

A closer look at East Asia's Free Trade Agreements

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Slow progress in global trade talks has led to a surge in free trade agreements (FTAs) across Asia. With the World Trade Organization (WTO) Doha Round trade talks stalled, Asian countries see FTAs as a means to liberalise trade and investment and sustain economic recovery in the region. The surge in the number of FTAs — from three to about 50 in the last decade, with another 80 or so in the pipeline — has, however, sparked concerns about the Asian noodle bowl due to overlapping rules of origin (ROOs) requirements, which may be costly to business, especially small- and medium-sized enterprises (SMEs). Critics worry that this wave of agreements will undermine the multilateral liberalisation process.

As the dearth of empirical evidence on the business impacts of FTAs made it difficult to resolve this debate and explore policy implications, ADB conducted firm-level surveys in six countries, the results of which are published in the book, '*Asia's Free Trade Agreements: How is Business Responding?*' (Kawai and Wignaraja, 2011). Experts in the region looked at the issues using firm surveys in Japan, China, Korea, Singapore, Thailand, and the Philippines.

This book asks four important questions concerning the spread of FTAs and the Asian noodle bowl, among them: Are FTA preferences being used by firms? What are their costs and benefits? Are multiple ROOs a burden to business? Is there enough business support for firms to use FTAs?

On the whole, the study indicates that concerns about the Asian FTA noodle bowl effect are overstated and, surprisingly, SMEs are not unduly affected by them, at least at this time. As the number of FTAs grows, SMEs are able to export to multiple markets, and firms increasingly use FTA preferences, concerns about the Asian noodle bowl, however, could be more justified.

The study also reveals that the use of FTAs is higher than previously thought. About 28 per cent of firms in the sample use FTA preferences for exporting their goods and nearly 53 per cent plan to use them. Another finding is that the use of FTAs provides firms with more benefits than costs, because of preferential market access, which results in higher export sales; preferential tariffs that make it easier to import intermediate inputs; and improved business opportunities resulting from better trading environments.

The lack of information on the FTAs, and not the noodle bowl *per se*, is the biggest impediment to firms using FTAs, as indicated by 70 per cent of responding firms in the Philippines, 45 per cent in China, and 34 per cent in Korea. Other impediments cited by respondents are low margins of preference and delays and administrative costs. There is significant demand for more business support for East Asian SMEs to export through FTAs. The study indicates that various types of business support for firms — including

greater use of information technology-based systems of ROO administration, financial and training support, and enhanced consultations with business during FTA negotiations — would increase use of FTAs.

To overcome the potential Asian FTA noodle bowl problem in the future, the study suggests several measures, including rationalising ROOs, adopting coequals for ROOs, upgrading origin administration, harmonising regional ROOs, consolidating multiple, overlapping FTAs into a single region-wide FTA, and multilateralising Asian regionalism. Concluding the WTO Doha Round negotiation and avoiding protectionism would also be invaluable in boosting FTA use.

A region-wide FTA could provide clear economic benefits, such as increased market access to goods, services, skills and technology; increased market size, which would permit specialisation and realisation of economies of scale; easier foreign direct investment and technology transfer by multinational corporations; and simpler tariff schedules, rules and standards. It could also offer insurance against rising protectionist sentiments that pose a risk to Asia's trade and economic recovery.

Any region-wide agreement could be a series of linked agreements with variable coverage of members and issues. For now, there are two competing processes — the ASEAN+3 or +6 FTA (among the ten ASEAN countries plus China, Japan, and Korea in the case of ASEAN+3, and plus Australia, India and New Zealand in the case of ASEAN+6) and the Trans Pacific Partnership (TPP) agreement — that could form the future basis of a region-wide FTA. To realise the ASEAN+3 or +6 FTA, a trilateral FTA among China, Japan and Korea is needed and this should be connected with the existing ASEAN+1 FTAs. TPP aims to achieve high quality agreements and is an early step toward a larger APEC-wide FTA, which would require a more challenging task of forging a US-China FTA.

The biggest challenge lies in the political will of countries as well as geopolitical considerations in moving faster on either the ASEAN+3/+6 FTA or TPP process. Changing economic gravity — due to the rapid economic rise of China and India — would suggest that the ASEAN+3/+6 FTA is more attractive, while security considerations may convince some East Asian economies to prefer TPP as it strengthens ties with the US. But these two processes are not mutually exclusive, and the ASEAN+3/+6 approach can be complementary, and create synergy, with the TPP approach. Whichever avenue is to be taken, it is important to accelerate the liberalization of goods and services trade and investment, reduce behind-the-border barriers, and pursue domestic reforms. A harmonious Asia-Pacific would likely see a convergence between the two processes, a win-win solution for the Asia-Pacific community.

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