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The Politics of Trade Liberalisation

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Is an Asia Pacific Free Trade Agreement Politically Feasible?

Is an FTAAP Feasible?

An APEC Preferential Trade Agreement, which I will call the FTAAP, has been one part of the discussion of Asia Pacific cooperation at least since the first Pacific Trade and Development Conference in Honolulu in 1968. It was rejected then as being neither feasible nor desirable. There has been active discussion of an FTAAP several times since, with the same outcome: at the first Pacific Community Seminar in Canberra in 1979, that led to the Pacific Economic Cooperation Council and eventually to APEC; in the late 1980s as disillusionment with progress in the Uruguay Round generated a search for ambitious alternatives; and in the mid-1990s, as the establishment and early operation of the North American Free Trade Agreement (NAFTA) created anxieties in other trading partners of the United States and encouraged supporters of preferential trade that the times were right for a large preferential trading area in this region.

The FTAAP has emerged at this time as a focus of discussion for two inter-connected reasons. The first is the proliferation of bilateral preferential trading arrangements in the Asia Pacific region in the early years of this century and the realisation that they are raising transactions costs and threatening to distort the deepening integration into the global economy that has been a feature of the restoration of sustained rapid growth after the Asian financial crisis. The second is realisation that the open multilateral trading system is at a point of crisis, with the stalling and lowering of ambitions for the Doha Round of multilateral trade negotiations.

What were the grounds for past rejection of an FTAAP? If these reasons were valid in the past, have circumstances changed sufficiently to now justify a serious attempt to establish an FTAAP?

This presentation briefly addresses these questions. In the process, it must also consider whether an FTAAP is feasible; and if so, how it would now work in practice.

An Asia Pacific FTA was rejected in the 1960s and 1970s principally because it was seen as diverting the region from rapidly expanding and beneficent expansion of trade on a global basis, driven by comparative advantage and market opportunity. The cautions came most strongly from the United States, consistently with the strong commitment to multilateralism that had characterised that country's postwar international trade policies. By the 1980s, the United States commitment to multilateralism was more qualified, but there was considerable caution throughout the Asia Pacific community about dividing the community of market economies into blocs that discriminated against each other and against outsiders. In the Western Pacific, there was also concern that the introduction of trade discrimination, trade diversion and tit for tat exchange of decisions on liberalisation that would otherwise have been undertaken freely, would upset the rich process of unilateral trade liberalisation that was supporting rapid trade expansion and economic growth in every Western Pacific member of APEC, from China to New Zealand.

By the early 1990s, with negotiations on NAFTA moving forward, and the Uruguay Round of multilateral negotiations facing obstacles, there was more serious consideration of the FTAAP alternative. It was debated within the Eminent Persons Group established by APEC Heads of Government to advise on a path forward on APEC economic cooperation. The two reports of the Group, which recommended and discussed approaches to the goal of free and open trade and investment in the Asia Pacific region by 2010 (developed countries) and 2020 (developing countries) that was accepted by APEC Heads of Government at Bogor in 1994, contained contradictory messages on whether there was a place for an FTAAP.

One thread of argument, mainly favoured by Western Pacific APEC members, resisted discrimination against non-members, and saw free trade in the region emerging from continuation of the powerful momentum in unilateral liberalisation that was at that time well established in China, Vietnam, the Philippines, Indonesia, Malaysia, Thailand, Australia, New Zealand and, with qualifications in relation to the important case of agriculture, in Taiwan, Korea and Japan. Western Pacific economies tended to see free trade within the Asia Pacific region emerging from continuation of the open regionalism which would also deliver free and open trade with the world as a whole. The proponents of open regionalism saw close affinity between concerted unilateral liberalisation and active support for liberalisation within multilateral negotiations under the auspices of the GATT (and from 1995 the WTO). It was recognised that some of the hard knots of protectionism, for example in relation to agricultural subsidies as well as market access, could only be unwound in global negotiations. There was concern that pursuit of an FTAAP would weaken the multilateral system and the increasingly important ties with neighbouring non-APEC countries, including India after the historic initiation of outward-looking reform in 1991, and the successor states to the former Soviet Union. There was recognition that not all members of APEC would be able to extend to all others clean market access in the context of a formal preferential area, opening the possibility of major trade discrimination by some APEC members against others. The North American commitment to specific reciprocity in trade liberalisation was recognised—the strong tendency to avoid reductions in protection unless there were explicit and comparable “concessions” from the partners which would benefit from one’s own liberalisation. Western Pacific policy-makers handled this by accepting that, at first, new policy progress towards free and open trade would come mainly in the Western Pacific—which was understood in the context of recognition that the United States in the important manufacturing sector was already a relatively open economy. It was hoped that the United States would participate in the later stages of liberalisation, perhaps in a WTO context.

Some North American APEC participants, on the other hand, favoured a conventional preferential trading area, by implication considering it to be both feasible and desirable. The case for an FTAAP runs as a contrasting although broken thread through parts of the Eminent Persons’ Group reports. The supporters of this approach, led by Fred Bergsten, saw virtue in formal negotiations, reciprocity and binding agreements within Article 24 of the GATT. Some countries may not be able to make the commitments that were necessary for an agreement to be acceptable under Article 24 of the GATT (a binding plan and schedule for movement towards free trade in substantially all products within a defined short period). Discrimination against them would help them to make the necessary commitments in future. As for discrimination against non-APEC members, that would heighten their interest in multilateral liberalisation within the GATT and WTO.

Over the next several years, open regionalism was accepted as the APEC approach to free and open trade and investment in the Asia Pacific region. For several years it was immensely productive, with the Bogor declaration providing support for major liberalising initiatives in three of what were then amongst the more protectionist APEC members, China, Indonesia and the Philippines, and assistance against backsliding after far-reaching reductions in protection in Australia and New Zealand. Open Regionalism within APEC also contributed a favourable context for completion of the Uruguay Round, early WTO sectoral agreements in telecommunications and financial services, liberalising commitments around the entry of China and Taiwan into the WTO, and the launch of the Doha Rounds in favourable circumstances at the Shanghai APEC Summit in 2001.

Has anything changed since the most recent discussion and rejection of an FTAAP?

The most important change in the early twenty first century—and it is of truly historic dimension—is the proliferation of bilateral preferential trade agreements and discussions. This is not the place either to list the changes nor to analyse the reasons for them.

The proliferation of preferential trade and its discussion has contributed to the loss of interest in unilateral liberalisation in the Western Pacific economies in which it had been well established. It has diverted political focus and administrative capacity from multilateral trade negotiations. For the proponents of preferential trade agreements, there has been, so far, only disappointment: preferential agreements have been partial, excluding industries and sectors with highest protection and opportunity for beneficial trade expansion; little trade creation; increasing awareness that trade diversion is diverting some trade and will increasingly divert trade from its most efficient paths; frustration with the high transactions costs associated with rules of origin and realisation that the rules are costly to meet, often prohibitively so, in all but the largest economies; awareness that the preferential agreements since NAFTA have mainly involved relatively unimportant bilateral trading relationships; and recognition that the current pattern of proliferation, rather than putting in place stepping stones towards genuine regional global free trade, is establishing political economy barriers to further liberalisation.

It is the proponents and not the sceptics on preferential trade who have led the re-examination of an FTAAP. But as a long-time sceptic, I do acknowledge that the case against a regional free trade agreement is not as strong as it was. The opportunity cost is no longer an expanding system of multilateral, liberal trade, but a spaghetti bowl of increasingly distorting arrangements. It is possible at once to abhor the new directions in Asia Pacific trade in the early twenty first century, and to hold the view that a comprehensive FTAAP, covering all sectors and industries, with uniform and liberal rules of origin along the lines of the ASEAN FTA or the old arrangements under the ANZCERTA, would be a step forward.

Let me say at once that I do not hold that view. I fear that if we were able to put in place such an FTA it would entrench mutual antipathy on trade and other trade relations between APEC members and other significant elements in the world trading system, including Europe, India, many Latin American countries. Maybe, as proponents of an FTAAP argue, this would propel the outsiders into more serious engagement in multilateral negotiations. But maybe not: would the new Asia Pacific political economy be conducive to recommitment to the multilateral enterprise?

But I do not want to linger in assessment of the relative merits of bilateral distortion and a clean regional free trade agreement.

The compelling point is that an FTAAP that embraces all APEC members; removes protection, including through subsidies, in all sectors; and which has uniform and liberal rules of origin, is not remotely feasible in any time frame that is relevant to the APEC Heads of Government meeting in Sydney later this year.

Does anyone think that, in the contemporary environment of trans-Pacific economic relations, the US Congress would be prepared to extend to China free access to its goods and services markets?

Why does anyone think that the removal of protection in agriculture would be easier in an APEC than a global context? Here the crucial barrier is United States politics (behind which agricultural protectionism in Japan, Taiwan and Korea would gather), and the absence of European liberalisation removes what would be potentially an important impetus to political progress in the US. And would the US modify its demands for (at least partly economically distorting) changes in intellectual property laws in the context of regional negotiations, in areas in which some other APEC members have shown no interest in movement?

On rules of origin, where the US has insisted on restrictive, product-by-product arrangement on the NAFTA model in all of its bilateral trade negotiations so far, does anyone think that ASEAN style open-ness would be acceptable?

The questions only need to be asked for even the enthusiasts for an FTAAP to realise that the road ahead would be costly in terms of political and administrative commitment, uncertain in outcome, and incomplete in the best possible circumstances. Incompleteness in membership, sectoral scope and quality of rules would carry large costs.

So why contemplate this difficult and doubtful road?

Far better to focus on the things that we know that APEC can do well. Sharing ideas and experiences about trade and other economic reform. Rebuilding support for multilateral and unilateral trade liberalisation. Cooperating on trade facilitation. And providing a constructive framework for consideration at the highest political levels of emerging issues in regional international economic relations.