Dhaka Roundtable on

Reviving the Multilateral Trading System: Post-Bali Issues

23 – 24 November 2014
The Westin Dhaka, Bangladesh

Session 4

Mega Trade-Blocs
Implications and Coping Strategies for the Excluded

The Challenge of Mega Trade Blocs
Is there a hope for the excluded?

Biswajit Dhar
Jawaharlal Nehru University, New Delhi

Centre for Policy Dialogue (CPD)

in collaboration with

South African Institute of International Affairs (SAIIA)

African Perspectives. Global Insights.

Draft: Not to be quated

The Challenge of Mega Trade Blocs: Is there a hope for the excluded?[#]

Biswajit Dhar[*]

After being upstaged by the bilateral free trade agreements (FTAs), regional trade agreements (RTAs) have made a strong comeback over the past few years. Until last year, the interest in RTAs was focused entirely on the Trans Pacific Partnership (TPP), the US-led initiative, which took over the P-4 (Chile, New Zealand, Singapore and Brunei) initiative to form an FTA in 2008. The TPP has often been described as the "gold standard" of trade deals, "that will open markets, set high-standard trade rules, and address 21st-century issues in the global economy".[1] The United States' negotiating objectives have been articulated thus: "TPP will be a comprehensive deal, providing new and meaningful market access for goods and services; strong and enforceable labor standards and environmental commitments; groundbreaking new rules designed to ensure fair competition between state-owned enterprises (SOEs) and private companies; commitments that will improve the transparency and consistency of the regulatory environment to make it easier for small- and medium-sized businesses to operate across the region; a robust intellectual property (IP) rights framework to promote innovation, while supporting access to innovative and generic medicines and an open Internet; and obligations that will promote a thriving digital economy, including new rules to ensure the free flow of data.".[2] Currently, 12 countries are negotiating the TPP. This RTA was originally expected to be operational by the end of 2013, but the regularity with which it has missed the subsequent deadlines has made many observers to comment that the negotiations may not be concluded even in 2015.

In 2013, two more RTAs were unveiled, namely, the Regional Comprehensive Economic Partnership (RCEP) and the Trans Atlantic Trade and Investment Partnership (TTIP). The latter though not a RTA in the strict sense of the term, being negotiated between the US and the EU, is de facto, a RTA. The RCEP, which brings together the ASEAN and its 6 FTA partners, is seeking to establish the "ASEAN centrality" through the consolidation of all ASEAN+1 FTAs. When they initiated the negotiations, the 16-member RCEP set the end of 2015 as the targeted date for

[#] Presented in the Roundtable on Reviewing the Multilateral Trading System: Post-Bali issues, Dhaka, 22-23 November 2014.

[*] Professor of Economics, Jawaharlal Nehru University, New Delhi (email: bisjit@gmail.com).

[1] Office of the United States Trade Representative (n.d.), Trans-Pacific Partnership: Summary of U.S. Objectives, available at: http://www.ustr.gov/tpp/Summary-of-US-objectives.

[2] Office of the United States Trade Representative (n.d.), Trans-Pacific Partnership: Summary of U.S. Objectives, available at: http://www.ustr.gov/tpp/Summary-of-US-objectives.

concluding their negotiations. This date coincides with the formation of the ASEAN Economic Community (AEC).

The TTIP was launched with the objective "to increase trade and investment between the EU and the US by realising the untapped potential of a truly transatlantic market place, generating new economic opportunities for the creation of jobs and growth through increased market access and greater regulatory compatibility and setting the path for global standards".[3] Clearly, setting global regulatory standards would be the key objective of the TTIP partners.

The Free Trade Area of Asia Pacific (FTAAP) is the latest initiative at forming a regional economic arrangement that was taken in the Beijing Summit of the Asia Pacific Economic Cooperation (APEC) in early November this year. This idea is not a new one, having being proposed for the first time in 1966 by the Japanese economist Kiyoshi Kojima. Although Kojima's proposal for establishing a Pacific Free Trade Agreement received little attention, this idea led to the formation of Pacific Trade and Development Conference and then the Pacific Economic Cooperation Council in 1980 and then APEC in 1989. Within the APEC, FTAAP was first proposed in the Hanoi Summit in 2006.

The "Pathways to FTAAP"[4], which provide the broad contours of this initiative, provide two clear guidelines: (i) FTAAP should do more than achieve liberalization in its narrow sense; it should be comprehensive, high quality and incorporate and address "next generation" trade and investment issues; and (ii) FTAAP should take into consideration the importance of advancing conventional "at the border" trade and investment issues, and at the same time more actively working toward addressing non-tariff or "behind the border" barriers and other "next generation" trade and investment issues to further deepen economic integration in the region.

These mega regionals are clearly setting new pathways of economic integration amongst the participating countries. Each of these initiatives is aimed at setting new standards for trans-boundary transactions, many of which would be well beyond the contours of the multilateral trade rules. These agreements have brought with them an entirely new set of challenges for the global trading system. With the participating members of the RTAs framing their own rules for economic engagement, the RTAs bring with them a plethora of challenges for the non-members. Moreover, since these initiatives are driven by a small subset of countries, there are

[3] Council of the European Union (2013), "Directives for the Negotiation on a Comprehensive Trade and Investment Agreement, called the Transatlantic Trade and Investment Partnership, between the European Union and the United States of America", p.4.

[4] APEC (2014), 2014 Leaders' Declaration: The 22nd APEC Economic Leaders' Declaration - Beijing Agenda for an Integrated, Innovative and Interconnected Asia-Pacific, Annex A, November, available at: http://www.apec.org/Meeting-Papers/Leaders-Declarations/2014/2014_aelm/2014_aelm_annexa.aspx.

implications for other members of the grouping as well. That arises here is the following: how does the global community cope with the challenges that these mega regionals have brought with them? Following from the aforementioned, it can be surmised that both members and non-members need to consider seriously the dimensions of exclusion that these arrangements could unleash, and would therefore need to adopt strategies to address this critical issue.

Regional Trade Agreements: Dimensions of Exclusion

Since they began to be established, discussions centring on RTAs have focused on whether the agreements have militated against the interests the non-members. More recently, however, the RTAs have developed the tendency to add another level of exclusion, and this involved the members of the RTAs themselves. This dimension has appeared as the new RTAs have moved well beyond their traditional framework of exchanging tariff preferences among the members and have focused not only on incorporating all or at least most of the important multilateral rules-making areas of the WTO, but more often than not, even going beyond them. These areas include: the standards (SPS/TBT), intellectual property rights, investment and government procurement.

If one were to reflect on dynamics of the negotiations of the RTAs, one would see that that there are actual or potential areas of differences in almost all of the areas referred to above. In the TPP negotiations, for instance, members are deeply divided over standards that this agreement must adopt for protecting intellectual property rights and foreign investment. Information obtained from the leaked negotiating texts, indeed show that considerable gaps exist between the countries pushing for TRIPS-plus standards and the others that do not want to go any further than the TRIPS standards. More recently, there are indications that the US and the other countries pushing for TRIPS-plus standards in the TPP negotiations, could settle for a compromise and would agree to differentiated application of intellectual property standards.

Setting of norms and standards has always been the most challenging area for the trade negotiators for they are confronted with two sets of arguments. Their natural instincts would push them towards harmonising the standards, for this approach would reduce transactions costs. Thus, when all countries adopt the same standards, authorities in different countries would not be called upon to conduct detailed exercises to test the quality of the products; a routine inspection would suffice. However, if harmonisation is to be effective, the chosen standards must be of the highest levels. This is what we have learnt from the experiences that we have gathered from different forums: the preferred standards are always close to the highest available.

This process, however, raises questions as to whether all the countries have the capacities /capabilities to conform to the agreed standards. There is also an added question as to whether the highest standard is the most effective in addressing a problem that it is seeking to address. In case of standards, there are several instances where high standards would only increase the cost of compliance, and that their contribution to safety would be marginal, if any[5]. This high cost of compliance and /or adaptation would create exclusions; many developing and least developed economies would find it difficult to comply with the new sets of standards that are being put in place.

In the trade context, issues of investment and intellectual property rights are closely intertwined. Advanced countries are using the mega-regionals that they are a part of to enhance the rights of the investors and intellectual property owners explicitly to increase the control over the market. Thus, when developing countries look for enhanced flows of investment, this is linked to the state of intellectual property protection. These countries are therefore encouraged to adopt the highest standards of intellectual property protection, the so-called TRIPS-plus standards. This demand for higher intellectual property ignores the fact that developing countries need flexibilities even within the TRIPS Agreement for addressing their critical needs of access to medicines, which was recognised through the Doha Declaration on TRIPS and Public Health[6]. Ratcheting up of intellectual property standards would make their impact felt on two counts. One, prices of medicines would be higher and as a consequence, patients in developing countries would be denied access to affordable medicines. And, two, the market for technology could become more constricted making it difficult for the small and medium enterprises (SMEs) to get access to the technologies they need to improve their competitiveness. The latter dimension could have a much wider impact: with the SMEs getting adversely affected, the formation of regional production networks, which has been seen as one of the major prospective gains from the formation of RTAs, could suffer a setback.

Investment agreements have generally adopted a template which provides high levels of protection to foreign investors and includes the investor-state dispute settlement (ISDS) mechanism that allows a foreign investor to litigate against its host government using private international arbitration mechanisms under the rules of the International Centre for Settlement

[5] See for instance, Meyer, Nico, Tamas Fenyes, Martin Breitenbach and Ernst Idsardi (2010), Bilateral and Regional Trade Agreements and Technical Barriers to Trade: An African Perspective, OECD Trade Policy Working Paper No. 96, available at: http://www.oecd.org/tad/45489713.pdf.

[6] WTO (2001), Declaration on the TRIPS Agreement and Public Health: Adopted on 14 November 2001, Ministerial Conference, Fourth Session, WT/MIN(01)/DEC/2, November.

of Investment Disputes (ICSID)[7] or United Nations Commission on International Trade Law (UNCITRAL)[8] rules. In recent years, the number of ISDS cases has increased substantially[9], a development that has made several governments to re-think about these investment agreements. South Africa and India are among the countries that are reviewing their bilateral investment treaties, while Indonesia has decided to let the agreements lapse when they come up for review[10].

The framework of economic integration agreements epitomised by the mega-regionals are, without doubt, driven by short-term sentiments. Taking cognisance of the development imperatives does not seem to be part of the DNA of these agreements. It is therefore important for the excluded to actively consider a path that does not follow the one traversed by the existing economic integration agreements, which have encouraged countries to trade on the basis of their initial comparative advantage, but have not provided the opportunities to participating countries to climb the development ladder and hence defy their comparative advantage[11]. While the development experiences of the present day advanced countries are rife with examples where countries have defied their comparative advantage over time, the FTAs have tended to deny a historical truism.

The way forward is to develop economic partnership agreements, which seek to realise the objectives that were emphasised in the Marrakesh Agreement Establishing the WTO[12]. One of the ways of achieving this objective would be to make the mega-regionals incorporate plans to improve the capacities of the participating countries so that they can be put on a level playing field. The elements of such a framework can be spelt out, for instance, in the context of RCEP. The development dimension of RCEP is an integral part of its negotiating agenda, but has not

[7] ICSID is an autonomous international institution established under the Convention on the Settlement of Investment Disputes between States and nationals and legal persons of other States. It is a multilateral treaty formulated by the Executive Directors of the World Bank, which came into force in 1966.

[8] UNCITRAL provides the rules for commercial arbitration, including investor-state dispute resolution. These rules were first adopted in 1976.

[9] In 2012 and 2013, the total number of disputes has been 58 and 57 respectively, the most recorded for two consecutive years. For details, see, the UNCTAD publication, "Recent Developments in Investor-State Dispute Settlement (ISDS)".

[10] Economist (2014), "Investor-state dispute settlement: The arbitration game", October 11, available at: http://www.economist.com/news/finance-and-economics/21623756-governments-are-souring-treaties-protect-foreign-investors-arbitration.

[11] See Ha-Joon Chang's arguments in Lin, Justin and Ha-Joon Chang (2009), "Should Industrial Policy in Developing Countries Conform to Comparative Advantage or Defy it? A Debate Between Justin Lin and Ha-Joon Chang", Development Policy Review, 27 (5): 483-502.

[12] GATT (1994), Agreement Establishing the World Trade Organization.

been focused in the discussions that have taken place around this economic formation well enough[13].

RCEP as a development partnership forum

The negotiating mandate of RCEP, which was elaborated in the "Guiding Principles and Objectives for Negotiating the RCEP" adopted by the Ministers of the proposed regional forum in August 2012, mentioned at least two features of the proposed agreement that make it quite different from the conventional FTAs. The first of these was that "RCEP will recognise ... interests of ASEAN's FTA Partners in supporting and contributing to economic integration, equitable economic development and strengthening economic cooperation among the participating countries". In other words, the economic development and cooperation were expected to be the building blocks of RCEP.

The second contrasting dimension was that RCEP negotiating mandate, includes economic and technical cooperation as one of its negotiating planks, which "will aim at narrowing development gaps among the parties and maximizing mutual benefits from the implementation of the ... agreement". The Guidelines further clarify that "economic and technical cooperation provisions in the RCEP will build upon existing economic cooperation arrangements between ASEAN and ASEAN's FTA partners participating in the RCEP".

It is important to note here that ASEAN members have viewed "technical and development cooperation" as a *sine qua non* for economic integration not only within their region, but between ASEAN and other parts of the world as well. This was highlighted in the Initiative for ASEAN Integration (IAI), launched in November 2000. The IAI stated that technical and development cooperation would "address the development divide and accelerate the economic integration of the less developed ASEAN Member Countries so that the benefits of ASEAN integration are shared and enjoyed by all ASEAN Member Countries". When it was launched, IAI identified the following as the priority areas, namely, infrastructure, human resource development, information and communications technologies, capacity building for regional economic integration, energy, investment climate, tourism, poverty reduction and improvement in the quality of life. RCEP members need to begin serious engagement at least on all these issues in order to give effect to the spirit of the negotiating mandate.

Over the past few years, a number of regional organizations have made sustained efforts to improve the connectivity within the East Asian Region, thus giving effect to these critical

[13] Andrew Elek makes some reference to this dimension. See Elek, Anrew (2014), "RCEP will help get Asian integration back on track", East Asia Forum, 7 June, available at: http://www.eastasiaforum.org/2014/06/07/rcep-will-help-get-asian-integration-back-on-track/.

"regional public goods". These efforts are intended to take full advantage of the "economics of neighbourhood", which can provide a strong impetus for regional integration. An ADB study conducted in 2012 has argued that the Asian economies can "unlock their vast economic potential, achieve sustained and inclusive rapid growth, and reduce poverty".[14] A more recent ADBI study has pointed out that "cooperation on infrastructure and trade facilitation (e.g., transport, customs clearance, and product standards) and services (e.g., financial services and labor services) would likely lead to a reduction in trade costs and result in welfare gains well in excess of gains from mere tariff liberalization".[15] In keeping with this understanding about the importance of connectivity, ADB is supporting a range of infrastructure projects in the East Asian region that can eventually result in the narrowing of the development gaps.

Effectively connecting the East Asian region is undeniably a critical factor for achieving objectives of the RCEP. Since the middle of the last decade, the East Asia Summit (EAS) process has been engaged in working out the details of the connectivity plan in the region. The most significant of these is the Comprehensive Asia Development Plan (CADP) aimed at improving connectivity within the East Asian region. CADP provided "a grand spatial design of economic infrastructure and industrial placement, and will claim to pursue both deepening economic integration and narrowing development gaps at the same time".[16] The infrastructure development plan spelt out in the CADP designed not only to support the production networks that already exist in the East Asian region, but, perhaps more importantly, to bring in countries and sub-regions, which did not figure in the networks very prominently. Prominent among that figure in the latter category are countries are the least developed countries in ASEAN, namely Lao PDR, Cambodia and Myanmar. Myanmar's opening to the outside world at the beginning of this decade has opened a plethora of possibilities of a better connectivity between India and ASEAN. It raised expectations of an early implementation of the Mekong India Economic Corridor, which proposes to connect "Ho Chi Minh City, Phnom Penh, Bangkok, and Dawei by road, and further to Chennai (Madras) in India by sea route".[17] The MIEC increased the prospects of India participating in a more holistic manner in the production networks that are already existing, or are expected to come up in the East Asian region.

[14] Bhattacharyay, Biswa Nath, Masahiro Kawai, Rajat M. Nag (2012), Infrastructure for Asian Connectivity, ADBI and Edward Elgar, UK, p. 2.

[15] Asian Development Bank Institute (2013), Connecting South Asia and Southeast Asia: interim report, ABD/ADBI, Tokyo, p. x.

[16] ERIA (2010), The Comprehensive Asia Development Plan, ERIA Research Project Report 2009-7-1, available at: http://www.eria.org/publications/research_project_reports/the-comprehensive-asia-development-plan.html, p. 1.

[17] ERIA (2010), The Comprehensive Asia Development Plan, ERIA Research Project Report 2009-7-1, available at: http://www.eria.org/publications/research_project_reports/the-comprehensive-asia-development-plan.html, p. 90.

Another significant initiative is the Trans Asian Railway Network, the UNESCAP idea that has, of late, received increased attention. The initiatives at developing hard infrastructure have to be coupled with the setting up of a digital platform, along the lines spelt out in the ASEAN ICT Masterplan 2015, which was adopted in 2012.

With these developments afoot, RCEP can provide the overall framework through which a strong and viable East Asian region can be developed. RCEP therefore needs to have two tracks: the first, a regional cooperation and development track and the second, a market integration track. The first track should tie-in all the initiatives of building regional infrastructure. This would enable the RCEP members to provide a coordinated approach to development of "regional public goods" like the infrastructure projects mentioned in the foregoing. Fast tracking the latter would merely enable the countries that are better prepared to benefit from the process, and this could exacerbate the existing inequities in the region. Since the RCEP is focusing on generating growth impulses through the regional production networks, the two-phased approach would enable the lagging countries equal opportunities to secure the more coveted slots in these networks.

These regional connectivity projects in East Asia would receive a significant boost with China proposing the so-called "Silk Road" initiatives, including the Silk Road Economic Belt and the 21st century Maritime Silk Road. Together with the formation of the Asian Infrastructure Investment Bank, an institution that has already received the support of India and the United States, the economic cooperation dimension can take-off quite smoothly.

Such an approach of twin-tracking trade integration and building of "regional public goods" should be ideally suited to the interests of all countries, which have been somewhat hesitant in pursuing the "liberalization alone" agenda that seem to have driven the bilateral and the regional trade integration processes thus far. These countries would clearly see a trade-off from which they could benefit – they would agree to trade liberalization since there is a possibility for them to improve their economic efficiencies and become more effective players in the integrated markets.