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Session: Is an APEC FTA Feasible?

1.1.2

Relating it to an East Asian Summit FTA

Purpose: Information

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Relating FTA Asia Pacific to East Asia FTA

The *Free Trade Area of the Asia Pacific (FTAAP)* was proposed by APEC Business Advisory Council (ABAC)ⁱ and adopted by APEC Leaders meeting in Hanoi in November 2006, and its official study was agreed upon to launch throughout this year. A report by the PECC study groupⁱⁱ was attached to the ABAC proposal. Dr. Bergsten presented a strong case for *FTAAP* but Dr. Charles Morrison, President of PECC, summarized, based on cautious reservations made by other members, that it is politically difficult to achieve the *FTAAP* and recommended APEC to pursue a *Credible 2007 Trade Agenda* for the time being.

Six months have passed since then, during which major moves have been witnessed in the environment surrounding this issue. While I had taken a cautious stance closer to Morrison's on *FTAAP*, I dare to adjust it while facing these moves and suggest that we need to highlight the APEC's study of *FTAAP* as a *Plan B* in case for the failure of current WTO's DDA negotiation.

Three Major Moves

First is of course the current difficulty in concluding the DDA negotiation. It is still a fifty percent probability whether its major participants come to an overall agreement before summer this year. Its prospective achievement, even if concluded, is small in comparison with its initial agenda and we need to prepare a *Plan B* to support the multilateral trade regime under WTO.

Second is the moves within the United States. The current Trade Promotion Authority (TPA) expires on July 1st and its renewal is uncertain at the Congress under the Democrat majority. The expanding trade deficit, the US-China trade frictions, and increasing protectionism at home tend to make the United States inward-looking. The possible slow-down of the US economy will further accelerate this tendency.

Third is the continued spread of regionalism. We have witnessed such major examples as the expansion of the European Union to 27 member countries on January 1st, prospects for ASEAN integration and progress toward *East Asian FTA (EAFTA)* highlighted at Cebu Conference in the middle of January, and the conclusion of the Korea-US FTA negotiation announced in early April. The KORUS FTA was submitted to the Congress just in time for the deadline of 90 days before the expiry of the current TPA so that the fast track treatment is applied and likely to be approved.

These regional moves can be evaluated positively as an achievement of their own efforts for regional integration and liberalization. However, while the WTO's momentum and discipline are weakened, they may lead to the division of the world economy into three or more blocs, although nobody wishes it. *Plan B* is needed to prevent it and keep the WTO discipline.

Prospect for East Asian FTA

Unlike Bergsten, I do not perceive the increasing momentum in East Asia negatively. It has the following characteristics.

First, there underlie integration efforts by ASEAN. It started with ASEAN Free Trade Agreement (AFTA) in 1992 and has been strengthened step by step toward an integrated ASEAN market since the East Asian crisis in 1997-98. It finally reached the explicit agenda for ASEAN Community and adoption of ASEAN Charter at the Cebu conference.ⁱⁱⁱ

Second, the ASEAN integration was expanded to ASEAN + Three in the recovery process from the East Asian crisis. It started with currency and financial cooperation (Chiang Mai Initiative)^{iv} but extended to trade and investment liberalization in the form of ASEAN + 1 FTA in which China and Korea have already concluded an FTA with ASEAN respectively and Japan is now finalizing its negotiation for ASEAN-Japan EPA (Economic Partnership Agreement, covering services as well). *EFTA* is set as a long-term target along the extension of these ASEAN + 1. The China-Japan-Korea Summit also held at the time of the Cebu conference agreed to accelerate their negotiation of the trilateral Investment Treaty,^v which is an intermediate step to a trilateral FTA and paves a road toward *EFTA*.

Third, this East Asian group has to maintain its open trade and investment regime. Each relies heavily on trade with the US, EU, and Australia, and both ASEAN and China have developed their economies relying on foreign direct investment. A variety of integration measures by ASEAN are addressed to attract FDI and available to the American, European, and Australian firms. Although neither US nor Australia is included in *EFTA*, each can support own firms' participation in East Asian development through its bilateral FTAs (Australia with Singapore and Thailand, and the United States with Singapore and Korea).

Fourth, East Asia Summit (EAS) started in 2005 with India, Australia, and new Zealand as well as ASEAN + 3 to consult on a variety of new cooperation issues as anti-terrorism, recovery from natural disaster, prevention of epidemics, and environmental conservation in the region.^{vi} Each of the three is negotiating an ASEAN + 1 type FTA, on the base of which *EFTA* can be expanded to *EASFTA*.

China and Japan as well as ASEAN have committed to the East Asian integration and they will proceed along the line agreed at the Cebu conference (ASEAN taking initiative while China-Japan-Korea jointly supporting). By 2015-2020, they will reach the stage of liberalization at which they will be able to accept *FTAAP* easily.

Promoting *EFTA* and *FTAAP* in Parallel

However, if only regionalization continues its momentum, while the WTO regime weakened, the world economy will be divided into three blocs of EU, North America, and East Asia or more. Facing this reality, I share with Bergsten the need for *Plan B* to strengthen the WTO regime or create its substitute.

The best solution is, of course, to conclude the DDA negotiation even with its small package within this year and set the next round in order to continue strengthening the WTO regime. However, major participants have got tired of negotiation for the past five years and seem not to get enthusiastic about preparing for another round.

Morrison's *Credible 2007 Trade Agenda* aims to achieve the Bogor target as close as possible while taking full advantage of the success of DDA. However, if DDA fails or is extended beyond 2008, there will be made little progress in liberalization toward the Bogor target. I do not regard the APEC activities a total failure. Although APEC has lost its drive for liberalization handicapped by its modality of unilateral liberalization, it has made some steady progress in facilitation and capacity building in advance of WTO. APEC should continue its current agenda for Mid-Term Stock-Take in 2010^{vii}, which, however, will not contribute much to strengthening the WTO regime.

In this circumstance, APEC's official launch of the *FTAAP* study, together with its possible adoption of more binding liberalization modality, will achieve a certain impact on avoiding the possible division of the world economy. *FTAAP* has a clear and greater economic gains comparable with the DDA liberalization, even though we anticipate considerable political difficulty in achieving it. Within the framework of the *FTAAP* consultation, we can also

discuss how to resolve the cross-Pacific imbalances, how to prevent the aggravation of the US-China trade conflicts, and how to guide East Asian regionalism as open as possible. These issues can be taken up by APEC within the *Credible 2007 Trade Agenda* but they cannot provide a *Plan B* by itself. APEC will not be able to attract the US interest and prevent its protectionism at home, as it has not been for the past decade. East Asians prefer to discuss *FTAAP* only in the extension of *EAFTA* and reluctant to take up *FTAAP* now. However, facing the seriously weakened WTO discipline, we need to discuss *FTAAP* in parallel with *EAFTA*.

Finally, I would urge Japan to strengthen her efforts in this direction and support Australia promoting the *FTAAP* discussion. Japan has not made a visible contribution to the DDA negotiation. She has been delayed behind China and Korea in her FTA negotiation with ASEAN.^{viii} As regards FTA with Korea, Japan started her semi-official study with Korea as early as 1999^{ix} but has just been outstripped by the United States. All of these are often attributed to the political difficulty of dismantling her agricultural protection^x but more basically to the weak political leadership.

Japan succeeded the APEC host immediately after the Bogor declaration in 1994 and implemented the Osaka Action agenda with the unilateral liberalization modality. She has taken a strong initiative in promoting Mid-term Stock-take in order to achieve the Bogor target as close as possible. While learning from the past achievement of APEC, some Japanese realize the need for changing the APEC modality if it continues to be of some use. Japan should take more active initiative in both DDA and *FTAAP*. It will help strengthen its leadership in guiding toward *EAFTA*.

ⁱ ABAC, *Driving toward a prosperous and Harmonized APEC Community*, 2006, <http://www.abaconline.org>

ⁱⁱ PECC, *An APEC Trade Agenda? The Political Economy of a Free Trade Area of the Asia Pacific/ A Joint Study* by PECC and ABAC, <http://www.pecc.org/>

ⁱⁱⁱ Cebu Declaration for ASEAN Summit, www.aseansec.org. Chia and Scesastro reported concisely ASEAN's initiatives in promoting the ASEAN integration and extending it to ASEAN + Three and East Asia Summit.

^{iv} It consisted of the establishment of bilateral currency swap arrangement, joint surveillance of macro economic policies, and nurturing the Asia Bond market added at later stage. In early April 2007, ASEAN Finance Ministers agreed to pool a part of member countries' foreign exchange reserves, which will be further discussed at ASEAN + Three Finance Ministers meeting in May. If agreed, it will be a half-way to Asian Monetary Fund.

^v Joint Press Statement of the seventh Summit Meeting among China, Japan and Korea, www.mofa.jp

^{vi} Chair's Statement of the second East Asia Summit, www.apecsec.org.sg

^{vii} APEC Secretariat, *Bogor Goals Mid-term Stock-take: Project team Experts' Report*, www.apecsec.org and also The 18th APEC Ministerial Meeting Joint Statement, Nov. 2006, www.apecsec.org.sg

^{viii} It is partly because Japan negotiated bilateral EPA agreement with individual ASEAN members and have already concluded with Singapore, Philippines, and Malaysia and has just concluded one with Thailand in early April. Incidentally, I guided a joint Japan-ASEAN Think-tank study on ASEAN-Japan EPA at the JETRO/ Institute of Developing Economies (IDE), and stressed that an EPA with an integrated ASEAN would create a greater economic gain. ASEAN-Japan Research Institute Meeting, *ASEAN-Japan Comprehensive Economic Partnership: Vision and Tasks Ahead*, JETRO/IDE, July 2003

^{ix} I conducted a joint study of IDE and Korean Institute for International Economic Policy (KIEP) on the prospective gains from the Japan-Korea FTA in 1999-2000. It was followed by an official joint study and the inter-governmental negotiation started in 2003. The negotiation has been prolonged partly because of the resistance by fishing industry on the Japanese side but also because of the public resistance on Korean side. *Toward Closer Japan-Korea Economic relations in the 21st Century*, JETRO/IDE, May 2000

^x I produced a joint report with agricultural experts of five countries, China, Japan, Korea, New Zealand, and Thailand on a possible PECC package of agricultural negotiation in the DDA round in 2003 and suggested that Japan can offer much greater concession on agriculture than the current one. PECC Agricultural Trade Study Group, *WTO Agricultural Trade Negotiation: A Proposal for Progress*, PECC, Sep 2003

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**Relating FTA Asia Pacific to
East Asia FTA
by
Ippei Yamazawa**

**FTAAP was proposed by ABAC and
adopted by APEC Leaders’ meeting
and its official study launches this year**

- **PECC study summarized that it would
be politically difficult to implement**
- **and recommended APEC to pursue a
*Credible 2007 Trade Agenda***

But we need to highlight FTAAP, facing three major moves for the past six months

- **Current difficulty in concluding the DDA negotiation before Summer 2007.**

Its prospective achievement, even if concluded, is small

and we need to prepare a *Plan B* to support the multilateral trade regime under WTO.

- **Moves within the United States** The current TPA expires on July 1st and its renewal is uncertain. Expanding trade deficit, the US-China trade frictions, and increasing protectionism tend to make the US inward-looking.

- **Continued spread of regionalism** EU expanded to 27 members, ASEAN integration and progress to *EAFTA* highlighted at Cebu Conference, and Korea-US FTA negotiation announced.

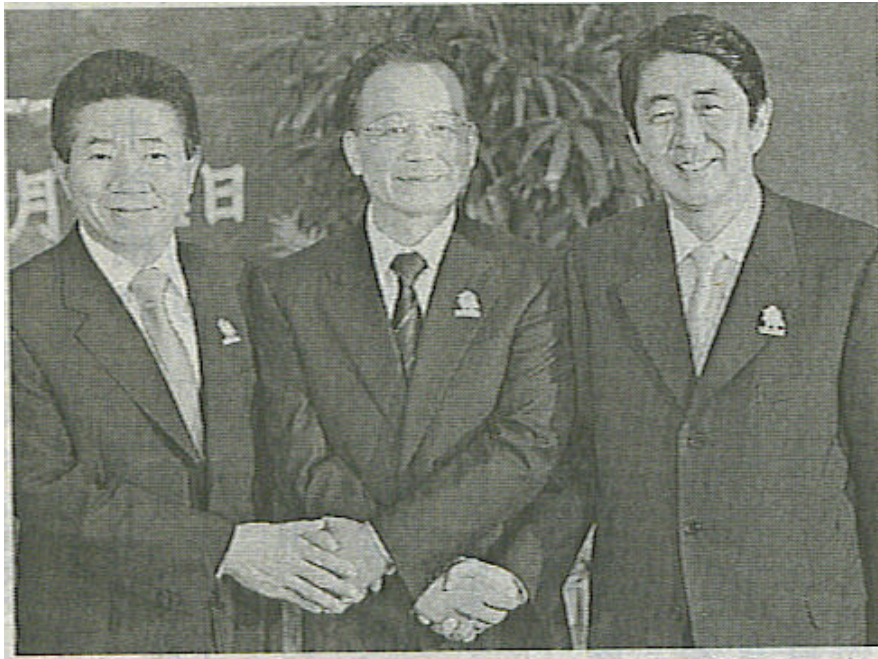


● **These regional moves can be evaluated positively as an achievement of their own efforts for regional integration and liberalization**

● **Facing weakened WTO's momentum and discipline, they may lead to the division of the world economy into three or more blocs**

Prospect for *East Asian FTA*

- First, there underlies **integration efforts by ASEAN**. It started with AFTA, strengthened toward integrated ASEAN market, finally reached explicit agenda for ASEAN Community and adoption of ASEAN Charter at Cebu Conf.
- Second, **it was expanded to ASEAN +3** in the recovery from the East Asian crisis: currency and financial cooperation to trade and investment liberalization in the form of ASEAN + 1 FTA. China-Japan-Korea Summit agreed to accelerate **trilateral Investment Treaty** negotiation, an intermediate step to trilateral FTA and paves a road toward *EFTA*



Prospect for *East Asian FTA* (contd)

- Third, **East Asian group has to maintain its open trade and investment regime**. Each relies heavily on trade with the US, EU, and Australia, and both ASEAN and China have developed relying on FDI. Both US and Australia can support their firms in East Asia through own bilateral FTAs (KOR-US, Aus-Thai)
- Fourth, **East Asia Summit** started in 2005 with India, Australia, and NZ as well as ASEAN + 3 to consult on a variety of new cooperation issues. Each is negotiating an ASEAN + 1 type FTA and *EAFTA* can be expanded to **EASFTA**

Prospect for *East Asian FTA* (contd)

- **China and Japan as well as ASEAN have committed to the East Asian integration and they will proceed along the line agreed at the Cebu conference** (ASEAN taking initiative while China-Japan-Korea jointly supporting).
- **By 2015-2020, they will reach the stage of liberalization at which they will be able to accept *FTAAP* easily**

Promoting *EAFTA* and *FTAAP* in Parallel

- If only regionalization continues its momentum, while the WTO regime weakened, **the world economy will be divided into three or more blocs**. Facing this reality, we need a Plan B.
- Best solution is to **conclude DDA negotiation** even with its small package within this year
- Morrison's *Credible 2007 Trade Agenda* aims to achieve the Bogor target as close as possible while taking full advantage of the success of DDA. If DDA fails or is extended beyond 2008, there will be made **little progress in liberalization toward the Bogor target**

Promoting *EAFTA* and *FTAAP* in Parallel (contd)

- In this circumstance, **APEC's official launch of the *FTAAP* study**, together with its possible adoption of more binding liberalization modality, **will achieve a certain impact** on avoiding the possible polarization of the world economy.
- *FTAAP* has a clear and greater economic gains comparable with the DDA liberalization, in spite of its political difficulty.

Promoting *EAFTA* and *FTAAP* in Parallel (contd)

- **Within the framework of the *FTAAP* consultation, we can also discuss how to resolve the cross-Pacific imbalances, how to prevent the aggravation of the US-China trade conflicts, and how to guide East Asian regionalism as open as possible.**
- **Facing the seriously weakened WTO discipline, we **need to discuss *FTAAP* in parallel with *EAFTA*.****