

Asia-Pacific Free Trade Talks Nearing the Finish Line

Setting the Agenda in the Struggle for Regional Markets,
Multilateral Rules and Geopolitical Leadership

Hanns Günther Hilpert

Asia is not only the world's most dynamic region in terms of trade, it is also an important pacesetter in trade policy. The US is currently negotiating with eleven partner countries over a Trans-Pacific Partnership (TPP); the members of the ASEAN+6 group are in talks over a Regional Comprehensive Economic Partnership (RCEP); while Japan, China and Korea are conducting trilateral trade negotiations (CJK FTA). The multilateral structures emerging from all these initiatives could, in the long term, be combined into a Free Trade Area of the Asia-Pacific (FTAAP). What are the motives behind these agreements? What are their chances of being implemented? When it comes to the trade and geopolitical power struggle that encompasses these talks, does the US or China have the upper hand? And what role remains for Europe's trade policy?

Asia's trade policy landscape has fundamentally changed in the early 21st century. Whereas the defining trend up to the end of the 1990s was unilateral, non-discriminatory liberalisation in line with the model of open regionalism, these days trade policy has swung towards discriminatory bilateralism: in 81 of the 263 bilateral free trade agreements currently registered with the World Trade Organisation (WTO), at least one of the contract partners is a country in the Asia-Pacific. According to data from the Asian Development Bank there are another 143 agreements currently under negotiation. The attitude of the region's decision-makers towards multilateral trade policy

has also changed: whereas the Asian and Pacific WTO members tried, at the time, to advance the Uruguay Round of multilateral trade negotiations with their own initiatives, there are no such initiatives in the current round of talks in Doha. By refusing to open up their agricultural markets, the heavy-weights China and India are even said to have contributed to the failure of the Doha Development Round. Meanwhile, current negotiations over the mega-deals TPP and RCEP are taking the regionalisation of trade policy into entirely new dimensions. In each case there are several countries involved (see Fig. 1, p. 2) and the trade volumes are huge (see Fig. 2, p. 2). Further,

Figure 1
Member states of the planned Asia-Pacific free trade zones

<i>Trans-Pacific Partnership (TPP)</i>		Australia Japan Peru	Brunei Malaysia Singapore	Canada Mexico US	Chile New Zealand Vietnam
<i>Regional Comprehensive Economic Partnership (RCEP)</i>	ASEAN	Brunei Malaysia Thailand	Cambodia Myanmar Vietnam	Indonesia Philippines	Laos Singapore
	+ 6	Australia New Zealand	China South Korea	India	Japan
<i>China-Japan-Korea Free Trade Agreement (CJK-FTA)</i>		China	Japan	South Korea	

the content of the agreements goes beyond tariff liberalisation of traded goods and deeply impacts the prospective signatory states' sovereignty of economic policy, in areas including investment law, freedom of establishment, competition, regulation of services, government procurement and intellectual property rights. Since the WTO is not continuing to develop the international trade rules in these areas multilaterally, the agreements, if signed, would also set the tone in terms of regulatory policy: they would significantly influence how global trade rules are shaped in the future.

Figure 2
Weight of TPP, RCEP and CJK in the global economy, 2012 (proportion in %)

	TPP	RCEP	CJK
Global populations	11.2	47.8	21.5
Global production	37.1	28.6	20.6
Global trade	26.2	28.9	18.2
Of which intra-trade	11.3	12.3	3.5

Source: International Monetary Fund.

The geopolitical dimension

The present negotiations are not only significant in terms of trade and regulatory policy. The establishment of trans-continental free trade zones also has a geopolitical dimension. The TPP and RCEP negotiations are a reflection of the strategic rivalry between the United States and China.

For the US, TPP is a key element of its "Pivot to Asia" strategy. By granting them preferential market access, the TPP aims to strengthen the Pacific states' ties to the US and counter the pull of the Chinese market. The TPP would create a trans-regional alliance of states with agreement on free internal trade and high regulatory standards. In principal China has the option of joining the TPP as it is a Pacific Rim country and an APEC member. However, it would then have to accept the previously negotiated regulations and, further still, accept what are more or less arbitrary special conditions. In China the TPP is therefore perceived as part of the US strategy to contain China.

An important component of China's counter-strategy is the regional trade partnership RCEP, even though this is a diplomatic initiative of the ASEAN community. An RCEP free trade zone would constitute a regionally limited trade policy zone where China, thanks to its political and economic weight, could take the driving seat. The US would almost certainly be permanently excluded from this zone, as an existing free trade agreement with the ASEAN community is a prerequisite for membership. China is also seeking bilateral free trade agreements with its neighbouring countries, having already struck such agreements with ASEAN in 2005, New Zealand in 2008 and most recently with South Korea and Australia. China is also conducting talks

over a trilateral agreement with Japan and South Korea.

The fact that trade policy is charged with geopolitical significance makes it harder to find and settle on compromises in negotiations, because the “win-win” situations intrinsic to trade policy tend to become zero-sum games of political power. Yet the main content of the TPP, RCEP and CJK negotiations revolves around removing tariffs and other barriers to trade. The participating countries have primarily economic motives. The current negotiations are determined by economic cost-benefit calculations and the domestic policies of the countries at the table.

The window of opportunity for TPP is closing

The negotiations over a TPP free trade agreement date back to the Trans-Pacific Partnership agreement (TPP), signed by Brunei, Chile, New Zealand and Singapore (P4) in 2005. At the APEC summit in 2009 the US, Australia and Peru declared their intention to enter into negotiations with the four founding nations and to join the TPP agreement upon the successful conclusion of these talks. Having hesitated initially, Malaysia, Vietnam (2010), Canada, Mexico (2012) and Japan (2013) started participating in the negotiations as well. Aside from granting tariff preferences and establishing rules of origin, the 29 chapters being worked out in the TPP talks aim to set down binding “WTO-plus” rules, which cover services, investment protection, right of establishment, sanitary and phytosanitary measures, technical barriers to trade, rules of competition for state-owned companies, government procurement, intellectual property rights, labour and environmental standards. However, neither the negotiations nor the envisaged TPP agreement are truly multilateral. The US insisted on bilateral negotiations with those countries with which it had not previously signed a free trade agreement (Brunei, New Zealand, Malaysia, Vietnam, Japan). As a result,

the TPP member states will continue to face different trade barriers when exporting goods to the US in the future.

Nevertheless, for the twelve participating countries the agreement of such an extensive trans-Pacific liberalisation agreement is an attractive and far-sighted venture for several reasons.

First, the TPP promises higher employment, income and economic output. According to calculations by the Peterson Institute for International Economics in Washington, the seven initiators alone (P4 + US, Australia, Peru) could attain around USD 200bn higher export revenues and around USD 130bn higher income by 2025. Gross domestic product (GDP) would increase by 0.38 percent in the US and by as much as 2.25 percent in New Zealand.

Second, for the small and medium-sized TPP countries, receiving preferential market access to the major economies of the US, Japan and Canada is an attractive prospect, and this goes some way to stabilising investment expectations.

Third, the multi-state approach of the TPP provides those countries that specialise in industrial production (Malaysia, Mexico, Vietnam) with opportunities to develop cross-border supply and production chains; because intermediate goods from outside of the TPP are recognised as TPP value added when exported. The trading entrepot Singapore could therefore cement its leading position as an international trade and logistics hub.

Fourth, as a “platinum-standard” agreement with binding requirements and legally enforceable norms, the TPP agreement can set the overall tone in trade policy. It would effectively be advancing the development of global trade rules, much like the US and the European Union are attempting to do via the Transatlantic Trade and Investment Partnership (TTIP). It is preferable to participate in the negotiation of the new trade rules now, rather than having to accept them later as a “fait accompli”.

Despite these benefits, the participants appear to be having great difficulty coming

to an agreement. They failed to meet an initial deadline for completing the negotiations, first at the end of 2012, then in 2013. US President Barack Obama's plan to reach a compromise among the heads of state and government at the APEC meeting on 10-11 November 2014 was also unsuccessful. As such, the remaining window of opportunity for a binding agreement may close. Positions on the key negotiating issues remain sharply divided.

Some US demands are being met with flat-out rejections. For instance, the call to prohibit currency manipulation, to set out stringent rules on industrial property protection and to establish investor-state dispute settlement proceedings. In political terms, Vietnam cannot realistically fulfil the requirement to bring about a level playing field for state-owned enterprises. Malaysia, Singapore and Japan would also run into difficulties if such a competition clause were strictly interpreted. Should the US get its way on these points, joining the TPP agreement would be out of the question for China for the time being.

Conversely, what the US is offering in terms of opening up its markets does not go far enough for many TPP partners. Japan, for example, is calling for the American automobile tariffs to be abolished completely, Australia wants America to open up its sugar market, and New Zealand is demanding the liberalisation of dairy product imports (in the US and Canada). Meanwhile, Japan is vehemently resisting a liberalisation of agricultural imports, particularly when it comes to the five "sacred" products: rice, wheat, beef and pork, dairy products and sugar. Although the LDP-led government still feels bound to a corresponding resolution of the party's TPP committee, there are visible signs of flexibility, e.g. in the import of pork. On the other side, the US farming lobby is insisting on Japan substantially opening up its agricultural market. If such measures are not forthcoming, the Republican representatives from the farming states of the Midwest will hardly vote in favour of a TPP agreement.

President Barack Obama already has a task on his hands to get temporary Trade Promotion Authority (TPA) for America's trade policy from Congress. TPA would allow the president to agree bilateral and multilateral trade agreements that Congress could subsequently only approve or reject as a package. Since the farming lobby holds great sway over the Republican majority, however, the chances of a TPA after the midterm congressional elections have not really improved. From the perspective of Japan and other TPP negotiating partners, there is therefore a risk that any agreement would be renegotiated by Congress. For this reason, they will continue to hold back with compromises and trade concessions to the US. Due to the timing of US legislative sessions, however, if no compromise is reached by April 2015 at the latest, there will be very little chance of getting the TPP agreement through Congress before the US presidential campaign gets underway. The negotiations are therefore most likely to be completed under Barack Obama's successor.

RCEP: trade liberalisation the "ASEAN Way"

The negotiations over a Regional Comprehensive Economic Partnership (RCEP) may be understood as a reaction to the TPP free trade initiative, but equally as an attempt to bring about the long-held vision of an Asian free trade zone. The planned RCEP agreement would apply to an area spanning the four sub-regions of South-East Asia, North Asia, South Asia and Oceania. Politically, the initiative increases the centrality of the ASEAN community for Asian regionalism. Whereas the TPP threatens to split the ASEAN community (and Asia) in the area of trade policy, the RCEP negotiations intend to demonstrate the ten ASEAN members' will and capacity to bring together the countries of the Asia-Pacific region to promote economic integration, economic growth and development. The RCEP notably has the political backing of

the highly populous states of China, India and Indonesia – countries that cannot fulfil the extensive liberalisation demands of the TPP.

In the RCEP negotiations ASEAN seeks to consolidate its existing “ASEAN+1” free trade agreements with Australia/New Zealand, China, Japan, South Korea and India into a “comprehensive, high quality, and mutually beneficial agreement establishing an open trade and investment environment,” as the Leaders’ Statement of the 16 participating countries from Phnom Penh on 20 November 2012 explains. Liberalising foreign trade between the six ASEAN partner countries, on the other hand, is not an explicit part of the negotiations.

Japan was able to largely assert its interests over China in the run-up to the negotiation process. Whereas China wanted to restrict the talks to the ASEAN members along with China, Japan and Korea (ASEAN+3), Japan insisted on also including India, Australia and New Zealand (ASEAN+6), as it feared that China would otherwise dominate the process. In terms of content, China was primarily interested in removing tariffs and liberalising trade. Japan was also looking to establish binding rules on additional areas of negotiation. Effectively the talks now also cover goods trade, services, investment, competition, intellectual property and dispute settlement – though the goals are considerably less ambitious than those of the TPP. The partners are also discussing economic and technical cooperation with the RCEP developing countries.

This wide-reaching agenda has not made the negotiations any easier, especially as the six ASEAN+1 agreements upon which they are based all vary considerably in terms of scope, reach and quality. Even the liberalisations of trade in goods are each based on different customs tariff lines and different rules of origin. Only four agreements included a liberalisation of services trade – and there was considerable variation in the sectors covered. With such discrepancies it is no wonder that no major breakthroughs have been made in the six negotiation

rounds to date. It may therefore not be possible to meet the planned completion deadline at the end of 2015.

To reach some kind of conclusion despite the economic and political divergence within the RCEP integration area and the varying levels of overall ambition, the participating states have agreed on a series of guiding principles. First, the envisaged RCEP agreement should neither replace the valid ASEAN+1 agreements nor reverse the liberalisation measures they stipulate, but rather create a platform for real progress. Second, the RCEP agreement should take the individual circumstances of the participating countries into account and, above all, ensure that the less developed economies receive special and differential treatment. Third, additional ASEAN+1 partner states should be able to join the RCEP agreement. Finally, the negotiating partners explicitly reaffirmed that the agreement should remain consistent with the WTO rules, in particular the General Agreement on Tariffs and Trade (GATT).

Alongside its external dimension (RCEP), the trade policy liberalisation of the ASEAN community has an internal dimension in the form of the planned ASEAN Economic Community (AEC). With their sights set once more on the end of 2015, ASEAN’s six old members (Brunei, Indonesia, Malaysia, Philippines, Singapore, Thailand – ASEAN-6) and four new members (Cambodia, Laos, Myanmar, Vietnam – CLMV) aim to create a common market where the principle of free movement of goods, services, capital and labour will apply. However, it is foreseeable that the AEC – like the ASEAN Free Trade Area (AFTA) at the time – will not arrive on schedule. The implementation of the necessary measures has stalled. Although 99 per cent of the customs tariffs have been removed (ASEAN-6) or reduced to under 5 per cent (CLMV), the numerous other trade barriers remain intact.

Both the RCEP and the AEC subscribe to the “ASEAN Way”: consensus must be reached when fixing goals and obligations. The consideration of economic interests

and political sensitivities favours a careful approach tailored to the specific situation, sometimes even foregoing legal enforceability. The experiences of ASEAN integration show that gradual progress can be made and the region is slowly becoming more integrated. However, it is also evident that rapid market liberalisation cannot be achieved in this manner, nor can pioneering new trade rules be enforced under these circumstances.

CJK FTA – the missing piece of the puzzle

Despite the considerable foreign policy tensions present in North-East Asia, the trilateral cooperation between China, Japan and South Korea has notably gained in stature and substance over recent years. In 2010 a secretariat was set up in Seoul to coordinate intergovernmental cooperation and support joint projects, for instance in the areas of environment protection, disaster management and cultural exchanges. In 2012 the three countries signed a trilateral investment agreement. At the same time they resolved to enter into the long-planned negotiations over a trilateral free trade agreement (China-Japan-Korea FTA, CJK FTA). Six rounds of talks were held regarding a liberalisation of goods trade, services trade, investment and intellectual property rights. However, the negotiations will not be completed by the end of 2015, as originally planned, since Japan's ambitions are too far removed from those of China and Korea. The latter two countries fear the predatory competition stemming from Japanese industrial imports, while they do not feel that they in turn would gain export market opportunities due to Japan's informal, non-tariff trade barriers. Japan, meanwhile, is resisting tariff and import liberalisations for agricultural products and insisting on protection clauses against cheap Chinese imports. It is therefore not surprising that China, Japan and Korea have so far not even managed to agree on the scope of the tariff lines to be included. The fact that interest

groups with strong political connections in all three countries – China's state-owned companies, Japan's farming lobby, Korea's agriculture and industry – are agitating against a liberalisation of imports does not help the cause. Although China and South Korea did recently manage to sign a pioneering bilateral free trade agreement, the trilateral negotiations are set to drag on for some time, not least because liberalising internal North-East Asian trade is not top of the trade policy agenda in any of the three countries.

A trilateral free trade agreement would nevertheless be central to the future of North-East Asia's regional trade policy integration. For one thing, China, Japan and Korea make up 44.9 percent of the ASEAN+6 group population, 72.1 percent of its GDP and 63.2 percent of its trade volume. They are also Asia's most significant trading nations. Second, North-East Asia's intraregional foreign trade is stagnating. Although the absolute figures continue to rise, from a relative point of view the trend is one of disintegration, as the three countries' trade with other global regions is growing more rapidly than their trade with one another, not least due to numerous bilateral free trade agreements with third countries. A trilateral CJK agreement could trigger a reversal of this trend. This would make CJK the missing piece required to complete the envisaged East Asian free trade zone. The successful completion of the investment agreement in 2012 showed that pragmatism and economic considerations can take the upper hand in North-East Asia and push geopolitical differences into the background.

What next: TPP dominance or FTAAP consolidation?

Although the prospects for the successful conclusion of the TPP or RCEP negotiations remain uncertain for the time being, a definitive failure of these trans-regional free trade initiatives is even less likely. The trade policy ambitions of the countries in the region already go beyond the TPP and

the RCEP. Back in 2010 the Pacific heads of state and government at their APEC meeting in Yokohama officially approved the trade policy initiatives TPP, ASEAN+3 and ASEAN+6 as appropriate preliminary stages on the path towards a Free Trade Area of the Asia-Pacific (FTAAP). At the last APEC meeting in Beijing in 2014 China proposed, not entirely unselfishly, an FTAAP feasibility study to pave the way for actual negotiations. Although this proposal was not taken up, due to US resistance, there is no question that all parties share the goal of free trade in the Asia-Pacific area.

Nevertheless, there are widely held concerns that Asia could be split in terms of trade policy, as hopes of a consolidation of the prospective TPP and RCEP agreements could prove deceptive. First, a rapprochement between China and the US is extremely difficult to realise due to the geopolitical rivalry between the two blocs. Second, the competing trade policy agreements are not compatible with one another. It is unimaginable that the industrialised countries of the TPP, particularly the US, would be prepared to make concessions on their hard-won agreements, in areas such as competition, industrial property rights, labour and environmental standards. Rather than the TPP and the RCEP being consolidated, it is therefore more likely that the TPP free trade zone will be successively expanded. South Korea and Thailand have already signalled their interest in joining.

In principle the TPP is open to all APEC member states, and if the negotiations reach a successful conclusion it could prove a very attractive prospect. On the one hand, it would offer privileged access to the import markets of the US, Japan and Canada. And on the other hand, the TPP regulation standards could be highly attractive since they are necessary and useful for international business transactions. The binding implementation of TPP standards would prove the ability of emerging nations to connect with the industrialised world, and as such would be a key argument in the international competition to attract business

and investment. Many developing nations in Asia (India, Indonesia, Cambodia, Laos, Myanmar) will of course not be willing or able to comply with the stringent TPP standards for the time being. The expansion of the TPP area will therefore not necessarily include every country in the region. The political resistance of China and the ASEAN community, fearful of losing its leading role in the process of East Asia's regional integration, should not be underestimated either. The TPP nonetheless has the potential to become the decisive trade policy framework for Asia, provided the domestic policy hurdles in Washington and Tokyo can be overcome. Should this succeed, the TPP will probably fill the institutional vacuum of Asia's soft regionalism. The comprehensive, binding regulations on the movement of goods, services and capital envisaged under the TPP would be fundamental for trade in the region. The TPP could also become the crucial blueprint for regulatory policy on a global level, as a further development of trade rules in a multilateral (WTO) or trans-Atlantic (TTIP) context only appears likely to happen in the even more distant future if at all.

What about Europe?

Europe is not participating in any of the Asia-Pacific free trade projects. Furthermore, it is taking a noticeably passive stance on the region's efforts to reshape the trade and regulatory policies of the world trade order. Europe would be negatively impacted by all the prospective agreements (TPP, RCEP, CJK-FTA), with simulations indicating that trade with Japan would suffer the most from trade deflection.

The EU would be spared such effects if it signed its own free trade agreements with Asian and Pacific trade partners, as it has already done with Chile, Mexico, Peru, Singapore, South Korea and most recently Canada (CETA, not yet ratified). The EU has also been conducting talks with India (since 2007), Malaysia (since 2010), Vietnam (since 2012), Japan (since 2013) and

above all with the US (since 2013). The agreement with the US, the Transatlantic Trade and Investment Partnership (TTIP), is very important in terms of regulatory policy. In consultation with the US, the EU has the opportunity to impose its own regulatory ideas for global trade and to actively participate in designing the future world trade order. There is no doubt that the TTIP is a key strategic development that will directly impact third countries as well. In trade policy with Asia, however, the EU lacks any clear definition, despite its weight as the world's largest trading power, and is thus missing out on the chance to set its own strategic priorities.

The secular opportunity to break down Japan's non-tariff trade obstacles and structural market barriers cannot be taken on single-handedly. While Japan is deftly playing its trading partners off against one another in four different mega-deals, the EU and the US are making no efforts to counter Japan's protectionist interest groups through joint, concerted pressure.

A successful conclusion of the negotiations with Singapore, Malaysia and Vietnam should be taken as a starting signal for a new attempt to negotiate with the ASEAN community, the EU's natural partner in Asia and the anchor of Asian regionalism. Myanmar, which is opening up politically, must not be seen as an obstacle to agreement on trade policy.

A trade policy that blanks out China to create an "Asia minus one" community is not sustainable. Pushing for China's isolation in trade policy via trans-regional mega-projects is something the West should avoid altogether. From Europe's point of view, it would be beneficial to enter into negotiations over a free trade agreement with China before it applies to join the TPP.

© Stiftung Wissenschaft und Politik, 2015
All rights reserved

These Comments reflect solely the author's views.

SWP
Stiftung Wissenschaft und Politik
German Institute for International and Security Affairs

Ludwigkirchplatz 3-4
10719 Berlin
Telephone +49 30 880 07-0
Fax +49 30 880 07-100
www.swp-berlin.org
swp@swp-berlin.org

ISSN 1861-1761

Translation by
English Express e.K., Berlin

(English version of
SWP-Aktuell 75/2014)