The TPP and the Quest for East Asian Regionalism

Beyond the Spaghetti Bowl

By Inkyo Cheong

The US is touting the so-called Trans-Pacific Partnership, a proposed trade agreement linking Asian and American economies, as a way to foster greater economic integration and propel growth for members. But one key problem is that it excludes China and could lead Beijing to develop its own Sino-centric trade bloc, writes Inkyo Cheong.

SINCE THE ASIAN financial crisis of 1997-1998, East Asian countries have pursued regional economic integration, although progress has been slow and many countries have faced obstacles. The two main drivers have been the Association of Southeast Asian Nations and more recently China. ASEAN has tried to develop separate free-trade agreements (FTAs) with China, Japan and South Korea, while China has preferred to reach a more comprehensive “ASEAN + 3” agreement that includes the three nations collectively. At the initiative of Japan, the idea of an ASEAN + 6 FTA, adding India, Australia and New Zealand into the mix, is now also on the table.1

More recently, another path to economic integration has been offered by the proposed Trans-Pacific Partnership (TPP). It has some merits. First, the US is leading negotiations to create the trade bloc. Second, its membership covers both sides of the Pacific. Third, it could be a milestone in the realization of the Asia-Pacific Economic Co-operation (APEC) forum’s 1994 Bogor Goals, which envision a free-trade area encompassing the entire Asia-Pacific region — in effect an APEC FTA. Finally, since Japan first announced in November 2011 that it wanted to participate in the TPP negotiations, the importance of the fledgling agreement has attracted greater interest.

If the TPP negotiations are moving toward an APEC FTA with a high-quality agreement,2 the opportunity cost of not participating would be significant for countries in the region. That means countries currently not participating would join the TPP negotiations. This process is called the domino effect in economic integration literature. On the other hand, there are some concerns that the TPP may actually hinder the progress of East Asian economic integration, and may result in a new struggle between the US and China for regional hegemony.3 The current TPP setup will keep China out in the cold for a very long time, because the TPP will not only be costly for China, it will also hinder its partners in the region and throughout the global economy.4

This essay attempts to analyze the progress and the major issues surrounding the current TPP negotiations, and also attempts to draw implications for East Asian economic integration.
HOW IT ALL BEGAN

The origins of the TPP go back to March 2006, when Brunei, Chile, New Zealand and Singapore agreed to a four-way FTA called the Pacific-4 (P4). Although the economic scale of the group was modest, its goal was not. Their vision was to use the agreement as the basis for a future pan-Pacific trade bloc, with trade liberalization taking place among member countries by 2015.

In 2008, five countries — the US, Australia, Malaysia, Peru and Vietnam — declared intentions to join the P4 agreement, which was later renamed the TPP to reflect geographical expansion. The US had been the first to embrace the P4 when then President George W. Bush announced its intention to participate in the talks. The US decided to join the TPP negotiations. Sixth round held in Singapore. March: P4 member countries have been adamant about pursuing the existing P4 agreement. These problem areas have kept the negotiations from going smoothly so far.

In terms of liberalization and coverage, it is unlikely that a final TPP agreement will be comparable to the KORUS FTA, which took more than five years to reach an agreement. It was negotiated due to political pressures in both countries. Given that the TPP’s nine member countries were unable to reach their initial goal by November 2011, raising the number of member countries will only add to the difficulties surrounding the negotiations.

NEGOTIATING MARKET ACCESS

It’s hard to assess the precise outlines of the negotiations so far, because they take place in secret and are still underway. According to various sources involved, the member countries have agreed on the number of chapters and other major structures of the agreement, but the specific content and sensitive issues have not been extensively negotiated. In other words, the talks are progressing slowly on market access and concessions but are producing only partial outcomes, while the core issues have not been discussed.

The goods sector is being negotiated based on bilateral negotiations, and the other sectors are being discussed in the context of commitments that will apply to all member countries. The “single version” of commitments is similar to a multilateral agreement.

In conclusion, the TPP’s setbacks have reinforced the challenges facing the region in terms of achieving a comprehensive and balanced agreement. The agreement’s future success will depend on the ability of the parties to overcome these obstacles and move forward with meaningful commitments.

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of TPP countries and is in negotiations with Australia and New Zealand.

The TPP member countries that haven’t concluded FTAs are currently negotiating for goods concessions, implying that market access for existing FTAs will be maintained regardless of the quality of the liberalization scheme. For example, Malaysia and Vietnam have poor market access for goods in FTAs with Australia and New Zealand. The TPP has agreed to a two-track approach for goods concessions in an attempt to reduce the schedule and burden of the negotiations, but this may dilute one of the TPP’s primary goals of merging the region into one large integrated market.

SENSITIVE ISSUES
Predictably, many TPP countries face difficulties with the negotiations, because the talks are fraught with sensitive issues. Australia and Vietnam, for example, are politically sensitive to the Investor-State Dispute Settlement (ISD) mechanisms, on which the US has taken a strong stand.

The issue is likely to be extremely thorny. Prime Minister Julia Gillard’s Labour Government has publicly rejected including ISD in any future trade agreements that Australia negotiates, and a climbdown from that position could be difficult since the existing US-Australia FTA has no ISD mechanism within it. The US is asking Australia to yield on the issue, pointing out that the US Congress is unlikely to ratify the TPP without an ISD clause. Vietnam is strongly opposed to ISD, but has not formally presented its opinion, choosing instead to allow Australia to take the lead in opposing it. Opinion is so divided among TPP members over ISD that failure to agree on the issue could turn out to be the ultimate deal breaker in the TPP negotiations.

Vietnam, in fact, has difficulties beyond dispute settlement in almost every sector, particularly services, investment, government procurement, protection of intellectual property rights, the environment and labor.

There are also differences among countries over whether to pursue a “negative list” or “positive list” approach to concessions on trade in services. The former approach involves the inclusion of all services sectors, except those specifically listed in the reservations, while the latter involves the voluntary inclusion of a number of sectors indicating what type of access and treatment is being permitted. Many countries — such as the US, Australia and New Zealand — want to negotiate concessions on services and investment using a negative list approach; Vietnam is negotiating on the basis of a positive list approach, because opening its market further could undermine domestic political support for the TPP. So far, Hanoi has not built any domestic consensus for a negative list approach, which, if adopted, could also present fundamental problems for other countries.

Vietnam’s motive for participating in the TPP is primarily to secure greater access to the US market and to improve security relations with the US. So far, however, Vietnam has not been a very active participant in the negotiations, because it lacks sufficient personnel with the expertise necessary to thoroughly analyze the agreement’s potential impact on its economy. For now, Vietnam hasn’t had to deal with domestic opposition to the TPP, because the negotiations are at an early stage. But it is expected that Vietnam will encounter domestic resistance on many issues such as market opening, government procurement, protection of intellectual property rights and so on.

New Zealand, on the other hand, has been one of the most active participants in the negotiations and has encouraged other countries to become more active. Nevertheless, it seems to be having trouble negotiating bilateral agreements with the US and Vietnam. The problem area between the US and New Zealand is opening the dairy products market. Although both countries are negotiating an agreement based on the current China-New Zealand FTA (concluded in 2008), their differences are considerable. New Zealand and Vietnam, which were locked in disagreements over goods concessions earlier in their negotiations, seem now to be making some progress after New Zealand proposed an initiative granting special treatment and development support to Vietnam.

CHALLENGES FOR THE US
US motives for joining the TPP negotiations are both economic and geopolitical. A 2009 report by the office of the US Trade Representative stated: “The TPP will serve to strengthen US trade and investment ties to the Trans-Pacific region, which is a priority given the economic significance of the region to the United States now and in the future. ... The TPP will also facilitate trade in the Trans-Pacific region, rationalize existing agreements, and support the multilateral trade agenda. In addition, it could serve as a vehicle for achieving the long-term APEC objective of generating a free-trade area in the Asia-Pacific.”

Geopolitical considerations are linked to the rising influence of China, raising speculation that the US is seeking to contain China. If the TPP proceeds on the terms currently set by the US, it will be very difficult for China to join. The result, according to Adelaide University Professor Christopher Findlay, may “drive the region apart with the systematic exclusion of non-members, including China. This wedge through the middle of the Pacific will be political as well as economic. China would have to join the TPP

The US is promoting the TPP while excluding China. This suggests that these two superpowers are drawing a line in the Asia-Pacific region on trade agreements, which is something that will hinder East Asian regional economic integration in the long run.

7 A foreign-affiliated tobacco company recently sued the Australian government based on the ISD, which was written into the Australia-Hong Kong FTA. This has been politically sensitive for Australia.
The TPP and the Quest for East Asian Regionalism

There is a "triple partner" for the TPP, and China has been playing a critical role in this process. As noted above, China is not currently included in the TPP, which means that the US may well be pursuing the TPP as a countermeasure against various FTAs under discussion between China and ASEAN under the ASEAN+ frameworks, because the US is currently excluded from these agreements. China has been a leader in establishing East Asian trading blocs, and this has signaled to the US that China-centered economic integration in East Asia might be a threat to American interests. It is perhaps for this reason the US is promoting the TPP while excluding China. This suggests that these two superpowers are drawing a line in the Asia-Pacific region on trade agreements, which is something that will hinder East Asian regional economic integration in the long run.

When Obama mentioned participation in the TPP at the 2009 APEC Summit in Singapore, he focused international attention on the negotiations. (Notably, Obama also mentioned the TPP as a priority in his latest State of the Union address.) However, the TPP will travel a bumpy road in the US. Obama officially informed Congress of the US’s participation on Dec. 14, 2009, but controversy surrounds the possible economic impact of the TPP. The Obama administration describes it as “the most powerful measure to merge the Asia-Pacific economy” and “the ring to connect the US and the fastest-growing regions in the world.” However, opinions held by domestic US opponents are equally strong.

Meanwhile, the negotiations themselves aren’t likely to be easy for the US. As noted above, there are serious difficulties on the ISD issue with Australia and the dairy product issue with New Zealand.

The US Trade Representative will likely take a year or two to reach a settlement on just these issues, but the overall negotiations seem certain to take much longer. Moreover, co-ordinating the opinions of the many interest groups in the US is also tough. For example, while US pharmaceutical companies insist on strengthening intellectual property rights, Oxfam is critical of the idea on the grounds that it will raise the price of medicine in foreign countries. Similarly, while the US cotton industry wants strict rules of origin on yarn, the US Chamber of Commerce, as well as giant retailer Wal-Mart, want less restrictive rules. Detroit automakers have lobbied the US government to exclude Japan from the talks. And given sentiments in Congress among Democrats on labor standards, human rights and intellectual property rights, coming to an agreement with Vietnam on these issues won’t be easy. Indeed, it’s not at all clear that the Obama administration could get the current Congress to ratify a TPP agreement.

Finally, excluding China from the TPP may not be in the long-term interests of the US, as it would encourage China to speed up the creation of a China-centered regional bloc in East Asia. As a 2011 article in Tokyo-based online magazine The Diplomat noted, there are at least three good reasons why the US cannot effectively isolate China from East Asia: first, China is too large to be contained; second, it is one of biggest regional economic players, and East Asian countries have incentives for closer linkages with it; third, most countries in Asia prefer a balance of power rather than a single power dominating the region.

JAPANESE DELICATE CHOICES

The Japanese government confirmed on March 15 this year that it does intend to participate in the TPP process, but it is unclear whether it will be able to overcome considerable domestic opposition to the TPP negotiations, consent from the nine member countries is needed. Most are in favor of Japan’s participation, although the US automobile industry objects.

Japan finds economic gains from improving trade rules through the TPP. The US and Japan are working towards a new free trade agreement that would provide a deeper level of economic integration in the Asia-Pacific region. This is a major improvement compared to previous agreements, and it has the potential to boost GDP growth across the region.

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national guidelines are set before official negotiations take place, and national representatives negotiate with foreign partners on behalf of their country. National-level decision-making is critical when dealing with sensitive issues, since this allows rational options to balance the interests of the nation and the concerns of domestic players with vested interests. In Japan’s case, however, ministries have traditionally retained special and powerful authority when dealing with sensitive issues. As a result, Japanese trade negotiators have in the past seen their primary mission as protecting their ministerial interests at the expense of the country’s overall national interests.

Due to this practice, it can be said that many past trade negotiations have been conducted at a ministerial level and not at a national level. This has often delayed important decisions and the government has displayed in voicing its intentions to join.

To be sure, there has been some weakening in recent years of the bureaucracy’s hold over Japan’s trade policy. When the Democratic Party broke the Liberal Democratic Party’s 50-year hold on power in 2009, it partially reformed the system by insisting that the Cabinet Office within the Prime Minister’s Office would decide major trade policies. This weakened the linkage between the Diet and the administration and reduced the participation of professional bureaucrats in decision-making. This theoretically implies that Japan’s national interests can now given more consideration in trade negotiations. But that arguably remains to be seen. Although the government confirmed in March this year that it does intend to join TPP talks, Japan’s recent FTA policies haven’t visibly changed, nor has domestic resistance to trade opening. For example, the Japanese government had said it would make a decision on participation in the TPP by June 2011, but postponed the official decision because of the earthquake and tsunami that struck northeastern Japan in March 2011. Only that November did the government say Japan would join “consultations toward participation.” But using the disaster as an excuse for postponing a decision was not very convincing, as it should not take much time for ministers to make such a decision. The real reason was that the government was worried about farmers voting against the ruling party, suggesting that the recent reforms have done little to affect Japan’s decision-making process.

SO WILL JAPAN JOIN?

The Japanese business sector is keen on Japan participating in the TPP. Business leaders argue that it could counter South Korea’s expanding FTA network and the continuing strong yen. They have often complained about the government’s passive stance on trade liberalization, which results from catering to the political interests of the farming sector. Moreover, if Japan doesn’t indicate a clear willingness to open up its agricultural sector, the US and other member countries are unlikely to support Japan’s participation in the TPP. Japan’s Agricultural Ministry, however, is digging in its heels, producing quantitative research showing the negative impact of the TPP on Japanese agricultural interests. The ministry has argued that Japan’s gross agricultural output could decrease by 4.1 trillion yen a year (see Table 4). Despite trade policy reforms, it remains difficult for the Japanese government not to be influenced by such vested interests. The anti-TPP camp has been sharply critical of Japan’s participation in the TPP, pointing to the negative impact on farming and fishing villages.

From a national point of view, the TPP would be beneficial for Japan, but even now that Prime Minister Shinzo Abe has announced it will participate, it will take strong political leadership to overcome the agricultural sector’s resistance.

WHAT’S REALLY IN IT FOR SOUTH KOREA?

The widest possible membership in the TPP has been sought for economic and strategic purposes, and proponents of the partnership proposed bringing Japan and South Korea in as a priority, envisioning this as a way to help reduce China’s influence on regional trade arrangements. But the potential effects of the TPP on the South Korean economy, of course, will depend on the completed agreement.

South Korea has so far successfully concluded eight bilateral FTAs with major trading partners including the US (implemented in 2012), the EU (2011), Peru (2011), India (2010) and ASEAN (2007). The FTAs with the US and EU are viewed as having very high standards with regard to market access, services, investment and rule making. In the South Korea-US FTA, the country opened a substantial part of its agricultural market and adopted a politically sensitive clause to protect foreign investors with an ISD mechanism, despite domestic opposition.

South Korea already has bilateral FTAs with most of the TPP member countries (see Table 5), and it is in talks currently with Australia and New Zealand. Given that fact, the only way to determine if membership will be beneficial for Seoul is to analyze the TPP’s marginal economic impact.

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**Table 4: The TPP’s Effect on Japanese Agriculture**

<table>
<thead>
<tr>
<th>Assumption</th>
<th>Effect on Economy</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tariff elimination on 19 major agricultural products (current average tariff rate is 10%)</td>
<td>On agriculture: Output decrease of 4.1 trillion yen every year Decline of national food self-sufficiency from 46% to 41%</td>
</tr>
</tbody>
</table>

**Table 5: Relationship between Korea and the TPP Member Countries**

<table>
<thead>
<tr>
<th>P4 member countries</th>
<th>Nominal GDP ($b)^*</th>
<th>Value of Korean exports ($b)</th>
<th>Share of Korean exports (%)</th>
<th>Status of FTAs with Korea</th>
</tr>
</thead>
<tbody>
<tr>
<td>Singapore</td>
<td>223</td>
<td>15</td>
<td>3.27</td>
<td>Concluded</td>
</tr>
<tr>
<td>Chile</td>
<td>203</td>
<td>3</td>
<td>0.63</td>
<td>Concluded</td>
</tr>
<tr>
<td>New Zealand</td>
<td>148**</td>
<td>1</td>
<td>0.20</td>
<td>In Negotiation</td>
</tr>
<tr>
<td>Brunei</td>
<td>13**</td>
<td>0.1</td>
<td>0.01</td>
<td>Concluded</td>
</tr>
<tr>
<td>United States</td>
<td>14,658</td>
<td>50</td>
<td>10.68</td>
<td>Concluded</td>
</tr>
<tr>
<td>Australia</td>
<td>1,236</td>
<td>7</td>
<td>1.42</td>
<td>Concluded</td>
</tr>
<tr>
<td>Malaysia</td>
<td>2,38</td>
<td>6</td>
<td>1.31</td>
<td>Almost concluded</td>
</tr>
<tr>
<td>Peru</td>
<td>153</td>
<td>1</td>
<td>0.20</td>
<td>Concluded</td>
</tr>
<tr>
<td>Vietnam</td>
<td>104</td>
<td>10</td>
<td>2.07</td>
<td>Concluded</td>
</tr>
</tbody>
</table>

* Nominal GDP and population as of 2010  ** Estimates as of 2010

Source: Various sources including IMF and Korea International Trade Association trade data

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**Table 4:** The TPP’s Effect on Japanese Agriculture

Korea’s total exports were $466 billion in 2010, of which nine TPP member countries absorbed 19.8 percent of the exports, for a total of $93 billion. Eighty percent of these exports go to the US, Singapore and Vietnam. The talks on the Korea-Australia FTA have almost been concluded except for the ISD issue; talks with New Zealand are progressing very slowly.

Since the terms relating to market access of existing FTAs will be included in the TPP agreement without changes, South Korea’s potential gains from the TPP would only come from the FTA with New Zealand. It can anticipate some ripple effects in other sectors including services, investment and regulatory reforms. At present, it isn’t likely that a final TPP agreement would adopt broader market access and more comprehensive coverage than Korea’s current FTAs.

For South Korea, New Zealand is a small market, absorbing only $900 million, or 0.2 percent, of its global exports. According to a government report published when the negotiations for an FTA with New Zealand began in 2009, South Korea’s GDP would increase by 0.05 percent, while New Zealand’s would grow 0.25 percent following conclusion of an FTA. Therefore, even if Korea were to join the TPP, the net economic effects would not be considerable.

In addition to the meager economic impact, it cannot be ignored that the negotiations required to settle the differences between South Korea and New Zealand will be tricky. Indeed, the history of attempts to forge an FTA between the two has not been promising. They began talks back in 1998, but a feasibility study wasn’t completed until 2008 because of sharp differences between the two sides. Government-level negotiations began in 2009 and have been held four times, but the differences were never narrowed. Both countries agreed to stop negotiating in May 2010 and have not scheduled any further negotiations since then.

**CONCLUSION**

The TPP is at a crossroads. It could result in significant Asia-Pacific economic integration, or it could spur the creation of two large, possibly competing regional trade blocs. If the TPP chooses “open regionalism” and includes China, it will contribute to regional integration. If not, China almost certainly will attempt to establish its own regional economic leadership, dividing the Asia-Pacific into a TPP and a China-centered bloc. This prospect could be reinforced with Japan’s participation in the TPP and the progress of the transatlantic FTA between the EU and the US.

If the TPP is to become the cornerstone of an APEC-wide FTA, it should be promoted for its economic value, not for geopolitical purposes. It should be open to all Asia-Pacific countries, including China, the world’s second-largest economy and a growth engine for the global economy. The scope and coverage of the TPP should be wide and comprehensive enough to induce a domino effect. If the TPP becomes a Pan-Asia-Pacific FTA and the quality of the agreement is high in terms of liberalization, the opportunity cost of not participating in the TPP would be significant. If the agreement is superior to existing bilateral FTAs in the region, it would create an opportunity to eliminate the existing spaghetti bowl of FTAs, inducing more countries to participate. This would be a natural way for the US to become more involved in East Asian economic integration, while at the same time avoiding the emergence of China-centered regionalism. It would also mean that East Asian countries would not be forced to choose between a US-led and a China-led trading arrangement.

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