liberalization rate, defined as the share of products subject to zero tariff rates in total number of products, under the AFTA has risen, indicating gradual trade liberalization. Reflecting the recognition of the importance of high level FTAs in terms of trade liberalization to gain benefits from FTAs, trade liberalization rates adopted for the enacted FTAs in Asia have become generally very high exceeding 95 percent. Noticeable exceptions are those FTAs involving Japan and India. Because of the difficulty in opening up agriculture sector due to strong opposition, Japan has excluded agricultural products from trade liberalization in its FTAs. As a consequence, trade liberalization rates for Japan's FTAs are quite low around 85 percent, while those for Japan's FTA partners are significantly higher around 95 percent¹⁰. Because of strong opposition from protectionist, India has difficulty opening up its market via FTAs, resulting in low trade liberalization for its FTAs. Indeed, India's trade liberalization rate for India-Singapore FTA is as low as 43.8 percent.

Let us turn to the discussions on the motives of East Asian countries behind their FTA strategies. Various common motives, despite the differences in their importance among the countries, can be identified. First, rapid expansion of FTAs in other parts of the world has made Asian economies realize the importance of establishing FTAs in order to maintain and expand their export opportunities¹¹. FTAs with this kind of market seeking objective are largely of defensive nature. A case in point is Japan's FTA with Mexico. Japanese firms were in disadvantageous position vis-à-vis US firms or EU firms in the Mexican market because the US and the EU had FTAs with Mexico, under which their firms had duty-free access to Mexico. In order to overcome this disadvantage, Japanese firms put pressure on the Japanese government to negotiate an FTA with Mexico. It should be noted here that a stalemate of the negotiations of the Doha Development Agenda under the auspices of the WTO turned the attention of the WTO members with an interest in trade liberalization to FTAs. The market seeking motive played a role

¹⁰ Information on trade liberalization rates are provided by the Ministry of Economy, Industry and Trade (METI).

¹¹ See Urata (2010) for the discussions on this point.



for FTAs between and among Asian economies, as trade barriers are still substantial for many sectors in Asian economies.

Second, countries interested in promoting structural domestic reform to achieve economic growth use FTAs as external pressure on the opposition to structural reform, in order to implement domestic structural reform. The motive of promoting domestic reform was important for Korea in pursuing an FTA with the US. Being sandwiched between China, a rapidly catching up economic giant, and Japan, highly competitive another economic giant, Korea needed to carry out structural reforms to maintain and improve competitiveness.

Third, rivalry among Asian economies over gaining a leadership role in the region has activated their FTA strategies. Both China and Japan, which are competing to become a ‘leader’ in the region, are keen on using FTAs to strengthen their relationships with ASEAN, Korea and other countries. Indeed, in November 2002 Japan proposed an economic partnership framework to ASEAN one day after China agreed to start FTA negotiations with ASEAN. It should also be noted that ASEAN, Korea and other countries consider FTAs as a means to maintain and increase their influence in Asia. ASEAN has been rigorously pursuing FTAs with major countries in order for them to take a “driver’s seat” in regional integration in Asia, while Korea is moving ahead of other countries such as Japan and China to take a lead in the FTA race.

Fourth, countries with active outward foreign direct investment would like to use FTAs to improve business environment in FDI recipient countries, so that multinational corporations (MNCs) can perform efficiently. This motive is sought by including FDI liberalization and facilitation in FTAs. As was pointed out earlier, this motive is one of the most important motives for Japan as many Japanese MNCs have invested in East Asia. This motive is likely to be more important for other Asian countries in the future, as the number of countries in East Asia with active outward FDI is bound to rise.

So far, we have discussed the motives behind bilateral and plurilateral FTAs. We now turn to the motives behind region-wide FTAs such as EAFTA, CEPEA or RCEP. Many countries in the region realize the importance of establishing a large region-wide, unified market to promote economic growth and reduce development gap as firms can expect benefits from exploiting scale economies. Besides, economic and technical cooperation may be provided efficiently under one region-wide framework by consolidating separate programs provided by individual countries.

The crises contributed to the discussions on the promotion of region-wide FTAs. The financial crisis in East Asia in the late 1990s increased the awareness among East Asian countries of the need for regional cooperation such as a region-wide FTA to avoid another crisis and to promote regional economic growth. The immediate concern about financial problems resulted in regional cooperation in financial areas. Specifically, bilateral currency swap arrangements to deal with the shortage in foreign exchange under the name of Chiang-Mai Initiative (CMI) were set up by ASEAN+3 countries in 2000, and then

it was expanded to become multilateral currency swap arrangement in 2009 under the name of CMI Multilateralization. Furthermore, ASEAN+3 countries are developing Asian Bond Market, in order to establish efficient and liquid bond markets in East Asia, with a view to better utilize East Asian savings for East Asian investments. It is also expected to contribute to the mitigation of currency and maturity mismatches in financing, which was one of the factors that led to the Asian financial crisis in 1997-1998.

The global financial crisis in 2008 also increased an interest among the East Asian countries for the establishment of a region-wide FTA. Unlike the case of the Asian financial crisis, for which financial linkage with the US and Europe was a cause of the problem, it was East Asia's dependence on the US and Europe for its exports that caused a sharp decline in East Asia's economic activities. A collapse of the housing bubble in the US led to the subprime mortgage crisis in 2008, which in turn spread to Europe. As a result of the subprime mortgage crisis, US and EU economies experienced a sharp decline in their economic activities, leading to a huge decline in their demand for imports. This decline in import demand in turn caused a decline in East Asia's exports to the US and EU, triggering a downward spiral. In order to avoid such negative impacts caused by factors outside the region, East Asian countries started to argue for the need to increase intra-regional dependence by establishing a region-wide FTA.

Finally, it should be noted that the TPP negotiations that began in 2010 put the pressure on some East Asian countries to speed up the process of setting up a region-wide FTA in East Asia. More specifically, China appears to have responded to Japan's indication of its intention to join the TPP negotiations by moving the process forward. As noted earlier, China changed its attitude toward a region-wide FTA by not holding on to ASEAN+3 FTA as China and Japan jointly proposed setting up three working groups for both ASEAN+3 or ASEAN+6 FTAs in August 2010. Furthermore, Japan's action has made China very interested in the formation of CJK FTA, as we discussed in the previous section.

IV. FTA Utilization

It is needless to repeat that the objective of an FTA is to promote foreign trade between/among FTA members. It is therefore important to assess the utilization of FTAs. Such a study would reveal the obstacles in using FTAs, thereby providing important policy implications for the construction of a meaningful region-wide FTA. With this in mind, we examine the utilization of FTAs by firms. Since the availability of the information required for such an analysis is limited, we can examine only some selected cases.

Two kinds of information have been used to assess the utilization of FTAs. One is trade data which are covered by FTA preferences. One can obtain the FTA utilization rate by dividing FTA trade data by overall trade. The computed FTA utilization rate is likely to be undervalued if trade subject to zero tariff rate is not excluded from the overall trade. Although this FTA utilization rate is the ideal measure, such measure may be computed for very few countries in Asia because of data unavailability.



The other information to assess FTA utilization that previous studies used is that obtained from a firm survey. Typical survey on FTA usage asks if a firm used FTA or not. FTA utilization is measured by dividing the number of FTA using firms by the number of surveyed firms. Some of the problems of the information obtained from this kind of firm survey include the followings, limited coverage, no information on traded value, and difficulty in determining the denominator. Firm surveys are generally conducted by sending out a questionnaire to selected firms or by conducting an interview with a small number of firms. Their coverage is naturally limited. The computed FTA utilization rate is based on the number of firms rather than the value of trade, as such it should be denoted as firm-level FTA utilization rate. Generally, one uses the number of surveyed firms as the denominator for the computation of the FTA utilization rate, but one should be careful not to include firms without trading relationships with the countries under question. Specifically, to compute Japan's FTA utilization rate for Japan-Singapore FTA, one should include only the firms trading with Singapore. In general, FTA utilization surveys try to obtain the information on the use of several FTAs, and thus it becomes difficult to isolate the information that is appropriate only for a particular FTA in question. Having indicated some possible problems in using the information obtained from firm surveys, it has to be emphasized that firm surveys provide important information for deriving policy implications. For example, firm surveys can provide the properties of firms using or not using FTAs.

Table 3 presents FTA utilization ratios for selected FTAs in East Asia. FTA utilization rates vary widely among different FTAs, ranging between 99 percent after adjusting for zero tariff rates for Australia and 2.6 percent for Korean exports to ASEAN. As one would expect, the FTA utilization rates derived from the firm survey tends to be lower than those computed by using trade data.

Analyses of the firm responses to the questionnaire reveal several interesting observations. One common finding from both ADBI and RIETI studies is that the size is an important factor for the use of FTAs. Large firms tend to use FTAs more than small firms because large firms can afford costs required to obtain the certificate of origin, which is needed to use an FTA. Such costs include learning about FTA provisions, obtaining information such as the sources of inputs to be submitted with the application for the certificate of origin. Small firms with limited human and financial resources cannot afford such costs.

The ADBI study showed the firms with larger foreign equity participation tend to use FTAs. This finding indicates that firms with extensive foreign networks can take advantage of tariff-free opportunities arisen from FTAs. Product based studies on Japan and Thailand for the RIETI study confirmed the expected positive relationship between high FTA preferential tariff margin (difference between applied and FTA tariff rates) and high use of FTAs.

ADBI and RIETI studies found similar impediments to FTA utilization. They include lack of information (knowledge) about FTAs, small FTA preferential tariff margin (differential between MFN tariff rate and FTA tariff rate), administrative costs associated with obtaining certificate of origin. As

indicated above, these costs are particularly high for small firms. These findings indicate the need to reduce costs for the use of FTAs by simplifying the procedures.

ADB study investigated the views of firms concerning the Spaghetti bowl effect or multiple ROOs and found that large and old firms with multiple FTA markets tend to have negative views. Unexpectedly, small firms are found not to be concerned with the Spaghetti bowl effect. It may be that large firms are engaged in trade with many countries and therefore they face the problems of multiple ROOs. By contrast, small firms tend to trade with a small number of countries, and thus do not face the multiple ROO problems. These findings appear to show that resolving the problem due to the spaghetti bowl effect, or multiple ROOs, would expand trade among FTA partners, contributing to the increase in FTA utilization rate.

Table 3 FTA Utilization Rate (%)

ADB Study (Exports)					
Japan	PRC	Korea	Singapore	Thailand	Philippines
29.0	45.1	20.8	17.3	24.9	20.0
RIETI Study (by destinations)					
Exports					
	Japan		Korea		Thailand
Mexico	32.9	Chile	96.9	Indonesia	61.5
Malaysia	12.2	ASEAN	2.6	Malaysia	25.2
Chile	23.7			Philippines	46.9
				Vietnam	46.6
				Australia	62.5
				Japan	22.7
Imports					
	Korea		Australia	adjusted for 0 tariff	
Chile	90.5	New Zealand	50.5	95.19-97.60	
Singapore	29.8	South Pacific	3.2	99.32-99.35	
EFTA	42.5	Singapore	2.9	90.99-91.44	
ASEAN	43.3	Thailand	42	75.97-73.86	
		US	23.2	69.42-82.51	
		Chile	6.5	96.05-96.33	

Note: ADB Study and Japan for RIETI Study use information obtained by firm surveys, while others in the RIETI Study use trade(customs) data.

Source: Kawai and Wignaraja (2011) for the ADB Study, For the RIETI Study, Takahashi and Urata (2010) for Japan, Cheong et.al (2010) for Korea, Pompret et.al. (2010) for Australia, and Kohpaiboon (2010) for Thailand.



IV. Establishment of a Region-wide FTA

Asia has seen a rapid increase of FTAs since the beginning of the 21st century. Many of these FTAs are bilateral or plurilateral and unlike the situations in North America or Europe, a region-wide FTA has not been established yet in Asia. Recognizing the benefits of a region-wide FTA with larger market, Asian countries have been examining the ways to establish a region-wide FTA, as was discussed in section II. Two region-wide FTA proposals were under study, East Asia FTA (EAFTA) comprised of ASEAN+3 (China, Japan, and Korea) and Comprehensive Economic Partnership in East Asia (CEPEA) comprised of ASEAN+6 (China, Japan, Korea, India, Australia, New Zealand). These two proposals appear to have been converged to Regional Comprehensive Economic Partnership (RCEP), so called ASEAN++, in 2011, when ASEAN decided to lead the RCEP, for which any +6 countries (CJK, India, Australia and New Zealand) can join. In addition to these three region-wide FTAs, TPP has become a possible FTA covering some countries in Asia as well as some countries on the other side of the Pacific.

In the discussions of region-wide FTAs, it is useful to know the benefits and costs of such FTAs. Tables 4 and 5 show the impacts of EAFTA and CEPEA on GDP and economic welfare, respectively, for their members and other selected countries. The figures are taken from the simulation exercise using the GTAP model conducted for Phase II of the CEPEA study. Two types of simulation were conducted for EAFTA and CEPEA. One considers tariff elimination only (Scenario 1 for CEPEA and Scenario 4 for EAFTA), and the other takes into account of comprehensive nature of the FTA by including trade facilitation and economic cooperation (Scenario 2 for CEPEA and Scenario 5 for EAFTA). In addition, one more scenario, in which agriculture and food products are excluded from tariff elimination, is adopted for CEPEA simulation (Scenario 3). The data used for the analysis are for 2004.

Three general patterns can be identified from the simulation results. First, both in terms of GDP and economic welfare, FTA members gain while non-members lose. These results are expected because FTA members can improve the use of existing resources such as labor and capital by exploiting newly emerged export opportunities from the formation of FTA, while non FTA members lose export opportunities as a result of discrimination. Second, the larger the FTA membership, the larger are the benefits obtained by FTA members. This relationship is also expected because a larger group provides greater business opportunities so that use or allocation of existing resources can be improved. This observation comes from a comparison of the impacts of CEPEA and EAFTA that shows CEPEA provides larger benefits to the members compared to EAFTA. Obviously India, Australia, and New Zealand gain from CEPEA, but they lose from EAFTA. For the countries that are neither CEPEA nor EAFTA members, the impacts of these two types of FTAs are very similar. Third, the more comprehensive the FTA, the greater is the benefit. A comparison of the results of scenarios 1 and 2 for CEPEA and scenarios 4 and 5 for EAFTA reveals that trade facilitation and economic cooperation increase the magnitude of benefits substantially.

Moreover, a comparison of scenarios 2 and 3 shows that exclusion of agriculture and food products lower the benefits for the CEPEA members. The decline in the magnitude of the benefits is large for developing members with large agricultural sectors.

Table 4 The Impacts of FTAs on GDP (% change)

	ASEAN+6			ASEAN+3	
	Scenario 1	Scenario 2	Scenario 3	Scenario 4	Scenario 5
China	-0.03	4.65	4.64	-0.05	4.49
Japan	0.04	0.64	0.56	0.02	0.63
Korea	0.38	2.67	2.28	0.34	2.64
Indonesia	0.13	4.35	4.13	0.11	4.15
Malaysia	0.62	9.53	8.95	0.57	9.24
Philippines	0.12	5.95	5.51	0.11	5.77
Singapore	-0.02	3.83	3.65	-0.02	3.63
Thailand	0.59	7.46	7.17	0.56	7.21
Vietnam	1.61	11.04	10.17	1.60	10.79
Cambodia	0.38	8.59	7.17	0.29	8.38
Myanmar	0.07	6.15	5.36	0.07	6.00
Lao PDR	0.40	5.99	4.69	0.40	5.94
Brunei and East Timor	1.86	6.98	6.14	1.86	6.92
Australia	0.11	1.27	1.20	-0.03	-0.03
New Zealand	0.08	1.94	1.77	-0.04	-0.02
India	0.45	3.40	2.70	-0.03	-0.07
Hong Kong	0.00	0.02	0.02	0.00	0.02
Chinese Taipei	-0.10	-0.18	-0.15	-0.11	-0.17
NAFTA	0.00	-0.02	-0.02	0.00	-0.02
EU25	-0.03	-0.09	-0.09	-0.02	-0.08
Latin America	-0.02	-0.05	-0.05	-0.02	-0.04
Rest of the world	-0.03	-0.08	-0.09	-0.03	-0.07

Source: CEPEA (2009)

Note: Scenario 1: ASEAN+6: tariff elimination

Scenario 2: ASEAN+6: tariff elimination, trade facilitation, cooperation

Scenario 3: ASEAN+6: tariff elimination (excluding agriculture and food products)
trade facilitation, cooperation

Scenario 4: ASEAN+3: tariff elimination

Scenario 5: ASEAN+3: tariff elimination, trade facilitation, cooperation



Table 5 The Impacts of FTAs on Welfare (Equivalent variation, % of GDP)

	ASEAN+6			ASEAN+3	
	Scenario 1	Scenario 2	Scenario 3	Scenario 4	Scenario 5
China	-0.03	4.37	4.30	-0.05	4.22
Japan	0.18	0.92	0.92	0.17	0.92
Korea	0.68	3.27	3.02	0.64	3.23
Indonesia	0.68	5.13	4.57	0.17	4.51
Malaysia	2.08	13.23	12.45	1.51	12.35
Philippines	-0.06	6.18	5.80	0.01	6.08
Singapore	0.97	7.40	6.82	0.86	6.86
Thailand	2.35	10.01	9.08	2.43	9.84
Vietnam	1.99	11.30	9.74	2.14	11.18
Cambodia	-0.06	7.08	6.02	-0.05	7.04
Myanmar	-0.47	6.01	5.48	-0.59	5.55
Lao PDR	-0.92	4.69	4.60	-0.84	4.72
Brunei and East Timor	5.74	13.35	12.68	5.55	12.84
Australia	0.84	2.49	1.87	-0.17	0.06
New Zealand	0.24	2.61	2.05	-0.21	-0.02
India	-0.19	2.77	2.44	-0.10	-0.09
Hong Kong	-0.48	-0.83	-0.76	-0.42	-0.72
Chinese Taipei	-0.92	-2.52	-2.45	-0.85	-2.39
NAFTA	-0.05	-0.15	-0.13	-0.04	-0.12
EU25	-0.07	-0.18	-0.18	-0.06	-0.15
Latin America	-0.07	-0.19	-0.14	-0.05	-0.15
Rest of the world	-0.10	-0.46	-0.47	-0.07	-0.36

Source: CEPEA (2009)

Note: Scenario 1: ASEAN+6: tariff elimination

Scenario 2: ASEAN+6: tariff elimination, trade facilitation, cooperation

Scenario 3: ASEAN+6: tariff elimination (excluding agriculture and food products)
trade facilitation, cooperation

Scenario 4: ASEAN+3: tariff elimination

Scenario 5: ASEAN+3: tariff elimination, trade facilitation, cooperation

The simulation results brought out the importance of trade facilitation for achieving benefits from FTAs. In the simulation exercise the impact of trade facilitation is considered by assuming import-augmenting technical progress, leading to import expansion. It is of interest to investigate the current conditions concerning trade facilitation for ASEAN+6 countries. The World Bank's Doing Business database reports time and cost associated with trading activities, which are affected by the efficiency, reliability, stability of government administration. Their findings, which are shown in Table 6, reveal wide variations in trading costs among the sample countries. In terms of ranking, which summaries the situations for six different categories, Singapore is ranked top among 183 countries. Hong Kong (2nd), Korea (4th), Japan (16th), Thailand (17th), and Malaysia (18th) are ranked high, while Lao PDR

(168th), Cambodia (120th) and India (120th) are ranked low. Compared to the situation in Singapore, time, documents, and costs required for trading in some countries are twice as much. Reducing time, documents and costs for trading promotes trade and attracts foreign direct investment, which in turn contribute to economic growth. This observation is important in designing FTAs.

Table 6 Trading Across Borders: Trade Facilitation (2011)

	Ranking (out of 183 countries)	Documents to export (number)	Time to export (days)	Cost to export (US\$ per container)	Documents to import (number)	Time to import (days)	Cost to import (US\$ per container)
China	60	8	21	500	5	24	545
Hong Kong	2	4	5	575	4	5	565
Japan	16	3	10	880	5	11	970
Korea, Rep.	4	3	7	680	3	7	695
Taiwan	23	6	12	655	6	12	720
Australia	30	6	9	1,060	5	8	1,119
New Zealand	27	7	10	855	5	9	825
India	109	8	16	1,095	9	20	1,070
Brunei Darussalam	35	6	19	680	6	15	745
Cambodia	120	9	22	732	10	26	872
Indonesia	39	4	17	644	7	27	660
Lao PDR	168	9	44	1,880	10	46	2,035
Malaysia	18	6	17	450	7	14	435
Myanmar	na	na	na	na	na	na	na
Philippines	51	7	15	630	8	14	730
Singapore	1	4	5	456	4	4	439
Thailand	17	5	14	625	5	13	750
Vietnam	68	6	22	580	8	21	670

Note: The data are for June 2011

Source: World Bank, Doing Business 2012

We saw earlier that ASEAN+6 FTA, or CEPEA, will bring large benefits to East Asian countries. Suppose the creation of CEPEA, under the name of RCEP, is a tentative goal for a region-wide FTA in East Asia, what should be a roadmap toward achieving this goal. Outright negotiation for CEPEA is one possibility and sequential negotiations beginning with EAFTA and then CEPEA is another possibility. Regardless of the choices, negotiations should be built on existing ASEAN+1 FTAs, because starting from scratch would be too complex as it involves either 13 or 16 countries.

With this observation in mind, we compare the contents of ASEAN+1 FTAs to identify similarities and differences. Such an analysis would reveal the challenges that policy makers have to overcome to establish a region-wide FTA. Let us begin with the agreements on trade in goods. Kuno (2011) undertook a detailed analysis and he first found that ASEAN+6 countries use different tariff classification for their tariff concessions, making it difficult to construct a rather straightforward and simple tariff schedules.



It is not only that different countries use different tariff schedules but also that the same countries use different schedules for their FTAs with different countries. An example of the former case can be found in ASEAN-Japan FTA, in which Japan uses HS2002 with 9 digit classification, while Singapore uses HS2002 with 8 digit classification. An example of the latter case may be found for Singapore, which uses HS2002 with 8 digit classification for ASEAN-Japan FTA but uses HS2007 with 8 digit classification for ASEAN-Korea FTA.

Tariff concessions of the same country differ depending on FTAs. Table 7 shows the level of tariff concessions (liberalization) by countries for five ASEAN+1 FTAs. Except for Singapore, which eliminated all the tariffs in all three FTAs, other ASEAN countries have different levels of tariff elimination for different FTAs. For example, Thailand eliminated 99 percent of tariffs in ASEAN-Australia/New Zealand FTA, but its tariff elimination rates for other FTAs. The tariff elimination rate is particularly low at 74.3 percent for ASEAN-India FTA. The level of tariff elimination committed by a country depends on various factors including its relative competitiveness of the sectors vis-a-vis FTA partners. A lack of common tariff elimination schedule among different FTAs makes it difficult to consolidate these different FTAs.

Table 7 Tariff Concessions in ASEAN+1 FTAs (%)

	AANZFTA	ACFTA	AIFTA	AJFTA	AKFTA
Brunei	99	99.9	82.6	96.1	97.8
Cambodia	86	86.7	84.1	na	85.5
Indonesia	93	89	50.4	88.1	90.3
Lao PDR	91	96.4	77.5	na	85.4
Malaysia	96	99.9	79.6	93.6	93.5
Myanmar	86	86.9	73.6	na	87.5
Philippines	95	86.5	75.8	96.8	97.9
Singapore	100	100	100	100	100
Thailand	99	88.3	74.3	96.9	93.7
Vietnam	91	na	69.7	na	83.8
Australia	100	--	--	--	--
New Zealand	100	--	--	--	--
China	--	94.6	--	--	--
India	--	--	74.3	--	--
Japan	--	--	--	86.5	--
Korea	--	--	--	--	92.2

Source: Kuno (2011)

Note: na indicates the data are not available.

AANZFTA: ASEAN-Australia-New Zealand FTA

ACFTA: ASEAN-China FTA

AIFTA: ASEAN-India FTA

AJFTA: ASEAN-Japan FTA

AKFTA: ASEAN-Korea FTA

Figures indicate the proportion of tariff elimination in terms of tariff lines.

On the tariff elimination rates, it should be noted that +1 countries, or Australia, New Zealand, China, India, Japan, and Korea, have different rates in their FTAs with ASEAN. Among them, Australia and New Zealand are most open as they committed to remove tariffs on all products, while India is most closed as it committed to remove tariff on 74.3 percent of the products. Among CJK, the countries with more or less open commitments are indicated in the order of China, Korea and Japan.

In FTAs the rules of origin (ROOs) play a very important role to ensure that preferential treatment is accorded to FTA members by avoiding trade deflection¹². There are four major ROOs that are adopted by ASEAN+1 FTAs, Wholly obtained or produced (WO), Regional Value Content (RVC), Change in Tariff Classification (CTC) and Specific Process Rule (SPR). A general rule is applied to all the products except those products that are subject to product specific rules (PSRs). The general rule is provided in the main text of the agreement, while PSRs are attached as Annex.

Except for ASEAN-China FTA and ASEAN-India FTA, the basic rule is a co-equal rule: RVC(40) or a change in tariff heading (CTH). RVC(40) requires a minimum 40% regional value content. CTH is equivalent to CTC at HS 4-digit level. For ASEAN-China FTA, the general rule is RVC(40). In the case of ASEAN-India FTA, the general rule is RVC(35) and CTSH (a change in tariff sub-heading). In other words, regional content requirement at 35 percent is less restrictive compared to other ASEAN+1 FTAs, but it has an additional requirement of a change in tariff classification, albeit at a higher-6 digit level.

Differences in the rules of origin (ROOs) adopted by five ASEAN+1 FTAs pose an obstacle in establishing a region-wide FTA, in which unified ROOs by product should be adopted. Meddala (2011) compared ROOs adopted by five ASEAN+1 FTAs at 6-digit HS lines. The figures in Table 8 show the number of HS lines that have common ROOs. According to her computation, all five FTAs have at least one common ROO in 64 percent of all HS lines. Moreover, in 90 percent of the time, three or more FTAs share a common ROO. These findings seem to indicate that harmonization of ROOs may not be a far-fetched idea among five ASEAN+1 FTAs.

Table 8 Commonality of ROOs across 5 ASEAN+1 FTAs

Degree of commonality	Frequency distribution of HS lines (6-digit HS2002)	
	No.	%
At least one common ROO in all 5 FTAs	3318	64.0
in only 4 FTAs	766	14.8
in only 3 FTAs	825	15.9
in only 2 FTAs	255	4.9
No common ROOs	23	0.4

Source: Meddala (2011)

¹² The discussions on ROOs draw on Meddala (2011).



Turning to trade in services and investment, agreements have not been included in all ASEAN+1 FTAs. Agreements on service trade are included in ASEAN-Australia/New Zealand FTA, ASEAN-China FTA, and ASEAN-Korea FTA, but not in ASEAN-Japan FTA or ASEAN-India FTA¹³. Ishido (2011) investigated the liberalization levels of the commitments by sectors under these three ASEAN+1 FTAs and ASEAN Framework Agreement in Services (AFAS). He found similarities in the level of liberalization commitments among them, as correlation coefficients, which are computed using country-average liberalization level by sector, between the pair of FTAs are greater than 0.615 (Table 9). Indeed, the correlation coefficient between ASEAN-Australia/New Zealand FTA and ASEAN-Korea FTA is as high as 0.870. These findings indicate that the sectoral patterns of liberalization/protection for trade in services under ASEAN+1 FTAs are similar and thus consolidating these FTAs into one FTA may be possible. However, it is important to note that consolidation of FTAs does not mean liberalization of trade in services.

Table 9 Correlation Coefficients of Service Trade Liberalization Commitments among ASEAN+1 FTAs

	AFAS	AANZFTA	ACFTA	AKFTA
AFAS	1			
AANZFTA	0.718	1		
ACFTA	0.615	0.826	1	
AKFTA	0.704	0.87	0.83	1

Note: AFAS: ASEAN Framework Agreement on Services
AANAFTA: ASEAN-Australia/New Zealand FTA
ACFTA: ASEAN-China FTA
AKFTA: ASEAN-Korea FTA
Source: Ishido (2011)

An agreement on investment is included in ASEAN-China FTA, ASEAN-Korea FTA and ASEAN-Australia/New Zealand FTA. The contents of agreement on investment in these FTAs, ASEAN Comprehensive Investment Area, and Japan-Singapore EPA (FTA) are shown in Table 10¹⁴. A comparison of these contents reveals that ASEAN-China FTA's investment regime is restrictive as it does not ensure national treatment before the establishment, while other FTAs and Japan-Singapore FTA provide it. Difference can be found in the level of liberalization concerning performance requirements. ASEAN-China FTA is most lenient in the application of performance requirements, while Japan-Singapore FTA is most strict. One finds wide variations in terms of market access given to foreign investment among ASEAN+3 countries. Table 11 shows the number of restricted sectors to foreign firms.

¹³ An agreement on trade in services is included in a chapter in Japan's bilateral FTAs with Brunei, Indonesia, Malaysia, the Philippines, Singapore, Thailand and Vietnam.

¹⁴ An agreement on investment is included in a chapter in Japan's bilateral FTAs with Brunei, Indonesia, Malaysia, the Philippines, Singapore and Thailand.

Singapore, Japan, Indonesia, and Brunei are open to foreign firms as the number of restricted sectors is lower than 20 (out of 89 sectors), while Thailand, Malaysia and the Philippines are relatively closed as the number of restricted sectors exceeds 50.

Table 10 Elements of Investment Agreement/Investment Chapter in FTAs

		ACIA	ACFTA	AKFTA	JS-EPA
Liberalization of Investment	National Treatment (pre-establishment)	⊙	△	⊙	⊙
	Most-Favoured-Nation Treatment (pre-establishment)	⊙	⊙	⊙	△
	Prohibition of Performance Requirement (PR)	⊙	△	⊙	⊙
	○=Absolutely prohibited ●=Permitted if required as a condition for granting interest X=no mention	Export requirement	X	X	○
		Export restriction	○	X	○
		Local content requirement	○	X	○
		Local procurement requirement	○	X	○
		Export and import balance requirement	○	X	○
		Domestic sale restriction requirement	X	X	○
		Technology transfer requirement	X	X	●
		Head office establishment requirement	X	X	●
		Research and development requirement	X	X	●
		Specific region supply requirement	X	X	●
		Local citizen employment requirement	X	X	X
		Officers' nationality requirement	X	X	○
	Reservations	Negative	-	Negative	Negative
Protection of Investment	National Treatment (post establishment)	⊙	⊙	⊙	⊙
	Most-Favoured-Nation Treatment (post establishment)	⊙	⊙	⊙	⊙
	Treatment of Investment	⊙	⊙	⊙	⊙
	Umbrella Clause	△	⊙	△	△
	Expropriation and Compensation	⊙	⊙	⊙	⊙
	Compensation in Cases of Strife	⊙	⊙	⊙	⊙
	Transfers	⊙	⊙	⊙	⊙
	Subrogation	⊙	⊙	⊙	⊙
	Investment Dispute Between an Investor and a Member State	⊙	⊙	⊙	⊙
	Disputes Between or Among Member States	⊙	⊙	⊙	⊙

Notes: ACIA=ASEAN Comprehensive Investment Area, ACFTA=ASEAN-China FTA, AKFTA=ASEAN-Korea FTA

JS-EPA=Japan-Singapore EPA, Investment Chapter

For items other than performance requirement, ⊙ indicates the presence of provision concerning the item and

△ indicates otherwise.

Source: Ministry of Economy, Trade and Industry, Japanese Government

Table 11 The number of sectors under restriction on foreign ownership (out of 89 ISIC 2-digit industries)

Brunei	18	Myanmar	23	China	40
Cambodia	23	Philippines	50	Japan	12
Indonesia	15	Singapore	10	Korea	21
Lao PDR	29	Thailand	63		
Malaysia	59	Vietnam	45		

Source: EAFTA (2009)



We have examined the liberalization frameworks concerning trade in goods, services and foreign direct investment adopted by ASEAN+5 FTAs. It is important to identify the commonalities and differences in order to make progress towards achieving a region-wide FTA. Having conducted an analysis on the liberalization frameworks, it should also be emphasized that trade and FDI facilitation measures such as customs procedures for the case of trade in goods and screening and appraisal procedures for the case of FDI play important roles in creating one unified market under a region-wide FTA.

V. Concluding Remarks

Asia has seen proliferation of FTAs in recent years. However, unlike the cases in Western Europe or North America, no region-wide FTAs have been established in Asia. Accordingly, concerns for a possible “spaghetti bowl” effect have arisen. To promote foreign trade by avoiding the negative impacts of the spaghetti bowl effect, Asian countries have begun studying the feasibility of establishing region-wide FTAs. Three region-wide FTAs have been proposed and studied. One is East Asia FTA (EAFTA) comprising of ASEAN+3 countries (10 ASEAN countries, China, Japan, and Korea), another is Comprehensive Economic Partnership in East Asia (CEPEA) comprising of ASEAN+6 countries (10 ASEAN countries, China, Japan, Korea, India, Australia and New Zealand), and Regional Comprehensive Economic Partnership (RCEP) comprising of ASEAN++ countries. For both EAFTA and CEPEA working groups comprising of government officials began stocktaking exercise the following four issues, rules of origin, tariff nomenclature, customs procedure and economic cooperation, in ASEAN+1 FTAs with a view to set up unified rules, which are necessary for the establishment of a region-wide FTA. The negotiation for ASEAN-led RCEP, whose members have not been confirmed yet, is likely to be launched at East Asian Summit in November 2012. RCEP is considered to supersede EAFTA and CEPEA.

While Asian countries work earnestly to set up a region-wide FTA in Asia, those Asian countries that are ready to join the TPP should do so. This is because the characteristics of the TPP on the one hand and an Asia-wide FTA on the other hand are different and they can complement each other. The TPP is a very high-level FTA with a number of high-standard rules on “behind-the-border” issues such as competition and intellectual property rights. As such, only countries with developed economic systems can join the TPP. By contrast, a region-wide FTA in Asia, RCEP, places an emphasis on economic cooperation to reduce development gap. Those RCEP countries that cannot join the TPP yet may join it after achieving economic growth and building a relevant economic system with necessary rules on policies.

Finally, it should be noted that the government is expected to provide negatively affected people from FTAs a temporary safety net, in order to successfully negotiate FTAs. Increased competition from increased imports, which result from FTAs, would reduce production and employment. Faced with potential threat of reduced income and/or job opportunities, the workers in non-competitive sectors

oppose FTAs. Recognizing that trade liberalization would promote economic growth but at the same time generate potential negative impacts on certain groups of people, the government should be ready to provide such assistance as temporary income compensation and training/education to those negatively impacted people so that they can upgrade their skills to obtain more productive and higher paying jobs. A combination of trade liberalization with appropriate structural adjustment assistance would improve the welfare level of the people.



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REI Development in Asia-Pacific and East Asia: State of Play and Issues for TPP

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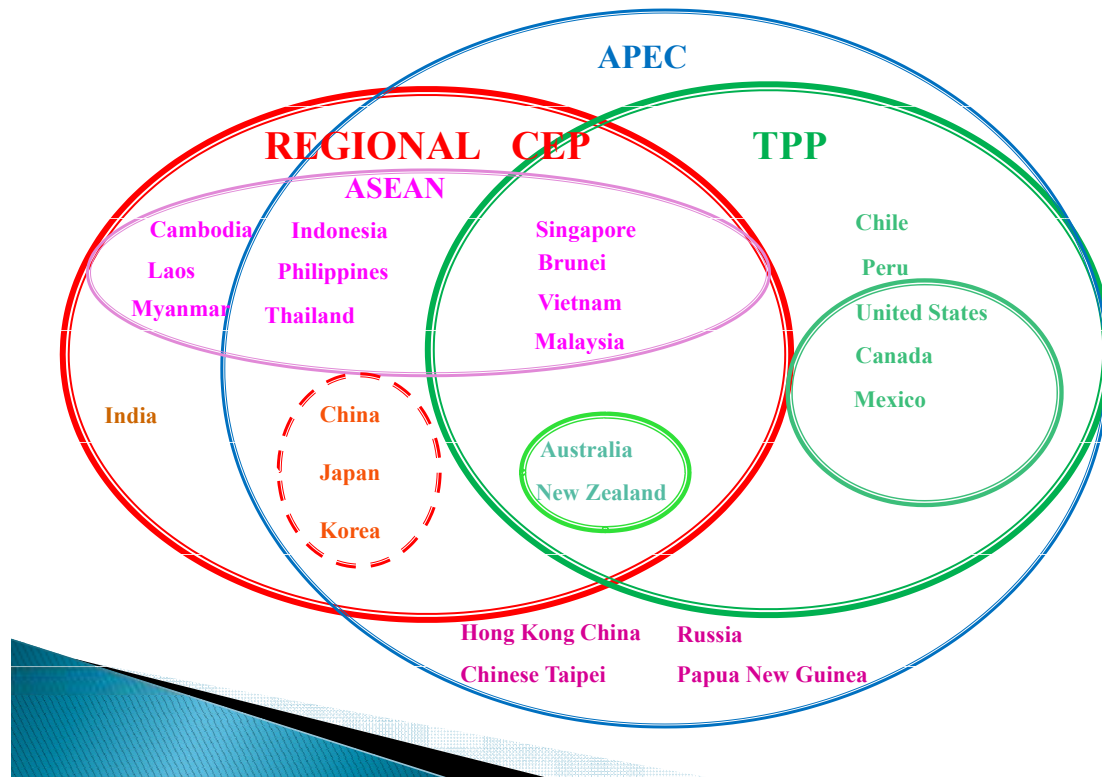
Presented at

27th Pacific Economic Community Seminar, Taipei, 4-5 October 2012

State of Play in the Region

- ▶ **APEC**
 - Remains committed to FTAAP as long term objective
 - Endorsed “two track” approach
 - Trans-Pacific Track – TPP
 - East Asian Track – now to be represented by RCEP
 - Achievement of FTAAP requires eventual convergence of the two tracks
- ▶ **TPP**
 - Recently completed 14th round of negotiations
 - Participants will increase to 11 at 15th round (Canada, Mexico)
- ▶ **RCEP**
 - Agreement to commence negotiations in 2013 to be formalised at ASEAN Summit in November 2011
- ▶ **Key Sub-Regional Developments**
 - ASEAN Economic Community (AEC)
 - Target date of 2015
 - CJK (China-Japan-Korea) FTA
 - Commencement of negotiations planned by end of 2012

CONFIGURATIONS OF ASIA-PACIFIC INTEGRATION



TPP – Key Features

- ▶ aims at “high quality”, “21st century” agreement
- ▶ wide-ranging agenda, including
 - Comprehensive market access
 - Emphasis on regional connectivity and supply chains
 - Business facilitation
 - Full inclusion of “Singapore Issues”
 - Regulatory coherence
 - Integration of SMEs
 - Development and capacity building
 - Technology and Innovation
 - Intellectual property
- ▶ orthodox negotiating modality aimed at legally-binding agreement based on single undertaking
- ▶ initially involved relatively small expansion of trade coverage by FTAs
 - Canada and Mexico will make a big difference
 - Japan would also make a big difference
- ▶ range of participants eventually included will be an important measure of success



Coverage by Existing FTAs of Bilateral Trade Between TPP Participants

	USA	Australia	Singapore	Chile	Peru	NZ	Viet Nam	Brunei	Malaysia	Canada	Mexico
USA		Bilateral	Bilateral	Bilateral	Bilateral					NAFTA	NAFTA
Australia	Bilateral		Bilateral AANZFTA	Bilateral		Bilateral	AANZFTA	AANZFTA	AANZFTA		
Singapore	Bilateral	Bilateral AANZFTA		TPSEP	Bilateral	Bilateral TPSEP AANZFTA	AFTA	AFTA	AFTA		
Chile	Bilateral	Bilateral	TPSEP		Bilateral	TPSEP		TPSEP	Bilateral	Bilateral	Bilateral
Peru	Bilateral		Bilateral	Bilateral						Bilateral	
NZ		Bilateral	Bilateral TPSEP AANZFTA	TPSEP			AANZFTA	TPSEP AANZFTA	AANZFTA		
Viet Nam		AANZFTA	AFTA			AANZFTA		AFTA	AFTA		
Brunei		AANZFTA	AFTA	TPSEP		AANZFTA	AFTA		AFTA		
Malaysia		AANZFTA	AFTA	Bilateral		AANZFTA	AFTA	AFTA			
Canada	NAFTA			Bilateral	Bilateral						NAFTA
Mexico	NAFTA			Bilateral						NAFTA	

TPP – State of Play

- ▶ intensive negotiation process (14 rounds to date)
- ▶ difficult issues in reconciling TPP with existing FTAs
- ▶ negotiation groups for over 20 issues
- ▶ report to 2012 APEC Summit highlighted customs, cross-border services, government procurement, telecommunications, competition policy, SMEs, competitiveness and business facilitation, cooperation and capacity building as areas where large measure of agreement exists
- ▶ several chapters understood to be provisionally complete
- ▶ tough bargaining ahead on a range of sensitive/difficult issues
- ▶ “single undertaking” means “nothing is agreed until everything is agreed”
- ▶ completion unlikely before late 2013, more likely 2014?
 - allows time to resolve sensitive/difficult issues in line with the “high quality, 21st century” ambition
 - uncertain effect of leadership transitions in key economies

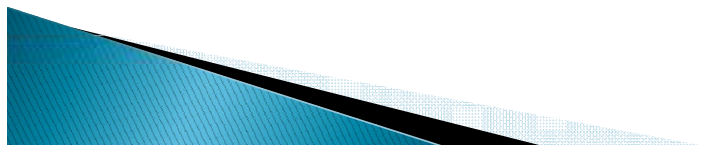
RCEP – Key Features

- ▶ **Clearly a response to TPP**
- ▶ **Guidelines from ASEAN leaders include**
 - “comprehensiveness.....broader and deeper engagement with significant improvements over existing ASEAN FTAs/CEPs with Dialogue Partners”
 - “maintain the centrality and proactive role of ASEAN”
- ▶ **Compromise between EAFTA (A+3) and CEPEA (A+6)**
 - open to all “+6” partners (immediately or with open accession later)
- ▶ **Differentiated from TPP by**
 - flexibility – “accomplished in a sequential manner or as a single undertaking or through any other agreed modality
 - special and differential treatment for ASEAN member states



RCEP – State of Play

- ▶ **negotiations to commence 2013**
- ▶ **aiming for completion in 2015 (also the target date for AEC)**
- ▶ **agenda**
 - working groups already established on goods, services and investment
 - potential for including “behind the border” issues in parallel with AEC
- ▶ **successful delivery of ASEAN’s AEC Blueprint by 2015 recognised as important for success of RCEP**





Difficult Issues in TPP – Market Access

- ▶ **Goods (“usual suspects”)**
 - Textiles and footwear
 - Sugar
 - Dairy
 - Poultry
 - Rules of Origin – how to facilitate integration, e.g.:
 - can “yarn forward” be dropped?
 - cumulation
 - US concerns over preference erosion in Mexico, Canada
- ▶ **Services**
 - Existing models unsatisfactory, new approaches needed
 - highlighted by PECC project
 - Novelty of negative list approach for some participants



Difficult Issues in TPP – Some Key Considerations

- ▶ **important to distinguish in negotiating positions between “high quality” best practice elements and narrow mercantilist interests**
 - “push back” against the latter is crucially important
 - often seems to be US v. the rest
(*examples: intellectual property, E-commerce*)
- ▶ **defending integrity of domestic policy processes in areas such as health, environment**
(*examples: ISDS, drug pricing and reimbursement programmes*)
- ▶ **accommodating interests and needs of developing countries**
(*exemplar: Vietnam*)
- ▶ **avoiding “one size fits all” approaches**
(*examples: SOEs, express delivery*)
- ▶ **facilitation v. forestalling of future membership expansion**
(*key question: future participation of China? also Korea, Indonesia*)



Difficult Issues in TPP – Intellectual Property

- ▶ **Wide-ranging agenda with many controversial issues**
 - Extension of patents, copyrights
 - Copyright limitations and exemptions (fair use etc)
 - Drug patents and access to test data
 - Internet retransmissions of TV signals
- ▶ **Potential costs and benefits are very large but analytical support is weak**
 - Basic analytical foundation is well understood (trade-off between monopoly costs and innovation/creativity)
 - Applications to specific cases sometimes involve plausible assertions weakly supported by detailed analysis and empirical evidence on incidence of costs and benefits (contrast to extensive analytical and empirical support for DDA agriculture and NAMA negotiations)
- ▶ **Background of failure of ACTA and domestic contestation in US suggests some key issues are not mature for crystallisation in trade agreements**

Difficult Issues in TPP – Drug Pricing and Reimbursement Programmes

- ▶ **Sustained attack by US pharmaceutical industry on programmes operated by some TPP participants to contain rising cost of public health provision**
- ▶ **Not fundamentally an IP issue but cost of weakening of these programmes potentially compounded by extensions of drug patents and other measures to limit availability of generic drugs**
- ▶ **Costs (to governments and patients) and benefits (to pharmaceutical companies) potentially very large**



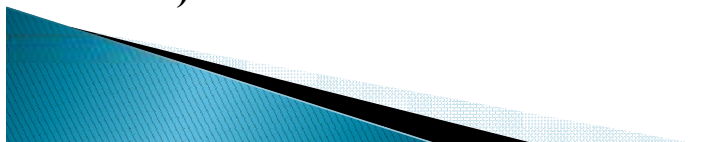
Difficult Issues in TPP – E-Commerce

- ▶ **Contested issues in TPP e.g. include**
 - **Data flow**
 - **Localisation of computer facilities**
- ▶ **Implications for**
 - **Flow of information and ideas**
 - **International research collaboration**
 - **Privacy**
 - **More generally, distribution of costs and benefits associated with use of internet**
- ▶ **Arguably, fundamental to development of national and global society**
- ▶ **Issues also fiercely contested at domestic level e.g. in US**
- ▶ **Negotiators need to listen to civil society on these issues**



Difficult Issues in TPP – SOEs

- ▶ **US proposals widely perceived as aimed against China**
 - **perception encouraged by rhetoric from some quarters of US business**
 - **proposed application at central government level only seen as biased (US has many SOEs at local levels)**
- ▶ **reservations also expressed by Singapore, Malaysia and Vietnam**
 - **Need to study implications for their business structures**
- ▶ **issue is essentially unfair competitive advantage**
- ▶ **Australia insists measures on SOEs should be accompanied by disciplines on government aid to agriculture (export competition – highly sensitive to the US)**



Difficult Issues in TPP – TPP and China

- ▶ **TPP widely perceived in Asia as an “anti-China initiative” by the US**
- ▶ **no support for this approach from other TPP participants**
- ▶ **Deputy USTR Marantis: “this is absolutely not a negotiations that’s directed at China....the whole purpose of TPP is to be a platform for regional integration”**
- ▶ **Jeff Schott (PIIE):**
 - **“its hard to conceive of a comprehensive Asia-Pacific trade agreement that does not eventually include China”**
 - **“China is on the mindset of everyone at the table in the TPP negotiations”**
 - **US-China cooperation needed “to confront the myriad problems facing the world economy”**
- ▶ **imperative that TPP negotiators do not create unnecessary barriers to eventual Chinese participation**

Concluding Remarks

- ▶ **Outcome of negotiations over next 12-18 months will determine**
 - **whether/how far TPP lives up to its “high quality, 21st century” ambitions**
 - **whether TPP becomes an effective springboard for Asia-Pacific economic integration**
- ▶ **Given**
 - **the scale of the effects of a region-wide Asia-Pacific agreement**
 - **the importance for social outcomes of some of the most contested issues,**

**The outcome is vitally important for the region and the global economy,
and
The endeavour demands a commensurate supporting response from the research community**



Session II

TPP vs. ASEAN plus N (or RCEP)





The Transpacific Partnership, Asian Track, and Effects on Non-Partners

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Note : This is the revised draft of a paper presented to the “27th Pacific Economic Community Seminar Regional Economic Integration: Review and Outlook”, 4-5 October, 2012, Taipei. The author is grateful to all participants at this conference and in particular to the paper’s discussant, Shiro Armstrong, for their comments. All remaining errors are attributable to the author alone.

I. Introduction

Globally the number of regional trading arrangements (RTAs, defined by the WTO to be a reciprocal trading agreement between two or more countries) has almost tripled since 1995. Asia has been a major participant in this rapid increase in RTAs; in fact, apart from the ASEAN Free-Trade Area (AFTA) in 1992, no Asian country had a significant RTA in place prior to 2000, whereas as of January 2012 there were 99 Asia-related RTAs signed and in effect and another 151 at various stages of negotiation. Many of these arrangements are intra-regional; Table 1 gives an inventory of these arrangements for the ASEAN+6 economies.¹ Clearly, Asia has embraced regionalism in a big way.

Liberalization at the multilateral level, however, has made less progress since 1995, when the last successful round of the General Agreement on Tariffs and Trade (GATT), the Uruguay Round, began implementation. On the one hand, the WTO system itself is functioning well, with the rule-based system being respected, a much-improved dispute settlement mechanism (over the GATT) in place, and rising membership, with even Russia joining in 2012. The WTO continues to be the pre-eminent institution of global government of trade. Yet, the Doha Development Agenda (DDA) negotiations came to an impasse at the 8th WTO Ministerial Meeting in December 2011 and attempts at other deliverables (e.g., duty-free/quota-free market access for least-developed economies; elimination of “nuisance tariffs”; an agreement on trade facilitation) were generally fruitless. The only ostensible major outcome of the 8th WTO Ministerial was a proposal for a plurilateral agreement on services. Moreover, the WTO agreement

1 ASEAN+3=ASEAN, Japan, South Korea and China; ASEAN+6=ASEAN+3, India, New Zealand and Australia.

Table 1: FTA Partnerships in East Asian Economies

	ASEAN	Brunei	Cambodia	Indonesia	Lao PDR	Malaysia	Myanmar	Philippines	Singapore	Thailand	Vietnam	PRC	Japan	South Korea	India
ASEAN	AEC	AEC	AEC	AEC	AEC	AEC	AEC	AEC	AEC	AEC	AEC	ACECA	ACEPA	ACECA	ACECA
Brunei	AEC		AEC	AEC	AEC	AEC	AEC	AEC	AEC/TSEPA	AEC	AEC	ACECA	ACEPA/FTA	ACECA	ACECA
Cambodia	AEC	AEC		AEC	AEC	AEC	AEC	AEC	AEC	AEC	AEC	ACECA	ACEPA	ACECA	ACECA
Indonesia	AEC	AEC	AEC		AEC	AEC/PTA-8*	AEC	AEC	AEC	AEC	AEC	ACECA	ACEPA/EPA	ACECA	ACECA
Lao PDR	AEC	AEC	AEC	AEC		AEC	AEC	AEC	AEC	AEC/PTA	AEC	ACECA/APTA	ACEPA	ACECA/APTA	ACECA/APTA
Malaysia	AEC	AEC	AEC	AEC/PTA-8*	AEC		AEC	AEC	AEC	AEC	AEC	ACECA	ACEPA/EPA	ACECA	ACECA/CECA
Myanmar	AEC	AEC	AEC	AEC	AEC	AEC		AEC	AEC	AEC	AEC	ACECA	ACEPA	ACECA	ACECA
Philippines	AEC	AEC	AEC	AEC	AEC	AEC	AEC		AEC	AEC	AEC	ACECA	ACEPA/EPA	ACECA	ACECA
Singapore	AEC	AEC/TSEPA	AEC	AEC	AEC	AEC	AEC	AEC		AEC	AEC	ACECA/FTA	ACEPA/EANP	ACECA/FTA	ACECA/CECA
Thailand	AEC	AEC	AEC	AEC	AEC/PTA	AEC	AEC	AEC	AEC		AEC	ACECA/FTA	ACEPA/EPA	ACECA	ACECA
Vietnam	AEC	AEC	AEC	AEC	AEC	AEC	AEC	AEC	AEC	AEC		ACECA	ACEPA/EPA	ACECA	ACECA
NE Asia															
PRC	ACECA	ACECA	ACECA	ACECA	ACECA/APTA	ACECA	ACECA	ACECA	ACECA/FTA	ACECA/FTA	ACECA			APTA	APTA
Japan	ACEPA	ACEPA/FTA	ACEPA	ACEPA/EPA	ACEPA	ACEPA/EPA	ACEPA	ACEPA/EPA	ACEPA/EANP	ACEPA/EPA	ACEPA/EPA				CEPA
South Korea	ACECA	ACECA	ACECA	ACECA	ACECA/APTA	ACECA	ACECA	ACECA	ACECA/FTA	ACECA	ACECA	APTA			CEPA/APTA
India	ACECA	ACECA	ACECA	ACECA	ACECA/APTA	ACECA/CECA	ACECA	ACECA	ACECA/CECA	ACECA	ACECA	APTA	CEPA	CEPA/APTA	

*Signed but not yet in effect.

ACECA	ASEAN-Comprehensive Economic Cooperation Agreement (ASEAN-PRC, ASEAN-Korea, ASEAN-India)
CERTA	Closer Economic Relations Trade Agreement
ACEPA	ASEAN Comprehensive Economic Partnership Agreement
EANP	Economic Agreement for a New-Age Partnership
AEC	ASEAN Economic Community
FTA	Free Trade Agreement
AFTA	ASEAN-Australia and New Zealand Free Trade Agreement
PTA	Preferential Trading Agreement
APTA	Asia-Pacific Trade Agreement
PTA-8	Preferential Tariff Arrangement - Group of Eight Developing Countries
CECA	Comprehensive Economic Cooperation Agreement
SEPA	Strategic Economic Partnership Agreement
CEP	Closer Economic Partnership
SPECA	South Pacific Regional Trade and Economic Cooperation Agreement
CEPA	Comprehensive Economic Partnership Agreement
TSEPA	Trans-Pacific Strategic Economic Partnership Agreement

itself has been criticized for not including (or covering insufficiently) a number of trade-related issues that, some argue, need to be addressed at the multilateral level in the 21st Century, e.g., export restrictions, competition policy (“competitive neutrality”), environmental-related measures (e.g., “environmental” dumping), and, of course, issues related to exchange-rate “manipulation.”

Nevertheless, from an economic perspective, a multilateral, non-discriminatory approach to trade and investment liberalization dominates a regional strategy; the cost of the latter manifests itself in the well-known effects of trade and investment diversion but also in perhaps less-appreciated areas of trade-related behind-the-border regulations. Be that as it may, for both economic and politically-related



motivations, RTAs have become the most influential dynamic in global commercial policy. Nowhere is this more apparent than in Asia.

In this paper, we will focus on the potential effects of various configurations of trade agreements in the Asia-Pacific region for non-partners. We begin in Section II with a brief review of why the DDA has not made much progress and arguably will unfortunately not move forward at least in the short term. This is followed in Section III with a brief discussion of “mega trends” in Asian regionalism in Section III, with a focus on a “Transpacific track” (the Transpacific Partnership, or TPP) and an “Asian track” (focusing mainly on ASEAN+3). This is followed in Section IV with analysis of the effects of these tracks on non-partner countries, drawing from on-going work with Peter Petri and Fan Zhai.² Section V concludes.

II. The Doha Development Impasse: Why We’re Stuck

Relative to previous negotiating rounds, the DDA has been characterized by far greater participation of developing countries, which have raised their expectations as to what they hope to receive from developed countries in terms of liberalization of certain labor-intensive, but especially agricultural, goods.³ Developed countries, on the other hand, pressed, *inter alia*, for deeper cuts in industrial tariffs in developing economies. This has given the impression of “North-South” tension at the DDA and has been blamed for the 2011 impasse, an impasse that will continue at least until mid-2013.

No doubt, the differences between the negotiating stances of the “North” and the “South” were in evidence throughout the entire DDA negotiations. This is, perhaps, quite predictable: negotiators focus on improving market access and facilitating the development of comparative advantage industries. For the North, this means concentrating on higher-value added manufactures; financial and other services; protection of intellectual property; and investment and trade facilitation, which facilitate foreign direct investment (FDI) flows. The South, on the other hand, naturally focuses on labor-intensive manufactures and resists liberalization of its most sensitive areas, as well as behind-the-border measures that may infringe on national sovereignty.

However, the actual situation is far more complex: negotiating stances are not completely dictated by North-South differences. In fact, there are also tensions across emerging market economies. Trade across the “BRICS” (Brazil, Russia, India, China and South Africa) has been rising considerably and productive and export structures between most of them (in particular, Brazil, India and China) are far more similar than, say, those of the key developed countries at the negotiating table at the DDA. *Ceteris paribus*, we would expect that political interests in these economies would be at least as sensitive (but, most likely, more sensitive) to competition due to liberalization under the DDA from fellow BRICS than from developed economies.

² Petri, Peter A., Michael G. Plummer, and Fan Zhai, *The Transpacific Partnership and Asia-Pacific Integration: A Quantitative Approach*, Peterson Institute of International Economics, forthcoming.

³ Part of this section draws from Plummer (2012).

In sum, the DDA will likely be stalled for some time, and more modest approaches to multilateral liberalization will themselves probably be limited. As the regionalism trend emerged in full force in the early 2000s side-by-side with DDA negotiations, we can expect that it will be the only game in town for at least the next few years (and, most likely, longer).

III. Pathways to the Free-trade Area of the Asia-Pacific: TPP and ASEAN+

Before starting, we should be explicit about what we mean by “Asian regionalism.” In particular, what will be the optimal configuration of Asian economies in RTAs? In general, wider FTA arrangements in Asia are expected to be better than smaller ones, as suggested by the theory of preferential trade agreements and underscored in such studies as Kawai and Wignaraja (2008) and Petri, et.al. (2012). The former study suggested that an Asia-wide FTA would be best (compared to bilaterals) from an economic point of view, but considering the strategic and political importance of the United States in Asia, perhaps an East Asia+NAFTA accord, or even the Free-Trade Area of the Asia Pacific (FTAAP), would be best. Petri, et.al. (forthcoming 2012) focuses on two “pathways” to the creation of the FTAAP; one track assumes the creation of the “TPP 9”⁴ in 2013, followed by the accessions of Canada, Mexico, Korea and Japan in 2014; and an Asian track, which assumes the creation of a Northeast Asian FTA in 2013 (i.e., between China, Japan and Korea) and an ASEAN+3 FTA in 2016. Both tracks then “merge” and include additional APEC members in creating the FTAAP in 2020, as planned at the November 2010 Yokohama APEC meeting (the “Yokohama Vision”). While the study estimates large gains along both tracks, by far the greatest gains accrue when the tracks are merged in 2020; indeed, gains rise by 2.5 fold in the FTAAP scenario, from a two-track cumulative total of \$766 billion to \$1,922 billion in 2025. Bigger is better in Asia-Pacific cooperation.

The study also considers other potential configurations along the “Asian track,” including the Regional Comprehensive Economic Partnership (RCEP), formally launched in November 2012 to be composed of ASEAN+3, Australia, New Zealand, and India. The proposal would include trade in goods; trade and business facilitation; trade in services; intellectual property protection; investment; economic and technical cooperation; dispute settlement and an open accession clause. Negotiations are scheduled to begin in 2013. In sum, it is an ASEAN-centered agreement with strong ambitions. However, our focus is on the ASEAN+3, with the belief that such an agreement is more likely than the realization of an ambitious, deep agreement with India, a country which has shown considerable ambivalence toward such liberalization and harmonization. Indeed, the decision to negotiate a trilateral China-Japan-Korean (CJK) FTA in May 2012, the first step in the creation of an “Asia track” FTA, may have been put on hold for

4 The “TPP 9” includes the original “P4” countries (Brunei Darussalam, Chile, New Zealand, and Singapore), Australia, Malaysia, Peru, the United States, and Vietnam.



much of the year, but in November 2012 the countries agreed to begin negotiations in early 2013, despite problematic territorial disputes. No doubt significant progress at the TPP has helped these countries overcome some of the political obstacles. The on-going series of bilateral FTAs may also be reducing endogenously obstacles to regional integration (Plummer and Wignaraja 2007), but significant obstacles remain.

IV. Effects of Asia-Pacific Integration on Non-partners

The potential economic effects of various configurations of FTAs in the Asia-Pacific region vary, but in general they tend to be strongly positive.⁵ However, the second-best nature of these accords generally produces a negative effect on non-partners, an analysis of which is often neglected in these studies in favor of the aggregate results. Below, we begin with a review of the effects of a “TPP track” and an “Asian track” based on our forthcoming study (Petri, et. al., 2012). This is followed by a specific focus on the implications for the EU, which is a grouping that is completely outside the process.

A. General Results on Excluded Asia-Pacific Partners

As referred to above, Petri, et. al. estimates the effects of Trans-Pacific and Asian integration using an advanced, 18-sector, 24-region, computable general equilibrium (CGE) model of the world economy. In sum, the model used in the study, developed by Zhai (2008), incorporates recent theoretical advances that emphasize firm heterogeneity as a factor in explaining trade flows. In this framework, trade liberalization affects not only sectoral specialization patterns, but also the range of varieties of goods and services available for consumption and production, and the mix of firms with different productivity levels in the output mix. Moreover, the study endeavors to capture all aspects of the TPP and Asian-track agreements, no mean feat given the complicated nature of “21st Century” agreements. It provides detailed results on income, trade, production, demand and employment.

Table 2 summarizes what the estimate income effects of the “TPP track” and “Asian tracks”, as detailed above; Table 3 shows the estimated effects on exports. All changes are calculated relative to the baseline, which includes incorporation of all existing trade agreements.⁶ Clearly, the implications of these different tracks vary across non-partner economies, with some (e.g., the United States under the Asian track) actually gaining (i.e., any trade diversion is overwhelmed by positive terms of trade and income effects). However, some economies are actually hurt fairly significantly; in particular, Chinese Taipei is negatively affected by both TPP and Asian Tracks to the tune of about 2 percent of GDP, which is a very large result for trade diversion in a CGE model. Once Chinese Taipei becomes included in the integration

⁵ See Petri, et. al. (forthcoming 2012) for a summary of these studies.

⁶ If the agreements had not been fully implemented by 2010, we assume that they would be implemented within a five-year period along the baseline. For example, the US-Korea FTA, which was signed in 2011, is implemented as part of the baseline.

process under the FTAAP, however, it becomes one of the biggest beneficiaries, with income expected to be higher by about 6 percent of GDP relative to the baseline. India is negatively affected throughout, as it is excluded from the TPP and Asian tracks in these examples (in the RCEP simulations, however, it does gain though these benefits are relatively low as a percentage of GDP).

Table 2. Income gains under alternative scenarios

Economy	GDP 2025 (billions of 2007 dollars)	Income gains in 2025 (billions of 2007 dollars)				Percent change from baseline			
		TPP track	Asian track	Both tracks	FTAAP	TPP track	Asian track	Both tracks	FTAA P
TPP track economies	26,502	128.7	7.8	135.6	405.4	0.5	0.0	0.5	1.5
United States	20,273	77.5	2.5	79.6	266.5	0.4	0.0	0.4	1.3
Australia	1,433	8.6	0.2	8.8	26.4	0.6	0.0	0.6	1.8
Asian track economies	20,084	-55.9	304.2	253.3	844.4	-0.3	1.5	1.3	4.2
China	17,249	-46.8	233.3	189.3	678.1	-0.3	1.4	1.1	3.9
Two-track economies	8,660	245.9	210.7	420.3	483.4	2.8	2.4	4.9	5.6
Japan	5,338	119.4	103.1	209.5	228.1	2.2	1.9	3.9	4.3
Vietnam	340	46.1	13.5	55.8	72.9	13.6	4.0	16.4	21.5
Others	47,977	-24.0	-22.9	-43.5	188.6	0.0	0.0	-0.1	0.4
Russia	2,865	-2.0	-2.6	-4.2	265.9	-0.1	-0.1	-0.1	9.3
Chinese Taipei	840	-2.9	-15.9	-17.6	53.0	-0.3	-1.9	-2.1	6.3
Europe	22,714	-3.4	4.7	1.1	-32.6	0.0	0.0	0.0	-0.1
India	5,233	-3.8	-7.9	-11.0	-29.5	-0.1	-0.2	-0.2	-0.6
Other ASEAN	83	-0.4	1.0	0.6	3.1	-0.5	1.1	0.7	3.7
Rest of world	16,241	-11.4	-2.0	-12.4	-71.4	-0.1	0.0	-0.1	-0.4
World	103,223	294.7	499.9	765.6	1921.7	0.3	0.5	0.7	1.9
<i>Memorandum</i>									
TPP	35,162	374.6	218.5	555.9	888.8	1.1	0.6	1.6	2.5
ASEAN+3	28,828	189.5	515.9	674.1	1330.8	0.7	1.8	2.3	4.6
APEC	58,951	313.7	504.2	787.3	2052.0	0.5	0.9	1.3	3.5

Source: Petri, et. al. (2012)

**Table 3. Export increases under alternative scenarios**

Economy	Exports 2025 (billions of 2007 dollars)	Export increases in 2025 (billions of 2007 dollars)				Percent change from baseline			
		TPP track	Asian track	Both tracks	FTAAP	TPP track	Asian track	Both tracks	FTAAP
TPP track economies	4,555	201.5	0.5	199.5	779.9	4.4	0.0	4.4	17.1
United States	2,813	124.2	2.1	124.6	575.9	4.4	0.1	4.4	20.5
Australia	332	14.9	0.2	15.0	52.8	4.5	0.1	4.5	15.9
Asian track economies	5,971	-73.8	618.4	544.1	1772.2	-1.2	10.4	9.1	29.7
China	4,597	-57.4	516.3	456.8	1505.3	-1.2	11.2	9.9	32.7
Two-track economies	2,817	406.4	416.7	740.6	852.1	14.4	14.8	26.3	30.3
Japan	1,252	175.7	220.7	364.5	423.1	14.0	17.6	29.1	33.8
Vietnam	239	89.1	24.0	102.6	137.7	37.3	10.1	42.9	57.6
Others	15,072	-90.4	-90.2	-179.6	-53.5	-0.6	-0.6	-1.2	-0.4
Russia	1,071	-4.4	-4.0	-8.6	301.0	-0.4	-0.4	-0.8	28.1
Chinese Taipei	712	-7.4	-37.7	-43.0	151.1	-1.0	-5.3	-6.0	21.2
Europe	7,431	-38.3	-28.3	-67.7	-268.2	-0.5	-0.4	-0.9	-3.6
India	869	-6.7	-7.5	-13.8	-44.7	-0.8	-0.9	-1.6	-5.1
Other ASEAN	34	-1.1	1.4	0.4	7.0	-3.2	4.3	1.1	20.8
Rest of world	4,955	-32.4	-14.2	-46.8	-199.7	-0.7	-0.3	-0.9	-4.0
World	28,415	443.7	945.4	1304.6	3350.7	1.6	3.3	4.6	11.8
<i>Memorandum</i>									
TPP	7,372	608.0	417.2	940.1	1632.0	8.2	5.7	12.8	22.1
ASEAN+3	8,822	331.5	1036.5	1285.1	2631.3	3.8	11.7	14.6	29.8
APEC	15,126	522.3	993.9	1432.6	3856.3	3.5	6.6	9.5	25.5

Source: Petri, et. al. (forthcoming 2012).

As seen from Table 3, the effects on export growth are (predictably) greater than in the case of income. Chinese Taipei, for example, is hit hardest with exports expected to fall by about 6 percent relative to the baseline. Its benefits from joining the FTAAP are clearly led by a surge in export growth, which are estimated to rise by 21 percent.

A final effect that we might explore concerns FDI. The attraction of FDI inflows is an important goal of RTAs, particularly in the context of developing economies (Krein and Plummer 2012). They bring in new (risk-sharing, non-debt-creating) capital flows, foreign exchange, easy access to foreign markets, and technology transfer. They also have a tendency to strengthen institutions within developing countries, including in the financial sector (see, for example, Prasad, Kose, Rogoff, and Wei, 2006), and create a more stable environment and internal “policy competition”. In doing so, they establish an attractive business environment within which multinationals can easily profit from a vertical division of labor and production and facilitate the emergence of multinationals within the developing region itself. In fact, stimulating FDI inflows by reducing business costs associated with multinational activity has always been a primary objective of ASEAN economic cooperation.

Nevertheless, while welfare-enhancing FDI might be induced via “investment creation” in RTAs, there is also the potential for an “investment direction” effect. Indeed, FDI patterns following an RTA may be similar to the effects of trade creation and trade diversion. A multinational corporation that believes an RTA will lead to greater economic dynamism through the effects mentioned above may be compelled to invest more in one of the members, thus resulting in investment creation. However, if the multinational decides to invest in the member because it now has preferential access to the FTA market, the result is investment diversion. In other words, although investing in an outsider might have been more cost effective, the multinational diverts investment to the FTA because of this regional accord. The motivation is exacerbated by stringent rules of origin in the context of sectors with high tariffs, as the incentive to produce within the confines of the RTA rises at the margin.

The investment diversion effect is difficult to estimate; anticipating changes in FDI due to a policy innovation is difficult given the many determinants of FDI, and separating investment diversion from investment creation is extremely difficult empirically (Plummer and Cheong 2008). However, we would anticipate that investment diversion would be correlated with trade diversion; sections in which tariff protection is high produce the greatest incentives for relocation, combined with restrictive rules of origin. The example of the automobile sector in the context of NAFTA is often cited in this regard: relatively high tariffs on automobiles in the large US market and the restrictive sectoral rules of origin (62.5 percent) combine to create a powerful incentive for foreign automakers to relocate FDI to North America from more competitive sources.

B. The Case of Europe

Europe presents an interesting case as a non-partner. It is obviously very experienced with regionalism; the EU constitutes the deepest economic cooperation arrangement in the world, and over three-fourths of its trade takes place within the context of one preferential trading agreement (including its own Single Market) or another. It has expanded from six Western European countries in 1957 to 27



countries spanning the continent, with the most recent member-states, Bulgaria and Romania, joining in 2007. More are in the process of accession negotiations, in sizes ranging from Macedonia to Turkey. Its economy is larger than that of the United States.

The share of Asia in total EU exports has also been rising, but from a small base and it remains relatively low: in 2011 approximately 8 percent of EU exports went to Asia, up from 7 percent in 2002.⁷ This would suggest a rise in Asia's share in EU's extra-regional exports from 10 percent to 12 percent. At the country level, China's share tripled from 1 percent in 2002 to 3 percent in 2011, while Japan's share has continued a secular decline in its importance for EU exports, from 2 percent in 2002 to 1 percent in 2011.

Given these rising economic ties and the fact that Asian economic growth has been the most dynamic in the world, one can easily understand why the EU has been nervous about Asia-Pacific economic cooperation. This has led to a number of studies focusing on the potential gains of the EU's joining in the FTA trend in Asia via bilateral and regional arrangements with Asian partners. For example, there are several CGE studies that have estimated the potential ex-ante effects of various EU-Asian accords. Francois (2007) estimated the effects of a few potential scenarios in the case of an EU-Korea agreement (which eventually was signed in 2010). He set up three possible scenarios, varying from a "soft" (partial) agreement to a full FTA. The intermediate case included a full reduction of manufacturing tariffs, a 50% reduction in barriers to trade in services, and a 40% reduction in agricultural protection without trade facilitation. Most of the gains in all scenarios were derived from liberalization of trade in services. The welfare effect of this scenario would be an increase of € 2.2 billion (0.03% of GDP) and € 4.3 (1.01% of GDP) for the EU and Korea, respectively. The full FTA scenario would essentially double the gains to the EU and increase gains to South Korea by 2.5 times. However, the aggregate numbers are projected to remain low.

CEPII (2006) also used a CGE model to estimate the potential effects of an ASEAN-EU FTA. It is a standard GTAP-based model, but includes FDI and services. Once again, the bulk of the gains accrue due to the liberalization of services, whose barriers are assumed to fall by 50%. But the welfare effects of the ASEAN-EU FTA are quite low: ASEAN's welfare rises by 2% of GDP relative to the baseline, while the EU gains a mere 0.1%.

In terms of the effects on the EU of Asia-Pacific economic cooperation from which it is excluded, the Petri, et.al. study suggests that the large gains generated by the Asian track actually lead to positive gains for Europe, with growth effects essentially offsetting any trade diversion effects in some of the Asian-track scenarios. However, with the TPP track and the FTAAP, Europe faces a negative impact on aggregate income of \$3 billion and \$32 billion, respectively, albeit in the context of a projected GDP of \$23 trillion in 2025. But trade will be fairly hard-hit: As seen in Table 3, in the FTAAP scenario EU

⁷ Figures taken from UN COMTRADE.

exports fall by 3.6 percent of the total (\$248 billion). While this effect would take place over a 12-year period, it is worrisome to a continent that is currently in the midst of an economic crisis.

Moreover, it is important to note that the pathways to the FTAAP would have an important cost in terms of some strategic interests of the EU. Certainly EU members would gain from a more stable and prosperous Asian region, where approximately 2/3 of the world's poor live. Also, EU firms active in Asia will be able to profit from enhanced efficiencies, and new export markets can be exploited. But the gains would certainly not be as great as if the EU were involved in the process; the EU would gain more from liberalisation at the multilateral level. The EU can (and is) negotiating accords with participants in Asian cooperation, but these are generally bilateral accords; some of the biggest gains from the Asian and Transpacific tracks derive from the ability of these regions to consolidate their many bilateral FTAs, thereby lowering the costs associated with rules of origin and increasing utilisation rates of commercial preferences inherent in the accords. The EU will not be able to do this, unless, of course, it pushed for an initiative at the ASEM, but that would take a sea-change in the direction of that organisation.

V. Conclusion: The Need for Open Regionalism

Given the impasse at the DDA, it is likely that the regionalism trend will continue to dominate international commercial policy. The more recent movement in the Asia-Pacific region in favor of regional trade groupings, as opposed to bilateral FTAs, could potentially address many of the shortcomings inherent in a bilateral approach, particularly with respect to the need to facilitate the expansion of existing production networks and the creation of new ones. But while the estimates of the economic effects of these groupings tend to be positive and in some cases significant, ultimately the implications of any regional grouping will depend on the substance of the accord that brings the countries together. Moreover, as we've seen in this paper, discriminatory trading agreements tend to have negative effects on non-partner countries, and large regional agreements could create a worrisome dynamic if the focus is inward rather than outward.

This leads us to two simple but critical policy conclusions: First, it is essential that policymakers return to DDA negotiations as soon as possible. There is no substitute for the "first best" approach of global trade liberalization; indeed, a strong push in favor of multilateral liberalization would reduce the potential negative effects of the regionalism trend and ensure that large regional trading arrangements do not threaten to divide the global economy. Second, these regional agreements need to adhere to the principle of "open regionalism", which has been the backbone of cooperation under APEC since its foundation, to the greatest extent possible. Hence, the TPP, ASEAN+3, or RCEP need to be focused on global trade and investment, rather than merely on intra-regional links.



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Assessing the Process and Gains from the Economic Integration in Asia Pacific Region

■ Bo Chen*

1. Introduction

Thanks to the most recent wave of globalization since 1980s, countries in Asia Pacific region have been experiencing marvelous economic growth. Many thus expect the 21st century to be the “Century of the Pacific”. To realize this expectation, regional organizations, such as Pacific Economic Cooperation Council (PECC) and Asia Pacific Economic Council (APEC), are dedicated to facilitating regional cooperation, especially the economic cooperation and integration.

It has been almost two decades since the birth of APEC. However, whether the economic integration really takes place and if so to what extent? The answers are not clear and under controversy. Nevertheless, countries in this region are still enthusiastically pursuing freer trade and tighter economic relationship. The “Trans-Pacific Pact” (TPP), ASEAN+N, and sub-regional and bilateral FTAs and PTAs are proposed or have been carried into effect. Though it may hurt some specific interest groups, trade barrier reduction no doubt results in an overall welfare gain to an economy. However, how much the gains are from these freer trade agreement? We are still lack of satisfactory measure.

In this paper, I summarize my research work as well as others’ to quantitatively answer the above-mentioned questions. That is, this paper assesses the process and gains from the economic integration in Asia Pacific Region.

2. The process of economic integration in Asia Pacific Region

APEC leaders have endorsed a proposal to investigate the idea of a Free Trade Agreement of the Asia-Pacific (FTAAP), which if successful, would constitute the largest regional trading bloc in the world. In 2010, APEC measured progress against its Bogor Target of “free and open trade” in developed member economies. While the goal of free and open trade was certainly not met by 2010, it may be possible to argue that APEC has made progress toward its broader goal of deeper economic integration in the region.

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Therefore, it is highly desired to develop a composite index, which can provide a measure of APEC's economic integration agenda and to track the progress of integration on an annual basis.

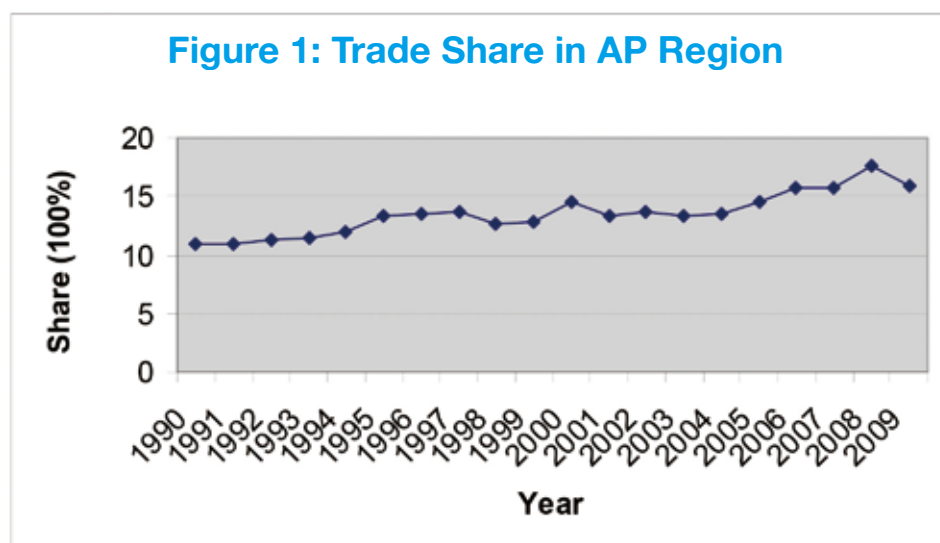
2.1 The flow Indicators

The process of economic integration is commonly defined as the freer movement of goods, services, labor, and capital across borders. So in the following, I first provide the stylized facts on these flows.

To avoid bias, As in Chen and Woo (hereafter CW, 2010) we first net out flows among AP economies that are part of a sub-regional unit. In particular, the sub-regional units we exclude are the so-called “Greater China” region (including Chinese Taipei, Hong Kong, and the People's Republic of China), ASEAN, NAFTA, and the Australia/New Zealand Closer Economic Relations Grouping. Accordingly, the trade and FDI data are calculated as the total of intra-AP flows net of flows among members of the sub-regional units. For instance, we exclude China's FDI flows with Hong Kong and Chinese Taipei when we calculate the total AP regional FDI inflows to and outflows from China. Ignoring the effects of sub-regional agreements may seriously overstate the level of integration in the AP region. For example, Mexican trade and FDI inflow increased rapidly after it became a member of NAFTA in 1992. However, most of the growth was due to increasing business with the United States and Canada rather than with the economies outside of NAFTA. A global economic integration index for Mexico that does not exclude the effects of NAFTA would provide a false reading of Mexico's integration with the world.

Figures 1 to 3 show, respectively, the share of AP intra-regional imports and exports (to regional GDP), the intra-regional FDI share (to regional Gross Capital Formation), and the intra-regional tourist share (to total annual international tourists hosted by all AP sample economies) from 1990 to 2009.

As illustrated in figure 1, the intra-regional trade share, though volatile, overall had been increasing and peaked in 2008, which indicates a closer trade relationship thanks to the effectiveness of regional trade agreements. Without exemption, the most recent global crisis also hit the intra-regional trade in Asia Pacific region. As a result, the trade share declined to its 2007 level in 2009.





Compared to trade share, the FDI measure, as shown in figure 2, has been much more volatile, with an overall slightly decreasing trend. However, the decline trend must be interpreted with caution. Two reasons, rather than disintegration, may account for the declining FDI share. First, even though there has been a large increase in FDI in many AP economies, much of the increase has been due to investment among economies belonging to the same sub-regional trade agreement, e.g. NAFTA. Another factor worth noting is the growing volume of FDI inflow from the tax havens such as the Cayman Islands and the British Virgin Islands. While much of this inflow may in fact originate from AP economies, we are unable to make this determination based on the available data. It is likely, therefore, that the investment measure of AP integration is understated.

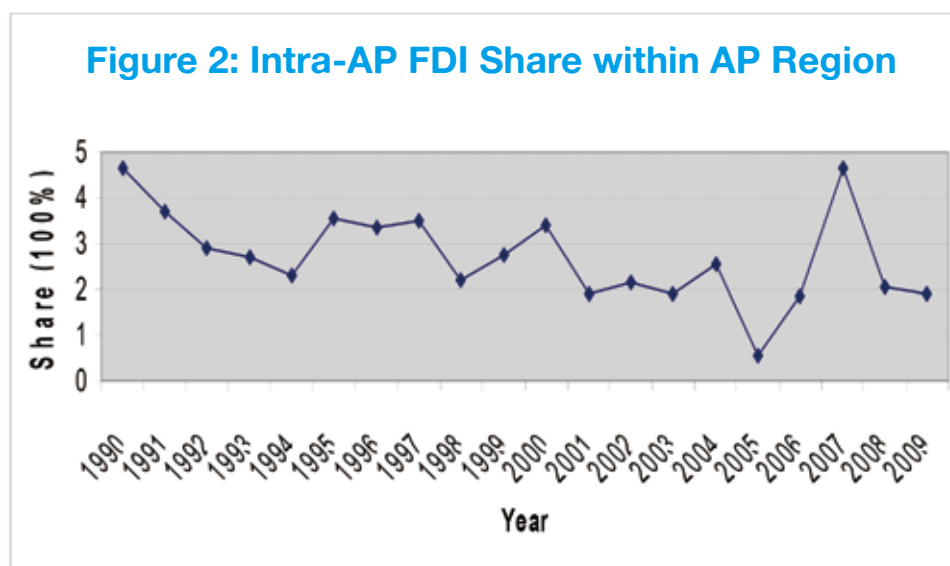
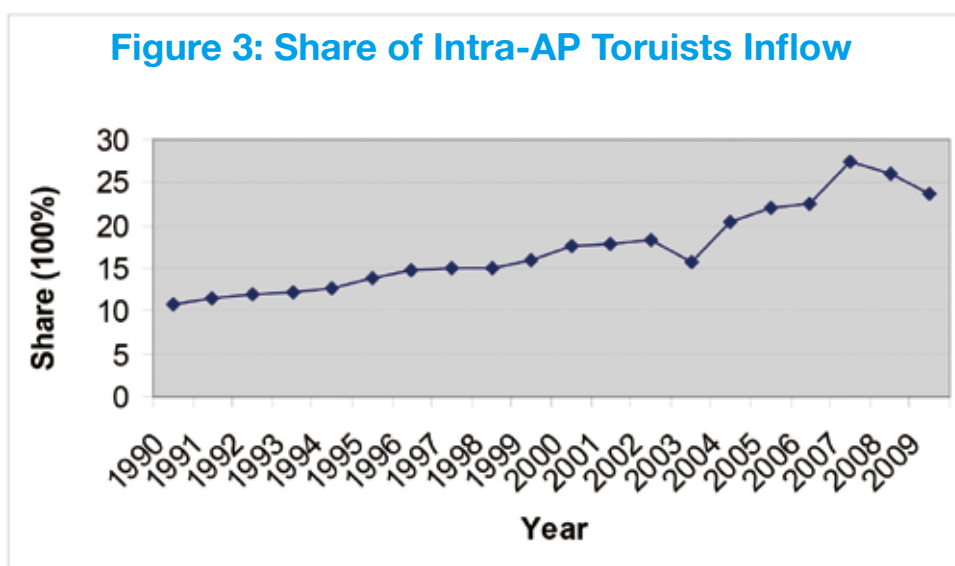


Figure 3 illustrates that tourist share had both increased steadily most of the time since 1990 but the trend was inversed after 2007.



Compared to trade, FDI and tourism indicators responded earlier to the most recent economic crisis which exhibit procyclical characteristic.

2.2. The stock indicators

Though the intra-regional flows are straightforward indicators for measuring economic integration, it is argued that the underlying economic integration should be an accumulative process, rather than the volatile yearly changes suggested by those flow indicators only. For example, to measure economic integration, Heshmati and Oh (2005) include GDP per capita, Cahill and Sanchez (2001) consider the relative size of the agriculture sector to GDP. We also need to check relevant “stock” indicators.

Given data availability, we select the following five stock indicators, which I refer to as convergence indicators: real GDP per capita, non-agriculture sectoral share (to GDP), urban resident ratio, life expectancy, and education expense share (to GNI) (as a proxy for investment in human resource).

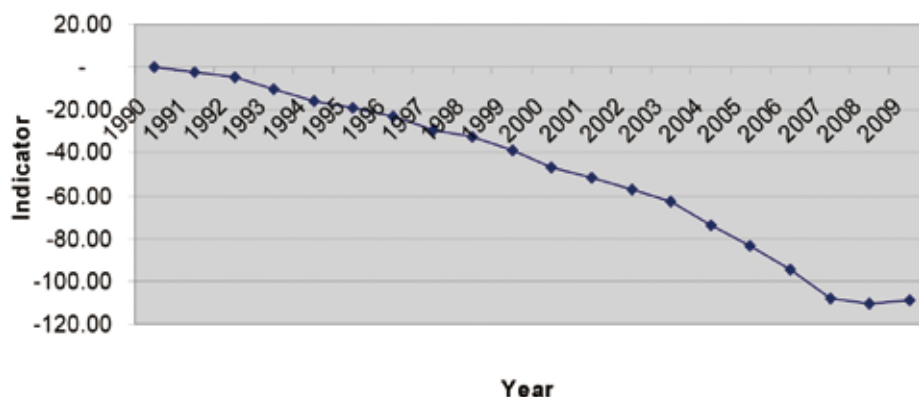
As in CW (2010), these indicators are constructed as follows,

$$Convergence.Indicator_{it} = 100 - \frac{Abs.Dev._t}{Abs.Dev._{1990}} * 100 \quad i=1,...,5 \text{ and } t=1990,...2009.$$

Compared to the base year (1990) indicator, which is normalized to zero, a positive indicator means that the absolute deviation of that year is smaller than that of the base year, i.e., there has been convergence compared to 1990; a negative number would imply the opposite, which is greater divergence.

As shown in figure 4a, the indicator of real GDP, reveals that the gap in real income among sample economies had been getting wider over time and kept stable after 2007, suggesting an economic divergence. Figure 4b reveals that the non-agriculture sectoral share is overall converging except that a temporary slight divergence during 2006 to 2008. Figures 4c clearly shows that the urban resident share is persistently converging. Another indicator that implies a divergence is the life expectancy shown in figures 4d: after peaked

Figure 4a: The Convergence Indicator of Real GDP per Capita



in 1995, the life expectancy shows larger difference across sample economies. On the contrary, figure 4e shows that the education expense ratio is converging after reached its bottom in 1993.



Figure 4b: The Convergence Indicator of Non-Agriculture Sectoral Share

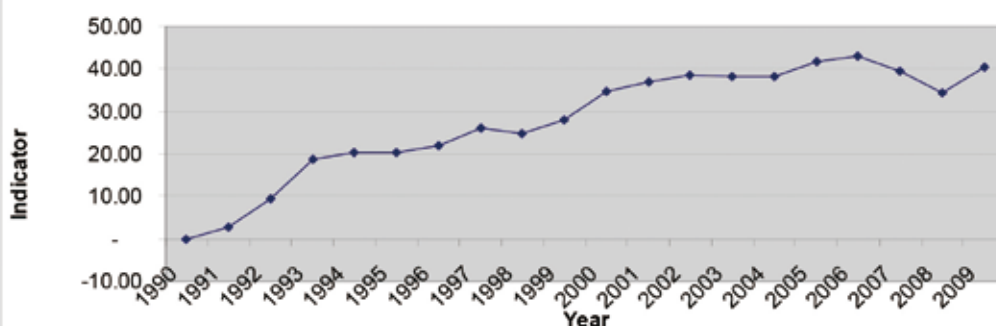


Figure 4c: The Convergence Indicator of Urban Resident Ratio

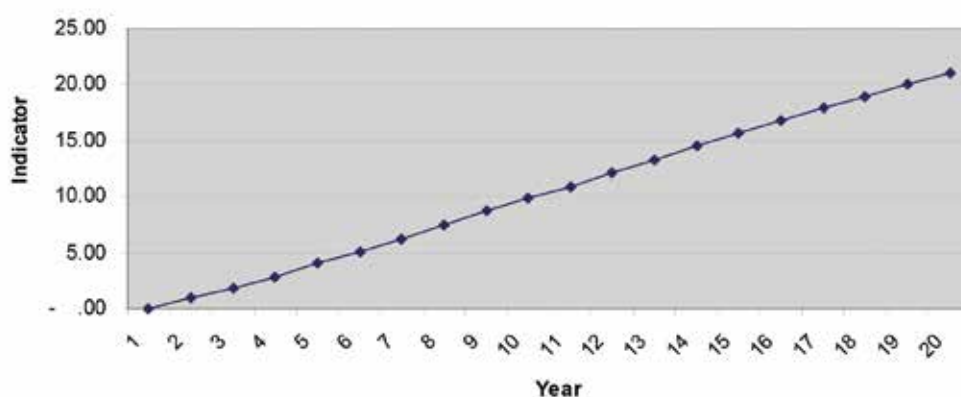


Figure 4d: The Convergence Indicator of Life Expectancy

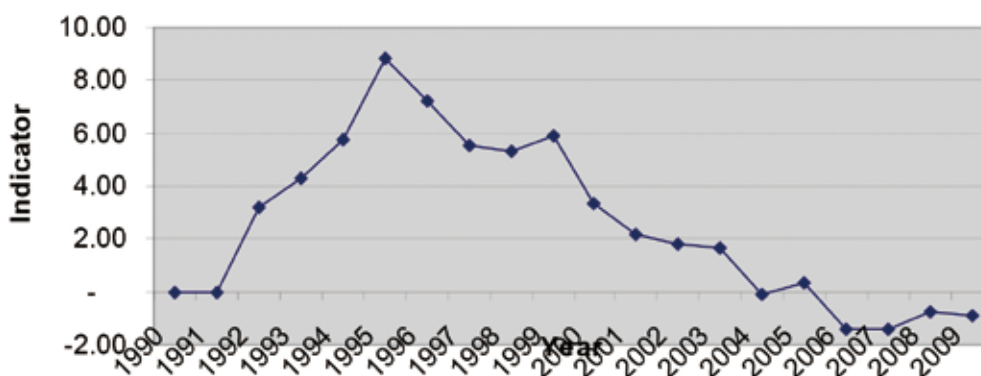
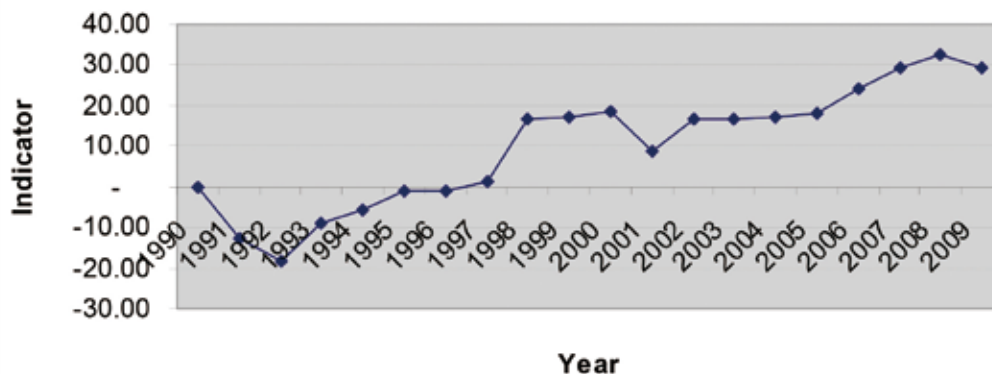


Figure 4e: The Convergence Indicator of Education Expense Ratio



2.3. Summarizing Indicators in composite indexes

After collecting relevant indicators, the next challenge is to reasonably summarize them in composite indexes. That is, we need to find a reliable approach to assign reasonable weights to various indicators. CW (2010) argue that the Principal Components Analysis (PCA) is a good approach with solid theoretical foundation. Examples of applying PCA can be found in the KOF index of globalization and the Trade and Development Index (TDI) reported by The United Nations Conference on Trade and Development (UNCTAD).

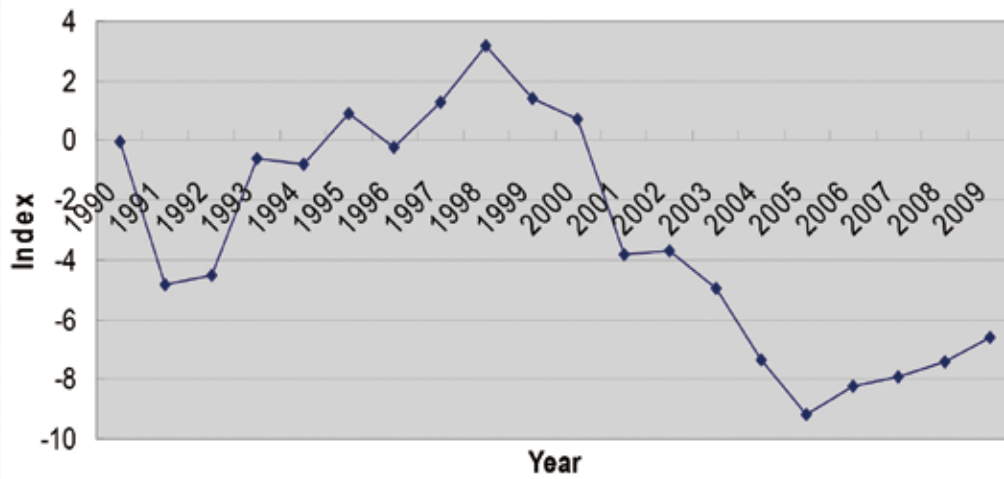
In particular, CW (2010) use a two-stage PCA to construct the indexes. In the first stage, they compute the weights for the five convergence indicators and construct a so call “convergence index” (CI). In the second stage, they apply PCA again to construct a composite economic integration index based on the three flow indicators (i.e. trade, FDI, and tourists) as well as the CI. The indexes have been updated annually in the States of the Region Report (SRR) by PECC since 2009. And to make the updated indexes comparable with the previous ones, we use a chained index approach.¹

Figure 4 shows that starting from 1990, which is the base year with CI normalized to zero, the CI series fluctuates over time, peaking at 7.31 in 1998 and falling to -3.35 in 2005. It is worth noting that CI has been increasing since 2005 though the level of convergence is still below that in 1990.

¹ The weights are changing as we update the index. We only keep the observations in the most recent 16 years in PCA to determine the weights. See CW (2010) and annual SRR for details.

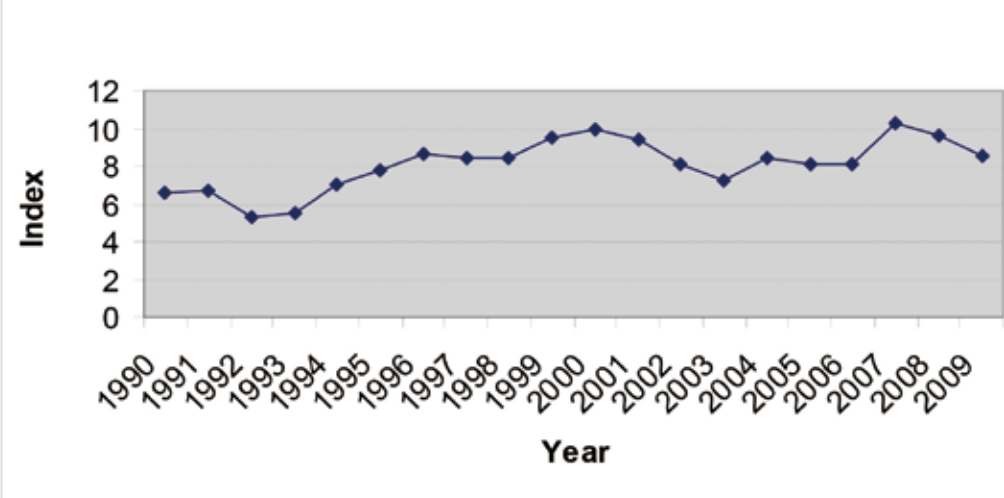


Figure 5: Updated Convergence Index



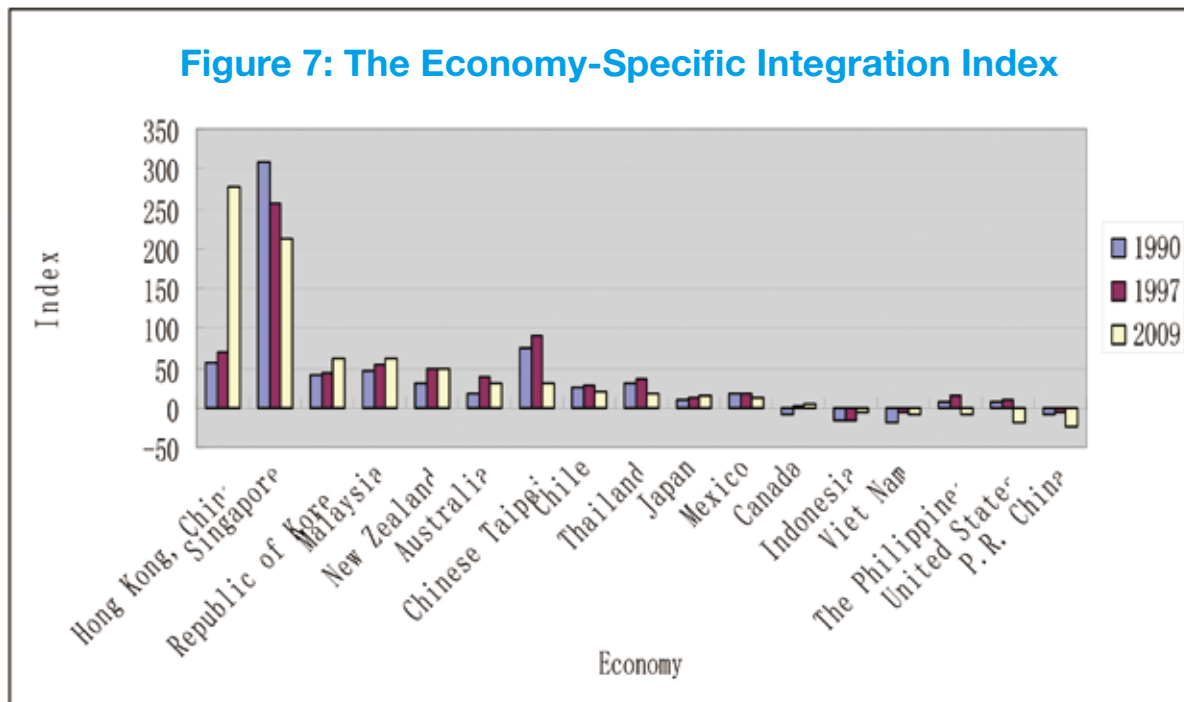
We show in figure 6 the composite integration index in AP region. Though the current level of economic integration is higher than that in 1990, the zigzag index during 1990 to 2009 implies a rather unsmoothed economic integration process. The recent global crisis also interrupts the integration process as economies are now more inward-looking and become more protective in trade.

Figure 6: Composite Economic



Finally, to see how each economy performed in 2009, we further break down the integration index to their three flow indicators and CIs as shown in figure 7 (which is the figure 2 in chapter 3 of SRR2012). Small open economies of Hong Kong (China) and Singapore have been the top two most integrated economies of the region since the beginning of the index. However, the two largest economies in this region, namely the U.S. and China, were the bottom two in the ranking. The reasons

are threefold. First, these two largest economies are more diversified in their international business. For instance, both economies have deep economic connections with Europe. Second, both of them have very important economic relations with their immediate neighbors, the US with Canada and Mexico, and China with Hong Kong, China and Chinese Taipei. Third, since both are so large that they, especially the U.S., rely relatively more on their domestic economies than other regional economies.



3. Gains from Integration: A Study on Reducing Trade Barriers

Though the economic integration process is zigzag, it is nevertheless the unanimously agreed ultimate goal. The most persuasive reason is the potential gains from integrated market. While the gains are theoretically clear, empirical gauge is challenging. In the following section, we choose to measure the gains from trade barrier reduction as an evidence of gains from economic integration.

There are two reasons for why we choose to investigate trade barrier reduction. First, trade barrier reduction is usually the first and most straightforward step towards economic integration. Second, thanks to WTO, trade data as well as the tariff data are now available at highly disaggregated level; more importantly, the coding system adopted by most countries are harmonized so that the trade data across countries can be comparable, which ensure the data reliability.

Existing measures on tariff barriers are mainly simple and value-weighted averages of all tariff lines.² Such measures, however, are neither theoretically solid nor empirically convincing. First of all,

² One common way is to use actual import volumes as weights. See, for example, Edwards (1998).



simple average neglects the huge difference of import values among imported goods, and therefore does not take into account the dispersed degrees of importance of different goods. Secondly, although the value-weighted average tariff rate does treat imported goods differently, it does so in a misleading way. Goods subject to higher tariffs will be imported less and thus receive lower weights. Therefore, value-weighted average tariff rates tend to underestimate the real restrictiveness. One extreme case is that a prohibitive tariff will not be counted in the weighted average tariff rate because the import volume is virtually zero. Furthermore, goods usually have different price elasticities of demand, that is, their responsiveness to price change (due to imposing tariff) varies vastly. Therefore, these types of measures, which lack solid theoretical support, are in general unsatisfactory gauges of real trade restrictiveness (Rodriguez and Rodrik, 2001).

The pioneering work by Anderson and Neary (1992, 1994, and 1996) proposes a uniform tariff (the so-called Trade Restrictiveness Index) that can obtain the same welfare for the importing country as its current tariff structure. Feenstra (1995) suggests that under a partial equilibrium environment³ the TRI can be simplified as,

$$(1) \quad TRI_t = \left[\frac{\sum_n s_{nt} \sigma_n t_{nt}^2}{\sum_n s_{nt} \sigma_n} \right]^{1/2}$$

That is, measuring TRI only requires knowledge of import demand elasticities (σ), import shares (s), and the tariff rates (t). This simplified TRI can be conveniently applied in econometric approaches that allow for highly disaggregated tariff lines.

Furthermore, Kee et al. (2008) suggested that the TRI can be further decomposed into three components, as follows:

$$(2) \quad TRI_t = \left[\sum_n s_{nt} \bar{\sigma}_{nt} t_{nt}^2 \right]^{1/2} = [E(\bar{\sigma}_{nt} t_{nt}^2)]^{1/2} = [\bar{t}_t^2 + \delta_t^2 + \rho_t]^{1/2}$$

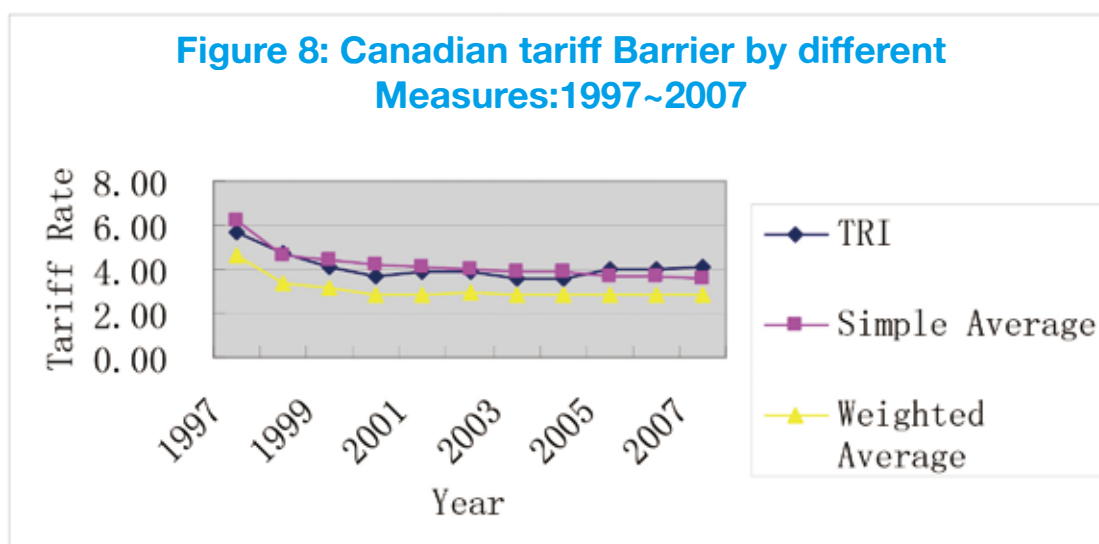
where \bar{t}_t denotes import-weighted tariffs; $\bar{t}_t = \sum_n s_{nt} t_{nt}$; δ_t^2 denotes variance of tariffs; $\delta_t^2 = \sum_n s_{nt} (t_{nt} - \bar{t}_t)^2$; $\bar{\sigma}_{nt}$ denotes the adjusted elasticities; $\bar{\sigma}_{nt} \equiv \frac{\sigma_n}{\sigma_t}$ with $\bar{\sigma}_t = \sum_n s_{nt} \sigma_n$; and ρ_t denotes the covariance: $\rho_t = Cov(\bar{\sigma}_{nt}, t_{nt}^2)$.

Equation (2) indicates that TRI should be higher than the value suggested by the weighted average tariff if the tariffs have large variances and are positively related to the import demand elasticities.

As an illustration of the trans-Pacific trade barrier reduction, Chen (2012) measures the dynamics of Canadian TRI during 1997 to 2007, and its different tariff barriers imposed to various Asia-Pacific countries: China, Japan, Korea, Thailand, Malaysia, and Indonesia.

³ A partial equilibrium method omits possible income and cross-price effects.

Figure 8 shows the TRI of Canada from 1997 to 2007. It illustrates that both the simple average and value-weighted average tariff imposed by Canada effectively reduced after 1997 even though its overall tariff rate was already at the fairly low level. However, the weighted average tariff rate is significantly lower than the simple average tariff. The trade restrictiveness indicated by TRI is interestingly quite close to the simple average tariff. Compared to the weighted average tariff, TRI is higher mainly due to the high variation of tariffs: higher tariff was imposed on imports with lower demand elasticities, i.e. machinery/electrical, transportation, and miscellaneous products.



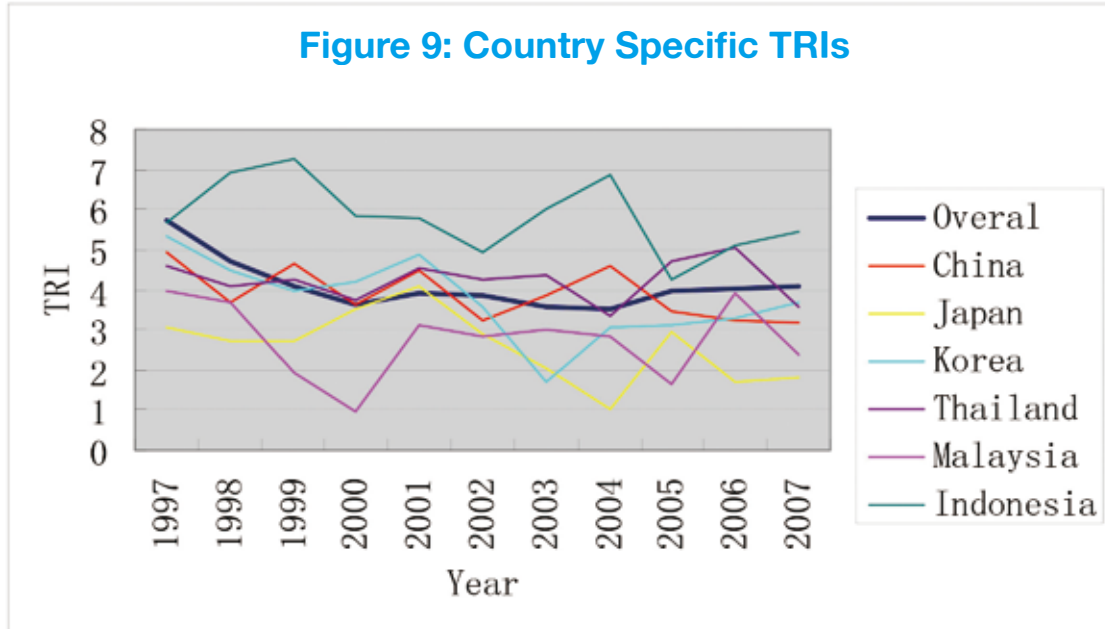
The general TRI takes into account of correlation of the heterogeneous tariff rates and the corresponding import demand. However, it is still not enough to address the heterogeneous tariff barriers facing various countries. In the following, I select 6 Asia-Pacific exporting countries, China, Japan, South Korea, Malaysia, Thailand, and Indonesia, to compute their country-specific TRI imposed by Canada.

Figure 9 depicts the country-specific TRIs for the 6 selected countries along with the overall TRI (by bold line). First of all, compared to the general TRI, most of the selected countries' TRIs were lower during that decade except Indonesia. Malaysia and Japan enjoyed very low tariff barrier, both of which faced average tariff less than 3%. Indonesia, on the other hand, faced an average tariff exceeding 5.55% compared to 4.29% average Canadian TRI worldwide. Second, South Korea faced a quite high tariff barrier in 1996 since the demand elasticities of those Korean products was relatively highly related to their corresponding tariff, which results in a strikingly high tariff facing Korea. But the situation quickly changed after 1996. Third, it is worth noting that China faced a similar tariff barrier to the general TRI, reflecting the fact that China's exports to Canada is quite diverse which is similar to Canadian aggregate import pattern.⁴ Fourth, except for China, Canadian tariff barriers to other selected countries are more

⁴ Rodrik (2006) and Schott (2008) document that China's export structure is quite similar to those of the developed countries such as U.S.



volatile. This finding suggests that most individual countries are exposed to heterogeneous products shocks: the shocks are mainly from changes in product-specific tariff policies or demand.



However, Feenstra's (1995) TRI only considers a small-open economy. That is, the underlying export supply is perfectly elastic (i.e., a horizontal inverse export supply curve), such that the tariff pass-through is complete to domestic demanders. As noted by Feenstra (1995), few goods and few countries actually face such a scenario, given the prevalent monopolistic competition market structure. Chen and MA (2012) propose a generalized trade restrictiveness index (GTRI) that takes not only the downward-sloping import demand into account, but the upward export supply as well, such that tariff burdens are partly shared by foreign export suppliers. That is, we relax the small open economy assumption and consider tariff imposition-related distortions to both foreign suppliers and domestic demanders. Our GTRI is shown in Equation (3) below.

$$(3) \quad GTRI_t = \left[\frac{\sum_n \frac{\varepsilon_n \sigma_n}{(\sigma_n + \varepsilon_n)} s_{nt} t_{nt}^2}{\sum_n \frac{\varepsilon_n \sigma_n}{(\sigma_n + \varepsilon_n)} s_{nt}} \right]^{1/2} = \left[\frac{\sum_n \frac{\sigma_n}{(\omega_n \sigma_n + 1)} s_{nt} t_{nt}^2}{\sum_n \frac{\sigma_n}{(\omega_n \sigma_n + 1)} s_{nt}} \right]^{1/2}$$

where ω is the inverse export supply elasticity.⁵

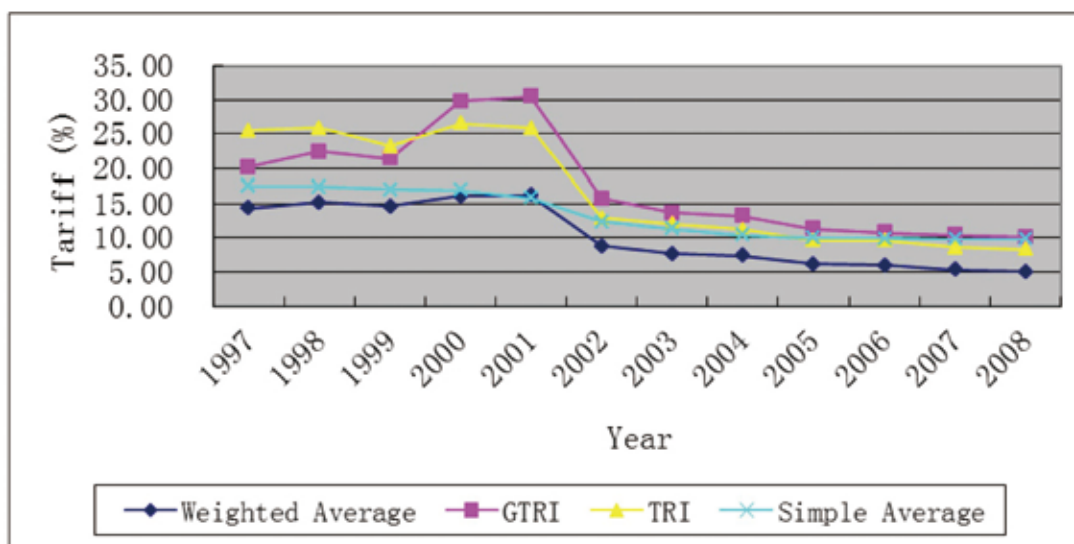
Therefore, when world supply is infinitely elastic, such as in the case of a small open economy, the GTRI degenerates to TRI.

Chen and Ma (2012) further apply the GTRI using the highly disaggregated Chinese import and tariff data from 1997 to 2008. As illustrated in figure 10, they find that prior to China's accession into the

⁵ We show the derivation of Equation (3) in Appendix 1.

World Trade Organization (WTO) in 2001, the country's tariff barrier was much higher than either the simple or the weighted average tariffs. The tariff barrier dropped dramatically after 2001 and gradually converged with the simple average tariff while remaining significantly higher than the weighted tariff. Our measure of GTRI indicates that after China's entry of the WTO, the tariff barrier reduction was much more pronounced than that measured using the simple or import-weighted average tariff, thus implying a significant reduction on the terms of trade.

Figure 10: China's Tariff Barriers under Various Measurement Approaches



Finally, since GTRI considers the tariff distortions to both domestic importers and foreign exporters, Chen and Ma (2012) also report the deadweight loss (DWL) to both parties, the terms of trade (TOT), and its gains in China owing to tariff barriers.

The general results are shown in Table 1. Column (1) shows that the DWL to China's consumers rises to US\$ 207 million in 2001, drastically drops in 2002 and 2003, and peaks in 2004 at US\$ 264 million. Losses then fluctuate over US\$ 210 million until 2008.⁶ Considering the decreasing GTRI after 2001, the larger loss is mainly attributed to the rapid increase in China's imports after 2001. That is, the base for calculating DWL has significantly expanded. Similar dynamic patterns are reported in the decomposed DWL because of average tariff and tariff variance. The alleviation of DWL resulting from tariff reduction can be better measured by the deadweight loss- gross national income ratio, as reported in the brackets in Column (1). China's income/welfare loss resulting from the existence of tariff barriers is reduced from 0.19 % in 1997 to 0.05 % in 2008. In other words, China has saved about 0.14 % in income from tariff distortion as a result of the WTO's effective removal of tariff barriers. Although the direct gains to China's consumers seem trivial, tariff reduction does benefit foreign suppliers and China's

⁶ The currency unit is current dollar. However, the dynamic pattern will not change even when using real dollar.



government. China's government has seen a substantial net increase in its terms of trade gain thanks to increased imports. Although world suppliers overall pay a larger cost after 2001, as shown in Column (2), these higher costs are again mainly attributed to a surging export base (or import base to China). The terms of trade situation reported in the brackets of Column (3) offer a finer measure for world suppliers. In 2001, world suppliers needed to lower prices by as much as 17.28% of what they would normally charge under free trade. However, this concession shrank to only 4.92% in 2008. Although China has given up much of its influence on tariffs, it nevertheless collected more gains from terms of trade owing to a surging import base. China's gains from terms of trade increased steadily from US\$ 3,939 million in 1997 to US\$ 15,990 million in 2008.

Table 1: Deadweight Loss and Terms of Trade gain in China:1997-2008

Year	(1) DWL to China's Importers	(2) DWL to foreign exporters	(3) TOT gain
1997	177.00 (0.0188)	165.98	3938.92 (14.15)
1998	150.87 (0.01500)	160.26	4820.29 (15.82)
1999	144.86 (0.0136)	167.06	6081.28 (15.40)
2000	192.86 (0.0163)	231.54	9111.85 (17.14)
2001	207.04 (0.0159)	269.92	10625.22 (17.28)
2002	121.75 (0.0085)	158.81	6578.51 (8.79)
2003	137.10 (0.0084)	178.07	8739.03 (7.76)
2004	264.46 (0.0137)	286.93	10881.53 (7.28)
2005	221.23 (0.0098)	229.00	10345.41 (6.19)
2006	244.83 (0.0092)	247.52	11933.41 (5.81)
2007	210.57 (0.0062)	226.10	13126.77 (5.14)
2008	221.10 (0.0051)	255.43	15990.89 (4.92)

Though the specific gains from trade barrier reduction to the AP economies are not particularly measured in Chen and Ma (2012), a significant part of them is undoubtedly reaped by the AP economies given the fact that more than two thirds of Chinese trade are with AP economies.

4. Conclusions and Discussions

Since late 1980s, political leaders have met regularly in APEC. One of the key themes in each summit is to advocate further economic cooperation and integration. However, almost two decades have passed since the birth of APEC, yet it is still highly controversial on whether the economic integration really takes place and if so to what extent.

In this paper, we quantitatively investigate the process and gains from the economic integration in Asia Pacific Region. As in CW (2010), we investigate the following eight indicators that are relevant

to economic integration: the convergence indicators of real GDP per capita, non-agriculture sectoral share, urban resident ratio, life expectancy, and education expense share, as well as intra-regional trade share, FDI flow, and tourist inflow. These data are collected from 17 APEC member economies, namely, Japan, Republic of Korea, People's Republic of China, Hong Kong, and Chinese Taipei from East Asia; Vietnam, Thailand, the Philippines, Indonesia Singapore, and Malaysia from Southeast Asia; the United States and Canada from North America; Chile and Mexico from Latin America; and Australia and New Zealand from Oceania. The data starts from 1990 and ends at 2009. We construct the so called convergence index and economic integration index and find that

1. during 1990 to 2009, the economic convergence was volatile, though CI had been increasing since 2005, the level of convergence was still below that in 1990.
2. the degree of economic integration in 2009 was higher than that in 1990, yet the zigzag index during 1990 to 2009 implies a rather unsmoothed economic integration process. The recent global crisis also interrupts the integration process as economies are now more inward-looking and become more protective in trade.
3. small open economies of Hong Kong (China) and Singapore have been the top two most integrated economies of the region since we began the index. However, the two largest economies in this region, namely the U.S. and China, were the bottom two in the ranking.

However, we should be cautious in interpreting the indexes. The rankings should not be read normatively as “league tables” in the sense that a higher ranking is superior to a lower ranking. Indeed, a low ranking may simply indicate that an economy is more oriented globally than regionally, as is likely the case for China and the United States. The measures chosen for inclusion in the composite index are neither comprehensive nor perfect. Due to data limit, many relevant indicators are omitted in the current indexes. Further research along this line may also consider the indicators along four dimensions: 1. macroeconomic indicators such as real GDP growth rate, real interest rate; 2. trade barrier indicators such as tariff barrier index, non-tariff barrier index; 3. Intra-regional Financial interdependence indicators such as equity market investment, bond inter-investment, bank claims, remittance; 4. tourism indicators such as tourism expenditure.

To further investigate the degree and gains from economic integration, we choose to study the tariff barrier reduction in Canada and China. According to Chen (2012), we find

1. country-specific TRIs for the 6 selected AP indicate that not all AP nations enjoy lower tariff than Canada imposes to its global imports. Some countries, such as Malaysia and Japan enjoyed very low tariff barrier, both of which faced average tariff less than 3%. Indonesia, on the other hand, faced an average tariff exceeding 5.55% compared to 4.29% average Canadian TRI worldwide.
2. except for China, Canadian tariff barriers to other selected countries are more volatile. This finding suggests that most individual countries are exposed to heterogeneous products shocks: the shocks are mainly from changes in product-specific tariff policies or demand.



Based on the GTRI approach, Chen and Ma (2012) further estimate the welfare gains to both China's importers and foreign exporters thanks to the reduction on China's Tariff barrier. China's income/welfare loss resulting from the existence of tariff barriers is reduced from 0.19‰ in 1997 to 0.05‰ in 2008. In other words, China has saved about 0.14‰ in income from tariff distortion as a result of the WTO's effective removal of tariff barriers. On the other hand, in 2001 world suppliers needed to lower prices by as much as 17.28% of what they would normally charge under free trade in China's market. However, this concession shrank to only 4.92% in 2008. Although China has given up much of its influence on tariffs, it nevertheless collected more gains from terms of trade owing to a surging import base. China's gains from terms of trade increased steadily from US\$ 3,939 million in 1997 to US\$ 15,990 million in 2008. Though the estimated gains are not specific to the AP economies, a significant part of them is undoubtedly reaped by the AP economies given more than two thirds of the trade that China have are with them.

Though future research on the U.S. and other AP economies are highly desired, the current research on Canada and China has already gave us some clear implications to the current AP economic integration status. First, according the Canadian TRIs to 6 AP countries, we do find some evidence that AP countries enjoy a overall lower tariff barrier from its trans-Pacific fellow country, which indicates the AP economic integration process, at least in terms of trade barrier, may have taken place, compared with their globalization process. Second, countries have already experienced welfare gains from freer trade, given the current tariff barrier, there still exists big potential welfare gains to countries engaging in freer trade. Thus, a trans-Pacific free trade agenda, either TPP or ASEAN+N, would be justified and advocated.

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