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TPP, RCEP and Global Trade Governance

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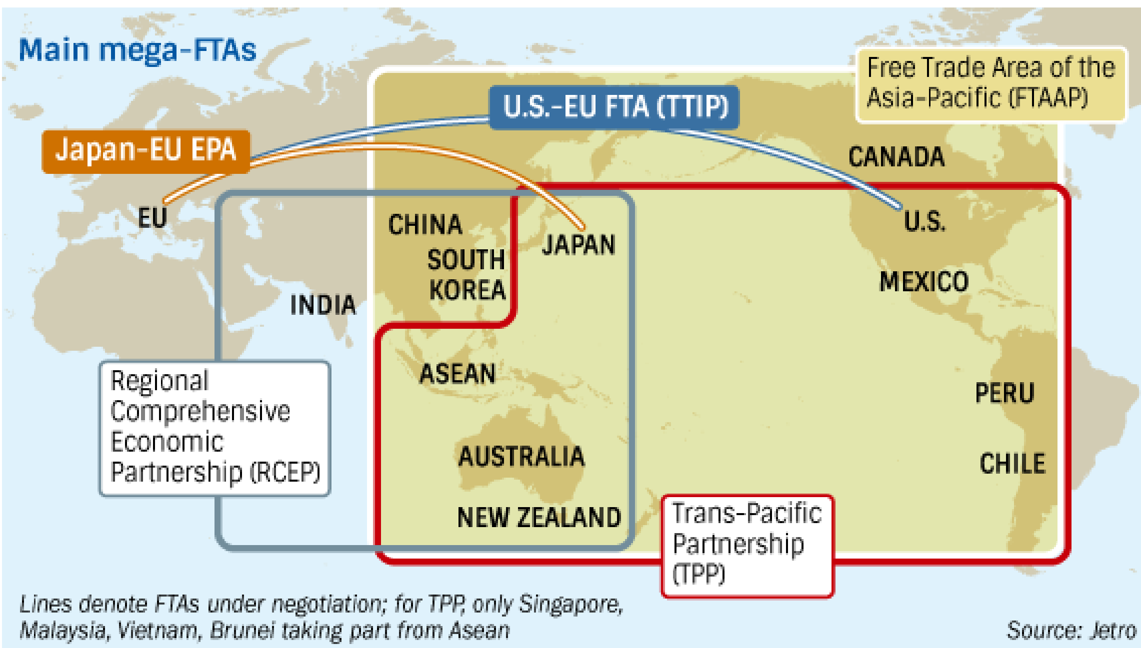
Prologue

The world today has entered into a new era of trade governance. With the long stalemate of the Doha Development Agenda (DDA) of the WTO, major trading countries have shifted their trade policy priority to negotiation of mega-FTAs such as TPP (Trans-Pacific Partnership), TTIP (Transatlantic Trade and Investment Partnership), Japan-EU EPA (Economic Partnership Agreement) and RCEP (East Asian Regional Comprehensive Economic Partnership) (See Figure 1).

Figure 1: Mega-FTAs in the world (December 2013)



(Source: Kazushi Kagaya, "Trading Up", *Nikkei Asian Review*, 5 December 2013. Available at [http://asia.nikkei.com/magazine/20131205-Rebalancing-act/Cover-Story/Trading-up]

Conclusion of these mega-FTA negotiations might drastically change the structure and function of global trade governance, from WTO-centered multilateral governance to plurilateral governance consisting of mega-FTAs. This possible change in global

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trade governance may have both advantages and disadvantages. One major advantage is that global trade governance will be equipped with trade/investment rules that meet the pressing needs of global value chains (GVCs). However, global trade governance without a formal multilateral trade organization may face the risk of marginalizing many developing countries including most LDCs. Also, it may not secure the optimal trade/investment rules and institutions for GVCs, as mega-FTAs may contain conflicting and inconsistent rules (risk of fragmentation).

Countries in East Asia must take on greater responsibility to avoid such risks of plurilateral trade governance, while fully achieving its advantages, than any other countries in the world, because they are engaged in the negotiation of two mega-FTAs, namely, TPP and RCEP. This paper argues that East Asian countries, in particular Japan and China, must play a critical role in the realization of the global trade governance of the 21st century by trying to assimilate the contents of TPP and RCEP, and expanding them to the rest of the world.

I. Global value chains (GVCs) as ascendant form of global trade (and investment)

To fully understand the drastic change in global trade governance, namely the stalemate of the DDA and the frenzy of mega-FTAs, we must realize the driving force that has brought this change. The changing pattern of global trade and investment, which is coined in such terms as globalization of value chains (GVCs), globalization of supply chains or international production networks, is the driving force. GVCs started in the 1970s in North America (Canada, US, and Mexico) in automotive industry and expanded in Central and East Europe (Germany and former socialist countries in the region) in a number of manufacturing industries in late 1980s to early 1990s. However, it was in East Asia in the mid-1990s on that GVCs developed on a full scale. Japanese firms took the initiative by aggressively investing in manufacturing sector (electronic appliances, machinery and automobiles) in several ASEAN countries (Thailand, Malaysia and Indonesia) and Taiwan, with US and EU as major export market. Later, Japanese firms expanded their production bases to China, India, and more recently to Vietnam and Myanmar.

Currently, the GVCs are getting more and more “global” both geographically and in its sectoral coverage, as firms are doing business globally regardless of their size, country of origin and their field of activity. In particular, services sector has become a major component of GVCs, not only because they provide services indispensable to globalization of manufacturing (e.g., transportation, telecommunication, logistics and financial services), but also because many service are traded globally (e.g., professional services such as lawyering and accounting, retail and wholesale, tourism, construction and civil engineering, water supply and even health services).

Innovation in information and telecommunication technology (ICT) and the resulting dramatic decline of costs in telecommunication and transportation were the major triggers to GVCs. However, GVCs would not have happened without the drastic change in the policy and regulations of international trade (goods trade and services trade) and investment (FDI and M&A). The Anglo-Saxon countries (US and UK) took the initiative in the latter, by conducting liberal domestic and external economic policy reforms in the early 1980s (Reaganomics and Thacherism). Other countries in Europe and later Japan followed suit. At the same time, several ASEAN countries also adopted export-promotion policy reform in the 1990s by unilaterally liberalizing import trade and inward investment.

Most of these economic policy reforms were conducted unilaterally in US, Europe and Japan. But, firms in these developed countries demanded the expansion of such policy reforms to cover their global business territory, as they needed a broad based trade and investment liberalization and a high level of liberal trade and investment rules throughout the countries within their business transactions (see Table 1 below).

Table 1: Policies needed for GVCs

① **Relating to reducing fixed costs for establishing GVCs**	Enhanced services for supporting production (financial, transportation, telecommunication, electricity, etc.); Investment liberalization/protection; Access to government procurement market; IPR protection; Competition policy; Regulatory/institutional harmonization
② **Relating to reducing service link costs**	Tariff reduction; Trade facilitation; Logistics infrastructure building; Liberalization/facilitation of business persons; Regulatory/institutional harmonization
③ **Relating to reducing production costs of each segment**	Human resources development; Development of supporting industries; Development of industrial agglomeration; Enhanced services for supporting production; Investment liberalization/protection; Access to government procurement market; IPR protection; Competition policy; Regulatory/institutional harmonization

(Source: Made by the author.)

The first attempt to establish such liberal economic policy reforms multilaterally, the OECD-sponsored Multilateral Agreement on Investment (MAI) failed in 1998. The second attempt was the DDA of the WTO that started in November 2001. However, perhaps due to the power structure of the WTO which was quite different from that of the GATT, members of the WTO found it much more cumbersome and time-consuming for multilateral trade negotiations to reach consensus. On almost all issues of the DDA agenda, key members, namely, US, EU, China, India and Brazil, couldn't reach agreement. Although the 9th Ministerial Meeting held in Bali in December 2013, could wrap up negotiations of the Agreement on Trade Facilitation, itself an indispensable component of global regulatory environment for GVCs, for the rest of the long list of DDA agenda, there is little hope for early conclusion.

In light of these, notably the DDA stalemate, major firms and industry associations in developed countries began to pressure their governments to shift the trade policy priority from WTO to the negotiation of mega-FTAs. Here again, US took the initiative in March 2008, when the Bush Administration announced its intension to join the follow-up negotiation of the then four-party Trans-Pacific Strategic Economic Partnership Agreement (sometimes called as P4, among New Zealand, Singapore, Chile and Brunei) on financial services and investment. US decided to join the P4 as a whole in September 2008. The Obama Administration succeeded this and TPP negotiation started in March 2010 with 8 members. The launch of TPP negotiation had a strong *domino* effects and triggered negotiations of other mega-FTAs, as they started in 2013 (see Table 2 below).

Table 2: Chronology of mega-FTA negotiations

	TPP	TTIP	Jap/EU	RCEP	JCK
Oct 2002	NZ, Singapore and Chile agreed on launching TSEPA negotiation.				
Apr 2005	5th meeting, Brunei joined.				
Jun	Negotiation wrapped up.				
May~Nov 2006	Members ratified TSEPA (P4).				
Mar 2008	P4 financial service/investment negotiation scheduled. US announced to join.				
Sep	US announced to join P4, Australia, Peru and Vietnam followed.				
Mar 2010	1st meeting (Melbourne)				
Jun	2nd meeting (San Francisco)				
Oct	3rd meeting (Brunei), Malaysia joined.				
Dec	4th meeting (Auckland), Vietnam joined.				
Feb 2011	5th meeting (Santiago)				
Mar~Apr	6th meeting (Singapore)				
Jun	7th meeting (Hoh Chi Ming City)				
Sep	8th meeting (Chicago)				
Oct	9th meeting (Lima)				

Nov	TPP leaders agreed on "a broad outlines of the agreement".				
Dec	10th meeting (Kuala Lumpur)				
Mar 2012	11th meeting (Melbourne)				
May	12th meeting (Dalas)				
Jul	13th meeting (Santiago)				
Sep	14th meeting (Leesburg)				
Dec	15th meeting (Auckland), Canada and Mexico joined.				
Mar 2013	16th meeting (Singapore)				**I.**
Apr			**I**		
May	17th meeting (Lima)			**I**	
Jun			**II**		
Jul	18th meeting (Kota Kinabalu)	**I**			**II**
Aug	19th meeting (Brunei)				
Sep				**II**	
Oct	TPP leaders announced "negotiation is proceeding to conclusion".	**II**	**III**		**III**
Nov	Mid-term meeting				
Dec	TPP ministers announced they found "possible landing points on major outstanding issues".	**III**			
Jan 2014	TPA Bill submitted to US Congress.		**IV**	**III**	
Feb	TPP Ministerial meeting				
Mar~Apr		**IV**	**V**		**IV**
Apr	Japan-US Summit			**IV**	
May	TPP Ministerial meeting		**EC MTR**		
Jun	TPP chief negotiators' meeting	**V**		**V**	**mid-mtg**
Jul		**VI**			
Aug					
Sep					
Oct					
Nov		**US MTE**			
Dec					
End 2015					

(Source: Made by the author)

II. TPP and RCEP: Confrontation or peaceful co-existence?

TPP, currently under negotiation among 12 countries in the Asia Pacific region, is most likely to become the first mega-FTA, as its negotiation may be wrapped up by, in an optimistic scenario, the end of 2014. It is also likely to become "a 21st century model FTA", as was envisioned by the then US Trade Representative Ronald Kirk, when he notified the intention of the Obama Administration's intention to join the enlarged TPP negotiation to the leaders of the US Congress in December 2014. There are two reasons for which TPP is likely to become a 21st century model FTA. First, TPP is aiming at a broad based trade and investment liberalization and a high level of liberal trade and investment rules throughout its member countries. Secondly, rules and commitments of TPP are being referred to by the negotiators of other mega-

FTAs, notably TTIP and Japan-EU EPA, and will become *de facto* global standards for international trade and investment.

On the other hand, RCEP is rather a 20th century trade agreement, as its focus is liberalization of trade in goods and services, and it doesn't intend to cover wide range of regulations for GVCs. At best, RCEP will be a regional trade agreement with some WTO+ commitments (see Table 3 below).

Table 3: TPP and RCEP – their expected contents

TPP	WTO	TTIP	Jap/EU	RCEP
(1)Goods market access	○	○	○	○
(2)Rules of origin		○	○	○
(3)Trade facilitation	○	○	○	○
(4)SPS	○	○	○	○
(5)TBT	○	○	○	○
(6)Trade remedies	○	○	○	○
(7)Government procurement	△(GPA)	○	○	×
(8)Intellectual property rights	△（TRIPS）	○	○	△
(9)Competition policy	×	○	○	×
(10)Cross-border trade in services	△(GATS)	○	○	△
(11)Entry/stay of business persons	△(GATS)	○	○	△
(12)Financial services	△(GATS)	○	○	△
(13)Telecommunications	△(GATS)	○	○	△
(14)E-commerce	×	○	○	?
(15)Investment	△(TRIMs)	○	○	△
(16)Environment	×	○	○	×
(17)Labor	×	○	○	×
(18)Institutional matters	○	○	○	○
(19)Dispute settlement	◎	○	○	○
(20)Cooperation	○	○	○	○
(21)Cross-cutting issues				
Regulatory coherence	×	○	○	×
Cometitiveness and business faciliation	×	○	○	×
Promotion of SME utility	×	○	○	×
development	×	×	×	×

(Note: ○ refers to "yes", △ refers to "yes, but partially", × refers to "no", and ◎ refers to "yes, it's the best".) (Source: Made by the author)

What, then, will be the relationship between TPP and RCEP when they both are concluded? First, TPP and RCEP will co-exist as trade agreements with different membership and contents. Firms of a country which is party to both agreements will choose which agreement to apply, depending on the products traded, investments they make. This will of course add another complexity to the trade and investment in the region, but there'll be no way to avoid it. Secondly, TPP is likely to attract other countries of the Asia-Pacific region, as is shown by the notification of South Korea to join it and by the expressed interest by such countries as Taiwan, Philippines, Thailand, Columbia and Costa Rica, while RCEP will remain a trade agreement among ASEAN+6 members. Thirdly, major non-members to TPP that are the parties to RCEP, namely, China and India, will have to decide whether to join TPP or not in due course. However, it will be fairly difficult for these countries to join TPP, in light of its broad based trade and investment liberalization and a high level of liberal trade and investment rules. For instance, the TPP chapter on competition policy will provide stringent discipline against financial and regulatory preferences to state-owned enterprises (SOEs). It will be much difficult for China to accept them.

It is, therefore, safe to conclude that TPP and RCEP will co-exist, but their relationship may not be a friendly one. It may rather be a confrontation between a 21st century trade agreement and a 20th century trade agreement, and the former may gradually overwhelm the latter.

III. Beyond confrontation: Towards *WTO 2.0* and beyond

What was envisioned in the last two sections, namely the emergence of mega-FTAs, and TPP in particular, in the governance of global trade and investment, is, however, far from an optimal solution to the challenges of global trade governance today. TPP rules and commitments may become *de facto* global standards, but they have two intrinsic defects in achieving their goal of providing optimal trade and investment environment for GVCs. First, mega-FTAs will cover their members and exclude non-members, most of which will be LDCs. There will be a split between those included in "mega-FTA clubs" and those excluded. Poverty and income disparity in LDCs will worsen, and this might lead global insecurity. Secondly, membership of "mega-FTA clubs" will not automatically secure that they will be chosen by global firms. As is shown in Table 1 above, the rules and commitments of mega-FTAs are necessary conditions for GVCs but they are not sufficient conditions. Countries must develop human resources, supporting industries and industrial agglomeration to attract global firms. These measures are not covered by mega-FTAs. They are rather provided by the voluntary and unilateral efforts of each country. This means that even non-members of mega-FTAs may have a chance to join GVCs by unilaterally providing rules, commitments and policies that are needed for GVCs. Members of mega-FTAs cannot prevent such efforts.

In light of these, countries in East Asia should think seriously of transplanting rules and commitments mega-FTAs, notably TPP, to the WTO. WTO, with 160 members now, is equipped with several institutional mechanisms by which members with different stage of development and capability may come up with the rules and commitments in a gradual but steady manner (see Table 4 below).

Table 4: Institutional infrastructure of the WTO

functions	WTO	mega-FTAs
trade liberalization	◎（ S&D, critical mass）	△（S&D）
investment liberalization	△（TRIMs, GATS Mode 3 ）	△（S&D）
rule-making	◎（multilateral trade negotiation, plurilateral agreements）	○(WTO+ 、WTOx ）
S&D	◎（broad based S&D, capacity building, Aid-for-Trade）	△（limited S&D）
monitoring rule implemenation	◎（report and peer review at Commissions and Councils）	△（Joint Commission）
trade policy review	◎（TPRM）	△（Joint Commission）
dispute settlement	◎（ judicialized dispute settelement）	△（weak dispute settlement）

(Source: Made by the author)

By transplanting rules and commitments of mega-FTAs to WTO, those rules and commitments will become truly global, and WTO members, whether developed or developing, will get a chance to join GVCs gradually but steadily. WTO will be reinvigorated with new rules and commitments that will match the needs of GVCs, and we may coin it as *WTO 2.0*.

Japan and China should take the initiative in the creation of *WTO 2.0*. They will first try to assimilate rules and commitments of TPP and RCEP. They will then take the initiative in the launch of the second multilateral trade/investment negotiation of the WTO after the DDA, by transplanting the rules and commitments of TPP (and RCEP).

Epilogue

This paper argues that Japan should China must take the joint initiative in achieving an optimal plurilateral trade governance for the 21st century by assimilating the contents of TPP and RCEP and expanding them to the rest of the world. If Japan and China can manage to assimilate the contents of TPP and RCEP at a broad based trade and investment liberalization and a high level of trade and investment rules, as discussed in Section II above, the contents of TPP and RCEP will become *de facto* global standards by their reference in other mega-FTA negotiations (TTIP and Japan-EU EPA), because these four mega-FTAs combined will occupy over 90% of global trade and investment.

However, this must not be the ultimate goal of Japan and China's trade policy. The plurilateral trade (and investment) governance has two intrinsic defects in achieving an optimal global trade/investment regulatory/institutional environment for GVCs, namely, marginalization of many developing countries including most LDCs and the risk of fragmentation. Japan and China must, therefore, take the joint initiative to transplant the common contents of TPP and RCEP to the WTO and make the *de facto* global standards to truly global standards. I coined this as *WTO 2.0* (Section III).

Will the WTO 2.0 secure an optimal global trade governance of the 21st century? Unfortunately, the answer is negative. GVCs are realized not only by broad based trade/investment liberalization and a high level of trade/investment rules. They are also realized in a liberal and exponentially growing global financial market (GFM). Although the GFM of the 21st century, coupled with GVCs, may secure continuous growth and prosperity, it is also vulnerable to seemingly unexpected and unpredictable shocks. As was witnessed in the Global Financial Crisis of 2008 and ensuing crisis in Europe triggered by the default of Greek, such shocks, once occur, may endanger the GFM and GVCs as a whole, and its consequence may be detrimental to global wealth and prosperity, endangering global peace and security.

What is needed is, therefore, not only the *WTO 2.0*, but the comprehensive reinvention of global economic governance institutions. Such reinvention need not a whole destruction of existing institutions such as IMF, World Bank, G8, G20, OECD and Basel Committee, to mention a few. Rather it can be achieved by fine-tuning the functions of such institutions and by furthering their coordination and co-operation. I'd like to coin such reform as *Bretton Woods 2.0*. (See Table 4 below).

Table 5: Bretton Woods 2.0+α

What can mega-FTAs not provide	**Solutions by mega-FTAs**	**Solutions by others**	**Yet to be provided**
transparent and non-ccorrupt government	government procurement; regulatory coherence; business facilitation	GPA(WTO); Anti-corruption Conventions (OECD/UN)	*WTO2.0+Bretton Woods 2.0*
elimination of global tax havens	none	tax treaties	global tax treaty
global financial crisis	none	IMF; G8; central banks	*Bretton Woods 2.0*
Terrorist attacks	none	Anti-terrosim conventions; Homeland Security Act	??
global warming	environment	Kyoto Protocol	Kyoto Protocol implemented
labor migration	none	national immigration control; NAFTA; Japan-Indonesia EPA, etc.	global migration scheme; freedom of migration?
tsunami and earthquakes	none	none	??
secured supply of energy resources	none	IEA; Energy Charter Treaty; Russia-China deal?	global energy scheme
human rights protection	none	UN; ECHR, etc.	??
poverty reduction/fair income distribution?	none	WB, Regioanl DBs	*Bretton Woods 2.0*

(Source: Made by the author)

Here again, Japan and China should take the joint initiative by persuading other countries, notably US and EU, for the realization of global economic governance that can secure economic growth, peace and security not only to developing countries but also to the world’s most remote and backward people.