

From Spaghetti Bowl to Jigsaw Puzzle?

Addressing the Disarray in the World Trade System

Jayant Menon

Lead Economist (Trade and Regional Cooperation)
Office of Regional Economic Integration
Asian Development Bank
<jmenon@adb.org>

The views expressed in this presentation are those of the author and do not necessarily reflect the views and policies of the Asian Development Bank, or its Board of Governors or the governments they represent.

Outline

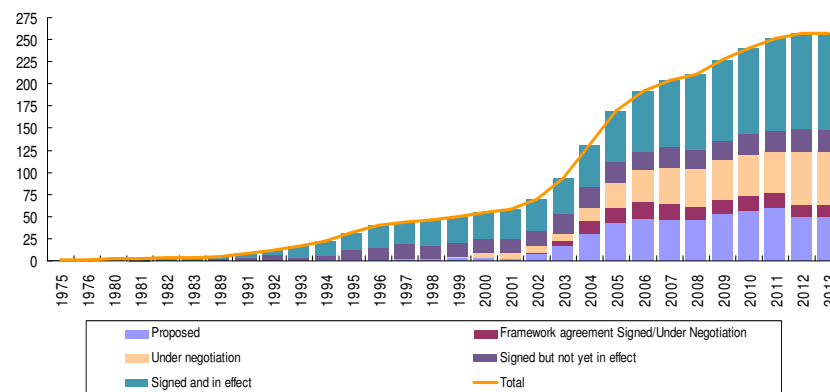
- State of Play- FTA proliferation
- Regional Puzzles- RCEP and TPP
- Global Puzzle
- The Way Forward
 - Tariff barriers
 - Non-Tariff Barriers

The views expressed in this presentation are the views of the author/s and do not necessarily reflect the views or policies of the Asian Development Bank, or its Board of Governors, or the governments they represent. ADB does not guarantee the accuracy of the data included in this presentation and accepts no responsibility for any consequence of their use. The countries listed in this presentation do not imply any view on ADB's part as to sovereignty or independent status or necessarily conform to ADB's terminology.

State of Play- FTAs proliferation

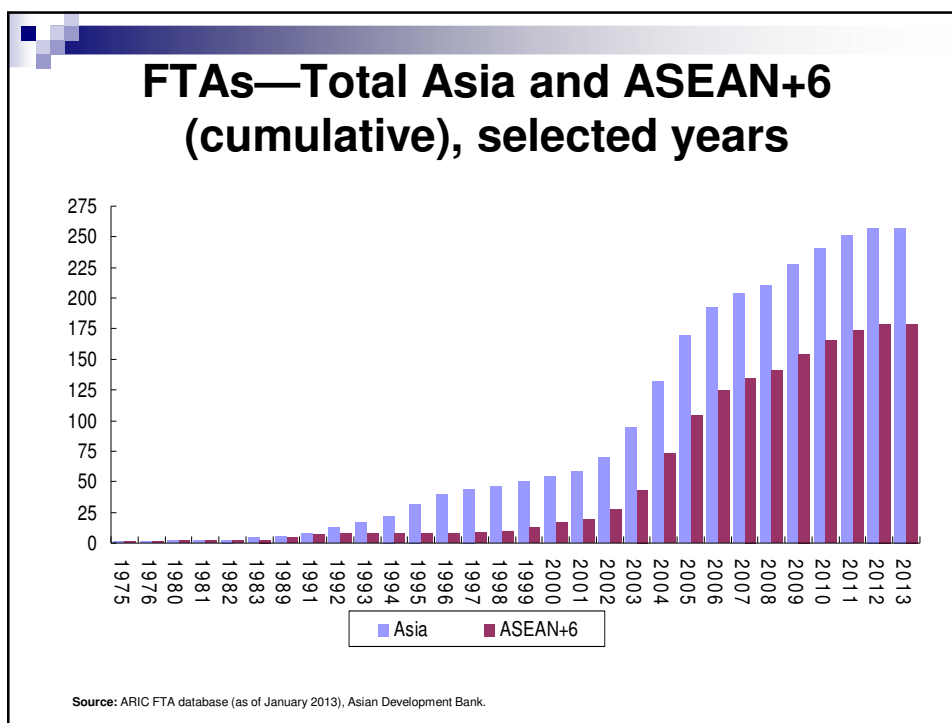
- Asia-Pacific party to 109 ratified FTAs, with more being negotiated
- How many FTAs do we need?
- Most bilateral, with 2 mega proposals: RCEP and TPP
- Most bilaterals in Asia-Pacific involve ASEAN+6 countries

FTAs by Status—Total Asia (cumulative), selected years



Notes: **Proposed** = the parties consider an FTA; governments or relevant ministries issue a joint statement on its desirability or establish a joint study group/joint task force to conduct feasibility studies. **Framework agreement signed/under negotiation** = the parties, through relevant ministries, negotiate the contents of a framework agreement (FA) that serves as a framework for future negotiations. **Under negotiation** = the parties, through relevant ministries, declare the official launch of negotiations, or start the first round of negotiations. **Signed but not yet in effect** = the parties sign the agreement after negotiations have been completed, but the agreement has yet to become effective. **Signed and in effect** = FTA provisions

Source: ARIC FTA database (as of January 2013), Asian Development Bank.



The Jigsaw Puzzles

- The rise of mega-regionals such as RCEP and TPP suggests that the world trade system is fragmenting to appear more like a jigsaw puzzle than a spaghetti bowl.
- There are both regional and global jigsaw puzzles to be solved, and in that order, to clean up the world trade system.
- How likely is this?

Regional Puzzle- RCEP

- The difficulties of FTA consolidation at the regional level are well known
- Like any jigsaw puzzle, we begin with disarray.
- But the RCEP puzzle is more than just messy—there is no solution because the pieces of the puzzle do not fit.
- The so-called pieces—the ASEAN+1 and bilateral FTAs—come in different shapes and sizes

Regional Puzzle- RCEP

- The only way to make the pieces fit is to reshape them: either to shave them down or to build them up.
- Shaving down the bits is a “race to the bottom”, where the lowest common denominator rules, making for an easier fit.
- Building them up is the opposite, where laggards lift their reform game to meet the standard set by the front-runner(s).

Regional Puzzle- RCEP

- Because harmonization implies consensus, a 'race to the bottom' likely-country with the lobby that has the most to lose is also least likely to compromise.
- Apparent losses to a country looking to retain protection outweigh the perceived benefits to others from liberalization
- Baldwin's (2006) asymmetric lobbying theory, which explains why potential losers tend to lobby harder

Regional Puzzle- RCEP

- Alternatively, countries exercising flexibility could result in conservatism—approximating the status quo and preserving the current spaghetti bowl
- The hoped-for 'race to the top' unlikely without political will and incentives to overcome pressure from vested interests
- The problem is that some countries may not see any carrot — and there is no stick.

Regional Puzzle- TPP

- Unlike RCEP, TPP is not aimed at consolidation since not all members have bilateral FTAs between them
- But also facing difficulties, having now missed 3 deadlines; latest was Oct 2013
- Not surprising, with TPP's agenda more wide ranging and ambitious than Doha.
- Although only 12, not 150 countries, diversity in negotiating positions remain

Regional Puzzle- TPP

- Concern that TPP degenerating into a series of bilateral deals, with a US-Japan agreement at its core.
- Each member seeking different “carve-outs”, which can only be accommodated through bilateral arrangements.
- With renewed uncertainty over “fast track”, members may not sign up for an agreement when it remains unclear what the key proponent can actually deliver

Global Puzzle

- All of the problems with solving the regional jigsaw puzzle are also present with global puzzle, plus more!
- Not only are some pieces of the jigsaw puzzle missing, there are also overlapping bits that are redundant and probably irreconcilable
- RCEP highlighted diversity between FTAs *within* a regional bloc, but diversity *between* blocs likely to be higher still

Global Puzzle

- How should the process of global consolidation of the regional blocs occur?
- Should it proceed sequentially, or should there be a kind of single undertaking?
- A sequential bloc by bloc, or bottom up approach, building on open accession clauses of existing agreements, has the same difficulties as solving the regional puzzle, but amplified by greater diversity.

Global Puzzle

- Method matters- if through MRAs rather than harmonization through regulatory convergence towards a regional standard, then the merging of different blocs or expansion is even more difficult.
- Countries looking to accede would not have had any input into the negotiated outcome, and would have to simply accept whatever has been agreed

Global Puzzle

- Since some countries are members of more than one plurilateral bloc, they would need to harmonize their accords across their blocs before proceeding to merge with other blocs.
- If the single undertaking option sounds like Doha, then it is because it is similar in process, and likely to be just as difficult to conclude- Enough said!

Global Puzzle

- Consolidation at the regional or global level may be just as difficult, if not more so, than starting from scratch, as there are no discrepancies to be resolved or policies to be reversed.
- Getting a pair of countries to agree on a specific set of terms will not necessarily facilitate similar breakthroughs with third parties.

Global Puzzle

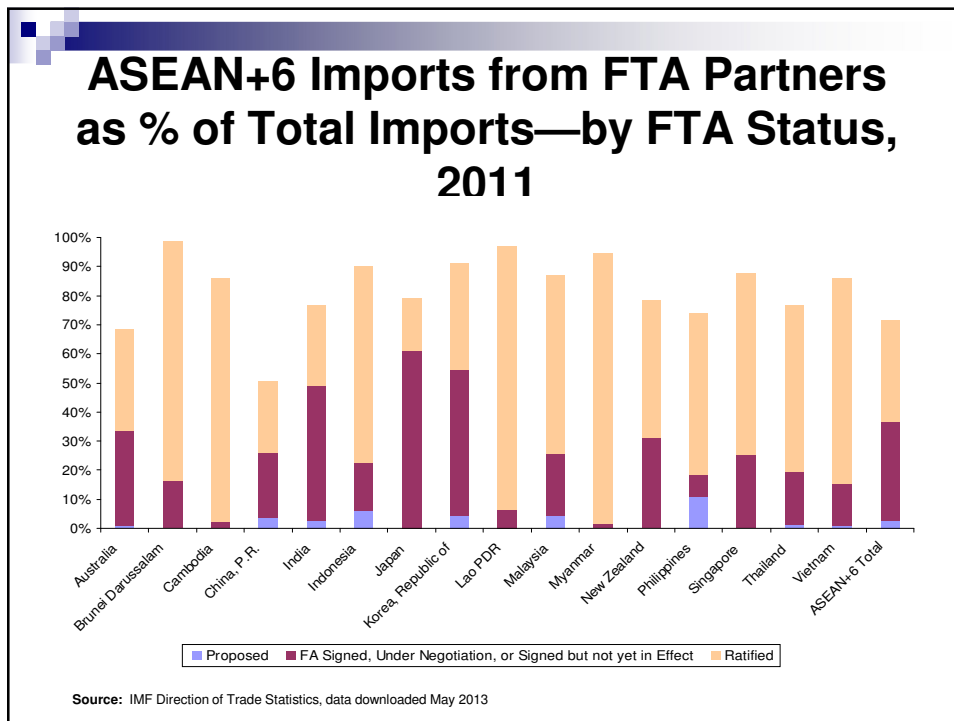
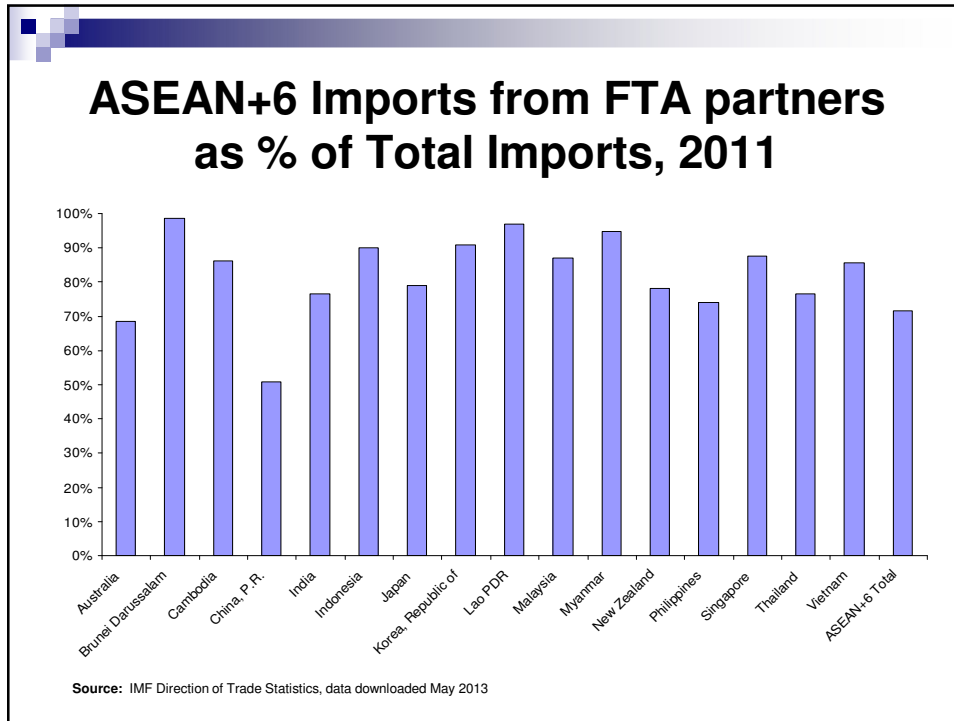
- To ignore this is to ignore ground realities and the political-economy of FTA negotiations.
- And anyone who has looked closely at the text of a free trade agreement will know how difficult the task of enmeshing even two similar agreements can be, let alone many different ones!

The Way Forward

- Given difficulties associated with solving both the regional and the global jigsaw puzzles, where do we go from here?
- While we are likely to continue muddling through with trying to conclude the mega-regionals for a while yet, with bilaterals continuing to proliferate- requiring future mega-regionals?- we could soon reach an inflection point, or at least a reflection point, if not a breaking point!

How much trade is or will be covered

- Using RCEP as an example, we match trade flows with FTA coverage
- Apart from China and Australia, $\frac{3}{4}$ of imports covered or about to be covered
- For ASEAN+6 as a group, more than $\frac{1}{3}$ of imports already covered by FTAs, with another $\frac{1}{3}$ about to be
- Similar pattern for exports



Goods, Value of Imports from FTA Partners (\$ million) and Share in Total Imports, 2011				
Country	Proposed	Under Negotiation or Signed but not yet in effect	Ratified	Total Imports from FTA partners
Australia	2,073.5	85,313.3	91,051.7	178,438.5
	0.8%	32.8%	35.0%	68.6%
Brunei Darussalam	0.0%	1,051.8	5,267.9	6,319.7
	0.0%	16.4%	82.3%	98.7%
Cambodia	19.4	285.9	10,568.0	10,873.3
	0.2%	2.3%	83.7%	86.1%
China, P.R.	61,403.0	393,988.8	428,091.6	883,483.4
	3.5%	22.6%	24.6%	50.7%
India	11,643.6	215,069.2	128,698.3	355,411.1
	2.5%	46.2%	27.7%	76.4%
Indonesia	11,206.3	28,483.0	119,985.7	159,675.0
	6.3%	16.1%	67.6%	90.0%
Japan	516.3	520,084.7	155,639.9	676,240.9
	0.1%	60.8%	18.2%	79.1%
Korea, Republic of	23,301.3	261,776.9	191,875.3	476,953.5
	4.4%	49.9%	36.6%	90.9%
Lao PDR	0.3	292.5	4,198.5	4,491.2
	0.0%	6.3%	90.6%	96.9%
Malaysia	8,199.9	40,083.8	114,938.2	163,222.0
	4.4%	21.4%	61.3%	87.0%
Myanmar	8.8	206.7	12,756.1	12,971.6
	0.1%	1.5%	93.2%	94.8%
New Zealand	176.3	11,247.1	17,244.7	28,668.0
	0.5%	30.6%	47.0%	78.1%
Philippines	6,586.1	4,447.1	33,452.5	44,485.7
	10.9%	7.4%	55.6%	74.0%
Singapore	141.6	92,555.1	228,260.1	320,956.8
	0.0%	25.3%	62.4%	87.7%
Thailand	3,061.9	41,233.9	131,155.0	175,450.9
	1.3%	18.0%	57.2%	76.6%
Vietnam	1,061.7	14,638.9	73,933.8	89,634.4
	1.0%	14.0%	70.7%	85.8%
ASEAN+6 Total	129,400.1	1,710,758.8	1,747,117.4	3,587,276.3
	2.6%	34.2%	34.9%	71.6%

Source: IMF Direction of Trade Statistics, data downloaded May 2013

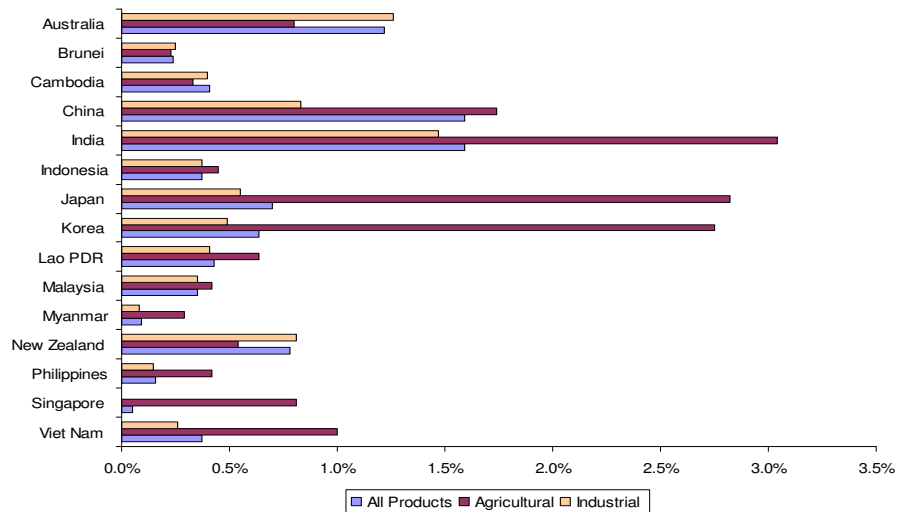
Goods, Value of Exports to FTA Partners (\$ million) and Share in Total Exports, 2011				
Country	Proposed	Under Negotiation or Signed but not yet in effect	Ratified	Total Exports to FTA partners
Australia	1,221.8	171,807.1	49,213.9	222,242.8
	0.5%	63.4%	18.2%	82.0%
Brunei Darussalam	0.0%	45.1	11,332.0	11,377.1
	0.0%	0.4%	98.7%	99.1%
Cambodia	0.2	1,683.6	1,371.6	3,055.4
	0.0%	25.8%	21.1%	46.9%
China, P.R.	65,252.7	250,016.5	612,477.6	927,746.8
	3.4%	13.1%	32.2%	48.8%
India	6,470.5	121,151.0	85,943.5	213,565.0
	2.1%	39.4%	28.0%	69.5%
Indonesia	16,711.6	31,688.3	134,433.4	182,833.3
	8.2%	15.6%	66.1%	89.8%
Japan	3,073.6	373,812.0	156,778.2	533,663.8
	0.4%	45.3%	19.0%	64.7%
Korea, Republic of	32,854.3	213,653.9	213,020.0	459,528.1
	5.8%	38.0%	37.9%	81.7%
Lao PDR	0.05	282.1	2,342.4	2,624.6
	0.0%	9.0%	75.1%	84.1%
Malaysia	6,451.9	48,901.1	143,227.3	198,580.4
	2.8%	21.4%	62.7%	87.0%
Myanmar	55.4	361.5	7,115.7	7,532.6
	0.7%	4.3%	85.6%	90.6%
New Zealand	350.6	9,409.4	17,925.1	27,685.1
	0.9%	25.0%	47.6%	73.5%
Philippines	7,154.2	5,950.6	26,617.5	39,722.2
	14.8%	12.3%	55.2%	82.4%
Singapore	1,332.9	52,044.1	272,857.4	326,234.4
	0.3%	12.6%	66.2%	79.1%
Thailand	3,976.0	52,744.6	121,767.4	178,488.1
	1.8%	24.0%	55.3%	81.0%
Vietnam	1,455.7	34,888.9	44,429.3	80,773.9
	1.6%	37.6%	47.8%	87.0%
ASEAN+6 Total	146,361.5	1,368,439.8	1,900,852.3	3,415,653.5
	2.9%	26.8%	37.3%	67.0%

Source: IMF Direction of Trade Statistics, data downloaded May 2013

How much travels preferentially?

- Margins of preference (MoPs) are small
- Highest for agri, in Japan, Korea and India, but still small overall
- 20% of intra-ASEAN trade preferential, with trade-weighted MoP only 2.3%
- 73% of intra-ASEAN trade at MFN zero, with more than 90% for some bilaterals
- Globally, only 15% of trade flows are conducted under preferential terms

Margins of Preference (ITC May 2013 data)



Note: Data unavailable for Thailand. In the calculation of MFN tariff averages, general tariffs (for non-WTO members) and non-MFN tariffs are included.

Source: ITC Market Access Map Country Tariff Averages, downloaded May 2013

Preferential trade by agreement/type of regime, 2008, selected regimes

Regime	Share of trade by preferential margin (PM) and MFN rate (in per cent of total trade)								Trade weighted pref. margin (percentage points)
	Preferential Trade						Total Non-Preferential, >0	Total MFN Zero	
	Total Preferential	PM>20%	PM 10.1% to 20%	PM 5.1% to 10%	PM 2.6% to 5%	PM 0.1% to 2.5%			
Intra-ASEAN	20.1	2.0	2.0	2.6	4.7	8.7	3.6	72.9	1.7
Singapore-USA	7.2	0.2	0.2	0.6	4.8	1.4	0.0	92.7	0.3
Japan-Singapore	3.1	0.0	0.0	0.1	2.4	0.6	1.9	94.0	0.1
Australia-Singapore	6.4	0.0	0.0	0.2	6.1	0.0	0.0	93.6	0.4
India-Singapore	20.0	0.0	0.0	8.7	6.6	4.6	16.2	59.6	1.0

Source: WTO World Trade Report, 2011

The Way Forward- Tariffs

- Almost all trade covered or about to be covered by an FTA, while almost all trade not affected & unlikely to be affected by it!
- All this while the costs of trying to negotiate new, or consolidate existing, and implement largely unused preferential arrangements continue to increase.
- For tariffs, time is ripe, or almost ripe, to consider harmonizing across existing FTAs, and multilateralizing preferences

The Way Forward- Non-Tariffs

- Many studies (eg WTO, 2011) confirm the failure of most Asian FTAs to deepen coverage to deal with trade facilitation and behind the border issues
- Even if they deepen, the need to be discriminatory in the exchange of concessions suggests problems
- Unlike tariffs, costly or impractical to remove NTBs or NTMs preferentially

The Way Forward- Non-Tariffs

- Even if they can be provided preferentially, proliferation of FTAs implies preference erosion, which increases with each FTA
- Resistance to multilateralization wanes with preference erosion, especially when net benefits are greater: no trade diversion, max trade creation, and no need to implement ROOs

The Way Forward

- Bali has shown that multilateral deals are still possible, sector-wise at least
- Single undertaking unlikely, and maybe less so now, but still may not be enough
- Would dilute but not remove preferences, or the contradictions
- Regionalism has remained, indeed thrived, despite many successful GATT Rounds

The Way Forward

- Time is ripe to seriously consider multilateralization of preferences as a way out of current mess of preferential deals-with or without more multilateralism
- History supports viability of unilateralism
- Very small share of trade travels preferentially at a high cost of implementing FTAs
- For NTBs, multilateralization is natural, & incumbency requires national reforms



Thank you!

For inquiry or comments, please contact:

Jayant Menon

Lead Economist (Trade and Regional Cooperation)
Office of Regional Economic Integration

Telephone: (63-2) 632-6205

Email: jmenon@adb.org