PACIFIC ECONOMIC COOPERATION COUNCIL

PTAs and the Future of East Asian Regionalism: an ASEAN Perspective

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PECC Trade Forum Seminar

RTAs and the Future of Regional Integration in East Asia and the Asia Pacific

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Reminder - where are we coming from

- Discussions in TF on RTA and developments in the region point to
  - recognition of proliferation: political imperative ensures continuation
  - how to manage proliferation: principles, common framework, convergence
    - MFN clause, liberal rules, unbundling
    - ASEAN -- still in a state of flux, no consensus

What is happening in ASEAN: Update and Evaluation

- PTAs in ASEAN:
  - Most progress in bilaterals by member country (S'pore lead, Thailand follow, now Malaysia and Philippines) - comprehensive but MFN?
  - Deepen ASEAN Economic integration: ASEAN Economic Community end 2003
  - ASEAN + 1 --- China most progress, Japan, India, US and EU
  - ASEAN + 3

What is current state of debate on regionalism?

- Economic rationale: development final goal achieved by:
  - competitiveness (scale, specialization) -- regional production center service third markets; already happening on the ground
    - FTA not needed - market driven integration will happen faster (FTA needs radical institutional change - private sector cannot wait)
  - policy reforms - commitment, greater transparency and predictability (binding)
    - what matters is national policy (unless FTA used to be bold - WTO plus; not clear this is the case)

So emerges as questions for ASEAN

- Market driven integration - yes, but can FTA (and which parts of FTA) help or hinder market driven integration?
- Relevancy means need to be BOLD, but reality is need to “unbundle”
  - by issue (trade and investment facil; joint infrastructure)
  - by sector (11 priority sectors in AEC) - positive list
  - by geography (bilaterals, or subregionals - Southern China with parts of Southeast Asia?)
  - Negotiations will be conducted bilaterally

Unbundling?

- Unbundling will mean carving out or buying in -- counter to “substantially all trade” definition in Article XXIV GATT and Article V in GATS
  - developing country FTA - enabling clause
    - (ASEAN, ASEAN+China, ASEAN+India)
  - but not for developed country - so cannot hold for FTA with developed partners
    - (bilaterals, ASEAN+Japan, ASEAN+US)

Where are we at?

- AFTA (0-5%) achieved 2002, zero tariff elimination target -- but estim. 5% intra ASEAN trade use preferential tariffs. How about NTBs, trade facilitation etc?
- AFAS: not GATS plus and restrictive compared with actual
  - e.g. health care: limits on ownership even though 100 percent or high equity caps in most countries; no commitments on mode 4 even though allow foreign health professionals.

Why does ASEAN need to move faster?

- All the imperatives set out by AEC for free flow of services
  - globalization
  - rapid pace of negotiations in bilateral and ASEAN+1 including services
  - single production base -- question? How does it extend to services?
    - Services that support regional production base and creation of regional services hubs in its own right (ASEAN medical hub, outsourcing possibilities -mode 1)

AEC - Bali Concord

- “ASEAN’s strategy shall consist of the integration of ASEAN and enhancing ASEAN’s economic competitiveness. The final goal of economic integration is free flow of goods, services, investment and a freer flow of capital, equitable economic development and reduced poverty and socio-economic disparities in year 2020.” (Bali Concord, December 2003).

Where do we want to go?

- Goals:
  - Free flow of goods and services by 2020 or earlier, and by 2010 for 11 priority sectors
  - **11 Priority Sectors and "champions"**
  - Indonesia: Wood-Based Products and Automotives;
  - Malaysia: Rubber-Based Products; Textiles and Apparels;
  - Myanmar: Agro-Based Products and Fisheries;
  - Philippines: Electronics;
  - Singapore: e-ASEAN and Healthcare; and
  - Thailand: Air Travel and Tourism

Goals

- MRA for professional services by 2008
- Important question for services: are we going for preferential liberalization or MFN liberalization?

Are preferences in services feasible?

- Measures affecting services trade are typically not tariff-like instruments, but:
  - Limitations on entry of firms
  - Foreign equity limitations
  - Quotas on outputs and foreign service workers
  - Requirements regarding the legal form of establishment
  - Regulatory measures
- Dealing with FDI: consistency with investment neg. (AIA) and can there be exclusionary rules of origin?

Example of preferences in services

- Bilateral air service agreements: preferential allocation of output quotas
- Preferential relaxation of foreign equity limitations (e.g., NAFTA)
- Preferential access to certain regions within a country (e.g., Hong Kong-China FTA)
- Preferential recognition of foreign qualifications (e.g., EU mutual recognition)

In general - go for MFN liberalization

- Gains from MFN liberalization likely larger because
  - Non-preferential liberalization offers access to the most competitive service providers
  - MFN liberalization avoids complexity for negotiators, administrators and businesses
  - Other gains from trade (economies of scale, more intense competition, knowledge spillovers) are likely to be bigger if liberalization is non-discriminatory

Trade diversion in preferential services liberalization can be costly

- Due to the importance of location-specific sunk costs in services:
  - second-best providers may benefit from first mover advantages
  - sequence of liberalization matters, benefits from eventual MFN liberalization may be smaller

Why then negotiate regionally?

- Political imperative - regional to push multilat?
- More efficient bargaining
  - Negotiations may be less complex
  - Less scope for free riding on MFN principle
- Certain forms of regulatory cooperation are more feasible and desirable within a smaller group of countries (regulatory harmonization, mutual recognition).**
- Innovation in rule-making**

Rules of origin in services

- From an economic perspective a liberal rule of origin is to be preferred, but then regional liberalization approaches MFN liberalization
- Possible approaches (foreign firm but choose to locate in ASEAN?):
  - Local incorporation
  - Local incorporation and substantial business operation
  - Domestic ownership and control

Example: Rules of origin adopted in Hong Kong-China FTA

- Detailed Annex on “Definition of Service Supplier and Related Requirements.” Criteria for Hong Kong service suppliers include:
  - Incorporation and possession of valid operating license
  - Substantive business operations for 3 years or more (5 years for certain services)
  - Must have paid profit tax in Hong Kong
  - More than 50 percent of employed staff must be local residents

How do we get there? Road map

- Some caveats integration of priority sectors
  - broad based (2020) with priority sectors (2010) - de facto positive list approach
    - justification for sector choice: single production base, outsourcing, social
    - sectoral but
      - not in vacuum of what AEC looks like finally (I.e similarity in app between sectors)
      - comprehensive keeping in mind overall objectives (not just to open up that sector), including links to other sectors and social issues

What? Milestones? Monitor?

- Weakness in negotiation framework
- If continue with GATS/AFAS framework
- what is important not negative or positive list approach but transparency and predictability in liberalization commitments and how ratchet up
- So…

Liberalization scenarios

- Possible end goals with measurable milestones
  - limited new commitments less liberal than status quo policies
  - new commitments that bind existing policies;
  - binding existing policies and committing to future reform; and
  - immediately committing to more liberal policies.
- All this can have different time lines (present and future), milestones measured against binding vs. current and future liberalizations

Healthcare -- goals

- Free flow of health care professionals by 2008
- Free flow of health care services and products by 2010 – integrating healthcare by 2010 (some countries already have plans up to 2010) – so is it too late?
- To achieve:
  -)provision of competitively priced, quality and equitable health care for ASEAN community
  -)notion of a health care regional production center for healthcare products and ASEAN as a hub for health and medical care (including health tourism)

Comprehensive

- Trade in goods - medical and health care products (eliminate tariff and non tariff, facilitation, standards etc)
- Trade in services
  - Mode 1: cross border supply
    - feasible with ICT. From back office of medical care facilities to clinical diagnostics
    - link to E-ASEAN, efficient telecommunication services, ITA (links to other services and goods sector, e-commerce, training and hrd)

Trade in services

- Mode 2: consumption abroad – patients going abroad
  - Eliminate visa requirements for intra ASEAN travel by ASEAN nationals
  - portability of health insurance (some not affected e.g. cosmetic surgery, dentistry not affected by lack of portability of insurance)
  - for health tourism (medical, retirement) – need to also link to travel and tourism sectors, land ownership, real estate

Trade in services

- Mode 3: allow 100% foreign ownership of medical establishments and health care facilities; facilitate investments
  - Observation: most countries have relaxed limits on foreign ownership - so some liberalization and binding at status quo; why not boom of foreign hospitals? Lack of effective demand, control prices, some domestic regulatory impediments?

Foreign investment restrictions in ASEAN health care

- Cambodia: no foreign equity restrictions and same as WTO accession commitment
- Indonesia: no foreign equity restrictions for healthcare facilities
- Malaysia: 70% compared with GATS (30%)
- Philippines: 40 percent cap on foreign ownership hospitals and related institutions
- Thailand: 49% cap though foreign investors can make request for majority share, but no record of this happening; evidence that hospital chains taken over by nominees
- Vietnam: no foreign equity restrictions

Trade in services

- Mode 4: Movement of personnel
- Eliminate visa requirements for intra ASEAN travel by ASEAN nationals
- Multilateral and ASEAN+1 agreements – access to markets of professionals
- MRA on health professionals? Recognition, certification, licensing.

Trade in services

- *Regional cooperation in domestic regulations, rules innovation (e.g. safeguards), standards*
  - eg. Domestic regulations - re ensuring sufficient quality and access for poor, brain drain issues

ASEAN and China

- Framework agreed end 2002 (on paper comprehensive - new generation FTA)
- Progress fastest compared with other initiatives
  - 2003 negotiate - HS1-8 for ASEAN+China, will finish rules of origin negotiations June, start this year.
  - Early harvest - bilateral agreements. E.g. Thailand-China, fruits -- part of agreement, how do other ASEAN countries accede to it?

ASEAN + China

- Other parts - services, investment, facilitation etc
  - not yet negotiated, focus still on goods
  - question - preferential? Prior to China open up for WTO (CEPA model or what?)

Conclusions

- AEC Progress??? Leadership and political will still lacking
- ASEAN+1 likely to progress slow; not clear how fast ASEAN+3 will progress despite rationale.
- Progress in PTA still in flux - not clear whether bilaterals will be main driver - if so then what are the consequences?

Conclusions

- Traditional benefits of regionalism a la East Asia?
  - Process is more important
  - unilateral and multilateral will continue, some scope for common external position?
  - Bottom up - driven by regional production center needs