

—SUMMARY—

International Symposium hosted by Japan Economic Foundation (JEF)
New Zealand Institute of International Affairs (NZIIA)

“Seeking the Optimum Future Shape for Regional Economic Integration in the Asia-Pacific Region”

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[The following summary is an edited version of the symposium transcript.]

WELCOMING REMARKS

Hon. Russell Marshall: The NZIIA is privileged to be associated with the Japan Economic Foundation in co-hosting this forum. This is the first occasion that our two organizations have collaborated in this way, and we at the institute look forward to further opportunities to working with the foundation.

Holding the 2010 seminar in Wellington is an opportunity to acknowledge the strength and significance of our longstanding relationship with Japan and a tribute to the contribution that New Zealand has made over many years to the process of trade liberalization in the Asian-Pacific region.

OPENING SPEECH

Mr. Noboru Hatakeyama: There are three phenomena that deserve our attention in efforts to promote FTAs in the region.

The first is that the recovery from the economic crisis since 2007 has not been as strong as anticipated. Many countries have implemented economic stimulus packages, but once their effects wear off, the world economy will decline once again. Given the deteriorated fiscal situation in many countries, deregulation, rather than government spending, will need to be used to stimulate the economy. Deregulation must be negotiated in the WTO. However, it has become obvious that the WTO Doha Development Round Negotiations will not be concluded this year. Accordingly, FTAs will

have to play the deregulation role instead.

The second phenomenon is that in the past few years, South Korea has been very keen to pursue FTAs, not only with Asian countries but also with countries in other areas. South Korea signed an FTA with the US in June 2007 and with the EU this month. This new attitude has stimulated competition from many countries in the region in seeking FTAs.

The third phenomenon is the signing of an Economic Cooperation Framework Agreement (ECFA) between China and Taiwan last June. The ECFA will not only strengthen the cross-strait economic relationship but should also significantly reduce obstacles to the signing of FTAs with Taiwan's other trade partners.

There are five big FTA movements in the region at present, and these movements should be expedited due to these three phenomena.

KEYNOTE ADDRESS

Hon. Tim Groser: There are two great drivers of the FTA process today and several important implications that flow from them.

The first is the enormous wealth creation process. The emerging economies are growing three to four times as fast as the developed countries, and the wealth process is spreading throughout the world.

The process we're seeing is a shift from a model of a single hegemonic power to a series of centers of power, based around essentially four capitals at the top-tier of power. We have the United States, around Washington; Brussels for the 27 European states; Beijing, which has a great history and culture; and New Delhi, the other great developing country superpower.

Below the top tier are extraordinarily important countries like Indonesia and Japan. Japan claims 8.3% of world GDP with "only" 126 million people. Japan still has great creativity and great power. Other states include Russia and Brazil. This multi-hegemonic power structure will be governing 65% to 70% of the people of the world.

The second driver is the growing sophistication of international trade, summarized as 'the integrated global supply chain.' Trade in intermediate goods is now 58% of world trade in goods and 73% of world trade in services.

If you're still involved in a vertically integrated production model and not taking part in the global supply chain, you've missed the plot. The Apple iPod is perhaps the most celebrated illustration of this.

So, these two trends are informing the way in which the world is going and provide the backdrop for the study and the issues we are going to be debating today.

One policy conclusion to flow from that is the inability of world governance structures, including the WTO, to keep pace with the massive shifts.

In the 1970s and 1980s, the power structure reflected the realities of world power. But the power groupings change, and we haven't quite got the power grouping in place to reflect the extraordinary changes we are witnessing. As long as the top tier group understands the limitations they face, they can provide leadership and direction. This is what we're waiting for to happen.

The second implication from the wealth transfer and the integrated global supply chain is the way in which the Asia-Pacific integration process is being put together. There is no chief architect. In fact, a good metaphor would be 'open source.' Even a small country like New Zealand can and has exercised fundamental influence on the structure of FTA development.

The character of FTAs has changed in the last few years. The number continues to proliferate, and the criticism of FTAs in the 1990s that they are of low quality is beginning to recede as we are seeing increasingly high-standard FTAs. The New Zealand-China FTA, which has now been in operation for 22 months, has led to a 77% increase in bilateral trade between our two countries. That is extremely high quality.

The first trend is towards high quality FTAs; the second is towards convergence. The long-term vision of a convergent FTA is the FTAAP, the Free Trade Area of the Asia Pacific. This is a super high-quality FTA with region-wide rules of origin. It's the leading candidate, but there are others on the drawing boards: ASEAN+3, ASEAN+6 (otherwise

known as CEPEA), and ASEAN+8.

TPP is another convergent FTA. Unlike CEPEA and ASEAN+3, negotiations are already underway. It was originally the Pacific-5, but it's taking shape as Pacific-8 and will be Pacific-9 in very near future.

The Obama administration is very strongly committed to this initiative, which is the one that it owns politically. This is very important for the United States and is their way to remain central to the process of trade and investment integration in the Asia Pacific.

I want to end on the debate underway in Tokyo. TPP is intended as a building block for the FTAAP. It's clear from the comments being made by Japanese ministers that the key issue is agriculture. I deeply understand and respect those sensitivities. But it's important that you know you're dealing with countries that want to see this great country take a fuller part in the process.

The tools for dealing with agriculture are there. They lie in the concept of progressive liberalization and the tools available in the "green box." I believe that Japan, with its enormous financial strength, through the combination of traditional modalities and financial strength will creatively use the green box to advance the internal process of agricultural reform.

SESSION 1

The Contribution of Free Trade Agreements

Moderator: Dr. Hank Lim

Dr. Hank Lim: We've heard much about the need for rebalancing, but we take for granted that East Asia and the Asia-Pacific region will continue to grow. This is not enough.

Growth following the global financial crisis must come from trade. The topic of the first session is thus very appropriate, because without trade, there will be no growth.

We know that FTAs contribute to growth, but in Asia they have been in the form of bilateral negotiations and of lower quality. As a result, the distortion effect is less, and the

trade creation effect is also not much.

We should examine all existing and forthcoming FTAs to reduce the distortion effects and increase the trade-creation effects.

Mr. Jayasena Jayasiri: Most of the panel members are analysts or researchers, but I am a practitioner; I negotiate and implement FTAs.

FTAs make four main contributions. First, while you may hear of regional FTAs, by nature they are actually bilateral FTAs, since each ASEAN country has individual tariff schedules.

From the Malaysian perspective, FTAs impact both the domestic economy and the regional environment; they enhance the competitiveness of domestic industries. Most FTAs require a reciprocal arrangement, so countries have to undertake liberalization.

FTAs prevent an avalanche of competition that can kill industries. Because you can stage the level of openness, industries can adjust while providing competition. The removal of tariffs and nontariff barriers and the requirement to meet standards inject competition.

FTAs also lead to domestic reforms and internationalization. Malaysia does not include labor and the environment into trade negotiations. But there is a need to consider this because some FTA partners require inclusion. Labor, the environment, and government procurement will be part of TPP negotiations.

The third point is that FTAs enhance trade performance. More companies are also taking advantage of FTAs, using the certificates of origin to export under FTAs.

The fourth point is that FTAs enhance the regional integration process. ASEAN negotiated its first FTA with China in 2005, and at that stage there was very limited progress in ASEAN. But the FTA negotiations compelled ASEAN and individual members to move faster in this area.

Prof. Robert Scollay: FTAs have a traditional role of breaking down trade barriers and an increasingly important role as catalysts for the wider process of economic integration.

We moved from a fairly limited 'regional trade architecture' in the 1990s to the 'noodle bowl' that we currently have with potential for very large region-wide groupings.

In terms of the traditional role, there are two views, one that FTAs don't really contribute to trade liberalization, and the second, more sophisticated view that nowadays tariffs don't matter. Both are wrong.

After the 30 or so Asia-Pacific FTAs were signed, there has been a wide variation in how much trade has liberalized, but the common characteristic is that by the tenth year, close to 100% of tariff lines have been reduced to zero.

The next big issue is making sure that FTAs are not just there on paper as agreements but that the availability of duty-free trade is actually utilized by traders. Most of the major trade players in the region are not covered by the existing architecture of bilateral FTAs, however, in particular, China, Japan, and Korea, and neither Japan nor China has an arrangement with the United States.

In the regional trade architecture, major potential additional benefits would come perhaps from CEPEA but to a much greater extent by moving to FTAAP.

There are a number of missing dimensions in the role of FTAs as promoting and catalyzing regional economic integration. In trade in goods, we need to look at the convergence of regulatory frameworks, rules of origin, product standards, and more comprehensive approach to trade facilitation.

Actual liberalization in trade in services lags a long way behind what's on paper because it involves regulatory and policy frameworks within economies, as well as deeper commitments in competition policy, government procurement, and investment.

Prof. Djisman Simandjuntak: Regional integration and cooperation remain very relevant. ASEAN is undergoing deepening integration due to the ASEAN free-trade area and attempts to move to an economic community. But in dealing with the rest of the world, each of us tends to go our own way. We negotiate different cooperation schemes with the EU.

Our trade is very dependent on CJK, and the lack of a CJK arrangement is one problem. We will also have to internalize two developments outside of East Asia. The first is cyclical development and structural issues, like climate change. The second is resource pooling, including human resources and energy. The third element is convergence.

Indonesia is open to discussing ASEAN+6 and beyond. But ASEAN's internal integration will also have to be strengthened. We have to stick to the timetable to build an ASEAN Economic Community.

Mr. Makoto Shiota: Asia and other emerging countries are now developing very rapidly and lead world's economic growth. The value added by the manufacturing sector, already has been higher than in EU and NAFTA. is higher in Asia. The middle- and high-income populations of Asia multiplied fourfold in a decade, and by 2020 it will again double . It is important to emphasize Asia-Pacific economy. As for CJK,. agreement was reached among the three countries this May for a trilateral initiative, and a report will be produced in two years.

As for CEPEA, Japan wants to contribute to the East Asian economic integration discussion. Former METI Minister Naoshima proposed a path toward ASEAN + 6 integration called "Initial Steps". Based on this plan, in September discussions began in the ASEAN-Plus Working Group among the ASEAN+6 countries covering rules of origin, tariff nomenclature, custom procedure, and economic cooperation. Long-term sustainable economic growth in this region becomes possible through the progress in both hard and soft infrastructure development. In August 2010, the AEM approved the Comprehensive Asia Development Plan. In line with this plan, Japan will bring concrete projects like the Mekong-Japan Economic and Industrial Cooperation Initiative to fruition.

In a recent policy speech, Prime Minister Kan said that Japan will work to build a better environment for shared growth and prosperity for the Asia-Pacific region through EPAs and FTAs and look into participating in the TPP with a view toward making the East Asian Community a reality.

Dr. Sangkyom Kim: There are distinctive factors governing decisions to have larger FTAs. Some advance domestic reforms that can attract FTI.

Progress in evolving small-scale FTAs into a region-wide one is slow, though. We need strong leadership to turn hub-and-spoke-type FTAs into a larger-scale economic community.

Our region has great diversity and poorly defined geographical scope. There are also unresolved political and historical issues. Utilizing a sub-regional group can be useful to creating a bigger one.

Prof. Shujiro Urata: Malaysia is now involved in TPP negotiations. What is the rationale for this? What has been the impact of the China-ASEAN FTA on various countries in the region? Everybody knows that agriculture is an obstacle. Can Japan really advance agricultural liberalization?

Mr. Jayasena Jayasiri: Malaysia has always negotiated in an incremental basis. Our participation in the TPP is seen as a stepping stone for FTAAP.

Bilateral negotiations have taken a permanent pause. The only way to engage the US is through the TPP.

Our trade with China has increased over the last three years. Most of Malaysia's duties were already zero before negotiations, but tariffs in China were positive. The tariff issue is becoming less important in negotiating FTAs, while investment is becoming more important.

Having an FTA with the US sends the right signals to investors, not just in Malaysia but a much bigger market of 3 billion people through our FTAs with China, India, and the rest of the region.

Prof. Djisman Simandjuntak: The China-ASEAN FTA has had a very strong impact on the expansion of trade between Indonesia and China. Dissatisfaction about the FTA with China should be overcome soon.

There is no way in which plurilateral arrangements can overcome problems that exist bilaterally. From the experiences of ASEAN, under plurilateral arrangement we can defuse a number of disputes, but they cannot be solved. Bilateral and plurilateral arrangements pose the same problem.

Prof. Robert Scollay: If an FTAAP can be established, it should be open to any country that wishes to join, whether they're in this region or not.

Secondly, the EU is already active in the FTA game in our region. So, there was an incentive for countries in this part of the world to expand the horizons in terms their FTA connections.

It will be difficult, though, to extend the scope of these FTAs from the traditional reduction of trade barriers to the deeper, wider regional economic integration

Dr. Hank Lim: Regional economic integration will depend very much on the US, China, and Japan, but smaller countries like New Zealand and Singapore can also play a very important role in the sectoral approach.

Mr. Noboru Hatakeyama: Russia and the United States were invited to the East Asia Summit by ASEAN diplomats. Will this be approved by leaders as well? Will the US and Russia be invited to CEPEA?

Prof. Djisman Simandjuntak: The East Asia Summit can have a number of windows, one for security issues, to which Russia and the United States are invited. But on the economic side, I think, we should let CEPEA first proceed in the current mode.

SESSION 2

The Post-Financial and Economic Crisis and FTAs: How Is the International System Coping in the Post-Economic Crisis Period; Next Step?

Moderator: Prof. Djisman Simandjuntak

Prof. Qin Yaqing: China's economy has grown very fast and is very much export-oriented. But it has a somewhat imbalanced economic development. Some regions are quite advanced and some regions are still very poor. There are gaps among social groups as well.

Before the financial crisis, China's export-oriented economy showed very dynamic development. Exports increased more than 25% annually. The top three destinations

were the United States, EU, and East Asia. Interregional trade occupies the largest proportion.

After the financial crisis, the growth rate clearly slowed down. The export value in 2009 was negative, especially to Western markets.

The Chinese government adopted the largest-ever stimulus package to invest in infrastructure, disaster-stricken regions, agriculture, environment and energy, education, and healthcare.

Measures were taken to rebalance exports and imports, clearing nontariff barriers and simplifying import procedures. The result was an export volume drop of roughly 16%.

Retail sales increased 17%, and the current account surplus dropped by 6%.

China's trade with the rest of the region also dropped sharply in 2009, but the drop in trade with ASEAN was roughly half of that with the US, EU, Japan, and ROK. The ASEAN economy recovered faster than those of other markets.

China expanded its domestic market and increased imports from East Asia. The China-ASEAN FTA is another important factor. China cut average tariffs from about 10% to 6.1%. ASEAN showed the same decrease.

China's economic structure and restructuring is heavily dependent on foreign markets, and domestically it's not very balanced. It's not easy to restructure the whole economy overnight.

The East Asian Community can push forward not only economic cooperation but also norm construction.

Prof. Simon Tay: In the post-crisis world, there have been great changes not only in economics but also in politics. And the changes have occurred not only in international relations but also internally in America, China, and other countries.

America is not in terminal decline and cannot be written off. But I agree that we are moving towards a more multilateral world, and relations with Asia must be more equal than they have been in the past.

The crisis has been a watershed that will lead to long-term changes. In the decade since the Asian crisis, Asia and America both grew, but the trajectories have been

radically different. Americans have begun engaging in what I call a 'blame game.' Rather than faulting the greed of Wall Street bankers, they've been talking about imbalances.

Even before the crisis, trends indicated that America's influence was changing. American military power was stretched to the point of breaking. There was a loss in America's soft power as well, as it did not uphold its own values in what we saw in Guantanamo and Abu Ghraib. Domestically, the Tea Party and other trends raised questions about America's commitment to engaging Asia and the world.

East Asia has been marked by increasing regionalism. China now occupies a bigger place, becoming the second-largest economy in the world. Some in Asia might say, "We no longer need the Americans." But I'm not one of them. Both America and Asia would lose out if they do not find a way to work together. What are at stake are existing trade patterns and economic interdependence, which have also helped smooth over political frictions on both sides of the Pacific.

Clearly, the demand for Asia is to have a more self-contained economy. Asian savings should be circulated to our own infrastructure projects, rather than being invested in Treasury Bills.

The mood over the last year has been restive. Many Americans turned against globalization, questioning whether trade is really free and fair. They also question China's democracy and human rights and are turning against trade with China.

On the Asian side, confidence is bordering on hubris. American pressure for a revaluation of the *renminbi* has become a bone of contention.

The Obama administration wants to engage with Asia, but the body politic is absent and weak. We need a shared future with more multilateralism, so I think the EAS engagement is good. We'll have to focus, though, so we may have to get rid of the APEC Summit.

Dr. Mignonne Man-Jung Chan: I would like to point out the importance of fiscal stability and caution the fact that the race to devalue currencies will have a strong negative

impact for regional integration.

The financial crisis will transform our conventional economic theories, trade theories, and re-evaluate the need for government intervention. It will also challenge business-government relations and how we evaluate current account balances. Stimulus packages have had a positive effect on many economies, but the unemployment rates in the US and EU remain high. On the negative side, the aggressive expansionary monetary and fiscal policies have spawned cross-border speculations. This will in turn affect investments and liberalization in services.

Now, in North and South Americas, people worry about currency manipulation, particularly in relevance to the East Asian countries.

However, the key issue is the contention on China's current account surplus and US trade deficit. Do we need another Plaza Accord? This basically would give the US more freedom to rebalance its large fiscal deficit. The question today is the danger of triggering a protectionist backlash. China has been trying to avoid a sudden in-flow of speculative capital and also to diversify the pegging of US dollars. In real terms, the trade-weighted RMB is up 7.5% over the past six months and fully 20% over the past five years. China's main concern is avoidance of Japan's "lost decade" after the 1985 Plaza Accord. This resistance toward rapid currency appreciation will also affect intra regional trade. The international financial architecture is an indispensable tool for long-term, foreign direct investment, which is usually a win-win situation.

Short-term capital is what we ought to watch. Taiwan's approach to managing currency exchange rates is to make sure fluctuations are based on economic fundamentals, not short-term capital flows. Important factors for improving intra-Asian trade are financial stability through monitoring of capital flows and facilitation of financial support.

Prof. Gary Hawke: We should try to minimize barriers while preserving the rules and institutions which make private interest compatible with social ambitions. We tend to think rather too much in terms of completed printed agreements than the removal of barriers to cross-border transactions.

The essence of the problem is to keep the focus on the outcome rather than on the means. It's easy to exaggerate the impact of the financial crisis in the Asian region,

including Australia and New Zealand. We shouldn't buy in to a sense of victimhood whereby Asia is always at the mercy of initiative from elsewhere.

There are two impacts which we should concentrate on. The first is that we are going to require a focused political effort. The second is that the crisis is leading to an emphasis on the integration of real and monetary economics.

There's never a politically 'right' time to undertake policy reform. When an economy is doing well, reform risks seem unnecessary; when an economy is doing badly, structural policy reform may seem like one burden too many. The emphasis should be on maintaining open regionalism.

Mr. Tony Nowell: Free trade is part of the answer to the global financial crisis. Global supply chains are becoming more complex and are moving faster and faster, and it is very important that we have the mechanisms in place for goods trade, for services development, and for people movement.

Two years ago, in the ABAC forum, we got a very aggressive response from a number of economies. Today, we're talking about a P10 under a TPP framework, and we're moving very rapidly towards an FTAAP.

Business is talking about non-traditional, open concepts under the FTAAP concept, such as balanced, inclusive, sustainable, innovative, and secure.

One rising issue is food security, which is very, very important across the APEC region. Another is promoting capacity building and financial inclusion, especially for SMEs, or what's now becoming known as SMMEs.

Dr. Hank Lim: As a result of the global economic and financial crisis, the East Asian region has become the most promising and dynamic, especially with the rapid rise of China and India. However, the economic potential must be accompanied by major policy shifts for balanced, sustainable, secure, innovative, and inclusive growth.

FTAs can contribute towards economic clustering, the division of labor, and specialization. To achieve the five growth objectives, you need to have more high-level FTAs.

FTA has proliferated in East Asia. Such proliferation does not automatically increase the number of international transaction, as the administrative costs for securing certificates of origin are quite high due to different rules of origin.

It is not necessary for the region to pursue the same financial regulatory reform as in the United States. However, it is imperative to streamline and harmonize rules and regulations across borders to facilitate cross-border trade.

Lower trade costs due to a FTA do not automatically result in the dispersion of economic activities. Rather they generate two countervailing forces of agglomeration and dispersion. Controlling these two forces is the key for deepening economic integration and narrowing development gaps.

Financial liberalization is still very much lagging behind. FTAs for services trade remain a major impediment to regional integration and a seamless marketplace. The region also needs to liberalize and harmonize transportation and logistics, communication and customs, and other technical barriers to trade and actively promote trade and investment facilitation and capacity building.

Dr. Thomas Aquino: We must recognize the domestic growth taking place in China that continued despite the slowdown in its export growth that enabled the region to withstand the consequences of the recession triggered by Wall Street.

We should focus on the value that FTAs can add and how businesses can be better helped, because they create the wealth.

Mr. Hidetoshi Nishimura: An FTA is the first step toward economic integration, which has good effect and bad effect. We must narrow the gaps at the same time.

SESSION 3

What Could Be the Optimum Future Shape for Regional Economic Integration in the Asia-Pacific Region?

Moderator: Prof. Simon Tay

Prof. Simon Tay: We will focus on the potential contribution of FTAAP and TPP as well as whether the East Asia Community is really necessary.

Mr. Noboru Hatakeyama: I will talk about five proposals for regional integration in this area: EAFTA, CEPEA, FTAAP, TPP, and CJK. Of these five, those covering almost all major Asian or Pacific countries are EAFTA, CEPEA, and FTAAP. EAFTA and CEPEA are proceeding in parallel with each other, but this parallel process cannot continue forever.

One of the merits of CEPEA is that its market is approximately 20% larger than that of EAFTA and even slightly larger than the US market. Another merit is that it includes India as well as New Zealand and Australia.

On the other hand, it should be possible for EAFTA to be concluded first and for CEPEA to be completed with three additional countries, which are not members of EAFTA, joining at a later stage. We have to decide which one will prevail, EAFTA or CEPEA.

Since China and Taiwan signed the ECFA, the EAFTA and the CEPEA should not refrain from inviting Taiwan to take part in negotiations. Taiwan has a bigger economy than any ASEAN member except Indonesia.

In his general policy speech in October, Prime Minister Kan stated that Japan would consider joining the TPP with the aim of establishing FTAAP. Last July, the government came up with a road map to establish FTAAP by 2020, taking advantage of Japan's hosting of the APEC Leaders' Meeting in Yokohama. So the wording regarding FTAAP should be changed from 'long-term prospective' to at least 'mid-term prospective.' I believe it will be possible for EAFTA or CEPEA and FTAAP to co-exist, EAFTA or CEPEA on the one hand and FTAAP on the other. Of the 21 APEC members, only 10 are members of the EAFTA. In addition, India should be invited to join APEC with a view to establishing FTAAP.

Of the five FTA proposals, the first to be concluded should be a CJK FTA. I discovered in 1997 that of the 30 largest economies by GDP only 5 had no FTAs. Those five at the time were Japan, China, South Korea, Hong Kong, and Taiwan. It is only natural for CJK to try to fill the FTA vacuum by establishing an FTA. If a high-quality EAFTA or CEPEA is concluded after CJK, the latter may be absorbed into the former.

Whatever scenario evolves regarding possible FTAs, agricultural reform is unavoidable before Japan will be able to accept it. The current DPJ government provides a direct subsidy to farmers to compensate for the gap between falling prices and the rising production costs. If the subsidy is given only when prices fall because of eliminated or reduced import tariffs, this subsidy system will become a powerful force for liberalization.

ASEAN is trying to create a single ASEAN Economic Community market by 2015. ASEAN would become that world's fourth largest market in the world.

In July this year, ASEAN foreign ministers decided to welcome the US and Russia to the East Asia Summit. If this is implemented, the number of the EAS members will increase from 16 to 18. Many questions remain on this decision, including whether either the US or Russia belongs to "East Asia" geographically. In particular, if these two countries want to enter CEPEA on which the governmental discussions have already started, it will make the situation more complex.

Dr. Sangkyom Kim: There are some distinguishing characteristics that we may derive from RTAs between APEC member economies. The first is that the trend of regional economic cooperation between APEC members is a relatively new concept. China, Japan, and Korea made relative slow progress in institutionalizing regional cooperation.

The RTAs implemented after the 1997 crisis are influenced by two factors. The first is that the division of labor between APEC economies has become increasingly horizontal, especially in Northeast Asia. The importance of intraregional trade has been rising, and the nature of interdependence is changing. The second factor is that the rapid spread of FTAs in East Asia is attributable to the 1997 crisis. This leads to the question on the need for strength in the regional institution architecture.

Most RTAs in the Asia-Pacific region have taken the form of bilateral agreements, seeking lower costs and easier negotiations, even though the gains are limited compared to larger scale FTAs.

With technology advancement, the distinction between intra- and inter-regional partnerships has dissipated. Most sub-regional RTAs within APEC have created a

complicated web of overlapping hub-and-spoke-type RTAs, resulting in the spaghetti bowl phenomenon.

In order to be a good RTA, it should have a trade creation effect for all participating members and for the world as a whole, providing incentives for RTAs to aim for a nondiscriminatory, global free-trade area. The negative effects of the proliferating hub-and-spoke-type RTAs should be mitigated by consolidating the sub-regional trade blocks into a large umbrella.

APEC's consolidated market size is 40% of the world population and 53% of world GDP. This is large enough to create a positive trade creation effect. Regional trade accounts for close to 60% for these economies, which is a promising factor in expecting a large trade creation effect. The simple averaged complementary index of the 21 APEC members is 53.7%, a figure not excessively high or low.

Judging from market structure alone, we may expect a significant trade creation effect after the establishment of single market in the APEC region. To quantitatively test the empirical outcome of the proposed FTAAP, I set up three scenarios. The first is the full elimination of tariffs, the second is full tariff and trade facilitation, and the third is trade facilitation with other service barrier reductions. The overall gain for all participating economies range from \$55 billion to \$284 billion and \$148 billion to \$636 billion on the static and capital accumulation models, respectively.

The first policy option we might consider is that in terms of regional institutional architecture the breakup of APEC into East Asia and Pacific regions would be insufficient trans-regional cooperation. Thus TPP has the potential to become a stepping stone to a high-quality and comprehensive RTA on a global scale. Our leaders should commit themselves to FTAAP to trigger the Japan, China, Korea FTA, ASEAN+3 FTA, and ASEAN+6 FTA, which can also become stepping stones to the creation of global free-trade environment.

Amb. Ong Keng Yong: The starting point for the ASEAN Economic Community is to organize the Southeast Asian economy into a single market and regional production base. The deadline used to be 2020, but now we have reached consensus to have it established by 2015. Not everything required for a single market or regional production base may be there by then, but we should have more than 50%—and this is enough to

keep it going.

Leaders still maintain that by 2015 the ASEAN Economic Community should be established. It will not be the same as the European Union because we started from different premises. The focus of the AEC is on harmonization of custom procedures, standards, and various other initiatives.

The most important thing is the removal of tariffs and nontariff barriers. In the last 10 years, we were able to negotiate five different free-trade area agreements, starting with China and Korea, Japan, Australia, New Zealand, and India.

We believe that these five FTAs will be the starting point for a broader regional free-trade area arrangement. CEPEA is based on the membership of the East Asia Summit, which has 16 members. We want to loop all 16 countries into one economic partnership. The question is whether China would participate. China will participate if there are good reasons, namely, the participation of America, Japan, and Korea.

There is a proposal for the US and Russia to join the East Asia Summit. If you care about geography, Australia and New Zealand should not be there either. The most important thing about membership in the East Asia Summit is the sense of the future. If you feel that your future is in trading with Asia, you should be in the East Asia Summit.

Eventually we may call it something else. If America and Russia join, they must be convinced to be part of CEPEA. The important thing is that ASEAN must be credible.

The idea behind TPP is to root the United States in the region in working with the other big economies, namely Japan, China, Korea, Australia, and New Zealand. The latest meeting of the TPP partners in Brunei just two days ago covered almost 11 countries, and there were more than 300 officials and representatives coming together to brainstorm.

Our emphasis in TPP is to move CEPEA forward and to convince China to participate. If we can do that, we can further develop TPP as a complementary form for CEPEA. When we have the US and China in the TPP, we can then look at an FTA for Asia-Pacific.

Prof. Shujiro Urata: What is the optimum form of regional integration? My answer for the medium term is the coexistence of CEPEA or EAFTA and TPP and eventually FTAAP.

TPP is a very attractive arrangement. FTAAP will be the largest arrangement as far as the membership is concerned. But establishing FTAAP from scratch will be difficult because it has 21 members. So TPP will be a very effective vehicle to reach this final goal.

TPP has already been established, and the number of potential partners is increasing. One challenge is the size of membership and the level of trade liberalization.

At the moment, the original four members are trying to get 100% trade liberalization within 10 years. This may be possible for the four countries, but when other countries join 100% is not realistic.

So the original four members have to give in to requests from new members about the level of trade liberalization, maybe 95% or 97%. If the level of trade liberalization comes down to 95%, then I think Japan and other countries can join TPP. I don't think the US can accept 100% either. So, there has to be a compromise between the size of membership and the level of trade liberalization. This is a big challenge.

One important contribution that CEPEA can make is to provide economic assistance. The big difference between TPP and CEPEA is the priority given to economic cooperation in the latter. Without it, it is very difficult to achieve stable and well-balanced growth in this region.

TPP is a building block kind of approach, which is different from the WTO/GATT approach.

Prof. Qin Yaqing: The question of an optimum future shape for regional integration is hard to answer. Several things are important. The first is the complementarity of mechanisms and platforms. People call East Asian regional economic cooperation a spaghetti bowl because you have so many mechanisms. But there are two sides to this. On the one hand, everything seems entangled, but on the other hand all these mechanisms can complement each other. The key is how we can make them

complementary and compete in a benign way to promote regional economic cooperation.

The second point is to take a practical approach. Pragmatism is a feature of East Asia culture. We need to analyze all the mechanisms to see what we can accomplish. The East Asian Economic Community is a priority.

The third point is that from the very beginning we have featured open regionalism and inclusiveness. This can help us in many ways, sometimes beyond the economic dimension. Inviting Taiwan is a somewhat politically sensitive issue, though, since China always thinks that sovereignty is very important for national interest. The issue will depend on the cross-strait relations and also on the processes within the mainland of China and Taiwan.

Dr. Mignonne Man-Jung Chan:

For me, ECFA symbolizes the vision and political will of China and Taiwan to sideline differences and maximize common interests.

ECFA is also significant as we need to adhere to open regionalism. With Taiwan's accession to the Government Procurement Agreement, we want to fulfill our obligation as well as enjoy the FTAs that we are entitled to as a WTO member. There are three indispensable factors that are all crucial for Taiwan's expanding international community role.

The first is the Taiwanese people's aspirations, the second is mainland China's goodwill, and the third is the support of the international community.

The most crucial element in all schemes of human construct that have emerged recently is that we listen to the aspirations of all members in the region; otherwise it just won't work sooner or later.

Mr. Jayasena Jayasiri: The only FTA that is going to be a reality is the TPP because negotiations have already started, although other regional initiatives were launched long before TPP. There is great misunderstanding about TPP. I had similar misunderstandings until I was in Brunei last week.

The TPP started with four countries, and when they invited others to join, there were not

many takers. In 2007 the US started negotiating, and their terms of entry were that the US would set the ground rules for future members.

If there is some form of agreement reached by APEC 2011 in Honolulu, then it is an indication that the TPP will survive. But if not, then it may become a drawn-out process like the Doha Development Agenda.

The larger the membership of any FTA, the greater is the economic benefit. But from a negotiator's point of view, the larger the membership, the greater the nightmare of negotiating and chances of it failing. The DDA has taken 10 years, and still it has not seen the light of day. Negotiating in the WTO is no different from negotiating with more than 10 or 11 members.

There was a suggestion that CEPEA could be the optimum future for the East Asia regional integration with Russia and the US. We have to ask ourselves, "Did the US engage with ASEAN on any FTA or regional integration?" The EU cannot engage with ASEAN collectively because of political differences, and it's no different with the US. It's very difficult for us to envisage a CEPEA with US participation and all 10 ASEAN members.

At the end of the day, I think it is political exigency that is going to decide what is going to be the optimal equation or formula for integration in this region.

Dr. Thomas Aquino: TPP is ahead because it's there. But to get from four to anywhere, it's going to be a big question mark.

FTAAP fulfills most of the qualities of an optimal FTA now, but the question is what role will be assigned to APEC considering it is not a negotiating body. Ambassador Ong made a very good analysis of possible trends in the FTA formation or the sequential approach.

The past couple of years have been a bureaucratic nightmare because of negotiations for many FTAs. Businessmen become bored looking at which tariff schedules to pursue.

Amb. Ong Keng Yong: My feeling is that whether it's EAFTA or CEPEA or TPP or FTAAP, it doesn't matter. The most important thing is that all of us feel that there is some

usefulness in negotiating this kind of mechanism. The alternative is for us to be out of the room, and the question is whether any country can afford not to be at the table, especially if the United States or China decided to go and join the table.

I don't think that CJK FTA can come about very soon because there is so much historical problems, so much distrust among the three participants. But actually on the ground, the integration of Korean, Japanese, and Chinese business activities is very substantial. Investment and trade are already in the wedding room. The marriage is only awaiting consummation.

Prof. Shujiro Urata: One of the issues which Koreans raise in Japan-Korea FTA is that if we have FTA between these two countries, then the trade deficit will be even larger, so they don't want to see that happen. If we can get three of us, China, Japan and Korea, together, then this issue may be overcome. This is because Korea has a trade surplus vis-a-vis China, China has a surplus vis-a-vis Japan, and Japan has a surplus vis-a-vis Korea.

So CJK has a better chance than Japan-Korea or Japan-China.

Dr. Hank Lim: I think the debate over whether or not everybody wants to be at the table is over. We're at the second stage of deepening. Deepening is the convergence of the four regional architectures. And the next is sequencing. Which of the four comes first?

In order to materialize EAFTA, CJK is very important. CJK is a precondition for EAFTA. As for CEPEA, it will emerge after EAFTA and CJK because each reinforces the other. Once Japan and China are at the same table, then CEPEA will come.

TPP is a trigger mechanism to revive APEC and FTAAP. So, EAFTA, CEPEA, TPP and FTAAP will come in that sequence. Otherwise, it will be very difficult to achieve convergence.

Mr. Noboru Hatakeyama: If we have to wait until the completion of the CJK before having EAFTA or CEPEA, it may take a long time. I hope that political relationship between us will be much better in the near future, in which case CJK might be realized, but I am not too optimistic on this point. TPP will be the first among the five proposals, I think, and maybe FTAAP might be the second one.

Prof. Simon Tay: While economic logic is a part of the equation, there seems to be questions of political will. So questions of whether China and the USA are going to move forward are critical.

CONCLUDING SESSION

Mr. Noboru Hatakeyama: Although it was rather vague, a loose consensus emerged today that there are two visions, a Pacific version and East Asian version of an FTA. The Pacific version is starting from TPP with the aim of ending up with FTAAP, and the East Asian vision may start from CJK to reach an East Asia FTA or CEPEA.

In the case of FTAAP or TPP, the US is a member of APEC, so there is no argument of whether or not the US should be invited. When it comes to EAFTA or CEPEA, whether or not to invite the US and Taiwan must be discussed further.

Thank you very much for joining us this afternoon.

Mr. Brian Lynch: With such a wealth of solid and substantial and thought-provoking material, it is extremely difficult to be able to digest all that material on the spot; one needs to go away for a period of calm and composed reflection. But the thoughts that came through here will not be lost and we will be preparing a report to be carried in our bimonthly journal.