

China and the TPP: Rule Making and Trade Gains

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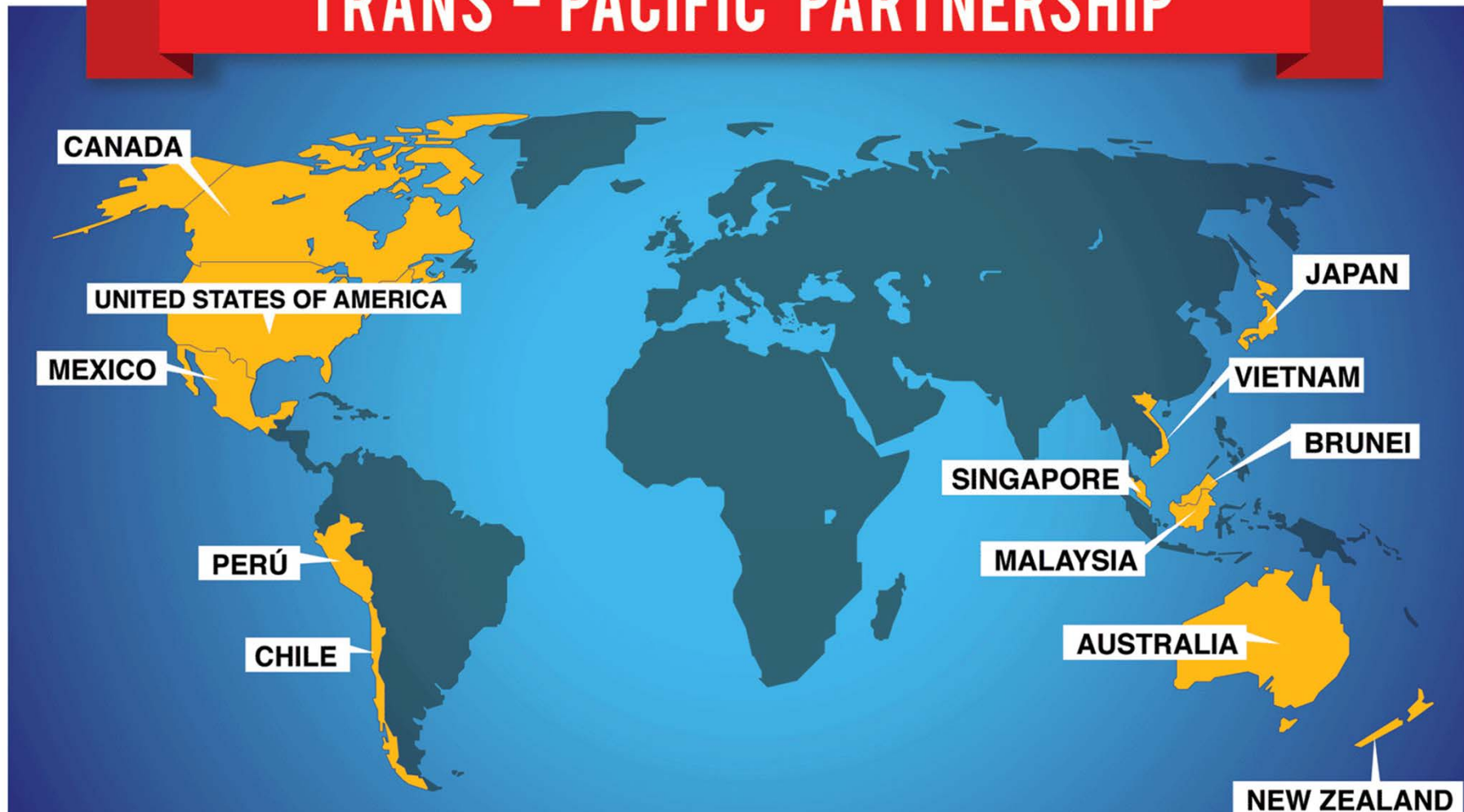
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What's the TPP?

TRANS - PACIFIC PARTNERSHIP



The emergence of mega-FTAs

- WTO multilateral trade agreement
- Bilateral and regional FTAs
- Mega-FTAs
 - TPP (Trans-Pacific Partnership)
 - TTIP (Transatlantic Trade and Investment Partnership)
 - RCEP (Regional Comprehensive Economic Partnership)
 - FTAAP (Free Trade Area of the Asia-Pacific)

TPP's three roles as a mega-FTA

- Strategic game-playing and rule-making platform
- Trade gains capturing and redistributing mechanism
- Driving force to reconstruct regional production networks

1. TPP AS A RULE-MAKING PLATFORM



TPP reveals the US' new trade and investment rules

- In recent years, the US has found that the trade and investment rules established since the 1950s can not fully support American firms to take their full advantages.
- The US needs new rules in order to promote the US economy and restrain competitors' advantages.

TPP Leaders' Report to APEC (Nov. 2011)

- Our negotiating teams have held nine rounds of negotiations and we are pleased to report that they have established the broad outlines of **a next-generation, transformative agreement that will further elevate our trade and investment relationships, create the foundation of a Free Trade Area of the Asia Pacific, and support jobs, economic growth, and higher living standards in our countries.** Negotiating an agreement of this scope and ambition is a complex and time-consuming exercise, but we are confident that the successful development of this framework will provide us the structure and momentum we need to successfully conclude this agreement. Below we detail the five features that will define **this historic agreement and set a new standard for trade agreements in the future.**
- In reporting to Leaders on the achievement of the broad outlines of an agreement, the Trade Ministers identified five defining features that will make TPP a **landmark, 21st-century trade agreement, setting a new standard for global trade and incorporating next-generation issues that will boost the competitiveness of TPP countries in the global economy.**

The US advantages and TPP rule making

- US advantages mainly focus on the field of knowledge creation. In order to bring these advantages into full play, the US tries to:
 - strengthen the protection of intellectual property (TPP chapter 18);
 - promote 100% market access of trade in services, particularly the financial sector and professional sectors (TPP chapters 10–14);
 - reduce investment restrictions (TPP chapter 9).

As a trade-off, the US also sets 100% zero-tariff as one of the goals in negotiation

- According to the TPP tariff reduction schedules, the zero-rated tariff lines will account for 90.52% of the total in the first year after TPP implementation, and will increase to 94.29% in the sixth year, and 96.13% in the eleventh year, respectively.

Table 2 The number of US non-zero tariff lines after TPP implementation

Year	Australia	Brunei	Canada	Chile	Japan	Malaysia	Mexico	Peru	Singapore	New Zealand	Vietnam
1	675	922	572	445	1593	1016	693	918	403	1225	2145
2	675	922	572	445	1593	1016	693	918	403	1225	2145
3	675	922	572	445	1593	1016	693	918	403	1225	2145
4	675	922	572	445	1593	1016	693	918	403	1224	1526
5	675	922	572	445	1593	1016	693	918	403	1224	1418
6	562	529	458	332	1041	587	357	802	290	764	674
7	562	529	458	332	1039	587	357	595	290	758	669
8	562	526	458	332	1036	584	357	592	290	755	664
9	562	526	458	332	1036	584	357	592	290	732	664
10	562	526	458	332	1036	584	357	592	290	732	664
11	562	302	448	313	471	315	290	589	290	407	344

Sources: Calculated according to TPP tariff reduction schedule at the 8-digit HS code level.

The US disadvantages and TPP rule making

- Different from the US, the emerging economies mainly have the advantages of low-cost labour, weak environmental regulations, and government support.
- Accordingly, TPP lays down
 - Labour standard (TPP chapter 19)
 - Environmental requirements (TPP chapter 20)
 - Rules on government support
 - Negative list (TPP chapters 9–10)
 - Transparency and anti-corruption (TPP chapter 26)
 - Government procurement (TPP chapter 15)
 - Competition (TPP chapter 16)
 - State owned enterprises clauses (TPP chapter 17)

- It's not a true or false question. It's just a strategic game-playing and all participants seek their own interests. Therefore, from China's standpoint, to some extent, TPP is almost a “trap” at least for now.

TPP is the newest attempt at a sequential negotiation policy by the US

- “Sequential negotiation” means the US tries to transform the FTA/RTA’s rules into multilateral trade and investment rules, by forming trade blocs to strengthen the bargaining power in order to achieve the lead role in the rule-making for the world economy (Li, 2003).
- The new rules introduced by mega-FTAs are likely to be the new issues for future negotiation in the WTO. Even if TPP rules cannot appear in WTO negotiations, the US will probably bring them into plurilateral agreements such as the Trade in Services Agreement (TiSA) (Shen, 2014).

The ways to ensure US leadership in rule-making

- The TPP negotiating parties were chosen carefully in order to take advantage of US' predominant influence.
- TPP closed-door negotiation is conducive to not only eliminating possible effects from outside, but also reinforcing US leadership in rule making.
- TPP is not the final goal for the US, because only if the TPP rules become the rules accepted across the world will US interests be ensured for the future.

The effects of TPP rules are already apparent

- Most FTA/RTAs under negotiation or reached recently in the Asia-Pacific region declared that they take high-level market access and high-standard trade and investment rules as their main goals.
- The basic principles advocated in the TPP have already become the example for future FTA negotiations, at least for the FTAs between China and developed economies.
 - China-South Korea FTA
 - China-Australia FTA
 - FTA among China, Japan, and South Korea
 - The upgrading FTA between China and New Zealand
- To some extent then, it is true that even though the US has decided to quit TPP the rule-making goal of the TPP has already been partly achieved.

2. TPP AS A TRADE GAINS CAPTURING AND REDISTRIBUTING MECHANISM



TPP helps to tap the foreign market

- The TPP can help US firms tap the other 11 TPP countries' commodity goods market as well as service market, especially the countries without bilateral FTAs with the US, such as Japan, Vietnam, Malaysia and so on.



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TPP also redistributes the trade interests within economies

- Theoretically, foreign trade and cross-border capital movements can affect domestic industries or sectors differently.
- Some sectors gain while some make losses. This is also true for the TPP.

3. TPP AS A DRIVING FORCE TO RECONSTRUCT REGIONAL PRODUCTION NETWORKS



Rules of origin as barriers to non-TPP countries

- To non-TPP countries, the accumulating rules of origin make it much more difficult to tap TPP countries' markets.
- It will enlarge the trade and investment diversion effect by inducing multinationals to reconstruct their production network across the Asia-Pacific region and lead to the shift of jobs from outside TPP to inside.

The impacts of TPP on the regional production network

- Part of a multinationals' production will shift into the TPP region.
- Part of new plants will gather within the TPP region.
- Assembling and manufacturing production shifts will be accelerated from non-TPP economies (e.g. China) to TPP members which have supportive business environments such as Vietnam and Malaysia.

The future pattern of Asian-pacific regional production network

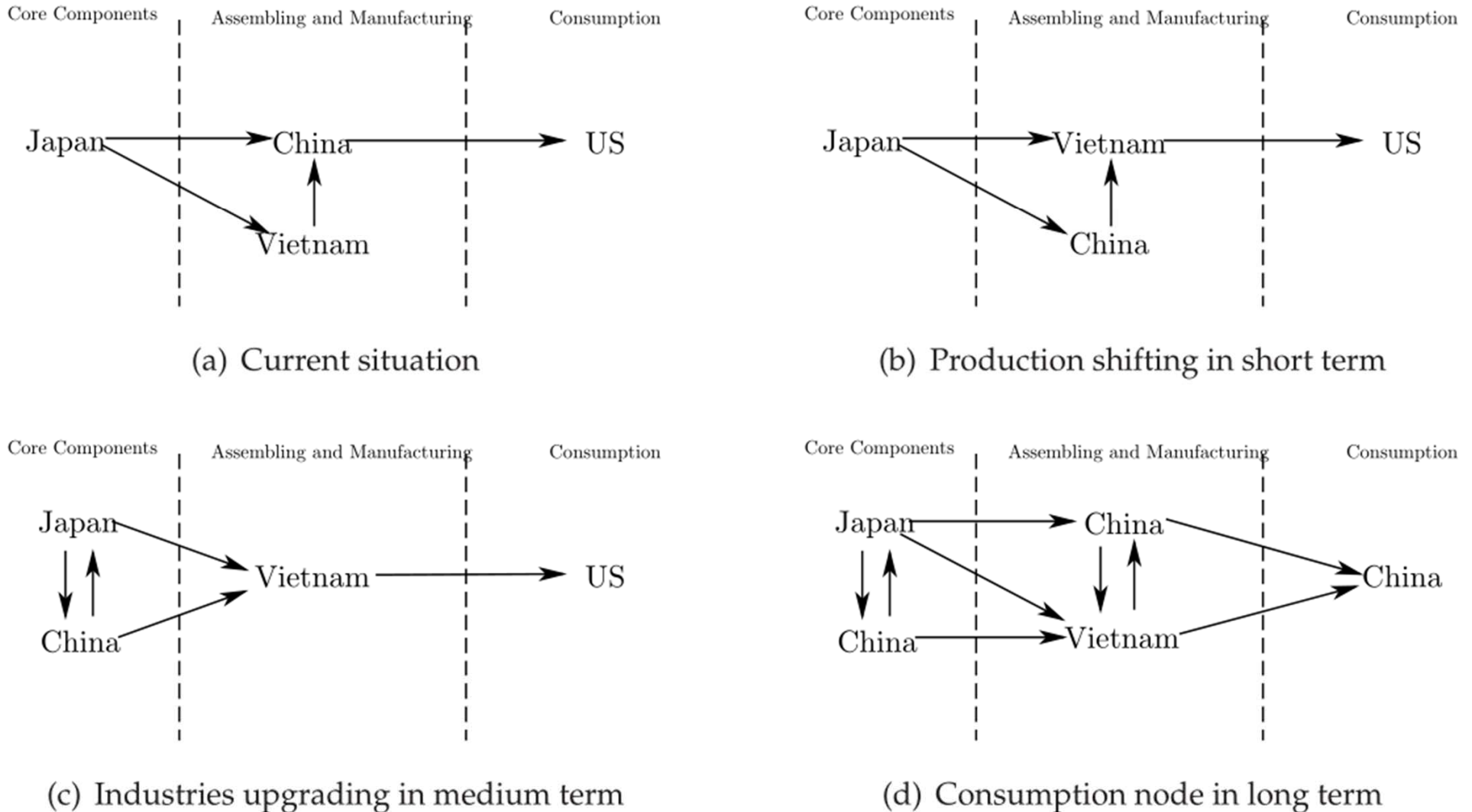


Figure 1 Current situation and development trends of Asian-pacific regional production network

4. TPP AND CHINA'S CHOICES



China's choice based on the decision index

- In order to find China's optimal choice allowing for the economic, political, and rule-making factors, we calculate the composite decision index by using principal component analysis, based on the TPP simulation data from GTAP model (Hertel, 1997).

Table 5 The simulation result of China's participation into Asian-pacific regional economic integration

No.	Scenario	Economic Impact					Rule-Making Impact	Political Impact	
		Welfare Change (Million USD)	GDP Growth Rate Change (%)	Terms of Trade Change (%)	Trade Balance Change (Million USD)	Export Change (%)			Import Change (%)
1	TPP	-3137.84	-0.24	-0.16	-559.58	-0.27	-0.29	0	-2
2	RCEP	12932.61	0.25	-0.32	-4592.34	4.90	6.71	-2	5
3	CJKFTA	9811.73	0.04	-0.38	-3007.07	3.62	4.91	-2	4
4	TPP + RCEP + CJKFTA	11004.63	0.10	-0.41	-4968.87	4.74	6.54	-2	2
5	TPP with China	58494.18	1.67	0.15	7103.44	6.14	7.10	-5	0
6	TPP with China + RCEP + CJKFTA	60534.99	1.85	0.16	5803.92	7.85	9.41	-5	1
7	FTAAP	54248.93	1.46	-0.33	1956.34	8.34	10.42	-3	5

Sources: The economic impact index is derived from GTAP modeling with the shock of 100% market access. The rule-making index and political index are based on scoring by the author.

China's choice based on decision index

Table 6 The composite decision index

No.	Scenario	Economic Impact Index	Rule-Making Impact Index	Political Impact Index	Composite Decision Index
6	TPP with China + RCEP + CJKFTA	0.922	-5	1	1.296
5	TPP with China	0.770	-5	0	1.178
7	FTAAP	0.507	-3	5	0.470
2	RCEP	-0.385	-2	5	-0.452
4	TPP + RCEP + CJKFTA	-0.491	-2	2	-0.555
3	CJKFTA	-0.532	-2	4	-0.566
1	TPP	-0.792	0	-2	-1.371

Sources: The economic impact index is derived from GTAP modeling with the shock of 100% market access. The rule-making index and political index are based on scoring by the author.

Some TPP rules meet the needs of Chinese firm's foreign trade and “going global”

- China is not only a great market but also a major exporter and investor in the world. Some TPP rules can help Chinese firms exploit foreign markets, such as environmental protection, e-commerce, and intellectual property.
- In fact, China released “Some suggestions on accelerating the enforcement of FTA strategies” in December 2015. The suggestions point out clearly that China will speed up the progress of high-level FTA negotiations and the basic principles and development directions are similar to the TPP.
- In practice, China has completed the China-South Korea FTA and the China-Australia FTA as trials of high-level FTAs.

China will not accept the entirety of TPP rules directly

- At least for now, it is difficult for China to do it, because the internal adjustments need more time especially in service trade sectors such as the financial sector and the telecommunication sector.
- Although some scholars believe that participation in the TPP will trigger another round of “domestic reforms impelled by open policy”, this does not only need leadership and considerable political courage, but also the appropriate opportunities.

China also has her own interests in rule-making

- In recent years, China has tried to strengthen its international discourse right in rule-making. Although China has not brought forward China rules yet, China also has her own interests.
- In fact, China would rather seek China-version rules than China rules, because China-version rules follow the common rules of today at first and then merge China's principles to them.

China's principles in the field of economic integration

- The principle of gradually opening
- The principle of mutual benefit
- The principle of cooperation and development
- The principle of trial first

China also faces the challenge of choosing between bilateral FTAs and regional FTAs

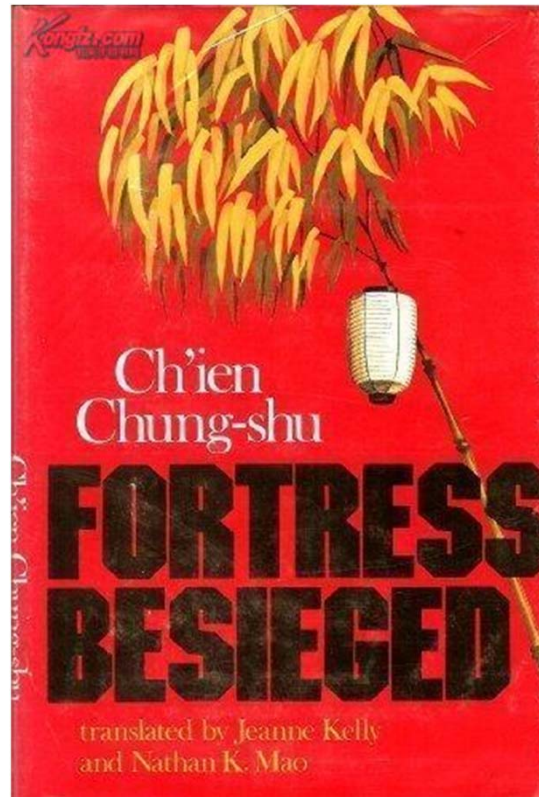
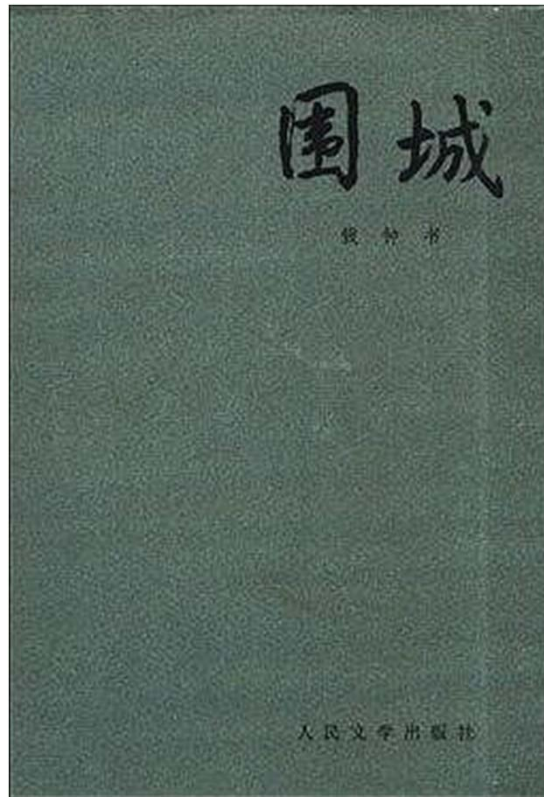
- For now, and different from the US, China chooses to work along both lines, not only trying to move forward the regional trade negotiations such as RCEP, CJKFTA, and even the future FTAAP, but also promoting bilateral FTAs.
- This can be regarded as an active policy response at a time when multilateral and regional trade agreements have become more and more difficult to achieve.

TPP and China's Choice

- From China's standpoint, TPP rules are not totally "bad". China also needs some part of them.
- China will likely mix up some TPP rules with China's own trade principles and therefore create a Chinese version of rules of trade and investment.
- Meanwhile, the US pulling out of the TPP weakens the strategic gaming platform of the TPP and makes it possible that the TPP will focus again on free trade. This is a substantial point for China to embrace part of the TPP.

Those who are outside want to get in, and those who are inside want to get out.

----*Fortress Besieged* by Ch'ien Chung-shu (Qian Zhongshu)



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Thank You!

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