East Asia Grapples with the Implications

Asia's mighty trading giants, which have for years benefited from the seemingly inexhaustible US appetite for their exports, have now run headlong into US President Donald Trump's fierce insistence that the terms of America's trade with them has been fundamentally unfair. That clash, which could yet lead to trade wars, could upend the global order that has prevailed for decades.
The TPP after Trump

By Jeffrey J. Schott

US President Donald Trump withdrew from the Trans-Pacific Partnership on his third day in office on Jan. 23, 2017, seemingly derailing implementation of the world’s most comprehensive free-trade agreement. Without its chief architect and largest economy, the TPP seemed destined for obscurity.

But, surprisingly, the TPP has survived largely intact. The 11 remaining signatories incorporated almost all of its provisions in a new, renamed Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP). The application of 22 TPP provisions, mostly included at US insistence, was suspended indefinitely, primarily to facilitate ratification in each country. The final deal was signed in Santiago, Chile, on March 8 this year. And, ironically, the new pact could well enter into force sooner and expand its membership faster than if Trump had not interceded.

Japanese Prime Minister Shinzo Abe and the leaders of the other 10 countries that signed the CPTPP deserve substantial credit for this constructive outcome. But in a perverse way, so does Trump. Without his unprecedented attacks on the rules-based post-war trading system, and threats to pull out of FTAs with Canada, Mexico, and South Korea as well as the World Trade Organization (WTO), the other TPP signatories might not have moved ahead with the trade pact with such a sense of urgency.

From TPP to CPTPP

The original TPP was notable for its large economic footprint, covering 12 countries that generate almost 40 percent of global output, and for its substantive obligations that achieved the most comprehensive updating of trading rules and trade reforms since the establishment of the WTO in 1995. And, equally important, the TPP complemented and reinforced US strategic engagement in the Asia-Pacific region at a time of growing Chinese influence. Some observers argued that the TPP was designed to “contain” China, an implausible goal for a trade pact whose members have substantial trade and investment ties with China. But, in fact, the aim was more pragmatic and realistic: to use the trade accord to help each country to “compete” more effectively against China.

In large measure, that is why the 11 remaining TPP signatories went forward with their regional FTA despite the US withdrawal. They recognized that the deal still generated important income gains for each country, although much less than with US participation, and that its trading rules established high-standard precedents for prospective regional and multilateral agreements. Given the lack of progress in WTO initiatives in recent years, the Asia-Pacific talks have been the principal platform for updating the world trade rulebook.

Perhaps most important, it complemented and reinforced domestic economic reforms, providing impetus to innovation and productivity growth essential for each economy to keep pace with China and other partners in the dynamic and competitive Asia-Pacific region.

Unlike the TPP, which required ratification by the US and Japan before it could enter into force, the CPTPP “goes live” 60 days after six of the 11 members ratify the deal. Mexico already has done so and progress on Canadian legislation has accelerated since Trump’s attack on Canada at the G-7 summit in early June. Clearly, the CPTPP has become part of “Plan B” for Mexico and Canada in case Trump also dumps the North American Free Trade Agreement (NAFTA). Japan, Australia, New Zealand and Singapore also expect to complete domestic approval of the CPTPP this year, so CPTPP reforms very likely will be implemented by early 2019 (for those countries having already ratified the pact).

Will the other CPTPP countries quickly follow suit?

Once the pact is implemented, other signatories will face increasing pressure to do so in order to receive the CPTPP trade preferences. Simply put, they can’t afford to stay out. Only Malaysia has voiced major concerns about the trade pact. Newly elected Malaysian Prime Minister Mahathir Mohamad, harking back to his plan for an East Asian Economic Caucus (EAEC) put forward in the 1980s during his previous period as prime minister, suggested that CPTPP revisions were needed to provide poorer members with special benefits to help them compete.

Today, the closest analogy to the EAEC is the Regional Comprehensive Economic Partnership (RCEP), the ongoing negotiations among the 10 members of the Association of Southeast Asian Nations and their six FTA partners. The CPTPP and RCEP are complementary arrangements, although the RCEP is less juridical and seeks more limited and incremental reforms. Those countries that want to use trade pacts to propel economic reform join both.

Seven of the 16 RCEP countries are also signatories to the CPTPP (see Table 1 overleaf) and others such as Indonesia and Thailand are considering joining. Mahathir’s throwback proposal is ill-suited to globalized markets of the 21st century and unlikely to garner support by any of the other countries. The poorest CPTPP economy, Vietnam, knows its success in attracting foreign investment depends importantly on the economic reforms the pact requires. Malaysia would likely lose trade and investment to Vietnam if it delays ratification. Mahathir’s alternatives are to rely on RCEP and slow-walk reform, or to deal bilaterally with China and the US — good luck with that! Seen in this light, Malaysia will likely conclude, albeit grudgingly, that it needs to implement the CPTPP along with the other 10 CPTPP signatories.

Expanding CPTPP Membership

By early 2019, the CPTPP will be open to new members. Those countries will have to accept existing CPTPP provisions and then negotiate their
The CPTPP: A Place for the US … and China?

Why did the US leave the TPP, and will it return to the CPTPP? Trump dumped TPP to put paid to a campaign promise to rewrite or revoke “bad” trade deals that he regards as responsible for the large US merchandise trade deficit. He and his cabinet argue that US negotiators paid too much and got too little in return, even though the TPP would have required few changes in US law and practice. Their critique seems to focus primarily on TPP rules on auto content that are even less restrictive than those in NAFTA—and Trump is trying to rewrite NAFTA’s automobile rules of origin to force auto companies to move more of their production of auto parts and final assembly of cars and trucks back to US plants.

In fact, US merchandise trade deficit is likely to suffer small losses as US firms lose sales to competitors benefiting from CPTPP tariff preferences. And it is also losing the predominant influence US officials have had throughout the postwar era in writing the rules for the international economic system based on American values and priorities. Leaving the TPP means not being at the negotiating table as the trading rules evolve in the CPTPP and are applied to e-commerce, support for state-owned enterprises (SOEs) and cross-border investment.

To be sure, the CPTPP countries have kept the door open for the US to join. But such a US policy reversal is unlikely in the near term, given Trump’s dismissive attitude toward regional and multilateral trade pacts. At times, Trump has tweeted that he would reconsider if the revised deal were substantially better. But what that really means is that he wants other countries to open their markets more to US exporters, and accept fewer US concessions, than provided in the original TPP. That deal is not on offer; indeed, it would not pass muster in political debates in the Japanese Diet or other legislatures.

But if US officials changed course and asked CPTPP countries to augment the deal (i.e., adding new provisions on e-commerce or disciplines on support for SOEs) instead of revising existing provisions, there could be a viable pathway for US participation. Such an enhanced deal could result from negotiations on US accession to the CPTPP or the formulation of a new, broader pact—drawing heavily on TPP/CPTPP precedents—that could include the US, China, and other Asia-Pacific nations. Such a prospect seems remote at a time of rising US-China trade tensions. But a new regional initiative, based on studies co-chaired by the US and China in the Asia-Pacific Economic Cooperation (APEC) forum, could yet emerge as the two economic superpowers search for ways to circumvent their current trade conflicts.

Perhaps the CPTPP may yet become the long-sought pathway for Asia-Pacific economic integration! Trump’s exit opened the door for China to assert a more pronounced leadership role in the region and to deepen its bilateral ties with the other TPP countries. As Table 1 shows, China already trades more with each of the CPTPP countries than the US, except for NAFTA partners Canada and Mexico. Together, the merchandise trade of the 11 countries with China exceeded US$860 billion in 2017 and represented almost 20 percent of their total merchandise trade. China has or is conducting or planning to negotiate trade pacts with each CPTPP member, except Mexico. And it also is negotiating upgrades to those pacts already in force.

Would China take the next step and ask to join the CPTPP? Chinese officials have been studying the TPP for several years to assess how its provisions would fit with their planned economic reforms and development strategies. In many areas, China could comply with CPTPP requirements; but chapters on intellectual property rights, labor, and SOEs cross red lines for Chinese policymakers. The CPTPP would have to be trimmed to accommodate Chinese participation, a prospect as unlikely as Trump’s reversal of his decision to withdraw from the TPP.

For the next few years, CPTPP membership will thus likely grow without the US or China. But that might be a good thing. As Trump breaks WTO rules with his protectionist policies, and China skirts WTO rules with its high-tech initiatives, we need the CPTPP members to continue working to reinforce the rules-based world trading system.

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