



Free Trade Agreements in The Asia Pacific

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Professor Urata's research interests include international economics, development economics, and industrial organization. He earned his M.A. and Ph.D. in economics from Stanford University. Prior to his current position, he served as a research associate at The Brookings Institution, an economist at The World Bank, and a director general at the Research Institute of People's Finance Corporation.

Major works: *Measuring the Costs of Protection in Japan* (with Hiroki KAWAI and Yoko SAZANAMI), Institute for International Economics, 1995, *Asia & Europe: Beyond Competing Regionalism* (co-authoring), Sussex Academic Press, 1998, and others.

This welcome addition to the growing literature on Asia Pacific free trade agreements (FTAs) contains eight chapters on different aspects of a sample of the FTAs in the region, each by internationally recognized experts on the issues being covered. The chapters divide nicely into two parts, and the initial overview chapter by Findlay and Urata provides a neat summary of the findings.

The first four chapters focus on the much-discussed issue of the quality of FTAs in the region, specifically in relation to provisions dealing with the potentially problematic issues of rules of origin, agricultural trade liberalization, services, investment, and bilateral safeguards. The authors of each chapter develop frameworks for analyzing the extent to which the provisions in question facilitate or restrict trade or investment, with a view to assessing their contribution to the quality of the FTAs in which they appear. This assessment turns out to be a difficult exercise, as it quickly becomes apparent that restrictiveness and liberalizing impact are multi-faceted concepts that tend to defy easy classification. The frameworks themselves are a helpful contribution to organizing our thinking about the contribution of FTAs to trade liberalization. By setting out detailed comparative information on the content of the provisions being analyzed in each of the FTAs in their sample, these chapters also make a most useful contribution to filling one of the gaps in the literature.

The remaining four chapters adopt a variety of approaches toward assessing the economic impact of FTAs in the region. As the authors of these chapters are all Japanese, there is an understandable emphasis on implications for Japan, although implications for other economies in the region are also addressed. Some of the

implications for Japan that are highlighted in these chapters may be of particular interest in the light of current debates over the future of Japan's policy toward FTAs.

Trade in goods: Rules of origin, agricultural trade and bilateral safeguards

The chapter by Cheong and Cho provides a most useful survey of the use of rules of origin in the FTAs being sampled, and the extent to which they restrict trade. The usefulness of the discussion could have been further enhanced by a slightly more detailed explanation of the concepts being used, for example the "build down" and "build up" approaches to calculating regional value content. By documenting the diversity of rules of origin in the region's FTAs, the chapter also highlights a potentially important obstacle to establishment of a region-wide FTA. The same chapter also provides detailed information on the degree of agricultural trade liberalization in the FTAs being sampled, in the process substantiating the commonly held perception that FTAs involving East Asian countries tend to display lower levels of agricultural trade liberalization.

It is apparent from the discussion by Cheong and Cho that the degree of restrictiveness in provisions such as rules of origin and agricultural trade cannot be simply explained on the basis of linear trends or country-specific interests and sensitivities. Complex negotiating dynamics also come into play. Thus, Japan made more concessions on agriculture to Mexico than to Singapore, partly because it also sought greater concessions from Mexico, but the FTA

with Mexico also exhibits more restrictive rules of origin. Among the FTAs in the sample, the United States generally provides relatively unrestricted access to the agricultural exports of its partners, though it applies a much more restrictive approach in its FTA with Australia, a major competitive threat to its own agricultural interests. Reciprocity also clearly plays a part in determining the degree of liberalization that can be agreed.

Services

The chapter on services by Ochiai, Dee and Findlay powerfully demonstrates the complexity involved in assessing the liberalizing impact of services trade agreements.

The authors provide an enormous amount of detail, and as they themselves comment, "the devil" is indeed "in the detail". For example, the apparently stronger liberalizing thrust of the negative-list approach can be undermined by extensive sector-specific reservations, and impressively broad sector coverage may appear less impressive when the depth and breadth of horizontal limitations is taken into account. The overriding impression is that, regardless of the approach used, countries have been quite successful in finding ways to limit the extent of genuine liberalization embodied in the services commitments in their FTAs. While FTAs generally achieve an increase in the degree of liberalization displayed in the partners' GATS commitments, as would be expected, even this observation is not universally true. The authors also point out that the wide diversity in structure and content of the services trade provisions of FTAs in the region is likely to be a significant obstacle to extending benefits to non-members or amalgamating existing FTAs into larger region-wide agreements.

Investment

The chapter by Urata and Susaya on investment in FTAs also contains an impressive amount of detail, highlighting the degree of liberalization or restrictiveness in terms of six different indicators. The authors see a link to the FDI (foreign direct investment) policies of the individual partner countries, and cite international comparative studies indicating that the FDI policies of most of the partner countries in the FTAs in the sample, all of whom are APEC members, are toward the restrictive end of the spectrum, at least by OECD standards. This is a sobering observation in the light of the emphasis that has been given in APEC's agenda over many years to investment liberalization.

Bilateral safeguards

The chapter by Kotera and Kitamura provides a welcome analysis of an aspect of FTAs that has received too little attention. After a careful analysis of the potential restrictiveness of the bilateral safeguards in their FTA sample, the authors come to perhaps their most interesting insight, which concerns the purpose of the bilateral safeguard provisions. While they may be ostensibly restrictive, these provisions may in fact be included as a way of "buying off" domestic opposition to FTAs, with little or no intention that they may be widely invoked in practice. An FTA that includes these bilateral safeguard provisions may be more comprehensive and liberalizing

in its coverage of goods trade than might have been the case if the bilateral safeguards had not been included. Information on the extent to which the bilateral safeguards are actually used would be needed to confirm whether this interpretation is in fact valid.

Economic impact of FTAs

The chapters by Abe and by Urata and Okabe use the now standard methodologies of, respectively, computable general equilibrium simulations and gravity modeling to provide assessments of the economic impact of FTAs in the region. The results of Abe's CGE analysis are unsurprising, and broadly in line with results produced by other researchers, but also instructive in relation to Japan.

Urata and Okabe perform their gravity modeling analysis first on aggregate trade data and then on trade data disaggregated by products. For most, but not all, of the FTAs in their sample, their results with aggregate trade data are broadly consistent with a growing body of gravity model results which typically although by no means uniformly indicate that trade creation effects predominate over trade diversion effects in most FTAs. When the trade data is disaggregated by product categories, however, their results are much more ambiguous, with trade diversion showing through in a number of cases.

The chapter by Takahashi and Urata contributes to the burgeoning literature on utilization of FTAs. Low utilization to date of FTAs by Japanese firms appears to be related both to the relatively minor roles in Japan's export trade of the partner countries in Japan's existing FTAs and to relatively low margins of preference. On the other hand, utilization is much greater by large firms than by small firms, suggesting that small firms may be disproportionately handicapped by the administrative requirements of FTAs.

There are often demands from policy makers for assessments of the impact of FTAs in the years immediately after their entry into force. CGE and gravity model analysis are not well suited to meeting this demand. The chapter by Ando, focuses on the impact of the Japan-Mexico FTA, provides an instructive example of how such analysis might be done, utilizing detailed knowledge of the relevant trade flows to differentiate between trade increases that might be attributed to the FTA and those that are clearly unrelated to it, and highlighting specific implementation steps that have demonstrably contributed to the facilitation of trade and investment.

Implications for Japan

Some of the findings by Abe and by Takahashi and Urata may be of particular interest in the context of current debates over the future of Japan's FTA policy. For example Abe finds that expanding the range of Japan's FTA partners can deliver significant welfare gains to Japan, and these gains are significantly further enhanced when agriculture is fully incorporated into the proposed FTAs. Accelerating the expansion of Japan's FTAs both improves the welfare outcome for Japan and reduces the potential negative trade diversion effects on other countries. Takahashi and Urata find that although Japanese firms were relatively uninterested in Japan's first three FTAs, they are likely to have been well pleased by Japan's more recent FTAs, and also have a very strong interest in FTAs with China and the United States, as well as being eager to see an FTA concluded with Korea.