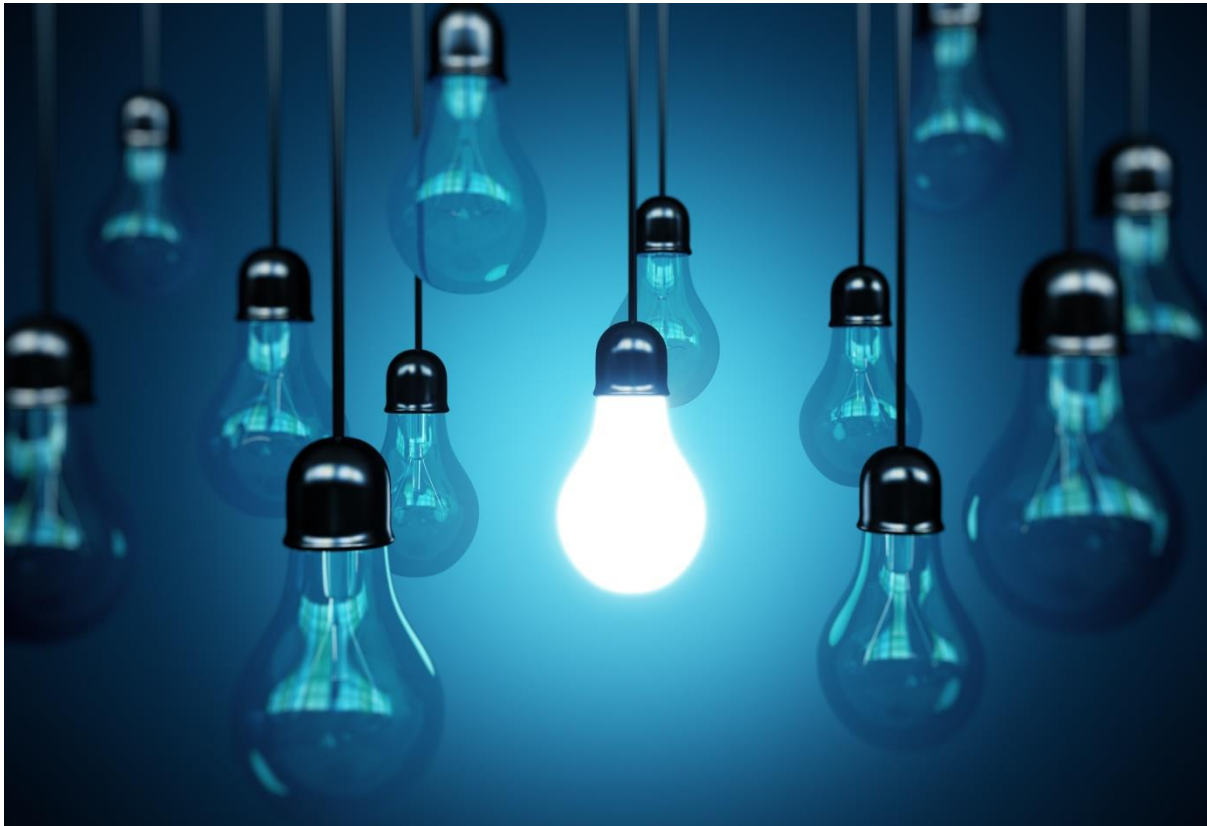




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# Trade in a turbulent time – towards a sustainable trade future<sup>1</sup>

By: [Kristen Bondiatti](#) – Program Director Trade Policy and Research, the Australian APEC Study Centre



At a turbulent time for trade, geopolitical tensions are driving policy fragmentation. Trade and investment patterns are shifting in response to economic changes. Supply chains are demanding more competitive services inputs.

Yet economic integration, not fragmentation, will continue to underpin future prosperity in the region.<sup>2</sup> Australia and New Zealand can build on their strong Trans-Tasman relationship to help make the case for economic openness and cooperation through thought leadership and policy innovation.



## Trade turbulence

### Policy fragmentation

Geopolitical tensions are creating serious challenges for trade and regional integration.<sup>34</sup> Governments, including the big traders, are now less in favour of economic integration. Domestic policies are increasingly focused on ‘reshoring’ and ‘friendshoring’ rather than on open markets.

Diverging frameworks are emerging. This is not new, but the differences in approaches among the major traders is becoming more marked. In the Asia Pacific region there is now the Comprehensive Progressive Partnership for the Trans Pacific (CPTPP) (without the US and China) and the Regional Comprehensive Economic Partnership (RCEP) (without the US and India). The US is leading negotiations on the Indo Pacific Economic Framework (IPEF) (without China and ostensibly with India). Negotiations for further liberalisation and for an effective dispute-settlement in the World Trade Organisation (WTO) remain stalled. Divergence is greater in some areas more than others; for example, on the treatment of state owned enterprises, national security, environmental subsidies and digital trade.

Further, new issues are emerging that affect trade but which have no agreed rules-based policy frameworks to guide them. They include frameworks for climate transition, for regulation of the digital economy and for supporting more inclusive growth.

### Shifting trade and investment patterns

Trade and investment patterns are shifting in response to policy and economic changes. For example, as populations shrink in China and labour costs rise, production bases are shifting to other economies, especially those in South East Asia.

At the same time, companies are reassessing economic and geopolitical risks, hoping to build more efficient and resilient supply chains. Many are diversifying their sources of supply and their export markets to better integrate into evolving regional value-adding chains.

Southeast Asia has been a particular beneficiary of diversification, driven not only by geopolitical issues, but also the region’s lower costs, its growing manufacturing capabilities and advantages under regional trade agreements.<sup>5</sup> Boston Consulting Group predicts Southeast Asia will gain an estimated US\$1 trillion in new trade through 2031 due in large part to new commerce, not only with China, but with Japan, the US and the EU.<sup>6</sup>

### The rise of the services economy

Digitisation and advances in technology are driving changes in the trade landscape. Much of this activity is closely linked with services. Some commentators have pointed to a new era of trade, and overall growth, around services, as along with skills and digitisation they become important across all areas of economic activity.<sup>7</sup>



Services need to be competitive to provide the value-added in regional value chains. At the same time, to function, regional value chains require efficient services, and increasingly digitised services.<sup>8</sup> Export opportunities across all sectors are now increasingly linked to the availability and efficiency of services inputs.<sup>9</sup> For APEC economies in the OECD Trade in Value-Added data set, the average embodied services content in gross manufactures exports is now 45 percent, up from 41 percent a decade ago.<sup>10</sup>

However, services trade faces large barriers. Domestic regulatory impediments are estimated to account for more than 55 per cent of services trade costs, which are twice as high as the costs for manufactured goods trade.<sup>11</sup>

## Towards a sustainable trade future

### Build cooperative policy making

Addressing new trade issues and managing geopolitical challenges will require cooperative solutions. Collaborative policy making is needed to help reconcile diverging approaches and build trust. Australia and New Zealand can continue to work together and with other economies in the region to advance this.

There are existing structures through which to work, including free trade agreements (FTAs) and APEC, plus many bilateral arrangements with trading partners. The key is how to use them effectively. APEC is valuable as a non-binding forum in which to engage in multi-stakeholder regional dialogue. It allows for conversations across government, as well as with business and academia. This helps to build cooperative approaches to common interests over time. It contributes to better policy making.

Existing FTAs also provide platforms to consider new issues and to build cooperative approaches on trade. The task of upgrading and expanding them – including the ASEAN/Australia /New Zealand Free Trade Agreement (AANZFTA), the RCEP and the CPTPP – will require collective action.

### Engage in creative policy thinking

Current challenges demonstrate the need for better frameworks to help address the most pressing trade issues. This includes digital trade, trade and sustainability, energy transition and inclusion, as well as issues that are still in need of reform, such as services, subsidies and agricultural trade.

Solutions also demand greater policy creativity. Frameworks which best guide trade now can be built on the same foundational principles – open markets, strong collaboration and partnerships, innovation and growth – but they might not look exactly the same as agreements of the past. The Singapore-Australia Green Economy Agreement and the Digital Economic Partnership Agreement (involving New Zealand, Singapore and Chile) are examples of new approaches.



Frameworks can address trade and investment in a more holistic way. The issues governments are confronting are cross-cutting and do not always fit with the way trade policy makers see trade; that is, as trade in goods or trade in services. For example, solutions to grow the 'green economy' will require cross-fora collaboration to bring multidisciplinary expertise to bear. Access to competitively priced goods, efficient services, open data, and diverse skills will be needed to operationalise investments and drive innovation. They involve agencies of trade, transport, standards, customs, digital and finance.

### **Support capacity building**

Efforts should be made to continue to build capacity and strengthen people and business linkages. These suffered during the pandemic years. The people-to-people linkages that are developed from capacity-building activities help to build the cooperation and deep bonds on common interests, such as climate transition.

### **Seize the Trans-Tasman opportunity**

Australia and New Zealand can lead cooperative efforts, engage in policy innovation and support capacity building initiatives to advance trade frameworks that address current challenges and drive regional integration over the longer term. They already have a strong bilateral relationship, shared interests in rules-based trade plus existing frameworks on which to build.

First, both can lead by building on the Australia New Zealand Closer Economic Relations Trade Agreement (CER). The 40<sup>th</sup> anniversary of the agreement this year is an opportunity to advance cooperative and creative trade policy that supports a shared and open region. For example, the CER single economic market could be expanded to include frameworks on digital trade, digitisation of services, environmental goods and services, and agricultural and environmental subsidies. Other economies could be encouraged to join, or to adopt CER-style frameworks.

Second, Australia and New Zealand can work together and with their partners in ASEAN and the region to advance outcomes in economic cooperation programs in the AANZFTA, the RCEP and the CPTPP, to develop regional approaches that add value to existing rules-based frameworks. Services regulation and structural reform are areas where capacity building can help support the conditions necessary for future trade and growth.

And third, while these are challenging times in which to envision an ambitious step forward in economic integration, there is also merit in revisiting the concept of a Free Trade Area of the Asia Pacific (FTAAP) as an ultimate goal, at least to engage in collaborative dialogue and generate fresh ideas on what might be possible for a sustainable trade future in the region.

*Kristen Bondiotti serves on the Secretariat for the Australian arm of the Pacific Economic Cooperation Council (AusAPECC), which is currently undertaking a PECC sponsored project to explore possible pathways toward a Free Trade Area of the Asia Pacific "FTAAP Pathways to Prosperity".*



<sup>1</sup> This brief was initially prepared for the Auckland Trade and Economic Policy School 2023 "Trans-Tasman, Regional and Global Initiatives for Sustainable Trade Futures," University of Auckland Public Policy Institute, 23-24 February 2023.

<sup>2</sup> See <https://www.pecc.org/resources/regional-cooperation/2734-state-of-the-region-2022-2023/file>.  
<https://www.pecc.org/resources/regional-cooperation/2703-state-of-the-region-2021-2022/file>

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<sup>4</sup> This is integration in the sense of removing barriers to allow exchange between economies, to expand linkages and coordinate policies for common objectives, such as enhancing competitiveness, increasing trade, facilitating regional production networks, and augmenting FDI flows and associated value chains. It is essentially what the global trade architecture is set up to support. See Armstrong and Pangestu at <https://press-files.anu.edu.au/downloads/press/n4106/html/ch02.xhtml>

<sup>5</sup> ASEAN's trade with China grew by 28 per cent in 2021, making ASEAN collectively now China's largest trading partner.

Vietnam, Malaysia and Thailand are China's top three trading partners in ASEAN. See [http://bn.china-embassy.gov.cn/eng/zwx/202201/t20220129\\_10636735.htm](http://bn.china-embassy.gov.cn/eng/zwx/202201/t20220129_10636735.htm) ASEAN has also attracted large amounts of export-oriented foreign direct investment. According to UNCTAD, the stock of inbound FDI in the ASEAN countries reached US\$ 2.9 trillion in 2020, equivalent to 95% of the combined GDP of the ten member states. UNCTAD FDI data. See <https://www.hinrichfoundation.com/research/article/ftas/aseans-import-dependency-intra-asean-trade/>

<sup>5</sup> APEC PSU. Refer note 8.

<sup>6</sup> See <https://www.bcg.com/publications/2023/protectionism-pandemic-war-and-future-of-trade>

<sup>7</sup> See <https://www.csiro.au/en/news/news-releases/2022/seven-megatrends-that-will-shape-the-next-20-years>

<sup>8</sup> Digitisation has expanded services trade, not only in pure digital services but also in digitally enabled services across other areas of the economy. APEC PSU. Refer note 8.

<sup>9</sup> *APEC Policy Brief on EAASR and ASCR: Services Competitiveness and Structural Reform* APEC Economic Committee and Group of Services, December 2022 (APEC Report) [https://www.apec.org/docs/default-source/publications/2022/12/apec-policy-brief-on-eaasr-and-ascr-services-competitiveness-and-structural-reform/22\\_ec-gos\\_apec-policy-brief-on-eaasr-and-ascr.pdf?sfvrsn=5cdc0567\\_2](https://www.apec.org/docs/default-source/publications/2022/12/apec-policy-brief-on-eaasr-and-ascr-services-competitiveness-and-structural-reform/22_ec-gos_apec-policy-brief-on-eaasr-and-ascr.pdf?sfvrsn=5cdc0567_2)

<sup>10</sup> APEC Report note 8, using OECD TiVA database.

<sup>11</sup> See APEC report, note 8. Furthermore, The OECD STRI report for 2023 notes there was an increase in the volume of regulatory changes in services over 2022 compared to 2021. However, across all major services sectors the increase in trade restrictiveness was 5 times higher than the year before  
[https://issuu.com/oecd.publishing/docs/stri\\_policy\\_trends\\_up\\_to\\_2023\\_final](https://issuu.com/oecd.publishing/docs/stri_policy_trends_up_to_2023_final)