

Draft

Trends of FTAs and Patterns of Trade in East Asia from the 1990s to 2110s

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I. Introduction

The East Asia region witnessed rapid expansion of intra-regional trade in the late 1980s and 1990s, resulting in “de-facto” regional economic integration. Behind this development was the formation of regional production networks by multinational corporations (MNCs). MNCs adopted the fragmentation strategy, under which they break up production process into a number of production sub-processes (blocks) and locate them in a country or a region where these sub-production processes can be performed most efficiently. MNCs actively trade parts and components connecting sub-processes and produce final products by assembling parts and components imported from various locations. MNCs were able to adopt the fragmentation strategy because of free and open business environment established by liberalization in trade and foreign direct investment (FDI) policies adopted by East Asian economies and because of reduction in transportation costs due to technological progress and deregulation.

Construction and use of regional production networks contributed to economic growth, which in turn led to further liberalization of trade and FDI policies, resulting in greater and deeper regional economic integration. Because of the importance of market forces, resulting from trade and FDI policy liberalization, in the formation of regional economic integration, such integration is characterized as market-driven regional economic integration¹.

In the late 1990s East Asia began to observe the emergence of institution-driven regionalization, which was promoted mainly by the establishment of free trade agreements (FTAs). An FTA is a trade policy, where tariffs on trade between and among FTA members are eliminated, while tariffs on imports from non-FTA members remain at the same level. East Asia was a late comer in the FTA frenzy, as other regions including Europe, North and South America and others began to establish FTAs in the late 1980s. Although East Asia was a late starter in the FTA race, it caught up with the rest of the world very quickly, first establishing mostly bilateral FTAs involving two countries and later moving to plurilateral and multilateral FTAs.

The objective of this paper is to provide an overview of the FTA developments in East Asia and to examine the patterns of trade, which are likely to have been affected by FTAs. Specifically, it attempts to examine the patterns of FTA developments in East Asia and then identify the factors that led to active formation of FTAs. The analysis of the developments of FTAs is performed more or less on chronological order, beginning with the 1990s, then 2000s, and finally in the 2010s before examining the trade patterns.

¹ See Urata (2004) for the discussions on market-driven and institution-driven regional economic integration in East Asia.

Although there are both economic as well as non-economic, particularly political, factors are at work behind the formation of FTAs, this paper focuses on economic factors. The main geographical focus is East Asia, but discussions are sometimes extended to include those countries/economies in Asia-Pacific.

II. 1990s: ASEAN Free Trade Area and Emergence of Discussions on Bilateral FTAs

Starting in the latter half of the 1980s, the movement towards forming regional economic integration, which is regionalization in terms of institutions, became active among the regions of the world. In Europe, the movement towards regional economic integration in institutions which started in the 1950s, accelerated. The European single market was formed in 1992, in which goods, services, labor and capital could move freely. The European Union (EU), which is an economic and political union, was established in 1993, and the currency union was established in 1999 by introducing a common currency, euro. In North America, through forming FTAs starting in the mid-1980s, the United States (US) promoted institutional regional economic integration. Among the FTAs to which the US is a party, North American Free Trade Area (NAFTA), which was founded with Canada and Mexico in 1994, is the largest in economic scale.

In contrast to other regions of the world, East Asia was inactive in pursuing institutional regional economic integration in the form of FTAs until the end of the 1990s. In fact, the ASEAN Free Trade Area (AFTA) comprised of ASEAN countries was the only major FTA established in East Asia before the turn of the century. ASEAN was founded in 1967 with political objectives but became increasingly active as an economic framework after the end of the East–West Cold War in 1989. AFTA was created by the ASEAN members of that time (Brunei, Indonesia, Malaysia, the Philippines, Singapore and Thailand), and came into effect in 1993. Thereafter, Vietnam, Myanmar, Lao PDR, and Cambodia, which had joined ASEAN, acceded to AFTA. Through AFTA tariffs were reduced in stages, and for the six original member countries tariffs on trade among the member nations (intra-regional tariffs) were abolished for all products aside from those which were considered exceptions to liberalization by 2010. For the four newer member countries, elimination of intra-regional tariffs is planned for 2018. Within ASEAN, not only is there the FTA regarding goods in the framework of AFTA² there is also an FTA on trade in services (AFAS) and an agreement regarding investment (AIA).³ These policy

² ATIGA (ASEAN Trade in Goods Agreement) was enacted in 2010.

³ AFAS (ASEAN Framework Agreement in Services) was founded in 1995 and AIA (ASEAN Investment Area) in 1998. In 2009, AIA developed into ACIA (ASEAN Comprehensive Investment Area), which contains more comprehensive contents.

and institutional initiatives toward economic integration in ASEAN were culminated by establishing the ASEAN Economic Community (AEC) in 2015. The main objective of AEC is to set up a single market and production base, where free movements of goods, services, investment and skilled personnel, is established⁴. While a remarkable progress has been made to achieve AEC, there still remain unfinished goals. To deal with the remaining issues and to complete AEC, a new target year of 2025 has been agreed to complete AEC by the ASEAN Economic Ministers⁵.

Several factors may be found behind the formation of AFTA and AEC⁶. Two important external motives are formation of regional economic integration frameworks in the rest of the world and competitive threat from China. Moves toward strengthening regional economic groups became active in the latter half of the 1980s as was discussed earlier (Figure 1). Intensified moves toward regional economic grouping in major areas in the world made ASEAN realize that FTA could be an important policy option to promote trade and not to be left out from the major markets.

Another factor was the increasing importance of China as a recipient of foreign direct investment (FDI). China became to attract FDI notably in the late 1980s, as multinational corporations (MNCs) from developed countries found China an attractive FDI destination. This is largely because of abundant availability of low-wage labor and potentially huge market in the future. Furthermore, the Chinese government improved inward FDI environment by implementing reform and market opening policy and providing various incentives to foreign investors. Faced with increasing amount of FDI being attracted to China, ASEAN Leaders and government officials became concerned with further expansion of FDI inflows to China at the expense of FDI inflows to the ASEAN region. One response to deal with this concern was to set up a region-wide market by establishing a free trade area. Indeed, for ASEAN China has been always regarded as a competitor in various aspects including as FDI host country/region and as an exporter in overseas markets such as the US. Indeed, ASEAN's schedule for the completion of AFTA and AEC were moved forward, as ASEAN thought competitive threat from China grew remarkably.

The internal dynamic of ASEAN has also contributed to deeper integration in the form of ASEAN Economic Community. Specifically, Asian Financial Crisis in 1997-1998 made the ASEAN Leaders realize the need to promote cooperation, in order to avoid another crisis. They expected that through various types of economic cooperation under

⁴ On ASEAN Economic Community, see, for example, ASEAN (2008).

⁵ See ASEAN (2017) on this point.

⁶ See ERIA (2014) on AFTA and AEC.

AEC would contribute to making ASEAN a resilient and competitive region, a region with equitable economic development.

Toward the end of 1990s, several countries in East Asia began to consider the establishment of bilateral FTAs. Among ASEAN countries, Singapore actively pursued FTAs. Singapore approached Japan and Korea for possible FTAs in 1998. Among North East Asian countries, Korea was the first country that began discussing FTAs. Korea and Chile began bilateral FTA negotiations in 1999. Compared to Korea, Japan was passive in pursuing FTAs. Mexico approached Japan to discuss possible bilateral FTA in 1998, while Korea and Singapore each approached Japan in 1998 and 1999. Japan and Korea are two major WTO members that did not have any FTAs at that time. Japan and Korea shared a view that they should not be involved in preferential and discriminatory trade agreements such as FTAs because they would violate a basic principle of non-discrimination in the WTO, thereby complicate the trading environment to discourage trade.

Both Japan and Korea changed their attitude toward FTAs and began to study their feasibility. Several reasons may be identified as the reasons behind their change in attitude. One is rapid increase in FTAs in the world. As discussed earlier, FTAs began to increase rapidly in the 1990s (Figure 1). One reason behind this rapid expansion of FTAs is slow progress in multinational trade liberalization under General Agreement on Tariffs and Trade (GATT) until 1994 and the World Trade Organization (WTO) after 1995. Faced with the situation, those countries interested in trade liberalization opted for FTAs with like-minded countries. FTAs tend to trigger the domino effect, because they are discriminatory trade policy. Those countries that are excluded from FTAs suffer from discrimination. In order to deal with the disadvantageous situation, those excluded countries try to join existing FTAs or set up their own new FTAs. This way the number of FTAs expanded.

Faced with discriminatory situation resulting from a rapid expansion of FTAs, Japan and Korea changed their attitude toward FTAs from negative to positive. Another reason is the break out of the Asian Financial Crisis (AFC). Korea suffered seriously from AFC that began in June 1997 in Thailand. The crisis spread through other Asian countries including Indonesia, Korea, Philippines and Malaysia. Faced with the crisis situation, Korea approached Japan and other countries, in order to obtain various types of cooperation including provision of emergency loans. Another type of economic cooperation sought by the leaders is the formation of FTAs. Many bilateral FTAs that were proposed and studied later became to be negotiated and then enacted in the 21st century, to which we turn in the next section.

III. 2000s: ASEAN+1 FTAs and Beginning of Discussions on Region-Wide FTAs: ASEAN+3FTA, ASEAN+6 FTA, CJK FTA and TPP

The early 2000s saw the enactment of a series of bilateral FTAs involving East Asian countries, beginning with Japan-Singapore FTA in 2002. While Japan and Korea became active in establishing FTAs, China did not show an interest in FTAs. However, after China joined the WTO in 2001 and established an access to the world market, it started to pursue regional strategies by using FTAs. China's approach toward FTAs was quite different from those of other countries in several respects, and thus many East Asian countries, especially Japan and Korea, were caught by surprise. First, unlike Japan and Korea that pursued bilateral FTAs, China approached ASEAN as a group to form an FTA. Second, China-ASEAN FTA contains the components that have not been incorporated in other FTAs. Specifically, China offered various schemes attractive to ASEAN and particularly to its new members such as economic cooperation for the new ASEAN members and advanced trade liberalization (early harvest) in tropical foods and other products.

Several factors may be considered behind China's active FTA policy. One is to maintain and expand export markets and another is reduced adjustment costs for trade liberalization as a result of substantial trade liberalization committed before its entry to the WTO. China started to have a concern about its export market because of the increase in FTAs and increase in protectionist measures against Chinese exports, particularly in the form of antidumping charges. Faced with these obstacles to the expansion of its exports, China considered FTAs as possible solution. China's positive attitude toward FTAs was attributable to the realization that China may not have to incur much additional adjustment costs from FTAs because it had already committed to substantial trade liberalization under the WTO. Besides these economic motives, it is commonly perceived that China uses FTAs as regional policy to increase and strengthen its economic and non-economic positions in East Asia.

China-ASEAN FTA triggered the Domino effect in that Japan, Korea, Australia-New Zealand, and India individually approached ASEAN to establish FTAs. Although there was a strong tendency for these FTAs to have been brought to ASEAN by the other party rather than ASEAN working towards them, the fact that partner countries were able to be made aware of the political and economic importance of ASEAN indicates high diplomatic abilities of ASEAN. China-ASEAN FTA was enacted in 2005. Other FTAs involving ASEAN as a group were enacted during the subsequent period, and by 2010 five ASEAN+1 FTAs (each with China, Japan, Korea, India, and Australia-New Zealand)

were enacted, making ASEAN a regional hub of FTAs in East Asia. Table 1 shows the level of trade liberalization for five ASEAN+1 FTA. The figures show the percentage of tariff lines (HS-6 digit) that are committed to be tariff elimination in total tariff lines. ASEAN+ANZ FTA has the highest level of tariff elimination, while ASEAN+India FTA has the lowest. These differences lead to difficulty in forming a region-wide FTA, which will be discussed in section IV.

The concept of an FTA that encompasses all countries of East Asia emerged in the late 1990s. At the ASEAN+3 (China, Japan, Korea) summit meeting in 1998, the East Asia Vision group was suggested to be established by President Kim Dae Jung of Korea, to study goals for long-term economic cooperation. This group submitted a policy proposal including the formation of an East Asian FTA (EAFTA) to its leaders in 2002. In 2005, a research group of private-sector experts was formed to examine the possibility of achieving an EAFTA, and after completing a first and second phase compiled a 2009 proposal that intergovernmental discussions should begin. Thereafter, a working group centered around the Chinese government was formed to discuss important themes such as the definition of rules of origin for the creation of an FTA at the regional level.

Soon after the research group for EAFTA was formed, Japan proposed the idea of a Comprehensive Economic Partnership for East Asia (CEPEA) in 2006 as an economic partnership agreement to include an FTA with the member countries of ASEAN+3+3 (ASEAN, China, Japan, Korea, India, Australia and New Zealand). ASEAN+3+3 (ASEAN+6) also comprises the members of the East Asian Summit meeting that was launched in 2005⁷. Considering the rivalry between Japan and China, and keeping in mind that China was the country that took the initiative in discussing the EAFTA, it can be understood that the backdrop to the CEPEA concept was Japan's strategy to play a leadership role in creating regional institutions in East Asia. A research group of private-sector researchers to study the feasibility of the CEPEA started in 2007, and it passed through first and second phases, proposing in 2009 that discussions between governments should begin. From this recommendation, just like the case of EAFTA, the government extracted important themes for achieving a CEPEA, including the rules of origin, and is furthering discussion under a working group.

The activities and research surrounding the EAFTA and CEPEA moved in parallel, often organizing discussions back to back. It is clear that China and Japan were respectively taking the leadership role in each group, but ASEAN countries, which did not want to deepen the opposition by aligning with one or the other, participated in both activities with equal weight. Amidst these circumstances, ASEAN countries were

⁷ Since then, the US and Russian joined the East Asian Summit group.

strengthening their voice in both frameworks and became to engage actively in order to take the lead in the discussions on regional integration in East Asia. Japan and China both participated in EAFTA and CEPEA activities for the reason that there is a common understanding that maintaining favorable relations between the two countries is important for the promotion of regional integration in East Asia. In fact, through EAFTA and CEPEA activities it may be considered that the rival attitudes of Japan and China seemed to have decreased.

One goal of founding EAFTA and CEPEA is to increase the level of economic activity by forming an integrated market in East Asia. In 2000s five ASEAN+1 FTAs were about to be completed, but these FTAs did not result in a unified single market. FTAs connecting +6 countries (China, Japan, Korea, India, Australia-New Zealand) were missing. If a single market like that of Europe were created in East Asia as well, the elements that carry out an important role in economic activity, such as people, goods and capital, would come to move actively, and economic growth and prosperity could be expected. More specifically, the expansion and smoother utilization of the regional production network that extends through East Asia would become possible as a result of forming a free and open single market, resulting in higher economic growth.

There is a view that an EAFTA or CEPEA that encompasses the East Asian countries can be founded by combining the existing ASEAN+1 FTAs. Theoretically this is not incorrect, but the contents of the ASEAN+1 FTAs are quite different for each FTA and so in reality it is not quite that easy. Furthermore, it is the delay in moving towards creating FTAs among the three countries of Japan, China and Korea that is hindering the founding of the EAFTA and CEPEA. Negotiations for a Japan–Korea FTA began in 2003, but were broken off in 2004 without coming to an agreement regarding the framework for negotiations. Japan wants to avoid market opening for its agricultural and fishery industries and Korea fears a negative effect on small and medium enterprises resulting from market opening in the area of manufactured products, and so between these countries opposing opinions over market opening are a barrier. Japan's industrial sector is extremely forward-looking regarding a Japan–China FTA but Japanese agriculture fears damage from market opening and is firm in its stance of opposition. Factors that make a Japan–South Korea and a Japan–China FTA difficult do not only include the economic factors mentioned above but also include problems of history and politics.

An idea of China-Japan-Korea (CJK) FTA was proposed informally by Chinese Premier Zhu Rongji at the leaders meeting in 2002. This proposal led to the initiation of a “private sector” study involving three countries. The study that began in 2003 continued until 2009 with a recommendation to begin a feasibility study involving government,

business, and academics. A joint research group of government, business, and academia was founded in 2010 by Japanese, Chinese and South Korean leaders to consider the feasibility of a trilateral FTA; and it produced a report in December 2011, indicating that the trilateral FTA would bring benefits to all three countries and recommending governments to decide on how to proceed with a possible trilateral FTA.

While East Asian countries became active in discussing the possible formation of region-wide FTAs, some economies/countries belonging to Asia-Pacific Economic Cooperation (APEC) began to discuss the formation of a region-wide FTA with high level of trade liberalization. At several APEC meetings in the 1990s, Australia, Chile, New Zealand, Singapore and the United States (P5) held informal discussions intended to discuss mechanisms for creating a new type of trade agreement among “like-minded” states⁸. Out of P5, Chile, Singapore and New Zealand, which shared very high enthusiasm for establishing a high-level FTA, launched the negotiations at the APEC Leaders' Summit in 2002. Brunei joined the negotiations in 2005⁹. P4, consisting of Chile, Singapore, New Zealand, and Brunei, was enacted in 2006.

It may be important to note that several attempts at trade liberalization under the APEC framework had been unsuccessful, leading to the formulation of P4. One is slow progress toward achieving the Bogor Goals of free trade and investment, and another is the failure of the Early Voluntary Sectoral Liberalization (EVSL). In Bogor in 1994 APEC Leaders committed to achieve free trade and investment by 2010 for industrialized economies and by 2020 for developing economies. APEC Leaders introduced the Osaka Action Agenda (OAA) in 1995 and the Manila Action Plan in 1996, in order to make progress toward the Bogor Goals, but the progress was disappointingly slow and small. The EVSL was an initiative developed by the APEC trade ministers in 1997 to liberalize the selective sectors, which were agreed upon by the APEC members, as a way to pursue the OAA¹⁰. The EVSL was not implemented as Japan refused to liberalize forestry and fish products, food and oil seeds. It should be noted that slow progress on multilateral trade liberalization negotiations under the WTO and the increasing number of FTAs in many parts of the world were also factors leading to the formation of P4.

P4 is a comprehensive FTA covering broad range of issues including trade in goods and services, rules of origin, trade remedies, sanitary and phytosanitary (SPS)

⁸ Elms and Lim (2012). Elms and Lim provides a detailed discussions on the origin and evolution of the TPP.

⁹ New Zealand Ministry of Foreign Affairs <http://www.mfat.govt.nz/Trade-and-Economic-Relations/2-Trade-Relationships-and-Agreements/Trans-Pacific/2-P4.php>

¹⁰ See, Okamoto (2000), for the detailed account of the discussions regarding the EVSL.

measures, technical barriers to trade (TBT), competition policy, intellectual property, government procurement, economic cooperation, and dispute settlement¹¹. P4 is a high level FTA requiring the members to eliminate tariffs on basically all the products by 2015. The primary objective of P4 is the establishment of a business friendly environment under which free trade and investment are achieved with fair competition and effective protection and enforcement of intellectual property rights¹². Another important objective is to support the APEC process toward the goals of free and open trade and investment. In other words, the founding members hoped P4 to become a foundation for a larger trade agreement by accepting new members.

In March 2008, P4 members began negotiations on trade in financial services and investment, in order to broaden P4's issue coverage. Broadening the issue coverage to meet the demands/needs of the businesses was one of notable characteristics of P4, which is known as a living agreement. In September that year the United States, which was interested in liberalization of financial services and investment, made an announcement to seek to join the expanded P4 negotiations. The Obama Administration, which began in January 2009, decided to join the expanded P4 negotiations in November 2009. Australia, Peru, and Vietnam quickly joined the US in expressing the intention of joining the negotiations. During this period the P4 became the Trans-Pacific Partnership (TPP). It should be noted that the emergence of the discussions on the formulation of region-wide FTAs in East Asia, in the forms of ASEAN+3 and ASEAN+6 FTAs made the US interested in TPP, which encompasses the countries in both sides of the Pacific, in order not to be kept out from East Asia.

Before closing this section on the discussion of region-wide FTA developments in 2000s, it should be noted that the US proposed a Free Trade Area of Asia-Pacific (FTAAP), which includes all APEC member economies, in 2006. An idea of an FTAAP was first presented by APEC Business Advisory Council (ABAC), representing business community, in 2005. This idea was taken up by the US government, which thought FTAAP would play an important role for the US businesses to maintain access to a fast growing East Asian market. At the APEC summit meeting that was held in Yokohama in 2010, an FTAAP was considered a primary means for regional economic integration in the Asia-Pacific, and EAFTA, CEPEA and the Trans-Pacific Strategic Economic Partnership (TPP) were considered the path to realizing FTAAP. China proposed a feasibility study for the realization of FTAAP at Beijing APEC in 2014. A feasibility study

¹¹ Trans-Pacific Strategic Economic Partnership Agreement

<http://www.mfat.govt.nz/downloads/trade-agreement/transpacific/main-agreement.pdf>

¹² *ibid.*

entitled “Collective Strategic Study on Issues Related to the Realization of the FTAAP” and headed jointly by China and the US was launched and the report was delivered at APEC Leaders’ meeting in Peru in 2016. Although a roadmap to the realization of the FTAAP was expected from the study, the report did not provide concrete plans to meet the expectation.

IV. 2010s: Negotiation of Mega FTAs: RCEP and TPP

Enlarged TPP negotiation with eight countries including Brunei, Chile, New Zealand, Singapore, Australia, Peru, the US, and Vietnam began in March 2010. After the negotiations began, four countries joined; Malaysia in October 2010, Canada and Mexico in 2012, and Japan in 2013. The fact that the number of negotiating countries increased during the negotiation process is quite unusual and it may reflect the importance of the TPP for many countries. TPP negotiations lasted for 5 years and 7 months before reaching an agreement in October 2015. The TPP agreement was signed by the TPP members in February 2016. The ratification process began after the signing. At the time of writing (May 2017), Japan and New Zealand ratified the TPP agreement. Enactment of the TPP is unlikely now that US President Donald Trump announced a withdrawal of the US from the TPP agreement. US ratification is a necessary condition for the enactment of the TPP treaty.

Turning to EAFTA and CEPEA, the government level discussions began in 2010, following the recommendations by feasibility studies. Discussions proceeded in parallel until 2011, when Japan and China jointly proposed the founding of a working group, in order to accelerate the formation of an EAFTA and CEPEA. This joint move by China and Japan, which were competing for a leadership role in the establishment of a region-wide FTA, resulted from a desire on the part of China to move forward an East Asian FTA, either EAFTA or CEPEA, in light of the fact that the TPP negotiations began to make progress.

While China and Japan were taking the lead in the formation of a region-wide FTA in East Asia, the ASEAN countries, which did not wish to deepen opposition by deciding an order of precedence, participated in both activities (EAFTA and CEPEA) with equal weight. But the joint proposal by China and Japan for accelerating EAFTA and CEPEA pushed the ASEAN countries, which feared losing a central role in the movement towards East Asian regional framework, to respond by proposing a Regional Comprehensive Economic Partnership (RCEP) in 2011. RCEP is a framework that does not specify membership such as ASEAN+3 or ASEAN+6, and that can be joined by East Asian countries that are prepared to sign an FTA with ASEAN. A statement was released

for launching RCEP negotiations at the ASEAN+6 summit meeting held in November 2012, and as a result, the movement towards founding an EAFTA and CEPEA were unified in RCEP. Negotiations did not begin until May 2013. It is argued that Japan's announcement about its participation in TPP negotiation in March 2013 pushed RCEP members, especially non-TPP members such as China, to begin negotiations. Indeed, it is interesting to note that the negotiations for CJK FTA and TTIP (Trans-Atlantic Trade and Investment Partnership involving the US and the EU) began in March and July 2013, respectively, possibly triggered by the intensification of TPP negotiations. This kind of chain-reaction or the Domino effect has been discerned concerning FTAs and such phenomenon is described as "competitive regionalism."¹³ RCEP negotiations missed the target for conclusion twice, December 2015 and December 2016. 18th round of negotiations finished in May 2017 and the prospects for reaching a conclusion by the end of 2017, another target, seem rather dim.

The remaining of this section provides a comparison of TPP and RCEP. The TPP text has been released and thus the contents are known. However, RCEP are still under negotiations, and thus discussions on the contents of RCEP, which are yet to be known, are bound to suffer from uncertainty. In the discussion on RCEP we rely on the limited information obtained from various sources including the official documents and press reports.

Let us compare TPP and RCEP in terms of their objectives, the contents and the quality of the agreements. The objectives of TPP and RCEP seem quite different. The objective of the TPP is to enhance trade and investment among the TPP partner countries, promote innovation, economic growth and development, and support the creation and retention of jobs¹⁴. These objectives are to be achieved by establishing a high-level, comprehensive, next generation trade agreement that liberalizes trade and investment and addresses new and traditional trade issues and 21st century challenges.¹⁵ It is further envisaged to become a model for other free trade agreements in the future.

The objective of RCEP is to achieve a modern, comprehensive, high-quality and mutually beneficial economic partnership agreement among the ASEAN Member States and ASEAN's FTA Partners, in order to support and contribute to economic integration,

¹³ Solis, et al (2009)

¹⁴ USTR website.

<http://www.ustr.gov/about-us/press-office/fact-sheets/2011/november/united-states-trans-pacific-partnership>

¹⁵ TPP Leaders' Statement on November 12, 2011. <http://www.ustr.gov/about-us/press-office/press-releases/2011/november/trans-pacific-partnership-leaders-statement>.

equitable economic development and strengthening economic cooperation among the participating countries.¹⁶

Although both TPP and RCEP are aimed to establish high-quality and comprehensive trade agreement, in order to promote economic growth and development, there are differences in their emphasis between economic growth and economic development. One of the most important elements for RCEP is to achieve equitable economic development through economic cooperation. By contrast, TPP does not put much emphasis on economic cooperation. It is only natural that RCEP puts an emphasis on economic cooperation as the RCEP members includes least-developed countries such as Cambodia, Lao PDR, and Myanmar, whose successful economic development is very important for region's sustainable economic growth and social stability.

The coverage of the issues for TPP and RCEP appears quite different. RCEP covers trade in goods, trade in services, investment, economic and technical cooperation, intellectual property, competition, dispute settlement and other issues, whereas TPP's coverage is broader and more comprehensive, including the following areas (Table 2): market access in industrial goods, agriculture, textiles, technical barriers to trade (TBT), sanitary and phytosanitary measures (SPS), rules of origin, customs cooperation, investment, services, financial services, telecommunications, E-commerce, business mobility, government procurement, competition, intellectual property, labor, environment, capacity building, trade remedies, and legal and institutional frameworks. In addition to these issue-specific areas, cross-cutting "horizontal issues" such as regulatory coherence, competitiveness, development, and small and medium enterprises are also addressed.

Having discussed the differences in the issue coverage between RCEP and TPP, the comparison made above is quite deceptive because the description of the issue coverage in RCEP (2012) is very rough and not detailed, compared to the case for TPP. If one considers the contents of the issue coverage of RCEP more in details, one realizes that the differences between the two are much less significant. Table 2 indicates that the major differences are environment, government procurement, labor, and cross-cutting horizontal issues such as regulatory coherence, which are covered in TPP but not in RCEP. Although these are only four issue areas out of many areas, these are regarded very important for developed countries such as the US, in order to achieve a level-playing field in competition and to achieve sustainable economic growth, while these issue areas pose

¹⁶ RCEP (2012) "Guiding Principles and Objectives for Negotiating the Regional Comprehensive Economic Partnership
<https://dfat.gov.au/trade/agreements/rcep/Documents/guiding-principles-rcep.pdf>

challenges to developing countries.

A closer look at the contents of TPP and RCEP revealed that the contents are similar with some important differences. What is likely to be quite different is the level of commitment or the quality of the contents of the agreements. One of the areas where the differences in the level of commitments are clearly seen is the level of trade liberalization, or market access in goods' trade. The TPP is seeking for complete elimination of tariffs, or 100 percent trade liberalization, although in reality trade liberalization rates (proportion of the number of tariff lines subject to tariff elimination in total number of tariff lines) for some members are lower than 100 percent because of political sensitivities concerning some products such as sugar for the US and the rice for Japan (Table 3). By contrast, the trade liberalization rate for RCEP is likely to be substantially lower compared to the case for TPP. Some observers predict 90 percent trade liberalization, considering the trade liberalization achieved by five ASEAN+1 FTAs. ASEAN countries achieved nearly 90 percent trade liberalization in each ASEAN+1 FTA (Table 1), while only 73.3 percent of tariff lines are commonly eliminated vis-à-vis their ASEAN+1 FTA partners. Considering that common tariff concessions are adopted in the RCEP negotiation, even achieving 90 percent trade liberalization requires significant efforts on the part of ASEAN members. Furthermore, it should be pointed out that India has the lowest trade liberalization rate at 78.8 percent in its FTA with ASEAN, indicating substantial difficulty in achieving 90 percent trade liberalization. If one considers that India is very much concerned with possible increase of imports from China, India is not likely to achieve the rate achieved in its FTA with ASEAN (78.8%). Non-ASEAN RCEP members also have to make enormous efforts in achieving 90 percent trade liberalization except for Australia and New Zealand, which have achieved 100 percent trade liberalization in their FTA with ASEAN.

Another major difference between TPP and RCEP is the treatment of the least-developed countries. ASEAN+6 trade ministers agreed to provide special and differential treatment to the least-developed ASEAN Member States in RCEP. Considering substantial differences in the levels of economic development of the RCEP negotiating members, this special and differential treatment is understandable and consistent with the arrangements adopted in ASEAN+1 FTAs. Specific examples of special and differential treatment of the least-developed ASEAN Member States in the ASEAN+1 FTA include the postponement of trade liberalization by new ASEAN members in ASEAN-China FTA. TPP does not provide special and differential treatment to the least-developed members in terms of the contents of the agreements, although it may provide different schedule for the implementation of the agreement to the least-developed countries.

Finally, it should be noted that the modes of agreement are likely to be different between TPP and RCEP. Despite very comprehensive contents as shown above, TPP members need to accept all of these contents/components from the outset in the form of single undertaking. Single undertaking has been a practice for the comprehensive FTAs involving the US. Contrary to TPP, RCEP is likely to adopt a gradual and sequential approach, where different components are negotiated and implemented under different time schedule, depending on the difficulty in reaching an agreement.

V. Changing Patterns of Intra-regional Trade in East Asia

We argued that East Asia has been witnessing the emergence of regional economic integration since the 1980s. We also argued that the characteristics of regional economic integration in East Asia changed from market-driven to institution-driven regional economic integration since the 1990s, particularly after the turn of the century. These discussions are presented without referring to the statistics. In this section we examine how trade patterns changed in East Asia. In particular, we are interested in the changes in the intra-regional trade patterns.

Figure 2 shows the changing patterns of intra-regional trade for ASEAN+3, ASEAN+6 and ASEAN member countries. Specifically, the share of intra-regional trade in region's overall trade (intra-regional trade share) is computed for the three groups of the countries. The figures for total goods show that ASEAN+6 has the highest share (35-45%), and ASEAN+3 has the second-highest share (30-40%), while ASEAN has the lowest share (20%). The intra-regional trade share for ASEAN+6 and ASEAN+3 rose notably from the mid-1980s through 2015 more or less steadily, while the intra-regional trade share for ASEAN stayed around the same level. These patterns reflect the fact that China's trade with East Asian countries including ASEAN countries increased significantly. More or less similar patterns may be found for intermediate goods and final goods for the three groups of countries, although the levels of intra-regional trade shares differ between them. Intra-regional trade share is higher for intermediate goods than final goods. This observation is attributable to the development of regional production networks, under which intermediate goods including parts and components are actively traded inside the East Asia region. A large increase in the intra-regional trade share observed for final goods for ASEAN+3 and ASEAN+6 appear to reflect the fact that the East Asian region has become a large market for final goods, thanks to rapid economic growth. In contrast to the cases of intermediate goods and final goods, the intra-regional trade share for primary goods declined for the three groups of the countries. This pattern may be explained by rapid industrialization of East Asian countries, resulting in a

reduction in the share of primary sector in their production structure.

We would like to find out if institution-driven regional economic integration contributed to a rise in intra-regional dependence. In order to examine the validity of this observation, we need rigorous statistical analysis, which we discuss later. Before we do so, let us see very roughly if the hypothesis may be supported by computing the trade intensity index, which measures the intensity of trade linkage between two countries/regions by taking into account of the magnitude of trade of the countries/regions. If the intensity is greater (smaller) than unity, then bilateral trade linkage is considered above (below) world average. Trade intensity index is regarded superior to intra-regional trade ratio in measuring the degree of bilateral trade linkage.

One could argue that institution-driven regional economic in the form of FTAs expanded intra-regional trade if the trade intensity index increased after the establishment of regional economic institution such as FTAs. With these observations in mind, let us see how the trade intensity index changed over time. One may detect a slight increase in the index for ASEAN from the early 1990s to mid-2000s, probably caused by the enactment of AFTA in 1993. The index for ASEAN+3 and ASEAN+6 declined over time, albeit a small decline. Although a number of bilateral FTAs involving East Asian countries have been established, there have not yet established ASEAN+3 or ASEAN+6 FTAs. ASEAN+1 FTAs began to be formed in the mid-2000s. Given these situations, it may not be surprising to observe a decline in the trade intensity index. Having made these observations, casual and visual observations are subject to inaccuracy. We need to conduct a rigorous statistical analysis in order to examine the impacts of FTAs on trade, to which we turn next.

There have been a large number of studies that examined the impacts of FTAs on trade by adopting statistical analysis. But studies on East Asian countries are rather few. One of them is Okabe and Urata (2014) that investigated the impacts of tariff reduction on intra-ASEAN trade. Their econometric analysis using trade data at product level revealed positive and statistically significant trade creation effects for a wide range of products. They also found that trade creation effects are smaller for new AFTA members compared to AFTA original members. They argue that the information about the merits of using AFTA may not have been spread to exporters in these countries. Studies on the impacts of ASEAN+1 FTAs on trade involving ASEAN+1 countries should be high on future research agenda.

VI. Concluding Remarks

Almost two decades have passed since the discussions on a region-wide FTA in

East Asia began. Substantial progress has been made, but a region-wide FTA has not yet been established. The TPP became very close to be enacted, but US withdrawal from the TPP has made it almost impossible for the TPP to be enacted. TPP countries without the US, or TPP11, are discussing the ways to form TPP11. Indeed, trade ministers from TPP11 countries agreed to conclude the talks by November this year.

As a result of the US withdrawal from the TPP, RCEP is receiving a lot of attention as an important region-wide FTA in East Asia. RCEP negotiations began in 2013 and after 4 years the negotiation team has not reached an agreement. Difficult issues have been identified and discussions on these issues appear to have reached a deadlock. One of the most difficult issues is the level of tariff elimination in the market access negotiations. Countries such as Australia and Japan demand high level of tariff elimination exceeding 90-95 percent, while countries such as India and China, particularly India, insist much lower level of tariff elimination. Possible conclusion may require either one of the following three options. One is to accept low level of tariff elimination. Another is to drop the countries that cannot accept high level of tariff elimination. The other alternative, which I think may be the best, is to set a high level target and allow countries to achieve the target with transition period, depending on the level of economic development.

In light of growing protectionism in the world, it is important for East Asia to fight against growing protectionism by concluding RCEP negotiations. Strong political will by the Leaders based on the understanding of the importance of RCEP for regional cooperation and economic growth is needed for the negotiations to reach an agreement. In order for the Leaders to commit to RCEP, they need strong support from business community and general public. Researchers and journalists, who have strong influence on the opinion of general public, need to provide evidence on the possible benefits of RCEP to the public.

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Table 1. Tariff Elimination Rates for ASEAN+1 FTAs

	ASEAN- ANZ	ASEAN- China	ASEAN- India	ASEAN- Japan	ASEAN- Korea	Average
Brunei	99.2	98.3	85.3	97.5	99.1	95.9
Cambodia	89.1	89.9	88.4	85.1	90.8	88.7
Indonesia	93.1	92.3	48.6	91.2	91.1	83.3
Lao PDR	91.8	97.4	80.1	86.3	90.0	89.1
Malaysia	97.3	92.6	79.7	93.9	92.4	91.2
Myanmar	88.1	93.6	76.6	84.9	91.6	86.9
Philippines	95.1	92.5	80.9	97.1	89.6	91.1
Singapore	100.0	100.0	100.0	100.0	100.0	100.0
Thailand	98.9	93.5	78.1	96.4	95.1	92.4
Vietnam	94.8	92.2	79.5	94.2	89.3	90.0
Australia	100.0					
China		94.7				
India			78.8			
Japan				91.9		
Korea					90.4	
New Zealand	100.0					
Average	95.6	94.3	79.6	92.6	92.7	90.9

Note: The share of tariff elimination in total # of imports, computed at HS 6-digit level

Source: Kuno et al (2015)

Table 2. Comparison of Issue Coverage for TPP and RCEP

	TPP	RCEP
Market Access for Goods	●	●
Rules of Origin and Origin Procedures	●	●
Textiles and Apparel	●	○
Customs Administration and Trade Facilitation	●	●
Trade Remedies	●	○
Sanitary and Phytosanitary Measures	●	○
Technical Barriers to Trade	●	○
Investment	●	●
Cross Border Trade in Services	●	●
Financial Services	●	○
Temporary Entry for Business Persons	●	
Telecommunications	●	○
Electronic Commerce	●	●
Government Procurement	●	
Competition Policy	●	●
State-Owned Enterprises and Designated Monopolies	●	
Intellectual Property	●	●
Labor	●	
Environment	●	
Cooperation and Capacity Building	●	●
Competitiveness and Business Facilitation	●	
Development	●	●
Small and Medium-Sized Enterprises	●	●
Regulatory Coherence	●	
Transparency and Anti-corruption	●	
Administrative and Institutional Provisions	●	
Dispute Settlement	●	●
Note: ● indicates the issue is covered, and ○ is likely to be covered.		
Sources: TPP are taken from the TPP text and RCEP are based on the information given by RCEP "Guiding Principle and Objectives for Negotiating RCEP" and other sources.		

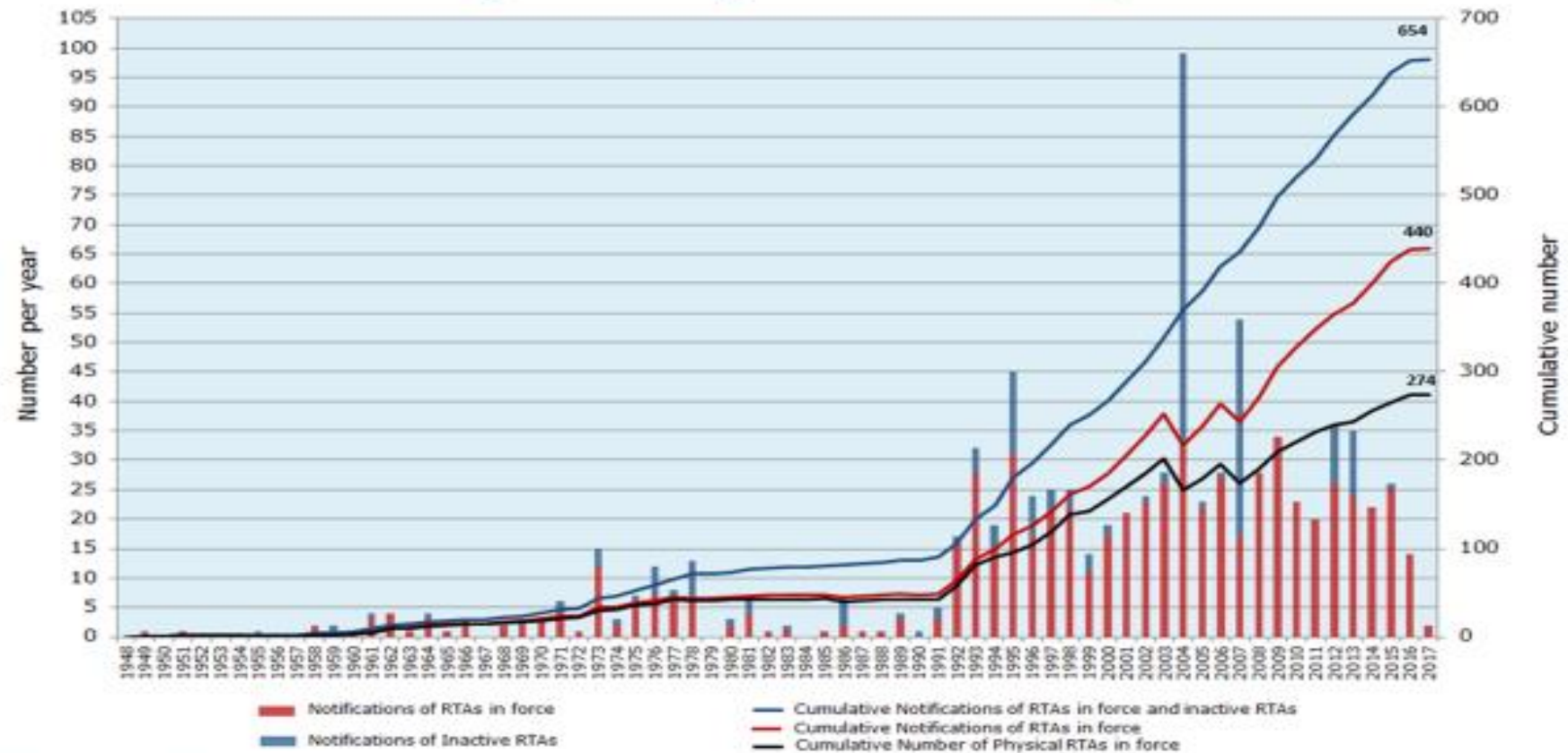
Table 3. Tariff Elimination Rates for TPP

	Actual Figures (2015)					TPP Commitments			
	Agricultural products		Manufactured products		Total	Agricultural products		Manufactured products	
	Final bound	MFN applied	Final bound	MFN applied	Eventual elimination	Immediate elimination	Eventual elimination	Immediate elimination	Eventual elimination
Australia	31.3	77.0	18.8	45.9	100	99.5	100	91.8	99.8
Brunei	0.0	98.5	0.0	78.5	100	98.6	100	70.2	96.4
Canada	46.0	59.6	25.8	78.5	99	86.2	94.1	96.9	100
Chile	0.0	0.0	0.0	0.3	100	96.3	99.5	94.7	100
Japan	34.1	36.5	55.9	55.7	95	51.3	81	95.3	100
Malaysia	12.9	75.0	5.0	64.1	100	96.7	99.6	78.8	100
Mexico	0.4	19.6	0.3	55.2	99	74.1	96.4	77	99.6
New Zealand	54.8	72.4	46.4	62.5	100	97.7	100	93.9	100
Peru	0.0	52.6	2.2	70.0	99	82.1	96	80.2	100
Singapore	4.1	99.8	17.0	100.0	100	100	100	100	100
United States	30.2	30.8	47.4	48.4	100	55.5	98.8	90.9	100
Viet Nam	8.7	15.5	15.0	38.8	100	42.6	99.4	70.2	100

Source: WTO Tariff Profiles, and Japanese Government, Cabinet Secretariat, TPP Section

Figure 1 RTAs in the World

Evolution of Regional Trade Agreements in the world, 1948-2017



Note: Notifications of RTAs: goods, services & accessions to an RTA are counted separately. Physical RTAs: goods, services & accessions to an RTA are counted together. The cumulative lines show the number of notifications/physical RTAs that were in force for a given year.
Source: RTA Section, WTO Secretariat, 5 May 2017.

Figure 2 Intra-regional Trade Shares

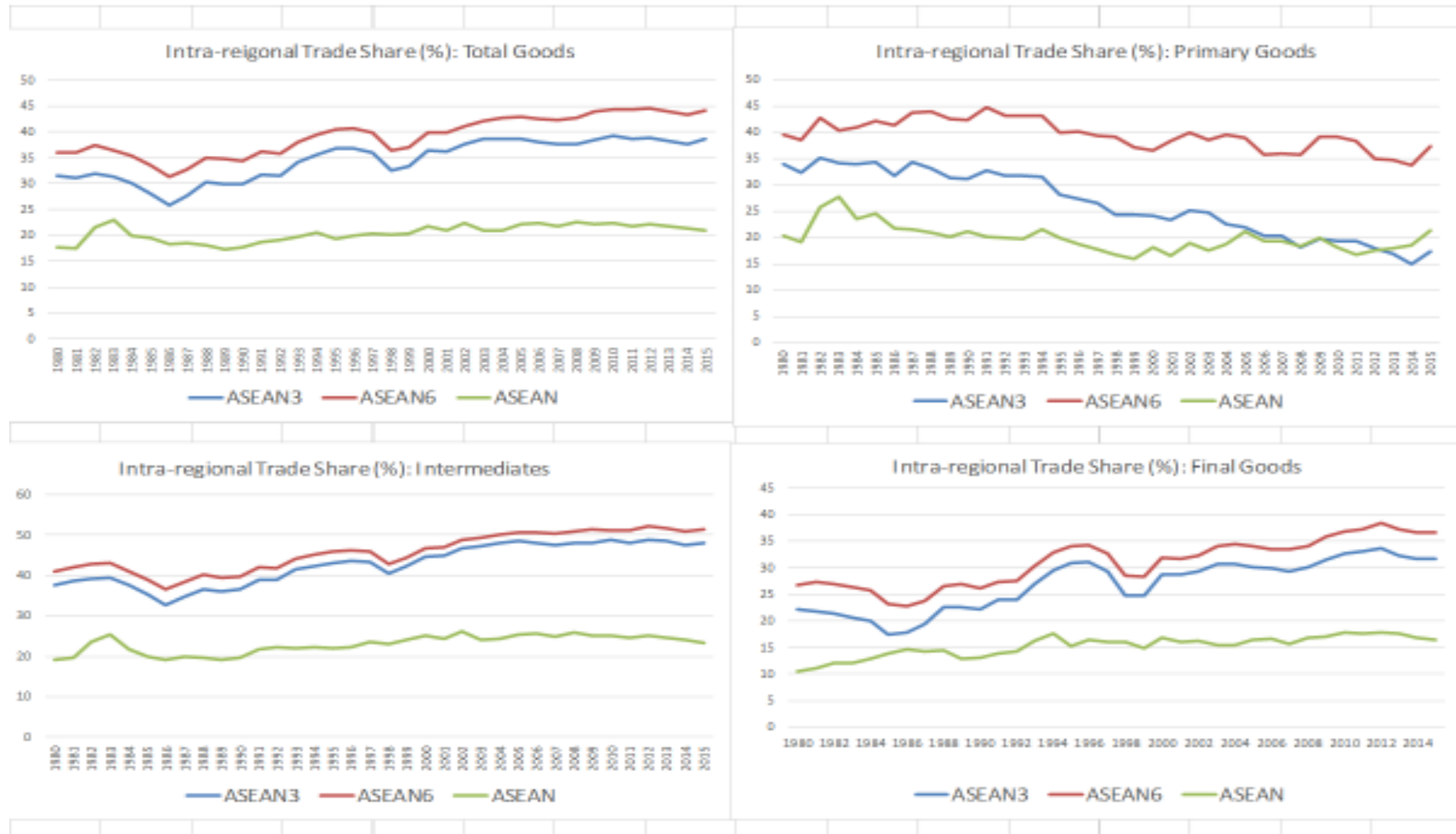


Figure 3 Trade Intensities

