

## **An EU-ASEAN Free Trade Agreement: Sharing Benefits of Globalisation?**

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## Abstract

In the aftermath of the stalled launch of a new WTO round of global trade talks (December 1999), Singapore and Japan initiated a joint study into the feasibility and desirability of a possible bilateral Free Trade Agreement. The subsequent negotiations led to a 'New-Age Economic Partnership Agreement' signed in January 2002, reducing barriers in trade and investment in goods as well as services, technical standards and public procurement. New initiatives for economic cooperation in, inter alia, human resource development, science and technology and SMEs were agreed. During 2000 talks had also begun between Singapore and the United States and these are resulting in a bilateral Free Trade Agreement (FTA). Responding to these developments, several other ASEAN countries initiated negotiations towards bilateral FTAs with other major players, most notably Thailand (with India) as well as Malaysia (with Japan and others). Moreover, China stated its intention to enter into a Free Trade Agreement with the ASEAN by 2012. It is against this background of deepening of trade and investment links between the several ASEAN Member States (Singapore, Malaysia, Thailand) and several major players that the question of a possible EU-ASEAN FTA is investigated. The stalling of the multi-lateral trade talks in Cancun in September 2003, implying that the Doha Development Agenda process will not be able to reach agreement within the time-frame set, also provides a new argument for assessing the scope for an inter-regional free trade agreement between EU and ASEAN.

This lecture note addresses the possible opportunities and risks to the European Union of entering into negotiations with ASEAN Member States with a view to realising a bilateral EU-Singapore FTA. It assesses the pre-feasibility of such a course of action, while noting a number of questions which deserve further policy discussion as well as economic and statistical analysis. At this stage a simple 'for or against' evaluation will be premature, in view of the multitude of scenarios at both the bilateral and multilateral levels.

The ASEAN's trade policy regime is opening up and the gains of further tariff elimination will be modest, because most ASEAN countries already apply low , while those of the EU on import from ASEAN are low as well – eg for Singapore the tariff rate is merely 1.04 per cent (trade weighted). Nevertheless, a further reduction could benefit both EU and ASEAN because a significant share of imports is intra-firm trade, with EU firms operating from ASEAN as a production platform for the EU markets.

Therefore for an EU-ASEAN FTA to be worthwhile, it must generate benefits on issues relating to non-tariff barriers to trade, e.g. technical standards, SPS and mutual recognition of testing. Further significant benefits to both the EU and Singapore may be realised by tackling the issue of further liberalisation of international trade in services (e.g. banking and insurance licences, air and sea transport). Finally, reducing restrictions on foreign direct investment in selected service sectors is bound to enhance investment flows from the EU to ASEAN.

An Inter-regional EU-ASEAN FTA could elaborate fresh rules for 'new' issues of public procurement, competition policy, intellectual property and dispute settlement – those very issues which led to failure to reach agreement in Cancun. In this respect the EU-Chile Free Trade agreement (10 June 2002) offers a very relevant template, with considerable scope for a EU-ASEAN agreement venturing deeper into these issues of 'behind the border' non-trade barriers and restrictions.

It goes without saying that any possible EU-ASEAN FTA must be “WTO-plus” – re-invigorating multi-lateral commitments made and anticipated and not allowing any back-peddalling on these commitments. It is equally pertinent that any EU agreement with ASEAN must offer the scope for replication and extension with other regions, such as the SAARC. Finally, the Doha Development Agenda (DDA) will remain the *leitmotiv* of multi-lateral trade talks for the coming years, despite its present lack of progress. The EU support for the DDA would imply a commitment, in principle, to extend benefits in areas of services liberalisation, offered to ASEAN also to other countries in Asia and elsewhere.

Some of the questions to be addressed with implications for EU external trade and relations policy more widely will relate to the precise nature of possible mechanisms to ensure that an inter-regional agreement will extend benefits to all ASEAN Member States, including the least developed countries (Laos, Cambodia, Myanmar). At a global political level, the more active use of inter-regional FTAs as instruments of external relations policy will place the EU at par with the US as executing a multi-track strategy encompassing multi-lateralism, regionalism as well as bi-lateralism. It is noteworthy that Japan has also chosen this direction in recent years.

Other pertinent questions to be answered will require further statistical and economic analysis. Statistical analysis should address the inadequate information on current flows of internationally traded services between the EU and ASEAN. Further economic analysis should seek to quantify the dynamic effects of a FTA resulting from increased investment flows, greater technology and human resources transfers as well as increased commercial presence of the EU in ASEAN and vice versa.

The structure of this lecture is to start by seeking to characterise the EU and ASEAN trade policy regimes in a consistent and comparable way, based on research by Messerlin (Chapter 1). It is argued that trade diversion effects of a possible EU-ASEAN FTA are likely to be limited and that trade creation effects of tariff reductions on goods alone will be very limited too (Chapter 2). However significant mutual benefits of an inter-regional FTA may accrue from reducing technical barriers to trade, in particular through harmonisation of technical standards, mutual recognition of testing and suitable SPS agreements for selected sectors (Chapter 3). Furthermore, accelerated removal of remaining non-tariff barriers on establishment and commercial presence in service sectors can lead to an increase of internationally traded services, which would provide a major new opportunity for EU exports. This will need to be addressed in the wider context of public procurement, competition policy and effective dispute settlement (Chapter 4). The possible risks of a EU-ASEAN FTA – mainly concern the EU’s political relations with some Member States of ASEAN (Myanmar) are addressed in Chapter 5 while Conclusions follow in Chapter 6.

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## Introduction

The European Commissioner for Trade, Mr Pascal Lamy, announced in 2002 an agreement for a very ambitious ' Association Agreement' between the EU and Chile. The Agreement will incorporate a Free Trade Area, a political dialogue and extensive co-operation. The agreement was initialled by the European Commission and a representative of the Chilean Government on June 10, 2002.<sup>1</sup> Speaking in Brussels, Mr Lamy coined the agreement a ' fourth generation plus' agreement, which was ' a good deal for both sides' . It will cover all areas of trade and go well beyond the respective WTO commitments of the EU and Chile. It is to include:

- a Free Trade Area in goods covering all sector including industrial, fisheries and agricultural goods;
- a fully-fledged free trade agreement in services;
- an investment agreement to encourage FDI in both directions and opening-up of public procurement markets;
- rules on competition and intellectual property; as well as
- an effective dispute settlement system.

(A summary of the highlights of the (draft) EU-Chile agreement is presented in the annex).

This EU-Chile free trade area followed Mr Lamy's recent statements at the Asia-Europe Foundation in Singapore (15 February, 2002) where he acknowledged that Minister for Trade of Singapore had made an ' immensely compelling political and economic case' for strengthening the ties between the EU and Singapore through a Free Trade Agreement. He proposed several ' tests' for such an agreement:

- first, does EU business support such an agreement?
- second, will it enhance the EU' s multilateral ambitions in the WTO (is it "WTOplus")? ; and
- third, that such an initiative must not detract but reinforce the pursuit of the Doha Development Agenda ("Doha-plus").

Subsequent detailed discussion indicated that the position of the EU on such a bilateral approach was one of concern of alienating other ASEAN Member States. Moreover, there was also concern about a likely negative impact on the DDA-process, with the EU seen to be favouring one small rich country which had ensured its support for the EU positions in the WTO. Hence, the EU response to Singapore was one of saying 'not yet', without closing the door irreversibly.

Which courses of action may be open to the European Union and the ASEAN to engage into a collaboration which would potentially lead to an agreement with all – if not more – of the desirable features of the above-mentioned EU-Chile agreement, while robustly ensuring business support and consistency with the DDA-process. This may be seen as a ' prefeasibility assessment' for a possible EU-ASEAN Free Trade Agreement, analysing both opportunities and risks.

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<sup>1</sup> The Commissioner noted that the Agreement was ' at his political level' . Following the initialling of the agreement on June 10, 2002 it will need to be approved by College of Commissioners. The text will be submitted to the Council and the European Parliament and the formal signing of the Agreement is expected to take place during the Autumn of 2002. The trade and institutional provisions will enter in force only after completion of the adoption procedures by the European institutions and the Chilean Congress. Parliaments of EU Member States will also have to ratify the Agreement. A summary and discussion of the highlights of the services sections of the draft Agreement is presented below.

## Chapter 1: EU and ASEAN's International Trade Policy Regimes

Europe's prominence in ASEAN is not merely a consequence of five centuries of shared history – a great deal of new investment and activities have developed and blossomed during the last three decades. Today's trade and investment flows between the EU and ASEAN are of critical economic importance for the EU – not merely because of their value, but also because of their strategic regional nature. Several indicators highlight this, in particular the extent of commercial presence of European firms in the region as well as the importance of intra-firm trade – firms in the EU importing from their own subsidiaries in the region.

In particular in the industrial goods sector one finds a great deal of presence and dominance of EU firms. For example, of Singapore's total chemical export to the EU nearly 80 per cent was supplied by three global firms – each of them a household name with their origins and majority ownership in the EU. This simple reality provides a strong and powerful business case in favour of a FTA because such an agreement will directly reduce the costs to EU-owned firms operating both in ASEAN and the EU. This European presence is certainly a reflection of the business-friendly environment of Singapore. The Economist Intelligence Unit's survey of best places to do business in Asia elected Singapore at the top spot for 2002, overtaking its arch-rival Hong Kong. However, the specific characteristics of Singapore's international trade and investment policy regimes, compared with other countries in the region, are the most important determinant.

Firms export more to or from markets subjected to the “best” trade policies (even if these policies still do not fit the free trade ideal) than to other markets, and trade policies “compete” with each other for attracting trade and investment flows. A Free Trade Agreement is seen by firms from a country as “improving” the trade policy regime of the country's trading partner. To get a sense of what may be the main interests of the EU in a FTA with ASEAN, it would be desirable to have a set of indices allowing broad comparisons between the trade policies of Singapore, the EU and other relevant countries. Giving the ASEAN a 'grade' for its trade policy regime, relative to competing countries, allows us to assess, though indirectly, the arguments in favour of a EU-ASEAN FTA. Some novel research into trade policy regime indicators allow us to do precisely that (Messerlin and Laird, 2002).

*Characterising Trade Policy Regimes.* When looking at foreign markets, firms ask a wider range of questions about trade policy than merely asking whether trade is 'free'. Key questions are as follows:

- first, is the examined trade policy simple to understand and to predict?
- second, will it guarantee secure access in the future?
- third—of course—is the openness in terms of market access (the free-trade component).

In order to answer these questions, three indices of “simplicity,” “irreversibility” and “openness” were constructed for a reference set of 39 countries.<sup>2</sup>

*ASEAN's Trade Policy Regime.* As one could expect, the general conclusion is that one of ASEAN Member States (Singapore) operates a trade regime which is one of the most “competitive” (open) in the world – but that this country is an exception within its own region. Singapore imposes zero tariffs on imports from all sources, with the exception of

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<sup>2</sup> Our analysis is based on data from WTO (2001), UNCTAD's TRAINS database and OECD. Appendix A provides the details of the method used and the table with full details for 39 countries.

certain alcoholic drinks. This approach has been largely responsible for Singapore's growth and global economic achievement during the past decades. Furthermore, the table also reveals that Hong Kong and Switzerland match Singapore's score on openness in industry -- but on irreversibility Singapore outperforms all other countries, including Hong Kong, Canada and the United States.

However, the scores of the other founding members of the ASEAN (Indonesia, Malaysia, Philippines and Thailand) are considerably different. (See Table 1).

Paradoxically, the high scores on the trade policy regime index may be an "impediment" to the conclusion of a FTA with the EU. This paradox arises because it tends to reduce the financial and economic interest of a FTA for EU Member States and firms. Moreover, the indices show that the EU's own trade policy regime is not as competitive as that of Singapore and some ASEAN countries; hence a FTA may mean that the EU will have to open its own markets.

In agriculture, the simplicity index puts all ASEAN countries in the higher deciles, because of a limited number of tariff lines and a relatively low percentage of non-ad valorem tariffs. On the indices of irreversibility both Indonesia and Thailand realize scores also be in the high range. With regard to openness, Philippines and Thailand score below the levels of the EU, but the other countries are above. When one compares these results with the EU indexes (suggesting a relatively complex, reversible and closed policy), it is easy to understand that the EU will be rather reluctant to open negotiations in agriculture in the context of this FTA. This was amply demonstrated at the Cancun meeting in September 2003.

In industry, ASEAN also exhibits considerable barriers, again with the exception of Singapore. The scores for the other ASEAN countries are somewhat lower than those of the EU for the simplicity and irreversibility indexes and considerably lower for openness. This may be due to the differences between applied and bound tariffs which ASEAN continues to operate across a large range of industrial products. In these conditions, an EU-ASEAN FTA will thus essentially be seen by EU authorities and firms as a mechanism to demand from the ASEAN countries a reduction of current applied tariffs of zero per cent (possibly with minor exceptions). In summary, in the manufacturing sector, a possible EU-ASEAN FTA will essentially aim at reducing the existing level of tariffs to zero, with the ASEAN having to make sharper reductions than the EU.

The concept used in Table 1 should not necessarily be interpreted as merely reflecting a protectionist intent. It may simply reveal the existence of a relatively complex regime of norms and standards – this certainly partly explains the EU's lower score.

<b>Table 1: Trade Policy Regime Indicators for ASEAN and selected countries</b>						
	<b>Agriculture</b>			<b>Industry</b>		
	<b>Simplicity</b>	<b>Irreversibility</b>	<b>Openness</b>	<b>Simplicity</b>	<b>Irreversibility</b>	<b>Openness</b>
<b>Countries:</b>						
<b>EU</b>	<b>4,8</b>	<b>6,8</b>	<b>7,0</b>	<b>6,6</b>	<b>6,3</b>	<b>9,6</b>
<b>Singapore</b>	<b>10,0</b>			<b>8,2</b>	<b>9,1</b>	<b>10,0</b>
<b>Indonesia</b>	<b>7.8</b>	<b>10</b>	<b>7.4</b>	<b>6.6</b>	<b>8.0</b>	<b>8.3</b>
<b>Malaysia</b>	<b>8.0</b>	<b>7.3</b>	<b>8.2</b>	<b>6.6</b>	<b>7.5</b>	<b>7.8</b>
<b>Philippines</b>	<b>7.8</b>	<b>8.3</b>	<b>6.7</b>	<b>7.6</b>	<b>7.6</b>	<b>8.7</b>
<b>Thailand</b>	<b>6.8</b>	<b>9.0</b>	<b>6.5</b>	<b>6.4</b>	<b>7.2</b>	<b>7.8</b>
USA	6,7	7,0	9,1	7,4	7,5	9,4
Chile				7,2	7,2	8,4
Switzerland	5,7	5,5	7,4	5,8	6,1	10,0
Hong Kong				8,4	8,4	10,0
Japan	8,6	9,7	7,7	8,8	8,7	9,6
<b>Averages by region (unweighted)</b>						
North America	6,7	8,0	9,2	7,8	8,2	9,6
Latin America	7,7	8,8	6,9	6,5	7,4	7,4
Europe	5,1	6,2	6,7	6,7	6,2	8,7
Pacific Asia	8,2	8,9	7,4	7,5	8,1	9,0
South-East Asia	7,0	9,0	4,9	6,1	6,8	5,9
Africa	6,8	6,7	6,0	7,3	7,3	6,9
<b>Note:</b>						
Number of observations	30	30	28	39	39	39
Minimum index	3,5	3,5	3,0	4,6	5,0	4,0
Maximum index	10,0	10,0	10,0	8,8	9,1	10,0
<i>Source: see Annex A and author's computations. See also Messerlin and Laird (2002).</i>						

The above analysis deals only with trade in goods -- not including services. To construct similar indices for services is not yet possible because of the lack of data in services. However, it can be surmised from our observations that liberalisation of trade in services will need to be a major component of a possible EU-ASEAN FTA for it to be of sufficient interest to the EU. Hence, we return to the issue of international trade in services below; the next Chapter will deal with the likely trade creation and diversion resulting from a EU-ASEAN FTA.

For any EU-ASEAN FTA to be worthwhile it will also have to tackle non-border regulatory issues – from norms to more subtle aspects, such as the remnants of an industrial policy through the Government Linked Corporations (GLCs) in Singapore and Malaysia and the status of State Owned Enterprises in e.g. Vietnam and Cambodia. This aspect has not been taken into account in Table 1 above, but was repeatedly underlined in the recent Trade Policy Review on ASEAN countries carried out by the WTO.

## CHAPTER 2: Trade Creation and Trade Diversion

Preferential trade agreements (PTAs) often raise fears of costly trade diversion. In the case of goods, the EU-ASEAN PTA is likely to generate limited trade diversion between the EU and ASEAN. This is entirely due to the high MFN tariff rates applied by most ASEAN countries, (except Singapore). Slashing these rates with the EU but not with other suppliers will persuade ASEAN consumers to stop buying goods from the rest of the world even if EU producers are less efficient than in the rest of the world. At the same time ASEAN's zero applied tariff rates will *not* ensure European consumers that the products they import from ASEAN are among those the most efficiently produced in the world (since ASEAN producers continue to protect their markets from the most efficient producers in the rest of the world).

This general remark needs several caveats.

- First, ASEAN tariffs in the context of a possible FTA will be *applied* zero rates. The very valuable characteristic of these tariffs to limit risks of trade diversion for both partners would disappear if ASEAN decides to keep the option of using its *bound* tariff rates. A useful FTA provision could thus be a commitment by both parties to bind their tariffs at zero.
- Second, the above assertion of limited risk of trade diversion is based on the tariff level alone. Protection in ASEAN, as in the rest of the world, can also be provided by non-tariff barriers (NTBs). Core NTBs (quantitative restrictions, minima prices, etc.) are quite prevalent in ASEAN's trade regime. The WTO Trade Policy Review on several ASEAN countries, portrays the norms and standards as occasionally discriminatory in intent. If correct, this feature suggests that risks of trade diversion would remain where norms and standards may be de facto discriminatory (except if because of good regulatory reasons).

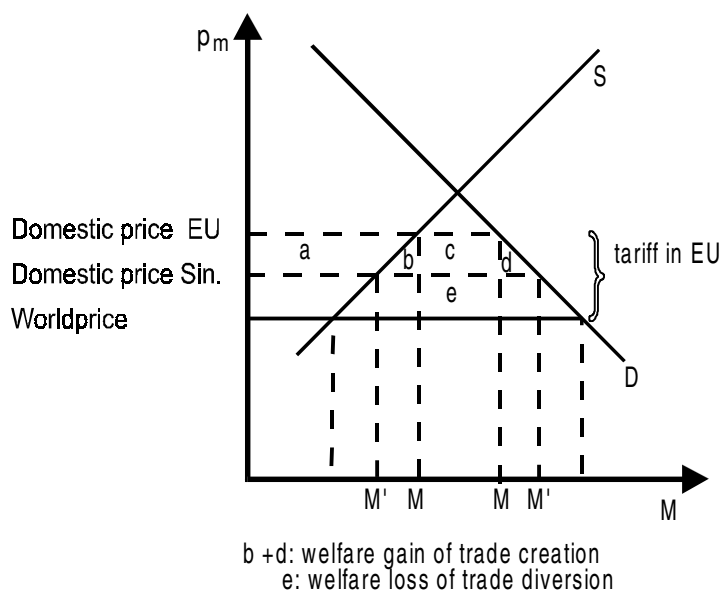
In this chapter we shall examine the scope for trade creation and trade diversion, starting from the standard welfare theory of trade.

### Welfare Theory

The welfare implications of the creation of a FTA between two trading entities, such as the EU and ASEAN, can be understood intuitively by looking at only one product group. Assume that the price level for that product in the EU is higher than in ASEAN, which in turn is above that prevailing in the rest of the world. Prior to the FTA, the EU is levying a non-discriminatory import duty on the product, such that the price of the products coming from the rest of the world, after duty payment, will be equal to the EU price. The products coming from ASEAN would be uncompetitive in the EU market after duty payment. Therefore, prior to the creation of the FTA, all imports of the product at issue in the EU will come from the most competitive suppliers from elsewhere across the globe.

Naturally, a EU-ASEAN FTA implies that no further import duty will be levied by the EU on the product originating from the region. As Figure 1 below illustrates, the EU price of the product will drop to the ASEAN price level. As a result, imports will increase, but now the product from other suppliers in the rest of the world, after duty payment in the EU, will be uncompetitive, as their prices for the EU market are above those from ASEAN. Therefore, the imports that prior to the-FTA came from the 'rest of the world' are now supplied by

ASEAN countries. This is *trade diversion*. Its welfare effect can be measured by the area c in Figure 1.



**Figure 1: Trade creation and trade diversion**

On the other hand, as the price of the product in the EU market is lower than before, part of the former EU supply (i.e. that produced in the EU at a higher marginal cost than the price level after the FTA) will now be replaced by ASEAN imports – a substitution away from EU producers to sourcing from ASEAN. This is *trade creation* and its welfare effect can be measured by the surface of area b in Figure 1. In addition, because of the lower price, consumption in the EU will rise, leading to additional imports from ASEAN and thus further trade creation, the welfare effect of which can be measured by area d in Figure 1.

Standard economic theory on the *static* welfare effects of customs unions and free trade agreements concludes that:

- The welfare effect of *trade creation* will be larger the higher the price elasticities of supply and demand of the products at issue. In terms of the static, single product diagram it will make areas b and d larger for given domestic prices in EU and ASEAN;
- The welfare effect of *trade diversion* will be smaller, the closer the price levels of ASEAN compared to the rest of the world, or in other words, the larger the price differentials between ASEAN and the EU. It will make area e in the diagram larger.

Extensive qualitative and quantitative analysis will be required to assess the likelihood of trade creation and trade diversion in the case of an EU-ASEAN FTA. First needed are estimates of the price-elasticities, describing the slope of the demand and supply curves, as well as indicators of world price levels, ASEAN price levels and tariff and non-tariff barriers applied. EU statistics to assess the importance of bilateral trade flows between the EU and ASEAN, as well as between the EU and the rest of the world, will be required at a sufficient

level of product disaggregation. Moreover, one needs to estimate EU-ASEAN price elasticities in the short and the long run. Regarding price levels, one may use the implicit price indices in the EU external trade data or OECD Trade by Commodities data. By dividing, at a sufficiently disaggregated product level, the value of EU imports from ASEAN and/or other countries/parts of the world by the corresponding volume, we can construct time series, which allow us to compare changes in the relative price levels of the EU with ASEAN as well as the rest of the world. Experience shows that there are, however, serious calculation problems involved.<sup>3</sup> Furthermore, ASEAN prices still have to be increased with the tariff duties applied in the EU.

Finally, one also needs a measure of the tariff equivalent for the EU's non-tariff barriers (NTBs), at a sufficiently level of product group disaggregation. Whereas the average tariff duties data can be constructed quite readily, there are huge problems to estimate tariff equivalents of NTBs; often one can not do more than merely indicate the main types of BTBs which are likely to apply. Finally, an important element to be noted concerns the impact of the rules of origin that apply to EU imports. These can also quite dramatically change the picture.

The likelihood of trade creation and trade diversion can tentatively be assessed as follows:

*Unit value ASEAN prices compared to EU*

	<b>Higher</b>	<b>Lower</b>
<b>Higher</b>	No Trade diversion; No Trade creation	Trade diversion+Trade creation in EU
<b>Lower</b>	Trade diversion + Trade creation in ASEAN	Trade creation

*Unit value EU prices compared to the rest of the world:*

**Diagram 1: Trade Creation and Trade Diversion**

If prices in the EU compared to the rest of the world are high, and prices in ASEAN compared to the rest of the world are low, a FTA will evidently lead to both trade creation in the EU and trade diversion in favour of ASEAN. In the reverse case, there will be trade creation in ASEAN and trade diversion in favour of the EU. If both prices in the EU and in ASEAN as compared to world prices are low, this will rather lead to trade creation, without much scope for trade diversion, given the competitive position of both the EU and ASEAN in the world market for that product group.

However, diagram 1 implicitly assumes looking at the EU as a fully integrated single market. This ignores some basic realities: the EU market place is still segmented in important ways based on national borders. To some extent this reflects remaining technical and other standards, labelling requirements, etc., but also differences in production methods and

<sup>3</sup> The relative unit value (RUV) of each sector will need to be calculated as the ratio of the average unit value of exports for a country to the world average unit value. The price level in the world is the reference point, and the average RUV is therefore equal to 1. If the RUV is below or above unity, then the country exports its product at a lower or higher price than the world average unit price. The comparison of unit values for homogeneous products gives an indication of exporters' relative prices. However, as the new theories of international trade emphasize rightly, products are differentiated by quality, which is usually reflected in differences in price (ITC, 2000).

efficiency, market segmentation strategies of the producers, cultural differences, etc. Hence, EU data by member states indicate a range of relative unit values – not a single value. For our analysis this means one should also to look at cases where ASEAN's relative prices lie *within* the range of relative prices characterising the EU – above those of some countries and below those of others.

Similarly and much more pertinently, the ASEAN market is not at all integrated. There is enormous diversity within the ASEAN, both from the production as well as from the consumption point of view. This will inevitably have major implications for the approach to an inter-regional FTA. The effects are bound to be different for Singapore as compared with Laos PDR.

Given that tariff removal alone is unlikely to generate substantial economic benefits, then a free trade agreement between the EU and ASEAN will have a significant impact upon trade in goods only if it goes deeper and addresses 'behind the border' issues. In the next chapter we turn to the issues relating to technical barriers to trade and sanitary and phyto-sanitary measures as these influence the patterns and levels of international trade.

### **CHAPTER 3: Technical Barriers to Trade**

Technical barriers to trade (TBTs) can arise whenever a producer may have to alter his/her product in order to comply with differing partner country requirements such as for health, safety, environmental and consumer protection. Both governments (technical regulations) and non-governmental organisations (non-regulatory barriers, standards) can impose these requirements. The legal character of technical regulations distinguishes them from non-regulatory barriers or standards; namely, the latter are voluntary, not legally binding and arise from the self-interest of producers or consumers involved, for example, to improve the information in commercial transactions and ensure compatibility between products. The former mainly relates to either technical specifications or testing and certification requirements that ensure that the product complies with the relevant specifications (conformity assessments).

The need to adapt product design, re-organise production systems, and satisfy multiple testing and certification procedures can entail a significant cost (or technical trade barrier) for suppliers of exported goods to a particular country, the magnitude of which is likely to differ according to the nature of products, for example, the extent to which they pose a risk to users. The removal of TBTs is a central element of the Single Market of the EU, since it is crucial for the free movement of goods throughout the whole of the European Economic Space. The removal of such barriers will tend to promote trade and efficiency and serves to strengthen competition by undermining the fragmentation of markets.

#### **Removing Technical Barriers to Trade.**

EU policy related to standards, testing and certification requirements is currently based upon two approaches: enforcement of the principle of mutual recognition and if this fails, the harmonisation of technical standards in each member country. Application of mutual recognition requires a degree of trust between countries and regulatory authorities. It is based on the idea that products manufactured and tested in accordance with a partner country's regulations can offer equivalent levels of protection to those provided by corresponding

domestic rules and procedures. However, this tends to require accreditation of testing and certification bodies under what is known as a mutual recognition arrangement (MRA) between bodies because member states often regulate for the same product risks in slightly different ways (or in the same way but requiring duplication of conformity assessment). Mutual recognition tends to work where products are new and specialised and, as such, it seems to be relatively effective for equipment goods and consumer durables, but it encounters difficulties where the product risk is high and consumers or users are directly exposed to that risk.

Where ‘equivalence’ between levels of regulatory protection embodied in national regulations can not be assumed, the EU approach to removing technical barriers to trade is for the member states to reach agreement on a common set of legally binding requirements. Subsequently, no further legal impediments can prevent market access of complying products anywhere in the EU market. EU legislation harmonising technical specifications has involved two distinct approaches, the ‘old approach’ and the ‘new approach’. The old approach mainly applies to products (chemicals, motor vehicles, pharmaceuticals and foodstuffs) by which the nature of the risk requires extensive product-by-product or even component-by-component legislation and is carried out by means of detailed directives.

In the main achieving this type of harmonisation has been slow for two reasons. First, the process of harmonisation became highly technical, with attention being given to very detailed product categories including components. This resulted in extensive and drawn-out consultations. Secondly, the adoption of ‘old approach’ directives was based on unanimity in the Council, which means that the issuing of directives is a slow process. The limitations of this approach as a broad tool for tackling technical barriers to trade become clearly apparent in the 1970s and early 1980s when new national regulations were proliferating at a much faster rate than the production of European directives harmonising regulations.

These weaknesses have been addressed through the adoption of the ‘new approach’ whereby EU directives only indicate the ‘essential requirements’ that must be satisfied which leaves greater freedom to manufacturers as to how to satisfy those requirements, dispensing with the ‘old’ type of exhaustively detailed directives. The new approach also provides for more flexibility than the detailed harmonisation directives of the old approach by using the support of the established standardisation bodies, CEN, CENELEC and the national standard bodies, such that the satisfaction of the relevant standards is presumed to entail consistency with the minimum requirements in the legislation. New approach directives are adopted by a qualified majority in the Council.

### **Technical Barriers to External Trade.**

In addition to pursuing the removal of technical barriers to trade on internal trade within the Union, the EU has also sought to sign bilateral agreements with third countries. The free trade agreements with the Central and Eastern European countries contain provisions by which these countries agree to progressively adopt EU standards and regulations and harmonise their testing and conformity systems with those of the EU. This process is taking place very much in the context of accession to the EU.

Elsewhere the EU has sought to sign bilateral mutual recognition agreements relating to conformity assessment procedures, consistent with the WTO agreement on Technical Barriers

to Trade, such that products from the partner country can be assessed for conformity with EU regulations in the testing facilities of that country. Similarly EU exports can be tested for conformity with the partner countries regulations in EU accredited testing establishments.

In contrast, one may look at the example of the exportation of medicinal products from ASEAN, in particular the bulk pharmaceuticals (“Active Pharmaceutical Ingredients”) manufactured by several leading EU TNCs. For example, Singapore’s membership of the Pharmaceutical Industry Committee on Standards (PICS) – essentially a voluntary industrial cooperation that is not legally binding – facilitates exports of API to the EU. However, despite the certification and testing which takes place at the production place, some EU Member States still require re-testing of all batches of API before the product can be allowed into the country.

To date the EU has signed agreements with the US, New Zealand, Australia and mostly recently in April 2002 with Japan. These agreements are confined to particular sectors and in the main the sectors covered by new approach directives (or a subset of those sectors).

**Table 2: The Importance of Products Subject to Harmonised EU Regulations in EU Imports from Selected Asian Countries**

	Japan	Korea	Philippines	Malaysia	Indonesia	Singapore
<b>Old Approach</b>	<b>29.52</b>	<b>20.13</b>	<b>2.18</b>	<b>2.74</b>	<b>3.97</b>	<b>9.19</b>
<b>New Approach</b>	<b>15.86</b>	<b>16.49</b>	<b>25.26</b>	<b>22.20</b>	<b>5.27</b>	<b>22.12</b>
<b>Of which:</b>						
Machinery	4.2721	0.7798	0.8051	1.2574	0.6761	1.50
Electromagnetic	8.6028	9.4566	20.3563	14.6544	1.9657	13.08
Low Voltage	1.3326	0.4865	1.0699	1.0638	0.4142	2.26
Medical devices	1.1191	0.4030	0.0188	0.6104	0.1940	0.57
Packaging	0.0208	0.0223	0.0088	0.0268	0.0262	-
Pressure equipment	0.0994	0.0275	0.0000	0.0202	0.0014	-
Telecoms terminal equipment	1.2539	5.9381	3.5405	5.8655	0.1652	-
Active implantable medical devices	0.4092	0.0232	0.0048	0.1666	0.0119	0.91

Source: Brenton et al. (2001).

### Rules of Origin

Finally, in this section we also suggest that rules of origin could be an important element in a MRA between the EU and ASEAN. If ASEAN (or some Member State) has a comparative advantage in testing and laboratory facilities and is well endowed with professional staff in this activity then an MRA could help to establish or enhance the position of ASEAN as a regional hub for testing and conformity assessment for products from the whole of the region being exported to the EU. Rules of origin which restrict the testing and conformity activities

to products produced only in ASEAN would tend to constrain such a development.<sup>4</sup> Again the presence of EU service companies in ASEAN is an issue to consider. Many EU companies active in the fields of ‘research and testing’ are covering general research, soil exploration and analysis, oceanography, materials testing and quality control. An MRA would enable them to operate directly for the EU market from an ASEAN base.

By way of comparison we note the importance of products covered by new approach directives, and hence those that could be covered by an MRA, in EU imports from other Asian countries (Table 2). Such products account for one quarter of EU imports from the Philippines, 22 per cent of imports from Malaysia and around 15 to 16 per cent of imports from Japan and Korea. For Indonesia, new approach products account for a much smaller share of EU imports, just over 5 per cent in 2000. The table shows that again the key directives are those that relate to machinery and equipment; with electromagnetic compatibility being most important followed by machinery, low voltage and telecoms terminal equipment. This highlights firstly, the potential impact that the MRA with Japan could have on the exports of ASEAN to the EU if it leads to significant reductions in the costs of selling in the EU. Secondly, it shows the potential importance of an MRA with ASEAN with less restrictive rules of origin.

Along similar lines, a free trade agreement with ASEAN would be particularly attractive to the EU if a mutual recognition agreement on testing and conformity assessment were to provide for more effective access for EU producers of new approach products to neighbouring Asian countries. The ability to test products on a regional rather than individual market basis is likely to offer substantial gains to EU producers.

### **Sanitary and Phyto-sanitary regulations**

Similar to technical regulations the EU operates an elaborate system of sanitary and phyto-sanitary regulations (SPS) to ensure product quality and standards with respect to quality, hygiene, food safety, avoidance of environmental impact, pests and disease, etc. Most of these are particularly relevant to EU-ASEAN trade as the SPS regulations focus primarily on agricultural products.

For example, tropical cut-flowers, such as orchids, to be traded through the highly efficient EU-based flower auctions (e.g. in Aalsmeer, the Netherlands) for consumption within the EU or onward trade to, for example, the US markets, they need to meet very stringent SPS regulations. A protocol on this could define mutually agreed certifiable procedures to ensure that fumigation against pests can be carried out speedily, reducing time-in-transit and thus making the most of the precious life span of such tropical flowers from (some of the) ASEAN countries such as suppliers of tropical cut-flowers like Thailand or Malaysia.

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<sup>4</sup> In general, less restrictive rules of origin for mutual recognition of testing could have advantages for ASEAN (greater scope) as well as for the EU (reducing duplication). The disadvantage relates to lesser control over processes at the production stage increasing potential risks.

## Chapter 4: EU-ASEAN Trade in Services – a preliminary analysis

ASEAN is increasingly a service economy, whereas this is already the largely case for the European Community. The General Agreement on Trade in Services (GATS) is the first multi-lateral agreement covering international trade in services. GATS categorised international trade in services between WTO members according to four modes of supply of a service

- cross border supply from one territory into another;
- consumption abroad where a consumer utilises a service in the territory of another WTO member;
- commercial presence where a service supplier operates in the territory of another WTO member; and
- movement of natural persons where a natural person supplies a service in the territory of another WTO member.<sup>5</sup>

In short, the GATS definition is based on nationality, rather than on residence. In effect, the IMF standard definition does not cover trade resulting from commercial presence. Moreover, the IMF definition covers only part of the trade generated by the movement of natural persons – once a person working abroad has become a resident, he/she ceases to be considered as generating an internationally traded service. However, the GATS definitions and concepts would include those two examples.

ASEAN needs to make considerable efforts to improve the description of its international trade in services by adopting, to the extent possible, the ‘new’ definitions of trade in services. The international standard for recording of trade in services remains the IMF’s Balance of Payment Manual which records transactions between ‘residents’ and the rest of the world (non-residents). Some eleven categories of trade in services are classified, including transportation, financial services, etc.<sup>6</sup>

The stylised facts of ASEAN’s trade in services vis-a-vis the EU are not well documented. Below we summarise these for one ASEAN member state, but it is emphasized that even for Singapore the present statistical database of internationally traded services is inadequate and further research is absolutely essential.

### Stylised facts of EU-Singapore Trade in Services

Preliminary estimates for the 1999 flows in international trade in services revealed the following stylised facts:

- The EU was in deficit vis-à-vis Singapore to the tune of Euro 1.23 billion;
- The lion-share of both exports and imports were in the transportation sector, which covers freight, the carriage of passengers as well as auxilliary services, including port

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<sup>5</sup> Some examples of each mode of supply may help to clarify the distinction: cross border supply covers the international transportation of goods, consumption abroad includes tourism, a branch of a foreign bank trades through commercial presence and on-site development of software and other forms of technical assistance by foreign consultants is trade through the movement of natural persons.

<sup>6</sup> The eleven major components are (i) Transportation, (ii) Travel, (iii) Communications, (iv) Construction, (v) Insurance, (vi) Financial, (vii) Computer and Information, (viii) Royalties, (ix) Social, (x) Government and (xi) Other Business Services which include trade-related, business management, legal, accounting, architectural, advertising, engineering, research and development.

- services. For 1999 nearly 60 per cent of the imports and exports were in this sector and the EU's trade deficit amounted to Euro 760 million;
- Business services were the second largest component of trade (approximately 15 per cent) with the EU running a deficit in excess of Euro 170 million; these services tends to take the form of EU MNCs supporting subsidiaries in their Singaporean and regional operations;
  - Trade-related services were the third largest component, in particular merchanting, communications as well as chartering without crew.<sup>7</sup> EU trade deficits in these sectors at Euro 211 million exceeded those for business services, even though turnover in this sector was much smaller;
  - Even in the financial and insurance services, the EU only realised a deficit of Euro 86 million;
  - Finally, royalty payments were the only sector for which the EU realised a small trade surplus of Euro 82 million, though not enough to balance out the trade deficit incurred for technical services at Euro 83 million.

Furthermore, the role of the EU relative to the other major locomotive economies US and Japan leaves much to be desired. In 1997 the US realised a surplus of US \$ 0.7 billion on its trade-in-services account with Singapore, while all other main trading partners realised a trade-in-services deficit. US and Japanese deficits for transportation services were well below those of the EU, while the EU stood second after Japan for the purchase of trade-related services..

In summary, trade-in-services would appear to be a sector where the EU could potentially benefit from an FTA, provided that the precise terms of such an FTA would address the question of reducing barriers to trade in services and therewith realise efficiency gains for EU businesses. But liberalising services is a very difficult exercise for several well known reasons:

- services are delivered through cross-border trade, but also—above all at this stage of the world economy—through establishment, hence through foreign direct investment (FDI);
- barriers to market access in services exist at the borders and behind the borders;
- the protectionist impact of barriers is often difficult to assess and difficult to be dealt within the traditional WTO negotiating framework of reciprocal concessions.

In addition, regional liberalization in services is an exercise much more complex than its equivalent in goods. For all these reasons, this chapter aims ' just' at spelling out the main issues than at providing robust empirical evidence on the level of protection in ASEAN countries.

### **Negotiating with the EU in services**

The main goal of the EC “Single Market Programme” (SMP) launched in 1985 was to liberalize the European markets in services. However, for reasons mentioned at the start of this section (complexity of the instruments used for protecting services, inoperability of the traditional concepts of negotiations, such as reciprocity, in services), the Single Market in

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<sup>7</sup> Merchanting is the purchase and resale of goods by residents of the compiling economy without the good concerned entering or leaving Singapore.

services has still to come [Messerlin, 2001]. Barriers within the EU regarding services of foreign origin are still considerable too, as elsewhere in the world, and often differ between EU member states. Numerous examples may serve to illustrate this reality.<sup>8</sup>

Recent research from the OECD Secretariat allows one to get a more quantitative assessment of how much the SMP has really worked so far. Based on an international database on the regulations enforced in OECD countries, it provides indicators (from least (0) to most (6) restrictive) of regulatory and market environment in 1998. The seven services examined by the OECD research and shown in Table 3 allow to take into account the complexity of the SMP process: two services (air passenger and road freight) are included early in the SMP (late 1980s); two others (mobile and fixed telephony) have been incorporated late in the SMP (early 1990s); two others (electricity and railways) have been covered by SMP extensions (mid-late 1990s); lastly, retail distribution is not part of the SMP. Of course, such an exercise has strong limits: incomplete and imperfect information is a pervasive problem, assessing the effect of regulations on the degree of competition is a matter of delicate judgment, etc. However, statistical techniques allow to get interesting comparisons between countries from this (admittedly imperfect) large set of information.

Table provides two major lessons useful for negotiators launching liberalization in services. First is that the EU does not appear, on average, more open than the “rest of the OECD countries” (defined as the OECD countries not pertaining and not candidate to the EC) in all these sectors. Second, the indicators of the various EC Member states do not show the similarity which would reveal a strong impact of the SMP: certain Member states are still among the most open markets in the OECD region, whereas others are still among the most closed ones. These results are observed whether examined services have been subjected to the SMP or not, since a long time or not.

The OECD studies provide additional results in three services for which it has been possible to generate an “external liberalisation” element. In air and road transport, “barriers to entry” have been split into a component of public intervention in domestic markets and an element of “discrimination against foreign providers.” The EU exhibits a smaller indicator for foreign discrimination than the “rest of the OECD countries” in air transport only. However, this result (which mirrors SMP-related legal aspects such as the definition of what an EC carrier is) is more than compensated by a higher indicator for domestic entry barriers. In telecoms, estimated price deviations (from the OECD average) for each country have been decomposed into several components, including a foreign discrimination element. This exercise presents the EC member-states on average more homogeneous than suggested by Table -- and less expensive than the rest of the OECD countries. However, this result is not related to the liberalisation component, but to an element (the country economic structure) which captures, among other factors, the impact of technical progress.

This is very useful for negotiating purposes. First, it shows that negotiating liberalization in services with the EU should fully take into account member-states specificities. Negotiations

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<sup>8</sup> Under legislation enacted in the early 1990s, the French government requires non-EU lawyers to qualify as “avocats,” on the basis of full-fledged membership in the French bar. Legal consulting service providers in foreign and international law are required to be licensed in French law. Non-EU firms are not permitted to establish branch offices in France under their own names. Also, foreign lawyers and firms are not permitted to form partnerships with or hire French lawyers. The “legal consultant” category of lawyer no longer exists in France. It is important to note that other EU Member States have comparable regimes, creating significant barriers to trade within the EU as well as to non-EU resident firms.

should be as intensive with key member-states (which depend from the service sectors considered) as with the European Commission. Second, the EU will also gain a lot from liberalization in services since its services are also relatively severely protected.

These remarks deserve a caveat. Views strongly diverge about the costs and benefits of a PTA in services. It is often argued that trade diversion with a PTA in services may be more frequent and its costs larger than in the case of trade in goods. The reason would be the same than the above-mentioned possible role of NTBs in trade diversion since regulations in services may be interpreted as potential NTBs. There is thus a warning signal for negotiators. They should be careful not to create entrenched discriminatory situations for the EU and ASEAN service providers at the detriment of European and ASEAN consumers.

### **Restrictions on Foreign Investment**

A further study by the Australian Productivity Commission examines the degree of restrictions on Foreign Direct Investment across Southeast and East Asia, looking at five types of restrictions:

- foreign equity limits on all firms;
- foreign equity limits on existing firms;
- screening and approval of foreign investment;
- control and management restrictions; and
- input and operational restrictions.

Comparative indicators are constructed for selected ASEAN countries as well as the Hong Kong, the US and Australia, drawing on data from the APEC Action Plans as well as the countries' commitments under the GATS. An index is constructed with a range from 1 (where no foreign equity is permitted in the sector) to 0 – when there are no restrictions on FDI in any of the five areas mentioned above.

In general, it is found that communications, financial services and transport are 'subject to relatively stringent FDI controls' (APC, p 108). The results for selected ASEAN countries (Singapore, Philippines and Thailand) are compared to those of another major regional major player Hong Kong. The United States is introduced for reference in the absence of a similar index for the European Union. In summary, the table indicates that FDI restrictions in Singapore are much less than those of other ASEAN countries such as the Philippines or Thailand. However, if Singapore is compared to Hong Kong, one finds that in all-but-two services sectors the restrictions are greater than those in Hong Kong. The two exceptions are postal services, where foreign equity is not allowed in any of the countries reviewed including the US, and insurances, where FDI restrictions are less.

If one compares Singapore with the US regime, one finds that it is more restrictive in all services sectors, even though Singapore has the most liberal regime within ASEAN. In summary, these results would appear to reinforce our observation, made in the context of trade in services, that an FTA in this services sector which includes further reductions on FDI restrictions could offer positive benefits to EU investors.

<b>Table 3: FDI Restrictiveness Indices in ASEAN (Selected Countries) – GATS Service Sectors</b>					
	<b>United States</b>	<b>Singapore</b>	<b>Hong Kong</b>	<b>Philippines</b>	<b>Thailand</b>
Business	0.005	0.261	0.015	0.479	0.775
Communications	0.345	0.518	0.350	0.758	0.838
<i>Postal</i>	1.000	1.000	1.000	1.000	1.000
<i>Courier</i>	0.000	0.250	0.000	0.475	0.775
<i>Telecommunications</i>	0.200	0.571	0.200	0.975	0.804
<i>Audiovisual</i>	0.180	0.250	0.200	0.580	0.775
Construction	0.000	0.250	0.000	0.475	0.775
Distribution	0.000	0.250	0.050	0.475	0.775
Education	0.000	0.250	0.000	0.475	0.775
Environmental	0.000	0.250	0.000	0.475	0.775
Financial	0.200	0.378	0.233	0.954	0.875
<i>Insurance and related</i>	0.000	0.250	0.400	0.975	0.775
<i>Banking and other</i>	0.400	0.506	0.067	0.933	0.975
Health	0.000	0.250	0.000	0.475	0.775
Tourism	0.000	0.317	0.000	0.808	0.775
Recreational	0.000	0.250	0.000	0.475	0.775
Transport	0.025	0.250	0.093	0.975	0.780

Source: Australian Productivity Commission, 2001.

### **Broad Agenda Issues: Intellectual Property, Public Procurement and Competition Policy**

The discussion about services serves to illustrate that a possible EU-ASEAN FTA would need to tackle ‘broad’ issues of public procurement, intellectual property and competition policy. The EU-Chile FTA draft agreement demonstrates that a ‘broad’ agenda can be pursued successfully in the context of a FTA. In the opinion of this author, the central issue is the adoption of a competition policy by ASEAN that goes beyond the present disciplines of the WTO, which focus primarily on the avoidance of import and export cartels. We shall deal with the three broad issues in turn.

*Intellectual Property Rights.* IPR policy issues relate to the desirable time table for the adherence to existing and currently negotiated international conventions and legislative change to introduce these into force. For example, in the case of EU-Chile it is proposed that Chile will adhere, by the date of enforcement of the FTA, to the Paris Convention on Industrial Property, Berne Convention on artistic and literary works, Rome convention on performers, phonograph and broadcasting and the Convention on protection of new variety of plants.<sup>9</sup> However, some ASEAN countries do not yet pursue a ‘strong’ IPR regime and hence could consider becoming a member of WIPO, a party to the Paris Convention, the Patent Cooperation Treaty, etc. It is therefore likely that there could be a great deal of fruitful negotiation between the EU and ASEAN on issues of IPR and possible adherence to future conventions.

<sup>9</sup> Further commitments regarding Chile’s adherence to conventions at later dates are indicated in the Annex Table on EU-Chile FTA.

*Public Procurement.* Public procurement in ASEAN is carried out by individual ministries, department and statutory bodies. Only a few Member States of ASEAN acceded to the WTO Agreement on Government Procurement in 1997 and has implemented its provisions through the Government Procurement Act of 1998. At the procedural level the EU and ASEAN share a well-defined view with regard to the necessary transparency and the need for national treatment of foreign suppliers. However, in Cancun the differences of perception were brought out in the open.

*Competition Policy and Law.* Most ASEAN countries do not at present have a competition law, although a proposal is under consideration by for example the Thai Government. The possible introduction of a competition law raises a question – does openness to trade not provide a sufficiently effective mechanism?<sup>10</sup> In most of ASEAN competition is regulated at the decentralised level of the statutory boards, which have oversight and monitoring responsibilities and are knowledgeable and familiar with the specific sector market structure.

The EU viewpoint on competition policy is that the core competition principles on transparency, non-discrimination, procedural fairness and recognition of the costs of cartels are best realised through a legal framework implemented by an independent competition agency with an overview and responsibility of the economy as a whole. The objectives of the legal framework will include both economic efficiency as well as consumer welfare and hence a competition law is bound to interface with other regulatory processes, in particular regarding trade and investment policy, consumer protection and anti-corruption. Whether the appropriate legal approach is *ex ante* prescriptive (identifying unfair trade practices, bid rigging, etc) or *ex post* remedial (responding to complaints of business and demands of consumers) is a matter of judgment. The studies of EU investment in financial services in ASEAN as well as the latter's investments in EU demonstrate clearly that issues of competition are at the heart of the investment decision. Hence, a possible EU-ASEAN FTA would benefit from including a commitment to the introduction of a competition policy which sets out mutually agreeable disciplines and practices.

Finally, a possible EU-ASEAN FTA would also need to spell out the provisions for dispute settlement especially for those issues which are beyond the competence of the WTO dispute settlement system. Again the EU-Chile FTA agreement would appear to offer a useful template .

## **CHAPTER 5: Risks of an EU-ASEAN Free Trade Agreement**

In short, the business case for a EU-ASEAN FTA does indeed appear quite compelling, provided that the negotiations focus and successfully conclude in those areas where EU has significant interests already, in particular trade in services. But what are the risks for the European Union to engage into negotiations with ASEAN with the aim to achieve such an agreement?

According to author, the risks relates to a possible disturbance, which such a bi-lateral approach may cause to the already fragile EU-ASEAN relations and/or relations with other Asian developing countries. A 'fear' has been expressed by some in ASEAN countries that

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<sup>10</sup> For a summary discussion of this and related issues see 'Challenges in Implementing a Competition Policy and Law: An Agenda for Action', CUTS, New Delhi, 2002.

only some ‘fast-track’ countries will benefit from a FTA with the EU to the detriment of other ASEAN countries (Cambodia, Laos and Vietnam).

Above we have doubted the argument that any major trade diversion may result from a possible EU-ASEAN FTA. Nevertheless, populist voices may suggest that a FTA will mean that EU products will ‘flood’ the entire ASEAN regional markets. This perception is wholly unjustified because EU products imported into ASEAN will have to comply with the AFTA standards, rules of origin, etc. even if the tariffs are zero. In general, the asymmetries are more likely to favour an expansion of net ASEAN exports to the EU rather than vice versa.

Hence, the opportunities for ‘sourcing’ from within the ASEAN countries as well as any amendments to allow a flexible application of the rules of origin for selected sectors (eg electronic products and components) should deserve careful consideration.

Conversely, some populist voices may argue that an EU-ASEAN FTA will be a circuit for ‘flooding’ the EU markets with goods produced in e.g. China. To address this it will be important to devote attention to the rules of origin in the AFTA agreement as well as in the EU-ASEAN agreement. Products that have acquired ASEAN origin under AFTA and are traded by any ASEAN country can enter the EU benefiting from preferential treatment. However, if the relevant EU rules of origin are very restrictive, this will limit the trade benefits which ASEAN countries could realise.<sup>11</sup> As a result of present rules of origin it is quite unlikely that products which have been produced in China but received some very limited processing in, for example, Indonesia or Cambodia will qualify for preferential duty access. Specific exceptions may have to be considered to extend the benefits of a possible EU-ASEAN to other countries within the region – but these could be limited to named countries and sectors. At the same time, the rules of origin should enable growth and development opportunities to the ASEAN countries.

In assessing the risks of bi-lateralism and inter-regionalism jeopardising multi-lateralism, due cognisance will have to be given to the present policy shifts regarding this approach across East and South East Asia. In particular Japan has post-Seattle moved its external trade policy into a ‘multi-layered approach’. For Japan, as for the European Union, the WTO remains the essential foundation for a free trading system with its 144 members. Japan, like the European Union, also remains active in the promotion of flexible cooperation schemes like the ASEM and, in the case of Japan, the APEC. Nevertheless, Japan has increasingly moved to assess the scope and implications of possible ‘comprehensive economic partnerships’ with other countries too. Present initiatives for such a bilateral cooperation, following the conclusion of the Japan-Singapore Economic Partnership Agreement early 2002, focus on e.g. Japan-Mexico. This new-found enthusiasm for bilateral ties is partly in response to the drive towards an ASEAN-plus-Three and for a possible China-ASEAN free trade agreement.

Studies on FTAs commissioned by Japan’s Ministry of Economy, Trade and Industry (METI) focus on bilateral economic relations with Mexico (since 1999); Republic of Korea (since 2000); Chile and ASEAN (since 2001) and since Feb 2002 on Japan-ASEAN.<sup>12</sup> It is too early

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<sup>11</sup> According to the EU GSP products shall be considered as originating in a beneficiary country if (i) the product is wholly obtained in that country, or (ii) products obtained in the country in the manufacture of which products are used which have undergone sufficient working or processing. The EU also provides for regional cumulation of preferences, across ASEAN countries, subject to specific rules on processing and a minimum percentage of the ex-fob price which has been generated in the regional grouping of countries.

<sup>12</sup> Presentation by staff economist of the Trade Policy Bureau, Ministry of Economy, Trade and Industry at the 5<sup>th</sup> Global Conference on Global Economic Analysis, June 5-7, Taipei, Republic of China.

to say to what extent these studies will indeed provide intellectual and empirical support for the view that RTAs will be stepping stones for global trade liberalisation. Some recent studies argue that ' East Asian Regionalism' may be not necessarily be the most efficient (for a brief summary see the annex). Undoubtedly, Japan and China may stand to gain more from global trade liberalisation with improved access to large markets such as the United States and EU. Even if inter-regional trade liberalisation is only a ' second best'- a position which is a matter of ongoing controversy -- the first best outcome of global trade liberalisation may simply not be on offer in the short to medium run post-Cancun.. In the face of this reality, one could argue that an absence of the EU in the development of these new 'manifestations of regionalism' in Asia, while the US, Japan, China and others actively participate would not be in the best interest of EU business.

Finally, the Doha Development Agenda has become the *leitmotiv* of multi-lateral trade talks for the coming years – and will remain so despite the failure at Cancun. The EU's support to this agenda would be underscored by a commitment, in principle, to extend benefits negotiated with Chile also to ASEAN and progressively to other Doha signatories. Pluri-lateralising the 'positive externalities' of an EU-ASEAN FTA towards other credible partners could be a stepping stone towards the inter-regional and multi-lateral levels. This would amply justify the EU's engagement at an inter-regional level.

## Chapter 6: Conclusions and Recommendations

This section will conclude with a matrix table of the main areas to be included in a possible EU-ASEAN FTA as well as an informed guess of the EU and ASEAN perspectives and interests for these areas. But first we recapitulate the main observations of this report in the following six points:

- EU business is prominent and profitable in ASEAN and a possible EU-ASEAN FTA can enhance that prominence, whereas non-participation of the EU in ASEAN's bilateral FTA strategy will put its business at a disadvantage vis-à-vis the US, Australia and Japan;
- ASEAN international trade policy regime for goods is characterised by a moderate openness, but significant restrictions remain on FDI and establishment, impacting in particular on trade in services
- Significant gains can be realised through a EU-ASEAN mutual recognition agreement on conformity assessment, avoiding wasteful re-testing and facilitating the acceptance of EU standards
- Further significant gains can also be realised through the liberalisation in the services sectors, enhancing further EU commercial presence and compensating the EU deficit in trade in goods; realising these gains will also require commitments by ASEAN in the areas of public procurement and competition policy
- The risk that a inter-regional agreement would disturb the already fragile EU-ASEAN relations can best be addressed through (i) provisions and amendments to rules of origin to facilitate regionally integrated sourcing for selected sectors and countries; and (ii) outright excluding countries which do not comply with minimum standards in the fields of human rights and democratic governance .

<b>Table 4: EU-ASEAN FTA: Issues for Negotiation</b>			
	<b>EU Perspective and Interests</b>	<b>ASEAN's Perspectives and Interests</b>	<b>Remarks and Recommendations</b>
<b>Tariff Elimination</b> -Agricultural Goods  -Industrial Goods	Ensure minimal impact on domestic producers  Small loss of tariff revenue; welfare gains likely to accrue intra-firm and through consumer surplus	Extremely varied and divergent interests between Member States  Considerable gains to foreign and national producers	Exclude agriculture from negotiations all together???  Moderate scope for trade creation; some limited trade diversion to be expected
<b>Reduction of Non-Tariff Barriers to Trade in Goods</b> - Technical Regulations  - SPS	Promote use of EU standards  Ensure environmental and food safety from consumer's perspective	Promote research and testing capability across several centres in ASEAN  Scope for limited trade creation	EU-Japan MRA could be starting point; narrowly focus on key regulations and products for ASEAN  Select list of key -products and focus on these only, excluding others
<b>Trade in Services</b>	Further reduce restrictions on establishment and FDI  Obtain additional licenses in banking, insurance, airlines and other sectors  Attract inward ASEAN FDI	Attract SME and TNC inward investment  Develop own stock of intellectual property  Maintain financial market stability  Support internationalisation strategy of selected Asian TNCs	Harmonise EC's WTO-GATS requests and EU-ASEAN FTA Agreement  Ensure parity of EU with US, Japan and Australia
<b>Broad Agenda Issues</b> - public procurement  - competition policy	Define status of GLCs and SOE across ASEAN  Address excessive cartelisation and promote EU practices	Maintain 1998 status quo  Maintain informal ex-post remedial approach	Ensure WTO-plus character  Ensure WTO-plus character
<b>Technical Working Groups covering:</b>	Statistical data base for Trade in Service flows	Global and regional economic impacts of ASEAN's and East Asian bi-lateral strategies	Ensure independence of analysts

*Brussels, February, 2004*

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## Annex A: Highlights of EU-Chile FTA Agreement

Area	Key Features
1. Services (General)	<ul style="list-style-type: none"> <li>♣ The four modes of services supply in GATS are included.</li> <li>♣ Coverage excludes financial services (see separate chapter), audio-visual services, internal maritime transportation and air transportation (aircraft maintenance, commercialisation of air services and reserve computing system not excluded)</li> <li>♣ Parties will review agreement after 3 years of enforcement. Review of mode 4 of service supply will take place after 2 years.</li> <li>♣ International maritime transportation and telecommunications services are subject to particular regulations.</li> </ul>
2. Financial Services	<ul style="list-style-type: none"> <li>♣ Coverage includes banking services (administration and operation of current accounts, receipt of deposits and credit grants and issue of credit cards), insurance (general and life) and administration and intermediation of values (intermediation of stocks and bonds and portfolio and mutual funds management)</li> <li>♣ Excludes financial services derived from the activities of the monetary authority and the social security institutions.</li> <li>♣ The Parties keep the capacity to adopt, for prudential reasons, measures for the operators' protection that regulate the establishment of the other Party's providers.</li> </ul>
3. Investments (Goods)	The Parties acknowledge their commitments in Bilateral Agreements of Promotion and Protection of Investments signed between Chile and the EU Member Countries. (Agreements signed to this date)
4. Intellectual Property	<p>The International Conventions to which the Parties will adhere to are:</p> <ul style="list-style-type: none"> <li>♣ Those signed at the date of enforcement: TRIPS, Paris Convention on Industrial Property, Bern Convention on artistic and literary works, Rome convention on performers, phonograph and broadcasting and the Convention on protection of new variety of plants</li> <li>♣ Those to be signed on 1<sup>st</sup> January 2007: Nice Agreement on Registration of Trademarks, Treaty on WIPO Copyright, Treaty on phonographs and performances WIPO, Washington Treaty on cooperation on patents, and the Strasbourg Agreement on International classification of patents.</li> <li>♣ Those to be signed on 1<sup>st</sup> January 2009: Geneva convention on protection of phonograph producers, Locarno Agreement on patent procedures of micro-organisms and the Treaty on legislation to register trademarks.</li> <li>♣ Those which the Parties intend to adhere to in the future: Madrid Protocol and Agreement on international register of trademarks and the Vienna Agreement on international classification of figurative elements of trademarks.</li> </ul>
5. Government Procurement	<ul style="list-style-type: none"> <li>♣ Coverage includes all kinds of procurement of goods and services by State entities defined in the Agreement. Applies also to public work franchises.</li> <li>♣ Excludes contracts subject to international norms, goods and services acquisitions for their marketing, leasing contracts, employment contracts and some qualified services (financial, audio-visual, etc.).</li> <li>♣ Disciplines in national treatment, transparency, valuation (minimum thresholds of contract value), notification and the MFN clause (subject to negotiation) are recognised.</li> </ul>
7. Rules of Origin	<ul style="list-style-type: none"> <li>♣ Non wholly obtained products must comply with specific norms, which include the change of custom classification number, regional content value, and other specific requisites for the product or item.</li> <li>♣ Only captures of vessels in their own EEZ are to be considered originating. Captures in high sea are classified according to the vessel's flag.</li> </ul>
9. Defence of Competition Disciplines	<ul style="list-style-type: none"> <li>♣ Global Safeguards: Parties reiterated their commitments and obligations in the WTO, with some modifications in their bilateral relation.</li> <li>♣ Bilateral norms have effect only if Parties are principle providers.</li> <li>♣ A consultation system is established prior to the application of measures, in order to reach mutually acceptable solutions or offsets, to maintain balance of concessions.</li> <li>♣ The term for the application of a measure is reduced to 18 months in order to allow affected Party to retaliate.</li> <li>♣ Anti-dumping: Parties have reiterated their rights and obligations in the WTO.</li> </ul>
10. Dispute Settlement	<ul style="list-style-type: none"> <li>♣ Disputes related to the Parties obligations to the WTO and incorporated to the Agreement are settled by the WTO Dispute Settlement system.</li> <li>♣ Disputes related to the obligations substantially equivalent to the ones of the WTO are referred to the WTO system, unless otherwise agreed by Parties.</li> <li>♣ Disputes related to the obligations that go beyond the commitments of the WTO are referred to the Agreement's system.</li> </ul>

Other areas of agreement:

1/ Market Access: Application of 99.7% of tax phase out to the originating trade. Also, an emergency agriculture clause is stipulated with respect to tariff measure, prior consultation, provisional measures and offsets.

2/ Wine and Spirits Agreement: Regulates issues in relation to production and marketing of wines and spirits such as enological practices, trademarks and geographic indications and complementary quality denominations.

## **ANNEX B. Building the indices of Trade Policy Regimes (by Patrick Messerlin)**

For each country, each index for agriculture and for industry is calculated as a simple average of a series of basic indicators. Each basic indicator receives a score from 1 (worst) to 10 (best) that merely corresponds to the decile to which the country belongs for the indicator examined. It should be stressed that indexes are relative (an index of 10 means that this is the best performance observed in the sample, not the perfect performance possible) and that indexes of 10 do not necessarily exist (because they are the simple average of several different basic indicators).

Simplicity indices aim at capturing the information and other transaction costs which are imposed by a trade policy. They are intended to answer the question whether or not producers, traders, and investors need few efforts to understand the trade policy of a country. In agriculture, the index relies on six basic indicators. (1) Does the tariff schedule of the country examined include many tariff lines, meaning that more effort must be devoted to find the correct tariff line to be used, or that there are more risks of errors by or conflicts with the country's customs authorities than would be the case with a tariff schedule consisting of a more limited number of tariff lines? (2) What is the percentage of non-ad valorem bound tariffs, a low percentage implying more efforts to assess the real level of protection than a high percentage? This is because specific tariffs or combined specific-ad valorem tariffs entail a level of protection that varies with world prices. (3) What is the standard deviation of bound tariffs, a high deviation requiring more effort to find out the exact tariff rate? Risks in the face of very different rates are high, and the consequences potentially costly than a low standard deviation. A zero standard deviation signals an uniform tariff policy which has two advantages: it minimizes information and transaction costs of foreign exporters for finding out the nominal tariff rate (unique by definition) and it does not disturb the country's comparative advantage (the effective rate of protection of each industry is equal to the unique nominal tariff rate) so that foreign investors have no reason to make complex calculations in order to know the effective tariff rates that their production will face, if exported to or located in this country. (4) What is the percentage of non-duty free tariffs, a high percentage implying that risks of facing different tariffs (hence information costs) are higher than with a low percentage? (5) What is the number of product groups affected by the export subsidy reduction commitments signed by the country in question under the Uruguay Agriculture Agreement (UAA)—a small number suggesting a less complicated assessment of the support granted to the domestic producers of the examined country? Finally, (6) what is the number of tariff-quotas included in the country's UAA commitments, a high number requiring more efforts to investigate the exact impact of these tariff quotas than a low number? In industry, the simplicity index relies on five basic indicators. Indicators (1) to (4) are similar to the four first indicators in agriculture. Indicator (5) consists in the frequency of non-tariff measures (NTMs), a high frequency requiring more efforts to investigate the exact impact of these NTMs in the export market than a low frequency.

The irreversibility indices aim at capturing the risks that an existing trade policy could be reversed rapidly and substantially. Irreversibility is a major dimension of trade policy envisaged by producers, traders and investors—and by GATT-WTO with the concept of “bindings.” In agriculture, it relies on four indicators. The more irreversible a trade policy is, (1) the smaller the share of unbound tariffs in the tariff schedule—unbound tariffs exempt the country from the most stringent WTO discipline, that is, the need to renegotiate any increase of a tariff above the binding of ceiling rate; (2) the smaller the standard deviation of fill rates of tariff-quotas is—a wide dispersion reflects the impact of quota management methods if one

assumes that the tariff-quotas included in the UAA (3 to 5 percent of domestic consumption) are so small that they should be fulfilled at a similar (presumably high) rate; (3) the smaller the average use of export subsidy outlays is; and (4) the smaller the percentage of tariff lines potentially subjected to special agricultural safeguard (SAS) provisions (the rationale for such a relation is obvious). In industry, the irreversibility index relies on five indicators: (1) the smaller the share of unbound tariffs in the tariff schedule (as in agriculture); (2) the smaller the number of tariff lines with bound tariffs higher than 15 percent (because high unbound tariffs generate either higher risks of reversal, or risks of larger reversals); (3) the smaller the difference between the bound and applied tariffs; (4) the smaller the frequency of core NTBs; and (5) the smaller the number of antidumping cases (per hundred of millions of dollars of imports) initiated during the period 1995-99.

The openness index in agriculture relies on nine indicators. The more open a farm trade policy is, (1) the smaller the average bound tariff as estimated by the OECD, (2) the smaller the average bound tariff as estimated by the World Bank; (3) the smaller the average applied tariff; (4) the smaller the share of tariffs lower than 15 per cent; (5) the smaller the share of tariffs lower than 100 per cent; (6) the smaller the escalation index (the ratio of the average tariff on semi-processed goods with respect to the average tariff on unprocessed products, as calculated by the WTO, 2001, pp.68-69), in order to take into account the magnification of nominal protection introduced by the escalation process; (7) the lower the producer support estimate mirroring production subsidies (drawn from OECD); (8) lower the final post-Uruguay Round budgetary outlay commitment on export subsidies; and (9) the higher is the fill rate of the tariff quotas. The openness index in industry also relies on eight indicators. The more open the manufacturing trade policy for a given country—(1) the smaller the average bound tariff; (2) the smaller the average applied tariff; (3) the smaller the share of ‘peak’ tariffs (higher than 15 percent); (4) the smaller the escalation ratio (the ratio of the average tariff on finished products with respect to the average tariff on raw materials, as calculated by the WTO, 2001, pp.14-15); (5) the smaller the standard deviation of the applied tariffs (because a narrow range of tariff rates minimizes the risk and magnitude of effective protection); (6) the smaller the frequency of core NTBs; (7) the smaller the use of antidumping actions (per thousands of dollars); and (8) whether the country examined has signed or not the information technology agreement (ITA)—mirroring the fact that signing the ITA reflects the country’s will to be open to a technical progress key for liberalizing services.

**Annex Table A1: Trade Policy Regime Indicators for 39 selected countries.**

Countries	Regions	Agriculture			Industry		
		Simplicity	Irreversibility	Openness	Simplicity	Irreversibility	Openness
Canada	NA	7.8	9.0	9.3	8.2	8.6	8.8
USA	NA	6.7	7.0	9.1	7.4	7.5	9.4
Argentina	LAC	7.0	10.0	6.8	5.0	7.2	6.4
Brazil	LAC	7.0	10.0	8.0	5.2	7.6	6.9
Chile	LAC				7.2	7.2	8.4
Colombia	LAC	6.8	8.3	5.6	6.4	6.8	7.5
Costa Rica	LAC	8.5	8.5		7.4	8.1	8.4
El Salvador	LAC	10.0	9.0		6.8	8.6	8.5
Jamaica	LAC				8.0	8.0	7.0
Mexico	LAC	7.8	8.0	7.9	5.2	7.2	6.9
Peru	LAC				6.8	6.8	6.9
Venezuela	LAC	7.0	7.5	6.3	6.6	6.8	7.1
<b>EC</b>	<b>E</b>	<b>4.8</b>	<b>6.8</b>	<b>7.0</b>	<b>6.6</b>	<b>6.3</b>	<b>9.6</b>
Iceland	E	6.5	8.0	6.7	8.8	7.5	9.1
Norway	E	3.5	5.8	5.0	8.8	5.8	8.4
Switzerland	E	5.7	5.5	7.4	5.8	6.1	10.0
Turkey	E	3.8	5.5	6.3	4.6	5.0	7.8
Czech Rep.	E	6.8	8.5	8.7	7.2	7.8	9.3
Hungary	E	5.2	3.5	8.6	6.0	5.8	7.6
Poland	E	4.8	5.0	7.1	6.4	5.8	8.9
Romania	E	4.8	7.5	3.5	6.2	5.5	7.5
Australia	PA	9.2	9.8	8.9	7.2	8.7	9.1
Hong Kong	PA				8.4	8.4	10.0
<b>Indonesia</b>	<b>PA</b>	<b>7.8</b>	<b>10.0</b>	<b>7.4</b>	<b>6.6</b>	<b>8.0</b>	<b>8.3</b>
Japan	PA	8.6	9.7	7.7	8.8	8.7	9.6
Korea	PA	6.2	8.0	6.0	8.0	7.1	9.1
<b>Malaysia</b>	<b>PA</b>	<b>8.0</b>	<b>7.3</b>	<b>8.2</b>	<b>6.6</b>	<b>7.5</b>	<b>7.8</b>
New Zealand	PA	9.8	8.8	8.1	7.6	8.6	9.3
<b>Philippines</b>	<b>PA</b>	<b>7.8</b>	<b>8.3</b>	<b>6.7</b>	<b>7.6</b>	<b>7.6</b>	<b>8.7</b>
<b>Singapore</b>	<b>PA</b>	<b>10.0</b>			<b>8.2</b>	<b>9.1</b>	<b>10.0</b>
<b>Thailand</b>	<b>PA</b>	<b>6.8</b>	<b>9.0</b>	<b>6.5</b>	<b>6.4</b>	<b>7.2</b>	<b>7.8</b>
India	SEA	7.0	8.0	3.0	5.8	6.0	4.0
Sri Lanka	SEA	7.0	10.0	6.8	6.4	7.6	7.9
Cameroon	A				7.8	7.8	7.3
Chad	A				7.8	7.8	7.3
Gabon	A				8.0	8.0	7.4
South Africa	A	6.3	6.3	8.5	7.0	7.0	7.0
Tunisia	A	7.3	7.0	3.4	6.2	6.0	5.9
Zimbabwe	A				7.0	7.0	6.7
Number of observations		31	30	28	39	39	39
Minimum index		3.5	3.5	3.0	4.6	5.0	4.0
Maximum index		10.0	10.0	10.0	8.8	9.1	10.0
Averages by region (unweighted)							
North America	NA	7.3	8.0	9.2	7.8	8.1	9.6

Latin America	LAC	7.7	8.8	6.9	6.5	7.4	7.4
Europe	E	5.1	6.2	6.7	6.7	6.2	8.7
Pacific Asia	PA	8.2	8.9	7.4	7.5	8.1	9.0
South-East Asia	SEA	7.0	9.0	4.9	6.1	6.8	5.9
Africa	A	6.8	6.7	6.0	7.3	7.3	6.9
Averages by region (unweighted)							
All countries		7.0	7.8	6.9	7.0	7.3	8.1
Industrial countries		7.2	7.8	7.5	7.8	7.7	9.4
Developing countries		6.9	7.9	6.6	6.6	7.1	7.4

Source: see Annex A.

Author' s computations

Enlarged EC1		5.4	5.9	7.9	6.6	6.4	8.8
Enlarged EC2		5.0	6.1	6.9	6.2	6.1	8.4
All except E-EC1		7.2	8.1	6.8	7.0	7.4	8.0
All except E-EC2		7.4	8.3	7.0	7.1	7.5	8.0

	<b>Summary</b>
<p><b>1. Options and Implications of Free Trade Arrangements in East Asia</b></p> <p>By Jun Ma and Zhi Wang</p>	<p>Using a dynamic CGE model the authors estimate the impact of various FTA arrangements in East Asia on member and non-member countries. Four scenarios were simulated: ASEAN plus China/HK, ASEAN plus Japan, ASEAN plus China/HK, Japan and Korea and all of the above plus the US. Singapore emerges as the biggest winner in the first three scenarios, whose growth may be enhanced by as much as 4.5 percentage points over the next 10 years (ASEAN+3). Japan and China emerge as the biggest winners in an FTA with the US.</p> <p>The general trade pattern observed under the ASEAN plus China/HK scenario is that China will increase its net imports of land- and natural resource (LNR) intensive inputs and increase its net exports of labour and capital-intensive products. In response, ASEAN will be able to supply more of LNR-intensive products to China, mainly via Singapore (due to its strong agricultural processing capacity). Moreover, almost all FTA member countries will benefit from the cheaper intermediate manufactured inputs available from China since this will allow them to enhance their exports, mainly to the US and the EU. Finally, the authors find that Singapore will increase its production of petroleum products by 4.8% and processed food products by 5% in the next ten years under this scenario.</p>
<p><b>2. Emergent Trilateralism in the Pacific Basin: How Should China, Japan and the United States Respond to Regional Trade Initiatives?</b></p> <p>By Hiro Lee, David Roland-Holst and Dominique van der Mensbrugge</p>	<p>Using a dynamic CGE model the authors estimate the benefits of participation in a global trade liberalization scenario (GTL), a Northeast Asian Free Trade Area, ASEAN+3 and a US-Japan-China free trade with and without accelerated FDI to China from the US and Japan. The results show that GTL is the most attractive scenario for all countries considered except for China and Japan. However, because the WTO process is fraught with complications, this has provided the impetus to pursue regional arrangements. A trilateral arrangement between US, Japan and China in particular will bring larger benefits to Japan and China than a GTL, and about 80% of GTL's aggregate benefits to the US. The findings suggest that Japan and China may have the incentive to pursue Trilateralism as a desirable intermediate step to globalisation.</p> <p>In addition, China may have little incentive to joining an East Asian FTA. An East Asian FTA would divert China's large export capacity into a smaller market, leading to adverse terms of trade effects. In this way it is not clear why China would agree to such arrangements. China appears to be better off with a GTL strategy, or pursuing regional arrangements with large markets as the United States and Japan.</p>
<p><b>3. China and the WTO: Beginning of the End for East Asian Regionalism?</b></p> <p>By David Roland-Holst and Dominique van der Mensbrugge</p>	<p>Using a dynamic CGE model the authors assess various East Asia trade regimes at the global, regional and national levels as they may evolve over the next fifteen years. They find that GTL generates greater gains for the world and for a majority of countries, and dominates every East Asian regional grouping considered. Regional FTAs would benefit most FTA member countries but to a lesser extent than globalisation, since the former would induce significant trade diversion both within East Asia and with respect to the rest of the world. As in the previous paper, they find that China may be worse off in an East Asian FTA because of adverse terms of trade effects, even as most of the other members will be better off.</p> <p>The authors also look at the issue of structural congruence between the three levels of trade liberalization: unilateral (UTL), regional (RTL) and global (GTL). They investigate to what extent a transition from UTL to RTL to GTL induces harmonious shifts in output structure or otherwise. The findings show that for most countries the three different trade regimes induce resource pulls and shifts in output composition in significantly different directions. This implies that in a hypothetical transition from UTL to RTL to GTL, output in many sectors would</p>

	reverse themselves. Therefore, countries using regional agreements as a stepping-stone to globalisation may experience more costly structural adjustments en route to globalisation.
<b>4. Dynamic Effects of the ‘New Age’ Free Trade Agreement between Japan and Singapore</b>  By Thomas Hertel, Terrie Walmsley and Ken Itakura	Using a dynamic GTAP model the authors estimate the benefits of a Japan-Singapore Free Trade Agreement, in particular with respect to the application of certain ‘new-age’ features – implementation of uniform standards for e-commerce, liberalising rules governing direct trade in services and automating customs procedures in Japan. The findings show that if the FTA comprised of bilateral tariff cuts and some liberalisation in trade in services alone, global welfare gains would be uncertain. It is only when e-commerce and customs automatization are included that the benefits become significant.

Appendix 4

Product group	Share of EU Imports from Singapore (per cent)	Average tariff in EU	Average Tariff on Imports from Singapore	Key Non-Tariff Barriers for Singapore	EU Excess Demand Elasticity	EU Excess Supply Elasticity	Price World	Price Singapore	Price Range EU
Fresh food	0.4	20*	0.5*	Sanitary and Phytosanitary	low	low	1		
Processed food	0.5	16*	5*	Technical Regulations:Old Approach	low	low	1		
Wood products	1.2	3	0.7		average	high	1		
Textiles	0.1	7.6	6.6	Rules of Origin	average	high	1		
Chemicals	8.6	5	5.7	Technical Regulations:Old Approach	low	high	1		
Leather products	0.05	2.7	2.4	Rules of Origin	average	high	1		
Basic manufacturing	0.8	3.2	3.4		average	high	1		
Non-electric machinery	43.17	1.7	0.1	Technical Regulations: New Approach/Government Procurement	average	high	1		
Cons. Electronics		2.6	0.6	Technical Regulations: New Approach/Government Procurement	average	high	1		
Electronic components		2.6	0.6	Technical Regulations: New Approach/Government Procurement	average	high	1		
Electrical Machinery	38.4	2.6	0.6	Technical Regulations: New Approach/Government Procurement	average	high			
Transport equipment	1.4	4	1.8	Technical Regulations:Old Approach/Government Procurement	average	high	1		
Clothing	0.75	12.6	12	Rules of Origin	average	high	1		
Misc. Manufacturing	0.18	2.4	1.1	Technical Regulations: New Approach	average	high	1		
Minerals	0.06	0.7	0.3		low	high	1		

\* Note: Derived with a lower degree of precision than those for the industrial sectors

Source : ITC, EUROSTAT and calculations by the authors

Sector	Imports 2000	Sector Share	Weighted Average Tariff		Unweighted Average Tariff		Tariff Revenue		Share of Sector Imports with t=0		Share of Sector Imports with t>10		
			2000	2005	2000	2005	2000	2005	2000	2005	1997	2005	
Minerals	HS 25-27	9052	0.06	0.32	0.32	0.66	0.66	29	29	91.38	91.38	0.00	0.00
Pharmaceuticals	HS 30	11258	0.08	0.00	0.00	0.00	0.00	0.00	0.00	100.00	100.00	0.00	0.00
Inorganic, Organic Chemicals and Fertilizers	HS 28, 29 and 31	1176370	8.18	5.81	5.76	4.92	4.37	68289	67716	11.10	11.10	0.07	0.00
Other Chemicals	HS 32-38	53070	0.37	3.82	3.75	5.06	4.82	2029	1992	36.99	36.99	0.00	0.00
Plastics	HS 39-40	212806	1.48	5.11	4.56	6.04	5.10	11577	9717	22.42	22.82	0.00	0.00
Raw Hides and Skins	HS 41-43	7200	0.05	2.42	2.42	2.68	2.68	174	174	17.28	17.28	0.00	0.00
Wood	HS 44-46	33515	0.23	0.84	0.84	2.45	2.45	281	281	83.92	83.92	0.00	0.00
Wood Pulp	HS 47-49	132627	0.92	0.66	0.00	3.53	0.00	882	0	88.06	88.06	0.00	0.00
Textiles	HS 50-60	14798	0.10	6.59	4.32	7.55	6.18	975	639	0.32	1.12	0.85	0.00
Clothing	HS 61-63	108242	0.75	12.63	11.79	12.02	11.29	13670	12762	0.00	0.00	96.11	96.11
Footwear etc	HS 64-67	4794	0.03	8.70	8.70	8.05	8.05	417	417	0.00	0.00	26.07	26.07
Stone, Cement etc	HS 68-70	15077	0.10	4.12	4.12	3.86	3.86	629	629	4.15	4.15	3.22	3.22
Jewels	HS 71	78974	0.55	0.27	0.27	0.65	0.65	213	213	89.54	89.54	0.00	0.00
Iron and Steel	HS 72-73	36856	0.26	3.16	2.78	3.06	0.78	1571	1025	0.60	15.18	0.00	0.00
Base Metals	HS 74-83	76326	0.53	3.61	3.61	3.36	3.36	2754	2754	8.45	8.45	0.00	0.00
Non-electrical Machinery	HS 84	6204880	43.17	0.13	0.13	1.68	1.68	7936	7936	95.09	95.09	0.00	0.00
Electrical Machinery	HS 85	5515674	38.38	0.58	0.58	2.62	2.62	32236	32236	87.41	87.41	1.65	1.65
Motor Vehicles	HS 87	72185	0.50	4.96	4.96	6.24	6.24	3578	3578	0.16	0.16	0.58	0.58
Other Transport Equipment	HS 86,88,89	133545	0.93	0.06	0.06	1.65	1.65	82	82	97.40	97.40	0.00	0.00
Precision Instruments	HS 90-92	450014	3.13	1.10	1.10	2.24	2.24	4930	4930	68.68	68.68	0.00	0.00
Miscellaneous Manufactures	HS 94-96	25419	0.18	1.08	1.08	2.41	2.41	276	276	65.44	65.44	0.00	0.00
Total		14372682		1.04	1.03			152520	147370	80.84	80.89	1.38	1.37