Catalyst? TTIP's impact on the Rest

Edited by M. Sait Akman, Simon J. Evenett and Patrick Low

CEPR Press

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Economic Policy Research Foundation of Turkey

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1 T20 is a platform which brings together global think tanks and high-level experts in order to provide analytical depth to ongoing G20 discussions and produce ideas to help the G20 to deliver concrete and sustainable policy measures. The T20 chair does forward a summary of the ideas discussed at T20 meetings to the Sherpas.

2 Center for Multilateral Trade Studies (MUTS)

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Foreword

The ongoing Transatlantic Trade and Investment Partnership (TTIP) negotiations have the potential to be transformative for the world economy. This is because the two likely parties to it – the United States and the European Union – are key trade partners for almost every economy in the world.

This eBook directly addresses the consequences of TTIP for the countries not directly involved in the negotiations. It assesses this matter in the context of a multilateral trading world in which global value chains and pre-existing trade agreements will significantly impact the reaction to TTIP. Edited by Sait Akman of TEPAV, Simon Evenett of the University of St. Gallen, and Patrick Low of the Fung Global Institute, the eBook is made up of fifteen analyses by leading trade economists, and covers both systemic and national perspectives. It presents a debate that is very relevant to the current negotiations and is useful for academics and policymakers alike.

CEPR and TEPAV are grateful to Simon Evenett for his great efforts in bringing this eBook to fruition, and to the contributing authors for their valuable insights. We would also like to acknowledge contribution of editors in conceiving the idea and finalising the eBook, as well as Anil Shamdasani and Shreya Sinha for working on its publishing and launch processes.

CEPR is grateful for the support from the European Commission under its ESSEC programme towards the funding of its dissemination activities. The Centre acknowledges that this support does not constitute an endorsement of the contents of this eBook, which reflects the views only of the authors, and that the Commission cannot be held responsible for any use which may be made of the information contained therein. CEPR, which takes no institutional positions on economic policy matters, is delighted to provide a platform for an exchange of views on this critical topic.

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February 2015

Introduction

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The Transatlantic Trade and Investment Partnership: Where does it leave outsiders?

The Transatlantic Trade and Investment Partnership (TTIP) could transform trade and investment relationships between its two protagonists – the United States and the European Union. It could also have a far-reaching impact on third parties who have strong economic links with those economies. This eBook focuses on the second of these two propositions. What is TTIP likely to mean for the Rest?

According to World Trade Organization (WTO) trade data[1] for more than 70 countries, the highest value export destination is involved in TTIP's negotiation. For most other economies, the EU and the US will not be very far down the list of major export destinations. These are gross trade numbers and do not take account of trade dependency through supply chains. Nor do they say anything about investment relationships. However, the picture is clear – most economies in the world are likely to be affected by TTIP should it come to fruition with anything like the level of ambition sought by its architects.

The impact of TTIP on third countries will depend on a range of factors, which several contributions to this eBook touch upon. They include the degree of participation in global value chains that involve TTIP countries, the nature of pre-existing preferential

1 WTO Trade Profiles Database.

arrangements between TTIP economies and third countries, the economic structure of economies and what this means for the nature of involvement with parties to TTIP, and the ability of outsiders to align themselves with TTIP's regulatory arrangements.

The context for analysing the impact of TTIP on third parties is a world in which multilateral trade negotiations have largely stood still since the birth of the WTO two decades ago. It is also a world in which preferential trade agreements have multiplied several-fold in recent years, implicating virtually every nation in a certain degree of discriminatory engagement with its economic partners. The influence of the WTO has waned for both these reasons – its own negotiating stasis leaves the institution with an outdated agenda and preferentialism has spawned a myriad of other venues for doing business.

In the last five years or so, a new phenomenon has emerged – the so-called 'mega-regional' agreements. These are larger blocs of nations engaged in the construction of more deeply integrated economic areas. The three wide-ranging agreements under negotiation to which the 'mega' moniker is attached are TTIP, the Trans-Pacific Partnership (TPP) and the Regional Comprehensive Economic Partnership (RCEP).

TTIP's avowed intention is to focus in no small measure upon regulatory cohesion between its two parties. This takes on considerable importance in a world where the EU and the US represent a large chunk of global economic activity, and where regulatory behind-the-border policies have become the dominant determinant of the conditions of competition in the global economy.

Unlike tariff preferences, regulatory reforms agreed by a subset of nations need not be inherently discriminatory. Some regulatory reforms, such as trade facilitation, are unlikely to discriminate among trading partners. Others can be designed either way. This adds poignancy to an analysis of the discriminatory impact of regulatory reform, because choices in the details of policy design can make all the difference.

What follow in this eBook are 15 short commentaries on the implications of TTIP for outside parties. Seven of the chapters take a systemic perspective, asking questions about third country effects of regulatory reform and tariff preferences, the pros and cons of geographically selective regulatory convergence, and options for mitigating the potentially discriminatory consequences of TTIP.

The remaining eight chapters take national perspectives, examining the implications of TTIP for Australia, Brazil, China, India, Korea, Russia, South Africa and Turkey. While each of these countries has its own specificities, they are representative of larger economies with links to the EU and/or the US.

How far will TTIP succeed in meeting its declared objectives?

Those who worry about a negative impact from TTIP on third economies may be tempted to take solace in the idea that disagreement on key issues between the EU and US will both delay and dilute the content of the agreement. On the European side, public reservations have been strong on issues such as forced privatisation, the content of some mandatory standards, and investor-state dispute settlement. The *Financial Times* reported recently, for example, that a public consultation in the EU on prospective investment rules had produced an unprecedented level of negative responses against proposed investor-state dispute settlement provisions (Oliver 2015). Moreover, completing TTIP in 2015 is looking increasingly like a pipedream. As various contributors to this eBook point out, differences in approach and commercial interests in sectors such as agriculture, labour-intensive manufactures, culture, and a range of other services are proving challenging to bridge.

To the extent that a core theme of TTIP is regulatory compatibility, discussions on harmonisation, acceptance of equivalence, and mutual recognition figure prominently in the chapters. Full harmonisation would mean identical standards, certification (licensing), labelling, and conformity assessment procedures. Equivalence accepts that different standards, measures, and approaches may be pursued by trading partners, but that the pursuit of shared objectives makes trade restrictions in response to differences unjustifiable. Mutual recognition reflects acceptance of the proposition that even if differences in standards exist between trading partners, these do little or no harm and therefore do not justify market access restrictions. Many mutual recognition agreements focus on conformity assessment procedures and seek to reduce trade costs by ensuring that products are subject to a conformity assessment regime only once.

Most of the literature on regulatory cooperation tends to emphasise product-related rules and procedures. These include rules of origin, design and procedural aspects of standards, and a host of other tariff and non-tariff barriers. Measures aimed at foreign direct investment (FDI) are also crucial for access to markets within preferential zones. Nationality requirements on equity and management help to determine how restrictive preferential arrangements are to outsiders. The rights of individuals to work and reside within a jurisdiction are also important.

These policy elements are the raw material of the negotiations on behind-the-border regulation. The extent to which they are negotiated at the sectoral or product level may permit an inference on how far TTIP will go in integrating the markets of the US and the EU. Detail is the bedfellow of exceptionalism.

A tension that will complicate the negotiations is how to draw a line between *commercially driven protectionism* and *social preferences*. Consumers in the US and the EU seem to have fairly divergent risk preferences in some areas, such as in the case of genetically modified organisms. Similarly, social preferences for a domestic way of doing things may be a preoccupation of consumers, not producers. Negotiators have to agree on a distinction between legitimate producer aspirations for better market access and consumer attitudes that are ignored at the peril of governments who have staked their reputations on a robust result.

These are some of the considerations that may give comfort to those who believe that TTIP will not go very far. However, it would be foolhardy simply to assume there will be no significant result from the TTIP negotiations. Avoiding this lazy assumption provided one of the rationales for this eBook.

Motivations behind TTIP and their likely influence on third party outcomes

The motivations behind TTIP will shape the outcome. The EU negotiating mandate, which reflects in part objectives shared with the US, was released to the public by the EU Council in June 2013.[2] In market access, the objectives are to remove import duties on goods and restrictions on services, open up government procurement and facilitate investment. The mandate also calls for improved regulatory coherence and cooperation through dismantling unnecessary regulatory barriers. On rules, the parties seek to improve cooperation in setting standards. Taken at face value, this constitutes an "ambitious, comprehensive, and balanced"[3] enterprise aimed at raising income and creating jobs. However, from the perspective of third parties a number of key questions inevitably arise in regard to the consequences of TTIP.

Strategic considerations and their implications for inclusiveness

To what extent has geopolitics, informed by shifting power global power relationships, motivated this EU/US initiative? Several contributors to this volume raise questions in this context. It is hard to argue that TTIP has nothing to do with how power and influence will be configured in the world economy in years to come. TTIP strives for a transatlantic consensus to set the guiding principles of the international system (Hamilton 2014). Some of the language in documents and speeches, such as the reference to "set[ting] the path of global standards",[4] is revealing.

2 The mandate can be downloaded at http://data.consilium.europa.eu/doc/document/ST-11103-2013-DCL-1/en/pdf.

3 Ibid., paragraph 2.

4 This quotation is cited in the chapter by Aichele and Felbermayr in this eBook.

While it may be obvious that the desire to retain a certain dominance in global economic affairs imparts a certain logic to TTIP, it is less clear what this means for outsiders. One way of seeing this is that the parties to TTIP would like to be as inclusive as possible once they have set out the menu for cooperation. Another interpretation is that the EU and the US want to hunker down in a relationship of mutual economic dependence behind a fortress that will make them stronger for longer. The latter seems less probable than the former, which suggests that third parties have a good deal to play for in trying to ensure minimal discrimination in outcomes.

TTIP seemingly will not include an accession clause, but statements have indicated that the TTIP parties would be amenable to including other economies in their arrangement once it is complete. Indeed, there have also been suggestions that TTIP could be the central contribution to a reactivated WTO.

The problem with this, of course, is that it is very likely to be a 'take it or leave it' formulation, with no intention of opening issues up for renegotiation. This perception partly explains why we see a range of proposals, especially in the country-specific contributions to this eBook, for other courses of action to mitigate negative third party effects.

The likely economic consequences of TTIP for third parties

On the other hand, vested economic interests may trump strategic thinking. Analyses in the eBook identify both potentially negative and positive results for third parties from TTIP. Positive consequences could arise from deeper integration of the two largest economies in the world. If standards were harmonised, for example, exporters to the TTIP zone would only have to worry about compliance with a single regime in an enlarged market. In reality, this particular example does not reflect a likely outcome because the emphasis in the negotiations is on mutual recognition and equivalence and not on harmonisation. A second potential benefit from TTIP is an income effect. To the extent that efficiency gains are made and trade costs reduced, a growth dividend could be forthcoming from which all parties can benefit.

Negative outcomes flow essentially from three main sources that could hit both trade and investment. First, there may be a direct discriminatory effect that asserts itself though trade diversion. TTIP will be super-imposed on a series of existing preferential agreements. Tariff reductions in TTIP will shuffle effective tariff preference margins, for example, with preference erosion a significant possibility in some sectors and for some economies. Similar effects can occur with regulatory changes, including of a procedural nature, giving rise to what has been referred to as 'regulatory diversion'. Diversionary effects might be lessened for those countries that have negotiated agreements with a most-favoured-nation clause that automatically entitles them to new preferences within TTIP.

Second, import restrictions may increase as a result of new regulations or regulatory arrangements that impact market access. These would not be presented as import restrictions, but they would act like them. Third, new regulations might raise production costs in third party economies and reduce competitiveness.

One suggestion made for reducing the trade-restrictive and cost-increasing consequences of regulatory reform would be to require that convergence occurs to the least rigorous pre-existing standard. However, if most of the action on the regulatory front is going to be in the nature of mutual recognition or equivalence agreements, the risk of upward harmonisation would not seem great. On the other hand, many factors that impact on trade costs (such as the difficulties for developing countries in meeting stringent standards or regulations) would be in play in the regulatory field, with uncertain consequences for access.

The papers in the eBook take different views on how likely increased discrimination and market access restrictions will be in a post-TTIP world. These include: i) fears of far-reaching negative consequences; ii) the conjecture that only goods trade will be seriously affected because the prospects for progress in services look bleak; iii) predictions of minimal overall effects because of economic structures and the composition of trade and investment flows or because of the limited reach of the negotiated outcome; and iv) a greater emphasis on positive opportunities that will flow from closer EU/US integration.

Scope for countervailing action at the national level to mitigate any ill effects of TTIP

The national contributions to this eBook are where most of the proposals for remedial initiatives are made. As noted above, views differ as to the magnitude of the likely effects of TTIP. Some fear the worst and others believe the consequences will not be great. There were broadly three kinds of damage-minimising courses of action proposed.

First, several authors argued that vulnerability was in part a function of poor domestic policies and that perhaps this debate offered an opportunity to undertake reforms at home. These would be a mixture of additional market opening, measures to reduce administrative trade costs, and other kinds of domestic regulatory reforms. By making their own economies more competitive, the argument goes, it would be easier to withstand pressure arising from changed conditions in the country's major export markets.

Second, some authors were of the view that the TTIP protagonists were unconcerned about adverse third party effects. They suggested options for minimising such effects. These suggestions are diverse and include reducing secrecy in the negotiations, promoting dialogue, and designing integration approaches that would be least discriminatory towards outsiders and least corrosive of trading opportunities. The latter could include designing standards and regulation as inclusively as possible, flexible rules of origin, and preferential access to the TTIP market for outsiders.

A third proposal was to intensify cooperation with other countries as a means of counterbalancing the weight of TTIP. The main vehicle for such an approach would be to forge new or deeper preferential arrangements. Another suggestion is to work towards revitalising the WTO and to use it as an instrument for blunting preferentialism. This second option is attractive, but it has its challenges. Influential emerging economies and the major industrial countries, including the EU and the US, would need to be willing to work meaningfully to repair, reform, and update the WTO. Such a stance would weaken an alibi for preferentialism, which has it that a weakened WTO makes the institution's relative neglect essentially in the national interest – a contention that overlooks the fact that we are talking about the same decision-makers in both contexts.

Concluding remarks

The chapters in this eBook cannot do full justice to as complex an issue as how TTIP will affect the rest of the world. But they can and should stimulate thinking and offer some useful pointers as to the directions for future study.

In addition to the multiplicity of complex issues in play, the future of TTIP remains uncertain and much of the analysis presented here is partly speculative. That argues for maintaining a watchful eye on developments.

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Part I

Systemic perspectives

TTIP and the world trading system

Patrick Low[1]
Fung Global Institute

Introduction

New mega-regional trade agreements – which, besides the TTIP, are generally taken to include the Trans-Pacific Partnership (TPP) and the Regional Comprehensive Economic Partnership (RCEP) – have changed the landscape of preferential trade relationships and pose additional questions for the future and relevance of multilateralism and of the WTO. TTIP stands apart from TPP and RCEP for three main reasons. First, it is a prospective bilateral deal rather than a plurilateral one.[2] Second, the protagonists – the EU and US – are both advanced economies that are already integrated in important ways; TPP and RCEP face all the challenges of trying to seal agreements among economies at very different levels of development. Third, the major thrust of TTIP focuses on reducing barriers to trade arising from disparate regulations in the two economies.

The US and EU account for almost a half of the world's GDP and one-third of global trade, although bilateral trade flows amount to less than 5% of the total (Fontagne and Jean 2014). If significant convergence occurs in the regulatory environment of the two economies, pressure for conformity by third parties and the costs of exclusion will weigh most heavily on the EU's and US's trading partners.

An additional risk clearly exists that other regions could start aligning their own regulations, leading to divergence and reduced trade flows among significant groups

1 The views expressed in this chapter are those of the author and should not be attributed to the Fung Global Institute

2 TPP comprises 12 negotiating partners, and RCEP 16.

of countries. If the WTO were more efficient than it is today, multilateral oversight of these tendencies might have been able to mitigate them.

How successful TTIP will be remains an open question, partly because regulatory convergence between sovereign entities is no easy matter, and also because the whole conception of TTIP is running into stiff political headwinds. Difficulty in closing a package resembling initial negotiating objectives is not a challenge exclusive to TTIP – it is shared by the other mega-regionals and the WTO.

International trade cooperation, in whatever guise, has become increasingly infused with geopolitical rivalry among major economic powers, and in particular between the US and China. None of the mega-regionals include both China and the US as parties – RCEP is an exclusively Asia-region initiative and TPP excludes China. A common view is that these patterns of cooperation are a reflection of geopolitical rivalry between the world's two largest economies. In the light of these developments, the TTIP has been characterised as an attempt by the EU and the US – perhaps a last opportunity – to write the trade rules for the 21st century.[3]

As far as the WTO is concerned, it would be inaccurate to suggest that the negotiating paralysis of the last few years was simply the result of Sino-American tensions. Those rivalries have certainly been an influence, but without a greater degree of common purpose and shared priorities between the US and China, it is very difficult for anything else to move.

The rest of this chapter considers the effects of preferentialism on multilateralism. This is followed by reflections on the WTO's own difficulties burdening its effectiveness. The chapter concludes briefly with some ideas on how the WTO might reassert its centrality in managing today's splintered world of trade relationships.

3 See, for example, van Hamm (2013).

Where preferentialism leaves multilateralism

Preferentialism was embedded in the General Agreement on Tariffs and Trade (GATT) – the precursor to the WTO – at its inception in 1948 (Hudec 1975). Historical preference schemes were grandfathered and rules written for free trade areas and customs unions. These 'original sins' against non-discrimination were essential to the larger scheme, but arguably made it easier for slippage to become a norm.

Preferential trade agreements (PTAs) have multiplied greatly over the years, particularly since the 1990s; there are now more than 350 active agreements.[4] At the same time, provisions entering into force in 1979 have introduced permanent exceptions from the MFN principle for the benefit of developing countries. These are frequently referred to as special and differential treatment provisions.

Preferentialism and the core principle of non-discrimination were able to co-exist without excessive friction in the early years of GATT, but this has changed. On the regionalism front, a turning point occurred in the early 1980s, when the US departed from its aloof stance on PTAs. Its first preferential agreement was with Israel, followed by a bilateral with Canada and then the North American Free Trade Agreement in the early 1990s. The changed US position triggered much of what followed, as preferential arrangements became the new norm. Virtually no country was devoid of preferential trading partners, and in 2010 all WTO members belonged to, on average, no fewer than 13 PTAs apiece (WTO 2011).

Then the mega-regionals appeared, raising more fundamental questions about the continued centrality of the WTO in international trade relations. The impression that the WTO was in deep trouble has been generously fed by the inability of the institution to complete the Doha Round of trade negotiations, launched in 2001.

4 The WTO's 2011 *World Trade Report* (WTO 2011) stated that some 300 PTAs were in existence. The number has continued to multiply at a rapid rate.

A fundamental tension has persisted around the question of what the appropriate balance of rights and obligations should be between developed and developing countries within the system. Special and differential treatment has tended to be seen as binary, with no systematic mechanisms for determining entitlement or the circumstances in which access to such treatment is warranted. The lack of agreement on these matters has fed repetitious disagreement and stasis.

Nobody would be taken seriously if they argued that the only way forward for the WTO was to banish all forms of preferentialism. Preferential trade agreements and special and differential treatment have been useful, not just as safety valves, but as responses to different needs and priorities. The core problem is the GATT/WTO's poor record in managing these arrangements effectively. The mega-regionals, including TTIP, loom large as a potential threat to the full effectiveness of the WTO. But it would be a mistake to think of their emergence as an entirely unprecedented vote of no confidence against the WTO. There is a long-standing history upon which this new development has drawn.

What is wrong with the WTO?

Although part of what afflicts the WTO is exogenous – stemming from a shift in the global economic centre of gravity and geopolitical tensions – some of the WTO's difficulties have been manufactured behind its own doors. While the WTO still manages existing trade agreements and settles disputes, it seems to have lost its ability to produce results in negotiations.

A complex collection of factors explain this. One is that the GATT/WTO would have done better historically to de-emphasise efforts to liberalise trade and concentrate more on consolidation and the multilateralisation of gains made elsewhere. Rule-writing has been pursued with a far greater degree of success than market-opening. The same is true for dispute settlement.

The GATT/WTO's weakness as an instrument of trade liberalisation reflects its highly diverse and large membership. The central place accorded to the notion of reciprocity, combined with the MFN obligation on any agreed trade-opening package, has discouraged large countries from negotiating with smaller ones for fear of free-riding by other large trading partners.

An additional thorn in the side of progress has been the way that the WTO takes decisions. The default is consensus. Consensus can easily turn into veto, and has sometimes resembled a tool for blocking rather than a mechanism for inclusion. Urgent action is needed to raise the cost of frustrating majority interests.

Conclusion

International trade relationships in general face difficult times. This is as true for the mega-regionals as it is for the WTO. Fresh thinking is needed about how to manage change, especially when change is as rapid as it is today. In the past, the shifts in relative power occurring today would have led to armed conflict. In today's world, we are trying to manage this challenge through cooperation and agreements.

Success in achieving negotiated outcomes will need institutional adjustments, especially from the WTO. The WTO needs to rethink its mission and put more emphasis on what it can uniquely provide by way of global governance in a role of consolidation and oversight. The WTO is not, and never has been, a leader in market-opening. It has almost always been a consolidating force, except in the sphere of accessions, which raise a series of other considerations not discussed here. The WTO should stop aspiring to be what it is not and shouldering the consequential costs of failing to serve the essential purposes for which it was conceived. If it gets that right, TTIP and the other mega-regionals will look less forbidding and rivalrous.

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TTIP, regulatory diversion and third countries

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The goals of the Transatlantic Trade and Investment Partnership (TTIP) initiative are both straightforward and ambitious: to further integrate the transatlantic market place. To achieve this this objective one dimension is to remove remaining tariffs on transatlantic trade and similar policy measures that discriminate in favour of domestic providers of goods and services. Another dimension, one that looms much larger in public debates and advocacy of both proponents and opponents of deeper transatlantic integration, is greater 'regulatory coherence' – initiatives to reduce the market-segmenting and thus cost-raising effects of *differences* in regulatory regimes and standards that apply to products and suppliers on different sides of the Atlantic. The purpose of this chapter is to assess the relevance of both dimensions for third parties, drawing upon available evidence to gauge the seriousness of different potential TTIP-induced policy changes.

Third-country market access

The first dimension of TTIP relevant to third parties, in essence tariff-driven trade diversion, has attracted relatively little attention in public debate. It is, however, a feature of the agreement that will lead to the most immediate negative effects on firms located in other parts of the world. Companies located in jurisdictions that do not have free trade agreements or preferential access to the EU and US markets will confront more competition from EU (US) firms in the US (EU) markets. Companies that already have duty-free, quota-free access to the EU or US markets will suffer preference erosion.

How large are such effects going to be? Not very large in aggregate – because average tariffs are low and many rest-of-the-world suppliers already have duty-free quota-free (DFQF) access to the EU and/or US markets. While currently preferred suppliers will experience some losses, and MFN suppliers will incur trade diversion losses, such effects will be concentrated in areas where tariffs are currently relatively high, such as apparel in the US and motor vehicles in the EU (see tariffs in Table 1). Even then, in some of those sectors (e.g. apparel) there is likely to be only a limited impact as production has mostly moved offshore to non-EU and non-US locations.

The source of uncertainty in grasping the possible impact of TTIP on third countries is not tariffs, but rather what will happen to non-tariff barriers (NTBs). Third-country non-tariff effects hinge on several factors: (i) the extent to which potential reductions in NTBs are discriminatory; (ii) the extent to which such reductions would be realised at all; and (iii) the trade cost changes implied by an adjustment in regulatory measures. To distinguish from tariff-based trade diversion, we will refer to market access erosion from the regulatory elements of TTIP as regulatory trade creation and regulatory trade diversion. The scope for such effects has been stressed in recent assessments of prospective EU trade agreements,[1] and with good reason. The underlying logic is that insofar as regulatory cooperation is part of a deal, at least some of the associated changes will directly affect all firms and not just EU and US firms. This is because new regulations *might not* (but could) be formulated to explicitly and deliberately discriminate. We simply do not know yet what the mix of discrimination and non-discrimination will be. Regardless, this is clearly a departure from the mechanics of preferential tariff reductions. However, it is also notional, in that negotiators seem to believe in this possibility, but to varying extents and without strong evidence from past experience. In addition, as with investment treaties, firms may be able to relocate operational headquarters to qualify for better regulatory treatment.

1 See, for example, ECORYS (2009) and CEPR (2013). In those studies, this effect is referred to as regulatory spillovers.

Scope for trade cost reductions

Keeping in mind the scope for regulatory trade creation and diversion, we return to our basic question identified above – potential third country effects. Starting with possible trade cost reductions, we can ask how big might they be, and to what extent it matters if costs are reduced on a discriminatory basis. Here, we borrow from Egger et al. (2014) and will centre our discussion on Table 1. The table summarises two sets of information. The first is estimated trade cost reductions for goods, from a gravity-based assessment of other deep trade agreements involving the EU and US, along with the corresponding tariffs. The second set of information pertains to services, and collects a recent set of estimates from the World Bank and WTO. Starting with goods, the first columns in Table 1 report estimates of what are known as AVEs (ad valorem equivalents) for trade cost savings in other agreements involving the US and EU. On average, trade cost reductions are around 6.2%, or two to three times the level of mean tariffs. Right off the bat, it is clear that NTB-related aspects of the TTIP imply far greater changes in trade costs than tariffs. The sector coverage is also informative. Primary agriculture, chemicals and pharmaceuticals, and motor vehicles are the sectors where trade cost reductions, based on past agreements, are likely to see the greatest trade cost reductions. This provides an answer to the question of whether we can expect trade cost reductions, and what the AVEs would be (though not whether we get discrimination into the bargain). Tariff reductions are important as well (especially for the EU) for processed foods. In the case of motor vehicles, the EU has both high tariff and non-tariff barriers, and the likely shock to third-country market access could be potentially quite large.

Table 1 Trade cost reductions in TTIP scenario

	AVE % cost reductions		Tariffs	
	EU NTBs	US NTBs	EU tariffs	US tariffs
GOODS	6.2	6.2	2.1	1.3
Primary agriculture	23.2	23.2	3.3	2.2
Primary energy	0.0	0.0	0.0	0.1
Processed foods	6.4	6.4	15.8	5.0
Beverages and tobacco	22.6	22.6	5.9	0.8
Petrochemicals	0.0	0.0	1.8	1.6
Chemicals, pharmaceuticals	11.3	11.3	2.1	1.3
Metals, fabricated metals	0.0	0.0	1.8	1.2
Motor vehicles	19.7	19.7	7.9	1.1
Electrical machinery	0.0	0.0	0.6	0.3
Other machinery	7.8	7.8	1.2	0.7
Other manufactures	0.0	0.0	1.7	2.9
	AVE % cost reductions		GATS, best RTA	
	EU NTBs	US NTBs	EU	US
SERVICES	9.9	6.7	55.3, 64.4	55.4, 55.4
Construction	4.6	2.5	70.8, 83.3	83.3, 83.3
Air transport	12.5	5.5	66.3, 72.5	5.0, 28.8
Maritime transport	0.9	6.5	47.6, 63.1	0.0, 44
Other transport	14.9	0.0	57.1, 71.4	42.9, 64.3
Distribution	0.7	0.0	71.9, 87.5	100, 100
Communications	0.6	1.8	75.0, 78.1	78.3, 78.3
Banking	0.0	0.0	42.7, 42.7	29.2, 33.3
Insurance	0.0	0.0	57.5, 57.5	40.0, 50.0
Professional and business	17.7	21.0	58.8, 62.5	57.5, 62.5
Personal, recreational	4.4	2.5	47.6, 50.9	91.5, 91.5
Public services	*	*	32.5, 36.7	19.2, 31.7

Source: Combines parts of Tables 3-3 and 3-5 from Egger et al. (2014).

Matters are less clear when it comes to the effects of TTIP on market access in services. Such flows are not encumbered by tariffs, but both the EU and the US maintain policies that discriminate against foreign companies. The most blatant type of such restrictions involve prohibitions on the supply of services – examples include US laws that limit the provision of maritime cabotage services to US-flagged vessels and preclude a foreign-based airline from providing services on domestic routes. Other quota-like restrictions are conditional and discretionary – for example, economic needs tests that make temporary entry of foreign services providers conditional on a determination that there is insufficient local supply to satisfy demand. Another example would be a requirement that companies 'localise data', such as a prohibition on a services supplier moving data pertaining to a customer outside of the country of residence. Such a requirement does not stop a US firm from providing services to an EU consumer, but does raise the cost of doing so by requiring duplication of facilities and the need to create firewalls within its databases.

The lower section of Table 1 provides summary information on regulatory costs for services for the EU and the US. The first two columns provide estimated AVEs of market access restrictions in services on the basis of the World Bank's STRI database (Jafari and Tarr 2015) and are comparable to recent estimates from other sources. They represent actual levels of market access. The second two columns provide a different perspective. These provide scores from 0 to 100, where 0 means no binding commitments have been made and 100 means full commitments have been made to bind policies linked to market access for particular sectors either in GATS, or in the most ambitious PTA involving the EU or US. Similar estimates can be found in Borchert et al. (2011) who note that, in general, GATS commitments provide little in terms of bindings relative to actual policy.

From the last columns of Table 1 it is apparent that many sectors are relatively unbound both in the GATS and in the deepest commitments made by either the EU or the US within their respective trade agreements. There are exceptions, such as the distribution sector, construction, and communications. Yet these sectors are relatively open anyway. Where we see the highest protection – i.e. in professional and business services – both the EU and US are highly protective, and they are reticent to make actual commitments in these sectors in PTAs. As such, while we see little evidence of actual liberalisation under with the GATS or deep PTAs involving the US and EU, there is great potential given the size of barriers (the AVEs in the first columns). On the US side, other standouts are banking and insurance (high barriers, little evidence of actual binding commitments) and maritime services (same story).

How do we interpret the evidence on services? Based on past experience, neither the US nor the EU has shown a willingness to make binding commitments to open service sectors where protection actually matters. This does not mean we cannot envisage a situation where the EU and US depart from past behaviour. However, this would mean a break from the revealed unwillingness to negotiate concessions in services witnessed until now.

The policy challenge

The question, then, is how best to address the effects of differences in regulatory regimes across signatories keeping an eye on possible consequences for third parties. The 'traditional' approaches pursued in the EU context centre on harmonisation and mutual recognition. Both require agreement/convergence on a set of core substantive norms. If harmonisation could be implemented in a given policy domain, it would benefit EU and US-based companies, but also firms in the rest of the world as they would be able to focus on just one set of requirements. There may be more harmonisation as a result of TTIP, but at present it looks like this will (at best) pertain to new regulations, not to the existing stock of norms and standards.

In practice, the focus of attention in the TTIP context revolves around mutual recognition and the less known concept of 'equivalence' – where each party accepts that the regulatory regime that prevails in a partner country pursues very similar objectives, and regulators agree that the process through which regulatory objectives are pursued are equivalent to their own. A necessary condition for 'equivalence' to be feasible is trust: there must be a prior process of 'mutual assessment' or evaluation of the goals and approaches that are pursued in the relevant jurisdictions in order to allow a judgement to be made that the regime in a given country is 'equivalent enough' to be accepted. Such an approach can and will be subject to exceptions and exclusions for sectors or products that are deemed too sensitive to allow it to be applied, or where it is established that the underlying norms and preferences of the countries involved are too dissimilar for them to be regarded as equivalent. But in many cases, it is likely that EU and US regulatory objectives and enforcement are equivalent in terms of outcomes sought.

If success can be achieved in establishing equivalence, for third parties the question will be if they can participate in whatever processes are put in place. A key necessary condition for participation is that the jurisdictions concerned do indeed pursue equivalent objectives and have implementing procedures and institutions that are credible. In principle, there is no reason why third-party regulatory bodies should be excluded from processes used to establish equivalency, or mechanisms that result in mutual recognition. Indeed, restricting participation to only EU and US entities would greatly undermine the credibility of the claim that one of the rationales for the TTIP is to identify 21st century approaches to regulatory cooperation.

Closing comments

The TTIP goes beyond tariffs to behind-the-border sources of trade costs. While tariff concessions in a regional trade agreement are relatively straightforward to negotiate and their consequences relatively easy to understand, NTBs raise questions that are not so clear-cut. Yet they are at the core of likely third-country effects. Key factors include potential for trade cost reductions, the level of ambition achieved (will trade cost savings be realised?), and the extent to which cost savings will be discriminatory. Based on an overview of evidence from EU and US concessions in the context of other deep trade agreements, the greatest scope for loss in market access for third countries in goods is in primary agriculture (NTBs), motor vehicles (NTBs and tariffs), chemicals and pharmaceuticals (NTBs), and processed foods (NTBs and tariffs).

For NTBs, non-discriminatory reductions could mean improved market access from regulatory trade creation, or at least a moderation of regulatory trade diversion. For services, on the other hand, there is little evidence that either the EU or the US will actually make meaningful concessions at all, let alone that such concessions would yield substantive changes to market access for third countries. Perhaps in the Trade in

Services Agreement (TiSA) the observed pattern of services concessions in the GATS and regional trade agreements will be broken. Our expectations are not high, however, in the context of TTIP. As such, third-county effects in TTIP, following from both tariff concessions and NTB reductions, will be a bricks and mortar issue, affecting primary food and manufacturing exports from third countries.

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The impact of TTIP on third countries

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The Transatlantic Trade and Investment Partnership (TTIP) is an ambitious trade agreement currently being negotiated by the EU and the US. It will cover more than 45% of global value added. Its depth and sheer size will make it important for outsiders.

TTIP has at least two objectives: to provide "*increased market access*", and to achieve "*greater regulatory compatibility and to set the path of global standards*".[1] The first is classical; the second is relatively new in trade agreements.

Will a TTIP discriminate against outsiders?

The central question is whether the TTIP will discriminate against outsiders in the sense that it denies them preferences that the insiders mutually grant each other. Discrimination is inherent to the *market access* objective of the TTIP. It is most obvious in the case of tariffs or quotas, but it is also present in other elements of mutual market opening such as public procurement, certain aspects of services trade (e.g. the recognition of professional degrees), and investment liberalisation. To enjoy preferential access to the US market, EU exporters must prove that their products originate from within the EU according to the rules of origin (RoOs) laid down in the agreement, and vice versa. Then, how discriminatory the TTIP is depends on the strictness of those RoOs and whether they are enforced (or are enforceable).

1 See point 5 in the negotiation mandate of the EU Commission.

Transatlantic *regulatory cooperation*, in contrast, will not necessarily be discriminatory. If the TTIP results in truly global standards, all countries could effectively reduce their trade costs by adopting those standards. This could imply compliance costs that are high relative to the value of exports; hence, whether exporters will find it optimal to comply is not clear *ex ante*. Also, standards defined by rich industrialised countries may not suit poorer countries. Finally, in a Q&A paper, the EU Commission states that harmonisation of standards "is not on the agenda".[2] Rather, TTIP will include mutual recognition agreements (MRAs), for example in the automotive, chemical, pharmaceutical, medical device, and cosmetics industries. This means, that multiple standards will remain. Whether and how the recognition will extend to third countries depends on details. Is the mutual recognition agreement limited to products produced in the TTIP countries? Or does it apply to any good produced according to either standard, regardless of the producing country? And, if so, who carries out the conformity assessment and how?

In summary, some aspects of the TTIP will certainly be discriminatory; other aspects could help outsiders as well as insiders, but there is no guarantee that this will happen; much depends on the small print of the agreement.

Which countries are most vulnerable?

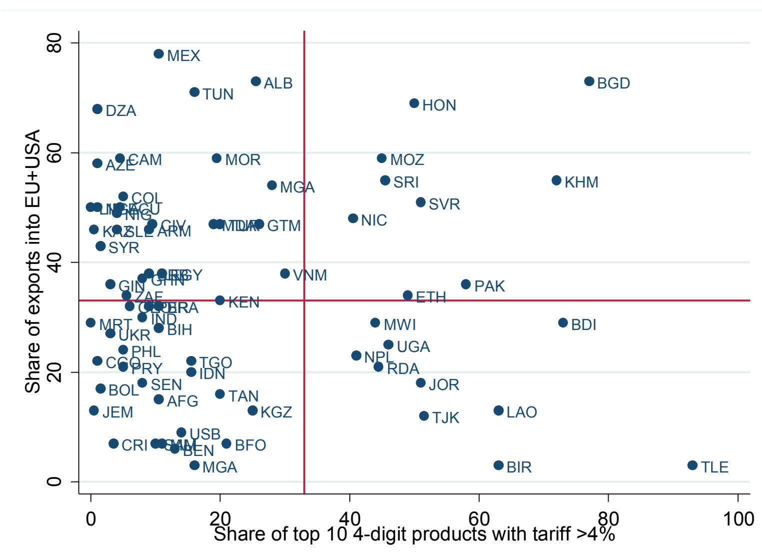
Quite a few developing countries export goods to the EU or the US that are currently subject to high import tariffs. Should these tariffs fall or be eliminated by TTIP, producers from developing countries will face tougher competition from EU or US firms. This is regardless of whether they are currently exempted from tariffs (through participation in a generalised system of preferences, or GSP, programme) or not. The more strongly a country's economy depends on exports of such goods to the TTIP countries, the more strongly it could be affected by trade diversion. Figure 1 plots

2 http://ec.europa.eu/trade/policy/in-focus/ttip/questions-and-answers/

countries' exports to the EU and the US as a share of total exports (y-axis) against the share of top ten export products affected by import tariffs of higher than 4% in both the EU and the US. Countries located in the top-right of the figure are vulnerable to trade diversion. For example, Bangladesh (BGD) and Cambodia (KHM) strongly rely on exporting textiles to the US. Right now, they are exempted from the 12% import tariff that the US levies on EU textiles. With TTIP, these tariffs vanish; producers from eastern Europe become more competitive, and may gain market share to the detriment of firms from Bangladesh and Cambodia.

Countries in the top-left of the figure depend heavily on exports to the EU and/or US, but trade diversion from preference erosion is not important. Yet, they may be affected by discriminatory regulatory cooperation. Some of these countries, such as Algeria (DZA), primarily sell raw materials – they are safe. Others, such as Mexico (MEX), sell industrial supplies and may be hurt if regulatory cooperation within TTIP favours insiders. Both groups of countries should, however, benefit if income in the TTIP countries goes up and their demand for raw materials or industrial supplies rises.

Figure 1 Export exposure and MFN tariffs, developing countries



Source: UN COMTRADE and WITS; own calculations and illustration.

Therefore, whether the TTIP helps or hurts developing and emerging economies depends on the strength of the negative trade diversion effect relative to the demand effect. To sort out this ambiguity, one needs to simulate counterfactual experiments using an appropriate model of the world economy.

Simulation results: The roles of sector detail and spillover effects

Much of the traditional literature on the *ex ante* assessment of trade policy initiatives uses computable general equilibrium (CGE) models. Recently, Costinot and Rodríguez-Clare (2015) propose smaller scale models that can be structurally estimated and applied to *ex ante* analysis. We discuss two simulation exercises that make use of these techniques.

Felbermayr et al. (2014) apply a single-sector macro setup based on Krugman (1980) to 176 countries using observations for the base year 2012. They employ econometric estimates on the average trade cost reduction found for about 200 existing trade agreements and take these as the best guess of what could happen within TTIP. They do not assume that trade cost savings spill over to outside countries. The authors find that real per capita income could, after an adjustment period of about ten years, be 4% and 5% higher in the US and Europe, respectively. This study also shows substantial losses for outsiders (see Table 1). On average, outsiders lose 0.9% of real GDP per capita. The losses are largest in close trade partners of the EU or the US (e.g. Mexico); for most developing countries they are much smaller. Compared to yearly trend growth rates of about 4%, a loss of 2% over ten years does not seem overly dramatic.

This view contrasts with the micro perspective adopted by Aichele et al. (2014), who use a multi-sector setup based on Eaton-Kortum (2002). This model is structurally estimated in the same way as Felbermayr et al. (2014), but features 32 sectors and incorporates national and international input-output linkages. While the scenarios cannot be easily compared numerically, Aichele et al. (2014) paint a much more optimistic picture: about 25% of the non-TTIP regions lose from the agreement, while 75% win, albeit only marginally. What is the reason for this discrepancy between the macro and the micro perspective?

Table 1 Change in real per capita income due to TTIP: Macro versus micro view (%)

	Macro view	Micro view		
	Default	Default	Spillovers	TTIP+Doha
EU	3,94	2,12	2,57	2,26
USA	4,89	2,68	3,25	2,77
EFTA	-1,91	0,15	0,55	0,48
Canada	-3,09	0,12	0,49	0,19
Australia & New Zealand	-1,80	0,08	0,20	0,55
Turkey	-1,56	0,10	0,35	0,30
Eurasian Customs Union	-0,96	0,17	0,28	0,89
China	-0,48	-0,23	0,20	0,41
East Asia	-0,51	-0,13	0,01	0,32
ASEAN	-0,07	-0,19	0,28	0,42
South Asia	-0,28	0,06	0,23	1,25
Central Asia	-0,57	0,20	0,50	0,21
Middle East & North Africa	-0,64	0,12	0,38	0,65
Subsaharan Africa	-0,50	0,10	0,37	0,81
South African CU	-1,58	0,15	0,38	0,67
Latin America & Caribbean	-0,87	0,11	0,38	0,44
MERCOSUR	-0,83	0,00	0,18	0,20
Pacific Alliance	-2,13	-0,07	0,25	-0,16

Notes: Spillovers: non-tariff trade costs on exports of non-TTIP countries into EU and USA fall by 20% of the reduction within TTIP. TTIP+Doha: TTIP basis scenario plus elimination of all remaining tariffs between WTO countries.

Sources: Macro view: Felbermayr et al. (2014); micro view: Aichele et al. (2014) Table 1 also shows what happens when trade cost savings within the TTIP spill over to third countries. In such a situation, TTIP could make all major regions better off. Importantly, these spillovers also increase the gains for TTIP signatories. Finally, the table shows what happens when the TTIP default scenario is accompanied by a full elimination of all tariffs between WTO countries worldwide. This is less beneficial than the spillover scenario for rich countries, but tends to benefit most developing countries more.

In a multi-sector approach, trade diversion can only happen when the TTIP insiders are competitive in the export industries of the outsiders. Moreover, due to the presence of input trade, outsiders can benefit from cost savings achieved within TTIP to improve their own competitiveness. This counteracts the trade diversion channel. Moreover, when output in TTIP countries expands, third countries may benefit by higher exports of inputs towards the EU or the US. The macro approach has no sector-level detail; nor does it allow for trade in intermediate inputs. It is still useful since – in a reduced form fashion – it sheds light on outcomes if the TTIP changes the pattern of comparative advantage across sectors and countries. This is certainly possible, at least in the long run when technologies and factor endowments adjust.

Conclusions

TTIP could certainly harm outsiders, in particular if it is ambitious on mutual market access and less so on regulatory cooperation. But much depends on the details of the arrangement. Generous rules of origin, inclusive mutual recognition of standards, and a parallel dismantling of remaining worldwide tariffs could help. Importantly, insiders also gain more from the agreement if it is more inclusive.

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An EU-US trade deal: Good or bad for the rest of the world?

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The launch of negotiations on a transatlantic trade and investment deal was widely welcomed. The prime minister of the UK, David Cameron, called it a “once-in-a-generation prize” and produced numbers on why everyone should be happy; gains of £100 billion for the EU, £80 billion for the US and £85 billion to the rest of the world. A *Financial Times* (2013) editorial reassured us that “[t]he common objection that bilateral deals divert trade as well as create new trade has little force when ‘bilateral’ already covers half the world economy”. But the focus on benefits, and more recently on impediments, is obscuring a serious downside. Developing-country exporters could be hurt by this deal unless a special effort is made to protect their interests.

The aspect of the deal that provokes the greatest excitement – its focus on regulatory barriers like mandatory product standards – should evoke the greatest concern. Since tariffs in the EU and US are low – on average less than 3% – the preferential lowering of these tiny tariffs will not seriously disadvantage outsiders except in some high-tariff products such as shoes. But with mandatory standards, such as those pertaining to safety, health, the environment, or simply compatibility, the conditions of market access are brutal and binary. Either you can meet the agreed standard and sell, or you can’t and don’t. And what you can do depends entirely on how the agreed standard is set.

The voluminous research on regionalism with its almost exclusive focus on tariffs and quotas provides only limited illumination on the implications of regional agreements on standards. Baldwin (2000) presented a useful analytical framework for the analysis of mutual-recognition agreements, but assumed identical countries with identical costs of complying with standards. Few previous studies have empirically explored the impact of shared standards on trade (see, for example, Swann et al. 1996, Moenius 2004, Shepherd 2007, Reyes 2011 and Oreficea et al. 2012). I draw here on my research with Maggie Chen (Chen and Mattoo 2008).

There are three main types of agreements dealing with technical barriers to trade.

- The simplest, and potentially most powerful, is the mutual recognition of existing standards, whereby a country grants unrestricted access of its market to products that meet any participating country's standards.

This was the approach taken in principle by the EU, with the spur of the *Cassis de Dijon* judgement of the European Court of Justice. Mutual-recognition agreements are, however, not likely to be an option if there is a significant difference in the initial standards of the countries, as became evident in the context of the EU.

- The second is a certain degree of harmonisation as a precondition for countries to allow products of other countries to access their markets.

The most important example of such harmonisation is the *New Approach* of the EU, which resulted in a set of directives from the European Commission laying out essential health and safety requirements for most regulated products. Available evidence suggests that harmonisation within the EU tended toward the high range of initial standards due to pressure from the EU's richer and more powerful members (see Vogel 1995). In many other cases, neither mutual recognition nor harmonisation of substantive standards may be deemed feasible or even desirable.

- The third type of agreement concerns mutually recognising each other's testing (conformity assessment) of own standards.

In such agreements, country A trusts country B to certify that the products made by country B conform to country A's standards. Examples of such initiatives are the intra-

EU mutual-recognition agreements on some industries and the EU's agreements with a number of other countries. A key element of such agreements is the rule of origin.

Examples

Previous mutual-recognition agreements between the EU and US and between the EU and Canada specify that conformity assessment done in one of the countries, in which products are manufactured or through which they are imported, is accepted by all relevant signatories. Other agreements, such as the one the EU has concluded with Australia and New Zealand, impose restrictive rules of origin which require that third-country products continue to meet the conformity assessment of each country in the region. That is also true of the EU's previous recognition agreements on professional services standards. While a Brazilian orange admitted for sale in Portugal can be sold anywhere else in the EU – thanks to the European Court of Justice's 1979 *Cassis de Dijon* ruling – a Brazilian engineer or accountant licensed in Portugal must still jump through separate hoops in other EU countries.

To intuitively see the potential implications of these different approaches, it is useful to draw a partial analogy between standards harmonisation and mutual recognition, on the one hand, and a customs union and a free trade area, on the other. As in the case of a customs union, the economic impact of standards harmonisation depends on the level at which the harmonised standard is set. Unlike the case of a customs union, standards harmonisation has a market integration effect that creates scale-economy benefits for the firms not just of participating but also third countries. The impact on the firms of a specific country depends on how the costs of meeting the new harmonised level of the standard compare with the benefits from economies of scale in integrated markets. If firms from some countries have a higher variable cost of meeting a standard and reap fewer scale-economy benefits in integrated markets than firms from other countries, then the former can suffer a decline in exports to the integrated market when harmonisation raises some destination countries' standards.

As in the case of a free trade area, the economic impact of a mutual-recognition agreement depends critically on the choice of rules of origin. For the participating countries, a mutual-recognition agreement is in effect a downward harmonisation of standards, since firms are now free to meet the least costly of the initial standards. Trade is stimulated not only by market integration but also by the reduced stringency of the standard. The analytical implications for imports from third countries differ dramatically with rules of origin. If firms of third countries are denied the benefits of the mutual-recognition agreement and must continue to meet the original standard in each market, then they will face unchanged absolute conditions but suffer a decline in relative competitiveness – and hence a decline in exports to the region. In contrast, if the firms of non-participating countries are also entitled to access the entire region by conforming to the least costly standard, then they too reap benefits.

New evidence

In order to test the empirical validity of these propositions, we constructed a dataset that directly identified policy initiatives of different types on standards for manufacturing industries in 42 countries over the period of 1986-2001. These include all OECD countries and 14 developing countries that are the largest exporters of manufactured goods outside the OECD and account for over 80% of non-OECD manufactured exports. The policy measures include each harmonisation directive and mutual-recognition agreement concluded between the countries in the set. We matched the policy measures, which often pertain to a specific attribute (e.g. safety) of a variety of products, with trade data at the SITC (revision 2) three-digit industry level. We then estimated the significance of the impacts of these measures on bilateral trade across countries and over time, controlling for other influences.

Our evidence broadly confirms the intuitive results spelled out above.

- Regional harmonisation significantly increases intra-regional trade in affected industries. Exports to the region of excluded developed countries also increase, but exports of excluded developing countries decline.

These asymmetric effects may arise because developing-country firms are hurt more by an increase in the stringency of standards and benefit less from economies of scale in integrated markets.

Otsuki et al. (2001) also found that when the EU decided in the late 1990s to harmonise aflatoxin standards across member states, eight states (including Italy, the Netherlands and Spain) drastically tightened previously acceptable national standards and as a result, African exports to Europe of cereals, dried fruits and nuts may have declined by as much as $670 million.

Chen and I also found that mutual-recognition agreements promote trade both within the region and with the rest of the world. But if they contain restrictive rules of origin, then intra-regional trade increases at the expense of trade with other countries, and developing-country exports suffer most.

Policy issues

Multilateral rules on trade have taken a permissive approach to regional agreements on mandatory standards. While it is neither feasible nor desirable to restrict the freedom of countries to harmonise or mutually recognise their standards, more could be done to strike a better balance between the interests of integrating and excluded countries. This is particularly important because few of the agreements on standards include developing countries, and the big differences in social preferences over issues such as safety and the environment suggest that few developing countries are likely to be party to such agreements with industrial countries in the foreseeable future.

Even in the absence of international rules, however, the EU and US could take two steps to avert any adverse consequences.

- First, they could generally favour mutual recognition, which is a more powerful liberalising tool and agree not to impose any restrictive rules of origin.

Just as producers in the EU and US would be able to supply both markets by fulfilling either the EU or US requirements, so would producers in third countries.

- Second, where they do consider harmonisation, there would be a presumption in favour of the less stringent of the original standards.

And any decision to harmonise their standards upward would require credible evidence that the less strict standard is not adequate to meet the relevant regulatory objective. This is akin to a test the WTO already applies to departures from established international standards.

With these two commitments in place, the rest of the world could follow the EU and US negotiations with hope rather than trepidation.

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Must TTIP-induced regulatory convergence benefit others?

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One of the central objectives of the negotiations for a Transatlantic Trade and Investment Partnership (TTIP) is to foster a convergence in business regulation between the EU and the US. Negotiators recognise that convergence will not lead to widespread harmonisation of regulatory standards. Rather, they hope that over time firms on one side of the Atlantic will find it less costly to meet regulatory requirements on the other side. In an era when tariffs are either very low or, in many cases, zero for goods imported by the EU and US, it is often argued that the costs of meeting regulatory requirements are, relatively speaking, now the larger barrier to international trade.[1]

A longstanding concern about regional trading arrangements (RTAs) is that they introduce discrimination against third parties. Since Viner's pioneering research, economists have analysed the effects of tariff-based discrimination created once a RTA comes into force. When it comes to so-called behind-the-border regulatory provisions of RTAs, however, there is a strong presumption in the 'multilateralising regionalism' literature that RTAs introduce at most limited discrimination and, in some cases, no discrimination at all (Baldwin et al. 2009). Recently, Baldwin (2014) concluded an

1 Erikson (2014) has argued that "[t]o deliver sizeable economic benefits, the EU and the US have to agree on a package of changes to regulatory policies and practices that are to some extent unknown but that still will be controversial. According to an impact assessment from CEPR (2013), 80% of the potential economic gains from TTIP would be generated by changes in non-tariff barriers and regulations, including service liberalisation and greater openness in public procurement."

assessment of the potential for discrimination in the non-tariff provisions of RTAs with the following remarks:

> *A key lesson from the above discussion is that discrimination is difficult with regard to many 21st century trade disciplines–rules of origin either make no sense, or are 'leaky' since nationality is difficult to pin down when it comes to services, companies and capital. This 'leakiness' of the rules of origin dilutes the discriminatory effects of RTA provisions. (p. 33)*

Given the prominence of regulatory convergence in the TTIP negotiations, whether or not this conclusion is the correct one assumes greater importance, in particular for third parties. The purpose of this chapter is revisit these claims.

This chapter complements that of Mattoo's in this volume. Regulations differ markedly across sectors of the economy. Some regulations must be met before a product or service can be sold in a jurisdiction and, as Mattoo argues, TTIP could result in regulations being adopted on both sides of the Atlantic that are more costly or harder for exporters from third parties to meet.[2] If TTIP-induced regulatory convergence amounts to convergence to higher standards, then Mattoo is concerned that this may become another barrier to entering markets on both sides of the Atlantic.

Other regulations concern the conduct of firms after their entry into a market. A point of departure between this chapter and Mattoo's is that we consider the enforcement associated with the regulation of conduct. For completeness sake, it should be noted that neither Mattoo nor we consider the effects of privately imposed and administered standards. This is not to imply that the latter are unimportant – indeed, many firms exporting from developing countries contend that they are. Rather, the point is that

2 Once one allows for the possibility the lobbying by domestic firms can influence the direction of regulatory change, then TTIP (and RTAs in general) can be used by such firms to raise their foreign rivals' costs by more. Those familiar with the industrial organisation literature will be aware of this 'raising rivals costs' argument (Salop and Scheffman 1983).

private standards are unlikely to be the focus of the TTIP and are therefore outside of the scope of this short analysis.

The remainder of this chapter is divided into three parts: some reflections on so-called leaky preferences created by provisions on regulatory matters in RTAs; identification of six potential sources of discrimination in regulatory enforcement; and some concluding remarks.

Leaky preferences can still harm third parties

The argument is often made that, as far as many behind-the-border provisions in RTAs are concerned, subsidiaries of companies that are owned by third parties that operate inside an RTA are treated similarly to those firms that are owned by citizens of the nations that signed the RTA.[3] In RTAs signed by the EU and the US, provisions with this characteristic can be found. Since precedent tends to matter in trade negotiations, the inclusion in TTIP of behind-the-border provisions that do not discriminate on the basis of the nationality of a foreign invested subsidiary cannot be ruled out. Are such provisions harmless to third parties?

Sometimes it is argued that discrimination on the basis of nationality of ownership is either harder or costlier to implement than discrimination on the basis of origin of imported goods. On other occasions, it is argued that discrimination is not necessary to meet the public policy objective of the regulation.

Either way, so the argument goes, the strongest possible preferences (on the basis of nationality of ownership) are eschewed and the benefits of any RTA-induced regulatory change are enjoyed by all firms operating inside the RTA, irrespective of nationality. As a result the benefits are said to ‘leak’ to certain commercial interests of third parties.

3 We leave to one side the interesting question as to whether, in an era of cross-border shareholdings and the like, it makes sense to refer to the nationality a firm.

But this is not the end of the story. The symmetric treatment within the RTA will induce firms from third parties to view more favourably supplying customers located in the RTA through commercial presence inside the RTA rather than outside the RTA. Consequently, leaky preferences could alter investment flows, potentially to the detriment of third parties.

The net effect on a third party is, therefore, going to be determined by the benefits arising to its existing subsidiaries operating inside the RTA in question and the loss of investment, value-added, and jobs (in the sector in question and among the suppliers to that sector) as firms relocate commercial activities from outside the RTA to inside the RTA. The *absence* of certain preferences does not necessarily imply the absence of losses by third parties.

Furthermore, the fact that discrimination on the basis of nationality of ownership is not happening at a point in time does not mean that circumstances (economic, political, or technological) cannot change and that discrimination won't occur in the future. For foreign investments with a long payback period, this consideration may be relevant and could raise risk premia. One way to limit such uncertainty would be to ban in an RTA such nationality-based discrimination against foreign investors (for more on this see the concluding remarks.)

Potential sources of discrimination in regulatory enforcement

There are also ways, sometimes subtle, in which RTAs can introduce discrimination in the enforcement of regulations on commerce within a jurisdiction. Since one stated purpose of TTIP is to reduce regulatory burdens on firms operating in the US and EU, then one might ask why US and EU negotiators would not ask for preferential treatment in the implementation of certain regulations compared to third parties? There is nothing preventing them from asking.

There are six ways in which RTAs can result in discrimination against third parties in regulatory enforcement. These are:

1. *Exemptions from a regulation for parties to an RTA*. A weaker variant is when the thresholds that trigger regulatory action are more favourable to RTA parties than to non-parties. Australia, for example, has granted certain RTA partners higher thresholds before transactions are referred to its Foreign Investment Review Board for examination. Of course, fully-fledged mutual recognition accords amount to an exemption from a trading partner's regulation so long as the counterpart regulatory standard is met at home.
2. *More favourable statutory tests and evidential standards for parties to an RTA*.
3. *In regulatory matters where time-to-market is commercially significant, parties to an RTA may receive faster (expedited) reviews.*
4. *Less invasive remedies or punishments for firms from parties to an RTA*.
5. *More expansive rights of appeal for firms from parties to an RTA*.
6. *Shifts in enforcement resources away from parties to an RTA to non-parties*. Should TTIP result in greater confidence in food safety standards implemented on the other side of the Atlantic, independent regulators in the EU and US might shift more of their enforcement resources to inspecting agricultural products and processed food from third parties. Such a shift might not be mentioned at all in any legal text for the TTIP.

Contrary to some assertions in the literature, it is possible to have a single regulator implement different regulatory rules depending on the location of the firm whose matters are before it. Those differences may be of considerable commercial importance to firms inside the RTA and could affect their competitive position vis-à-vis firms outside the RTA. For sure, such privileged treatment could be 'leaky' in the sense described in the previous section, but as argued there, that does not mean there are no adverse effects on third parties.

Should the TTIP negotiations be concluded, third parties may wish to check the provisions relating to regulatory matters to see if they contain any of the six forms of favouritism outlined above. That there are six highlights a key point, namely, that regulatory processes can be reformed through trade agreements in ways that introduce discrimination against third parties. TTIP-related preferences, and more generally RTA-related preferences, need not be confined to traditional border measures such as tariffs and quotas. Indeed, the prominence given to regulatory convergence in the TTIP could spawn a new generation of preferences that harm the commercial interests of third parties. Vigilance on the part of the latter would seem prudent.

Concluding remarks

One of the reasons why the effects of TTIP's provisions on third parties matter is the central role that discrimination is said to play in inducing those third parties to accept the 'multilateralisation' of the provision at the WTO or to seek to join this RTA. It is worth recalling that the essence of 'domino regionalism' was that third parties were harmed by tariff discrimination and to avoid these losses would have an incentive to join the club.[4] Whether the same logic applies to non-tariff measures is therefore important for assessing the likely future course of trade agreements, regional and multilateral, in the 21st century.

The purpose of this chapter has been to challenge the rather benign view of behind-the-border provisions in RTAs that has arisen in the 'multilateralising regionalism' literature. This benign view sits oddly with the pronounced goal of the EU and US to induce the spread of their regulatory norms to other countries once TTIP is concluded. In this chapter we have argued there are several sources of discrimination in regulatory

4 In the case of TTIP, however, we have argued elsewhere that third parties have alternatives to seeking to accede to TTIP (Aggarwal and Evenett 2015).

enforcement that are neither costly nor difficult to implement. Our findings then align with those of Mattoo in his chapter in this volume.[5]

The actual degree of discrimination against third parties from the behind-the-border provisions of any TTIP accord cannot readily be assessed before the terms of such an accord are made known. Even then, reallocation of enforcement effort from parties to TTIP to third parties may not be apparent until years after TTIP has come into force. For these reasons, it would seem unwise to dismiss out of hand the potential for discrimination in non-tariff measures. Experience may well lead us in the years to come to the conclusion that such discrimination is as bad as, and possibly worse than, more traditional tariff-based discrimination against third parties.

Balance also requires us to state that, in principle, TTIP could include provisions on regulatory matters that explicitly rule out discrimination on the basis of nationality during any stage in the administration of a regulation. This would be not dissimilar to the provisions[6] in the North American Free Trade Agreement that ban the use of performance requirements on foreign investors from any country not just investors from Canada, Mexico, and the US. Even if such provisions were included in TTIP – and to date there are no indications that they will be – then questions would still arise as to whether third parties or their commercial interests could enforce any ban on nationality-based discrimination.

5 And, for that matter, also with Winters (2014), who has argued "[t]he rhetoric surrounding TTIP is to create a framework for the gradual harmonisation of regulations, first across the Atlantic and then generalising out for the global good; this view is accepted by many of my colleagues and indeed sounds quite benign. The problem is that, while a benign outcome cannot be guaranteed, one can guarantee that the countries that are outside the club will perceive it quite differently and may act accordingly."

6 In particular, Article 1106.

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Could TTIP become an all-inclusive project? Some remarks concerning alternative responses

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The negotiation of mega-trade deals presages the start of a new era in the global trading system. A commonly held belief about the Transatlantic Trade and Investment Partnership (TTIP) is that it will generate gains for the parties involved, namely the EU and the US. However, its implications for the third parties and the multilateral trading system are less certain. Assessing the impact on non-TTIP economies is not straightforward, as negotiations to date do not yet provide a foreseeable future path to mitigate any attendant risks. However, one thing is clear. The global challenges brought by TTIP will be greater:

- the higher the risks and the consequences of *discriminatory impact*;
- the more restrictive and stringent the *regulatory measures* for extra-TTIP trade, and
- the less remote the possibility of finding *acceptable solutions* for increasing concerns of third countries.

Risk of discrimination

The most anticipated impact of TTIP negotiations relates to the risk of discrimination against third-country exports. Discrimination here leads to *trade diversion,* i.e. the substitution of lower-cost imports from third countries with the higher-cost imports of TTIP members due to differential tariff treatment. Such discrimination can lead to welfare losses, the magnitude of which depends on global trade patterns and competition dynamics. It seems that labour-intensive sectors are more vulnerable.

Fontagne et al. (2013) claims the trade diversion effects will be 'little' as existing trade patterns reveal that a TTIP-induced increase in transatlantic commerce does not replace third-country exports, but rather displaces domestic production instead. Other empirical analyses, including Felbermayr et. al (2014), find that the adverse welfare implications can be high for the EU's and US's trading partners. Such studies also highlight the vulnerability of countries with existing regional trade arrangements (RTAs) with the US or EU, such as Canada, Mexico, Switzerland, Chile, Japan, and Turkey. These nations are expected to face an *erosion of their trade preferences* once TTIP comes into force.

For larger economies with no such RTAs with the US or EU, the case seems to be equally alarming for their exports – in particular for Argentina in agriculture, and India, China and Brazil in manufacturing. Hence, many of these countries might be interested in 'docking' arrangements into any mega-trade deal to avoid or limit such losses. For example, Mexico's interest in being included in TTIP is no secret. Turkey's EU Minister Volkan Bozkir recently stated that Turkey might freeze its Customs Union deal with the EU if the planned TTIP does not include Turkey.[1]

Offsetting spillover benefits?

It has been contended that the harm done by trade diversion and preference erosion can be compensated through *spillover benefits*. Some studies show that in general equilibrium analyses, third countries also gain from the implementation of TTIP through the elimination of cost-increasing trade measures between the US and the EU. Accordingly, non-TTIP economies benefit from two developments. The first are *direct spillovers* that emanate from 'improved regulatory conditions' as a result of regulatory

1 Remarks to this effect were widely reported around 14 November 2014. See, for example, http://www.hurriyetdailynews.com/eu-backs-us-position-on-turkeys-inclusion-to-ttip.aspx?PageID=238&NID=74185&NewsCatID=429.

convergence between the TTIP members. Following this logic, outsiders will face less stringent and less divergent conditions in US and European markets.

Second, benefits may follow from *indirect spillovers,* which can accrue when third countries adopt harmonised TTIP standards (CEPR 2013, European Commission 2013). However, the cost-decreasing and trade-increasing impact is blurred when TTIP is regarded a global-standard-setting hegemonic power which non-TTIP signatories resist. The concerns are immense because it is not yet certain that TTIP negotiations will eventually induce 'lower trade costs' for third countries. Felbermayr et al. (2014) argue that three factors underlie this uncertainty: assumptions about indirect spillovers have no supportive evidence; TTIP is largely based on market access in goods and services with, in fact, little likelihood of regulatory convergence; and an automatic admission of third country products under mutual recognition has not been guaranteed.

Moreover, TTIP negotiators have not yet made assurances that regulatory barriers on the whole will not be more restrictive than those applicable today. Third countries worry that TTIP will be a 'game changer,' in the words of many policymakers on both sides of Atlantic, whereby standards and regulatory barriers are raised. TTIP negotiators refer to this as 'strengthening the multilateral system' in a wide range of areas of policy, from environment to labour standards, intellectual property issues, export restraints for raw materials, state-owned enterprises, competition policy, and localisation measures. But for many third countries, this is tantamount to dictating global rules and ultimately making non-TTIP economies bystanders and rule-takers.[2] The fears of many nations are hardly surprising when EU and US leaders frequently refer to the 'rise of emerging economies' as one of their main motivations for initiating the TTIP talks.

2 But, remarkably, many Europeans are equally concerned that TTIP will actually weaken the existing standards, ranging from food safety to environment, with the principal offending instrument being investor-state dispute settlement mechanisms.

Possible responses by third parties

It is probable that key third countries that expect TTIP to become a global rule-setter are unlikely to adopt a 'wait-and-see' policy. One possible response for them could be to pursue a 'proactive approach' to challenge the results of TTIP negotiations by WTO means, including initiating trade disputes. However, such disputes will lead to a dysfunctional WTO dispute settlement mechanism (apparently the most successful arm of the WTO) as it becomes preoccupied with many such cases. Many emerging powers may look to form rival blocs to deflect the effects of TTIP. But the temptation to do so may be tempered by realist instincts in those economies outside of TTIP that are involved significantly in global supply chains.

Another approach could for third parties to seek to 'dock' into TTIP. Two main routes could be considered. First, outsiders could seek for themselves a 'special status' from the EU and US to offset the discriminatory effects of TTIP. For example, outsiders could lobby for a *free trade agreement* with TTIP members as an insurance policy. But such third parties must be ready to face tougher standards and calls for extensive commercial concessions. Here it must be remembered that the new generation of FTAs were designed to be deep and comprehensive agreements to address domestic regulatory issues anyway.

The second route could be to develop an 'accession mechanism' in TTIP. An open-door policy reduces political tensions and reinforces trust among trading nations. In this context, it is better to seek all-embracing solutions. Yet such solutions should take account of the following factors as well.

To start with, a proper accession mechanism of direct relevance to third countries might give rise to optimism that counters concerns over a *Transatlantic Fortress!* At the moment, however, no such mechanism is expected to be included in TTIP, as the parties to the negotiation have made clear. Given the uncertainty, and the complex and protracted nature of developing an *accession mechanism* for a mega-deal, it may seem practical for many third countries to enter directly into bilateral negotiations with TTIP members. On the other hand, multiple individual efforts would lead to significant negotiating and related transaction costs for the US and the EU. There would in many cases also be an asymmetric power relationship for third countries seeking admission to TTIP. Indeed, while the creation of a vigorous accession mechanism sounds alluring, it is improbable that the TTIP parties would accept new members on an unconditional basis. This approach may also induce political costs of free-riding by third countries, which are not appreciated by the US and the EU.

Nor is the TTIP likely to be a typical international convention where the accession of a new member depends solely on the latter's ratification of the convention. It seems more realistic to expect that TTIP would set conditions for membership that others must accept before joining. Ideally, any accession criteria should be designed to motivate others to expand trade liberalisation and to accept better regulations so that global production networks can operate smoothly. This is also a vital strategy for US and European producers to take part sustainably in global chains.

Moreover, it should not be forgotten that most of the TTIP negotiations are said to be about regulatory barriers. The High Level Working Group (HLWG) of US and EU officials noted that the main objective here was to eliminate behind-the-border obstacles to trade. It also observed that adverse effects of non-tariff barriers could be reduced by pursuing 'new and innovative' approaches, mainly *harmonisation, equivalence* and *mutual recognition* of conformity assessment procedures which are often included in regional trade agreements among industrialised countries. Such choices tend to be dependent upon specific circumstances of particular regulations and standards; their transparency, impartiality and proportionality; the compatibility of market surveillance; and so on. Least costly alternative methods of facilitating trade could be the starting point. For example, mutual equivalence allows for potentially distinct ways of achieving accepted regulatory goals. Thus, countries can liberalise trade and maintain distinct domestic regulatory tools. However, full harmonisation or mutual recognition methods require more extensive talks to develop common rules and can damage third countries, especially when the latter are less capable of adopting these rules (Messerlin 2014).

The final point relates to the impact on multilateralism. It is often expressed that the Doha Development Round is already dead and any effort to reincarnate it is futile. A stringent and unrealistic 'single undertaking' and the 'consensus' requirement may have contributed to this. Recent years have shown that one agenda to make rules on many trade-related policy issues has not succeeded. However, mega-trade deals are sometimes said to be bringing multilateralisation by the back door if the WTO track is stuck. On this view, TTIP is said to be a 'game changer' to strengthen trade rules going beyond existing WTO disciplines (the so-called WTO+ provisions). But 'success' here depends on the ability to translate TTIP disciplines into WTO accords and on whether the former reflect best practice for other WTO members. Confidence-building measures – such as improving capacities of third countries to adopt higher standards, development of their infrastructure, or steps to enhance regulatory cooperation – facilitate the realisation of indirect spillovers.

Responses by third countries to TTIP largely rest on the US and EU's ability to effectively deploy soft power to advance trade-friendly norms that, in turn, encourage outsiders to become stakeholders, and on developing a plausible accession mechanism. It will be equally crucial to prove that TTIP is not being created to secure a transatlantic market against others. For their part, developing countries need to put multilateralism at the centre of their strategies. The WTO, in spite of its weaknesses, is the most plausible venue to discuss any best practices codified in TTIP.

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Towards rival trade regimes? TTIP and multilateralism as seen from the Beijing APEC summit

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A global trade regime forged in the crucible of war

In 1937, Franklin Roosevelt's Secretary of State Cordell Hull wrote: "I have never faltered, and I will never falter, in my belief that enduring peace and the welfare of nations are indissolubly connected with friendliness, fairness, equality and the maximum practicable degree of freedom in international trade".

Four years later, in August 1941, Roosevelt met with Winston Churchill and together they issued The Atlantic Charter which, in article 4, incorporated Hull's vision. In 1947, the General Agreement on Tariffs and Trade (GATT) came into existence. The rest, as the saying goes, is history. The second half of the 20th century was so markedly different from the first half.

The Atlantic Charter-inspired GATT trade regime was a roaring success. Its impact spread far beyond the North Atlantic. It allowed Japan to adopt an export-driven economic policy that raised it rapidly from the ashes of defeat in World War II. It also allowed the citizens of the 'Four Dragons' – Hong Kong, Singapore, the Republic of Korea and Taiwan – to rise from extreme poverty to enjoy high incomes. Most significant of all was the realisation by the Beijing leadership immediately after the death of Mao Zedong (in 1976) that China's route to prosperity lay not in rejecting globalisation, but embracing it. It was arguably a major institutional force in the victory of the West in the Cold War.

In 1986 China applied for, and in 2001 gained, membership to the WTO. The rest, as the saying goes, is the history of the early 21st century, as China rapidly emerged as the global mega-trader. Today, China is the first or second trading partner of countries around the world.

The world was reminded last year that trade continues to contribute to peace. The day of 6 June 2014 was a highly emotional one: gathered in Normandy to commemorate the 70th anniversary of the D-Day landings were not only the leaders of the allied nations, but also German chancellor Angela Merkel. Similarly, German war veterans embraced their former British, French, Canadian, American and other enemies.

The 21st (Pacific) Century

Jonathan Fenby wrote: "In 1949 Mao changed China; in 1979 Deng changed the world" (Fenby 2012). With China's rise and a revival in Indian economic growth, many refer to the 21st century as the Pacific Century.

The century from 1838 (the year of the First Opium War) to 1949 (Liberation) was what the Chinese refer to as their era of humiliation, when everything Chinese – society, economy, pride, order, sovereignty, etc. – plummeted. The Western powers and Japan played by no rules and simply plundered China.

From long-standing victim of mercantilism and imperialism, China has very recently emerged as a major actor in globalisation. China's rise has been awesome both in terms of scope and speed; and especially in the combination of scope and speed.

Whether China will become a contemporary 'imperialist' power is arguably the most critical question of the 21st century. In a brilliant documentary entitled the *Rise of the Great Powers*, CCTV traced the rise of the great global maritime commercial powers, of which to date there have been nine: Portugal, Spain, the Netherlands, Britain, France, Germany, Japan, Russia/USSR, and the US. In every single case, the rise of these nations entailed conquest, war, imperialism and (in most) slavery. The peaceful rise of a great power has never happened.

Can China, therefore, in the words of Chinese thought-leader Zheng Bijian, achieve great power status through a peaceful rise (Zheng 2005)? The answer to that question will in turn be determined by the answers to two fundamental questions:

1) Can China implement internal reforms – social, economic, environmental and political – to further its development?

2) How will the rest of the world (especially the US) react to China's rise and thereby set the global context?

The evolution of the global trade system will have a significant impact on the answers to both questions.

Leading international institutions stuck in the 20th century

The post-war (Bretton Woods) institutions served the world well in the second-half of the 20th century. All three – the WTO, the IMF and the World Bank – have failed miserably to adjust to the 21st century and to accommodate new actors.

Arguably, this has been most egregiously the case with the WTO: the Doha Round is a pathetic narrative. The causes for the failure are many; but it is arguably above all a failure of leadership on the part of the established dominant global power, the US. Washington has not succeeded in determining whether it should engage or contain China. It has also failed to reform and reinvigorate the rules-based multilateral global trade regime.

Since the collapse of the Cancún WTO ministerial meeting in 2003, the US has sought alternative alliances of the willing as a means of circumventing the multilateral trade regime. This was highlighted in a 22 September 2003 article in the *Financial Times* written by then US Trade Representative Robert Zoellick entitled "America will not wait for the won't do countries" (Zoellick 2003).

The most recent manifestation of this pursuit of alternatives is the negotiation of two 'mega-regional' trade agreements: TTIP (the Transatlantic Trade and Investment Partnership) and TPP (the Trans-Pacific Partnership). TPP, the Pacific-facing US initiative, excludes the mega-trader China. Both initiatives have implications not only for Chinese commercial interests, but also for Beijing's place in the global rule-making on trade.

Perspectives from the November 2014 Beijing APEC summit

The contemporary 21st-century Pacific, in contrast to its Atlantic counterpart, has been characterised by geopolitical turbulence. Though the Pacific region has witnessed fast growth rates of cross-border trade, there are potentially explosive territorial and other disputes.

There have been numerous pan-Pacific summits in the last decade, with very few tangible results. The Beijing APEC summit in the week of 9 November 2014 may turn out not only to be an exception, but also a major landmark; as the headline of the 13 November editorial in the *South China Morning Post* put it "A new world order takes shape as China rises".

Chinese President Xi Jinping announced that amid all the nascent alternative trade regimes, Beijing would pursue the creation of the Free Trade Area of the Asia-Pacific (FTAAP). Though China is excluded from TPP and the US is included in FTAAP, the two are clearly rival systems; this is a leadership contest. The member states of APEC unanimously endorsed the FTAAP proposal.

China's proposed leadership, as manifested at the APEC summit, encompasses more than trade. Most important is China's role in re-engineering the globe through massive investments in infrastructure. As China pursues the 'new silk road', both on land and at sea, it has also set up rival institutions to the World Bank – in particular, the Asian Infrastructure Investment Bank (AIIB). With Beijing having pledged initial capital of $40 billion, the AIIB provides a rival to the (US-dominated) World Bank and to the (Japanese-dominated) Asian Development Bank (ADB).

Previously, China and the US had been at loggerheads over climate change. Recent United Nations Framework-Convention on Climate Change (UNFCCC) summits in Copenhagen, Cancún and Durban failed. In November 2014 in Beijing, Barack Obama and Xi Jinping signed what is seen as an historic US-China climate change deal that may pave the way to a constructive UNFCCC summit in Paris in 2015.

Though China has, over the last decade, been the world's major manufacturing nation and global supply chain hub, it has been marginal in global finance. With its outward direct investments now surpassing inward direct investments, recent developments – notably the 'connect' between the Shanghai and Hong Kong stock exchanges – presage the emergence of China as a global financial power. Also, an increasing share of world trade with China is being denominated in renminbi.

The 21st century is the 'Pacific Century', but it is also the information technology (IT) century. Immediately after the Beijing APEC summit, the first World Internet Conference was held in Wuzhen, with the CEOs from China's emerging IT global players in attendance. In his opening remarks, Premier Li Keqiang commented that the Chinese represent 25% of global internet users. China intends to be an internet power – with all that that may imply.

Of the many Asian geopolitical fault-lines, the most acute is the fraught relationship between China and Japan. So bad have relations been during the past few years – the worst since the establishment of diplomatic relations between Beijing and Tokyo in 1972 – that the heads of government of these two colossi, the world's second and third biggest economies, had neither met nor spoken for over two years. There was intense speculation over whether they would at the Beijing APEC summit. They did. They shared a frosty handshake rather than a warm embrace; but it was a small step to peace.

A New World Order – or a New World Disorder?

In this period of profound transformation, the way forward for the world economy is far from clear. The Beijing APEC summit shed light on what shape the Pacific Century might take, and especially on China's leadership role and goals. Will there be one world market? Or rival markets? Seen in this context, does TTIP presage the preservation of an Atlantic order? And if so, does it complement or conflict with the emerging Pacific order?

Will the Pacific order bring peace and prosperity or will it, as was the case with the Atlantic order a century ago, bring mayhem and widespread misery? One thing is for sure – the emerging trade regime will have a significant impact. Will Cordell Hull's vision, as inscribed in the Atlantic Charter, become a reality in the Pacific as well? At times such as these, trade policymakers around the world have a huge responsibility.

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Part II

National perspectives

TTIP as seen from the Antipodes

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If the liberalisation of transatlantic services trade draws the WTO services negotiations out of the wilderness, and if improved transatlantic standards regulation is translated to the multilateral level, the successful conclusion of TTIP could be a global boon. Higher demand due economic growth induced by transatlantic integration also would be a good thing for the whole world, including Australia. Still, the trade discrimination now needed to achieve such integration – in the Atlantic or the Pacific – corrodes the world trading system to which the transatlantic powers gave birth.

TTIP, the biggest, most ambitious regional trade agreement ever attempted, has garnered little attention in Australia. It's a matter of perspective. Seen from the Atlantic Antipodes, the proverbial room is filled at present with trade elephants, and several of them are standing quite close by.

It is not the immediate prospect of a Trans-Pacific Partnership (TPP) or a pan-Asian Regional Comprehensive Economic Partnership (RCEP) (much less APEC's blue-sky FTAAP) that looms so large. Having stalled several times, there are now longer odds on a successful 'final push' in the TPP negotiations in what remains of the Obama presidency.

Rather, the completion of bilateral agreements with Australia's largest trading partners – China, Japan and Korea – in the past year has absorbed the interest of the business media and the commentariat. The recent promise of Indian Prime Minister Narendra

Modi, on a visit to Australia for the G20 Leaders Summit, to accelerate the pace of the negotiation of a bilateral agreement with India has also excited interest.[1]

The first two bilateral agreements are substantial agreements with Australia's largest trading partners. The third is with a partner (Korea) that last year was almost as important as the US for merchandise trade (both had a 6% share). Australia's largest European trading partner is the UK, which is ranked 12th with a 2% share of merchandise trade.

Table 1 TTIP parties represent a small share of Australian trade

Trading partner	Share of Australia's merchandise trade 2013 (%)
China	27
Japan	10
US	6
Korea, Republic of	6
Singapore	4
Thailand	3
New Zealand	3
Malaysia	3
India	2
Chinese Taipei	2
Indonesia	2
UK	2

Source: ITC Trade Map.

The acceleration of trade negotiations by the Abbott government has changed the landscape of Australia's trade agreements in just 12 months. Still, it is not clear that the commercial realities will change all that much. The demonstrated benefits of Australia's FTAs have been modest. Owing to the fast pace of growth and increasing market

1 The Japan agreement falls short of being comprehensive on agriculture, but both the Japan and Korea agreements include important benefits on goods trade as well as much needed additional access for services and some liberalisation of investment regulations. Details of the China deal are not available at the time of writing, but the government summaries suggest it too will create valuable opportunities in goods and services market access. Possibly adding to the value of the present deal, the Australia-China agreement also provides for a review and perhaps extension of liberalisation after three years.

openness in East Asia in the past decade, trade volumes under Australia's FTAs have not typically outperformed projections of the counterfactual case by much. The policy costs, too, have almost certainly been small. Attempts by modellers to find evidence of trade diversion in Australian FTAs have mostly been fruitless.[2]

The TTIP could spoil this happy story. At least on one reading (Felbermayr et al. 2013), third countries might suffer serious trade diversion penalties due to preferential cuts in non-tariff trade costs across the Atlantic. This projection shows especially severe impacts on third countries that now enjoy preferential access to US or EU markets. Australia would be among the biggest losers from TTIP, with real per-capita incomes falling more than 7% due to loss of sales in the US and EU, even after the agreement's boost to global demand is taken into account.

Is this projection grim or *Grimm*? The latter, most likely.[3] Still, trade models, like other folktales, often have a few simple truths to tell. In this case, the model reminds us that an agreement that makes deep cuts in trade costs between the US and EU will change the commercial outlook of millions of US and EU firms. In assessing their options for supply, production and investment, the transatlantic market – which already accounts for 46% of global demand – will look more attractive than ever. If trade and investment with third countries has higher costs, it may reduce the commercial opportunities for those countries in, and investment from, two of the world's largest markets.

One part of a remedy for countries outside TTIP, evidently, would be to take steps to match the lower trade costs of the TTIP region. Unilateral action to cut trade costs means cutting barriers to foreign competition and investment and improving the operations of

2 The Productivity Commission's 2010 review of Australia's bilateral FTAs has more background on the modest impacts and costs (see http://www.pc.gov.au/inquiries/completed/trade-agreements/report, accessed December 2014).

3 The authors of the IFO study choose a novel method for their projections. They estimate the actual increment in aggregate trade of participating countries due to the NAFTA agreement and the EU customs union as 80%. They then model the preferential trade-costs cuts needed to reproduce an equal increase in 2007 transatlantic trade and the impact of the resulting trade diversion on bilateral trades with third countries in which costs are unchanged.

trade infrastructure. Australia has room to move on all three. There is just no good reason why any Australian tariff in 2015 should be higher than zero; especially when the impact of our 'natural' barriers to trade, such as distance from markets, is taken into account.[4] Nor is there any evidence – after 40 years – of benefit from the delays and conditions imposed by our 'review' of foreign investments before establishment. The contrary is more likely.[5]

Still, the impact on trade costs of eliminating Australia's customs duties on imports from the EU and US is likely to be small; nearly zero in the case of the US. Also, liberalisation of FDI threshold 'review' costs may not make much impression on US and EU firms whose investments in Australia have mostly been resource-seeking. For investors in mines or farms or LNG production, the threshold compliance costs in different markets are probably not important in determining the location of the investment. It is certain that Australia would gain from cutting its tariff and investment barriers, but the biggest 'wins' will not be in exchange with the Atlantic partners.[6]

Then again, the biggest regulatory costs imposed on trade and investment between Australia and the parties to TTIP cannot be cut by unilateral action on Australia's part. They are non-tariff barriers (NTBs) such as quotas on imports of beef or dairy or restrictions on services market entry. Thanks to the 2004 Australia-US FTA, the quotas on goods trade (other than sugar) are now a problem only in the EU. But there is nothing Australia can do unilaterally to cut the costs of EU quotas.

4 The present simple average duty, ignoring anti-dumping penalties, is 2.7%. Duty-free imports somewhat reduce the simple average: collections are only just over 2% of the value of imports. Since currency movements are much larger than that, these duties are nothing more than a nuisance.

5 A good overview is contained in Kirchner (2014).

6 The justification for both, of course, is that an economy banks the benefits of unilateral reductions in trade costs for itself as an increment in returns on global trade. The 'input penalty' of even the low Australian tariff on domestic industry amounted to an annual bill of over $7bn in 2013 (according to the Productivity Commission's 2012-13 Trade Assistance Review, Table 4.1). Most of that penalty was paid by firms that enjoyed no offsetting benefits from the subsidy effect of the tariff.

Indeed, it is not yet clear how much the US and EU will do to cut the impact of these barriers as part of TTIP. If they should do so on a preferential basis, it will threaten trade diversion in the EU market away from Australian imports. Worse, in agriculture at least, an agreement with the US on farm commodities might reduce the prospect of future EU liberalisation of quotas on Australian imports. Offering similar access to Australia would compound the 'injury' to EU producers without the offset of reciprocal opportunities of the scale offered by the US market.[7]

The further liberalisation of services trade barriers, or facilitation of import competition, between the TTIP parties could be much more valuable to third countries, especially Australia. In some services markets (e.g. entertainment), the barriers to foreign competition are similar to those affecting goods trade (e.g. quotas). But in the valuable logistics, business and professional services markets, the biggest barriers are in establishment and accreditation and barriers to temporary residence. Preferential agreement between the TTIP partners to improve the terms of entry and operations for foreign services competitors would likely not divert or saturate demand, nor stand in the way of future extension of better access to third countries on a reciprocal basis.

A TTIP agreement that cuts services entry and operational barriers further than the half-hearted offers made in the Doha negotiations would boost the plurilateral TISA negotiations that have been grinding away for two years in the WTO. Article V of GATS permits preferential treatment in services only when the agreement has "substantial sectoral coverage". A scramble among other TISA participants to erode the discriminatory preference margins in the US and EU markets would see services markets opened on a broad front in at least 50 countries.

7 The picture might be very different in processed food. On a value-added basis, Australia could be a beneficiary of even discriminatory transatlantic liberalisation. Unfortunately, CGE modelling of the agreement is all on the basis of gross-values of trade.

As for the regulatory harmonisation that the US and EU hope to agree upon, although it could be the most valuable innovation of the TTIP, it may not offer all that much to third countries. At present it seems that the TTIP partners differ on how to achieve this objective. A compromise between them could see agreement to cooperate in creating future industrial standards and to adopt common procedures for the management of existing standards. On the content of specific standards, however, such as phytosanitary standards, the two partners may continue to diverge even if they adopt the same procedures.[8]

But not even markets comprising 45% of world production can decree a global standard without the buy-in of producers from elsewhere.[9] Whether Asia, or even Latin America and Africa, will buy-in is anyone's guess. The most plausible conditions under which the rest of the world might adhere to the standards agreed in any TTIP accord is if those standards were brought to international standards-setting institutions for multilateral adoption, or to the WTO for incorporation in a plurilateral agreement.[10] But that is a step beyond the ambitions sketched by the High Level Working Group for TTIP.

The details of TTIP are hard to make out, of course, when seen in a postcard prospect from the other side of the world. What is clear is the grandeur of the concept and the implied greeting on the other side: "No point in wishing you were here."

Seventy years ago, the transatlantic powers that devised the GATT had an offensive goal; mutually discriminatory trade blocs were squarely in their sights. For decades,

8 This compromise has been sketched by Schott and Cimino (2014). Simon Lester, in an article for ICTSD, is more sceptical about the room for compromise between the different EU and US approaches to standards (Lester 2014).

9 The US must surely have learned this from its own history. It has represented a remarkably constant share of world output (just over 25%) for the past 40 years, while the shares of Europe have declined and Asia risen. Yet the world has not gravitated to its industrial or consumer standards, much less its system of metrics.

10 Some of these multilateral standards institutions presently suffer from the same malaise of consensus decision-making that has driven governments to seek regional solutions in the first place. Their agendas move at the pace and with the ambition of the most reluctant participants. A WTO-hosted plurilateral agreement, necessarily offering MFN benefits to non-participants, would be a more suitable framework.

world trade – centred in the Atlantic – had been the victim of narrow discrimination. Measured in 1913 dollars, world imports and exports were just 4% higher in 1939 than they had been in 1913.[11] Despite the concessions made to discrimination in Article XXIV, the asset they built and that we inherit was a reciprocal but non-discriminatory system.

Nowadays, trade negotiations have defensive goals. The mammoth agreements under construction across the Atlantic and the Pacific and in Asia are mutually discriminatory, with no evident provisions for accession. The great legacy of the late 20th century trading system might not withstand such deal-making.

Maybe that's the biggest elephant in the room.

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TTIP and Brazil: Much ado about nothing?

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The Transatlantic Trade and Investment Partnership (TTIP) negotiations that started in February 2013 pose some interesting questions both for the future of the multilateral trade system and for outsiders. The TTIP is supposed to expand trade and investment between the US and the EU, while contributing to the alignment of regulations and technical standards among them. For its supporters, this mega-preferential agreement – that will potentially affect 30% of global merchandise trade, 20% of global FDI flows, and half of the world's economic product – is the model of things to come, a preferential trade agreement (PTA) with 'deep' integration provisions. According to this view, it will improve global governance of 21st century trade issues (e.g. the interface between trade and investment), eventually reinvigorating the world trade system by covering new topics that can later be 'multilateralised' in the WTO.

For critics, TTIP will further erode the relevance of the WTO while being a threat for non-members to the extent that it may foster trade diversion. From the Brazilian perspective, this is not good news. As a matter of trade strategy, Brazil has traditionally emphasised the multilateral track, while being a cautious 'customer' of preferential trade liberalisation schemes. It has followed an inward-oriented development strategy, with offensive trade interests being advanced in the multilateral setting. This is complemented by limited trade preferential deals typically linked to the Mercosur framework. This chapter discusses how Brazil could respond vis-à-vis the TTIP. First, however, a brief review of the Brazilian development strategy is provided to set the stage for the discussion on strategy.

Brazil's development strategy[1]

Brazil is an outlier among the large emerging economies in terms of its growth dynamics. Most of its growth over the last decade has been associated with an increasing labour force while capital accumulation remains anemic (typically below 20% of GDP) and the contribution of total factor productivity (a proxy for innovation) to growth has been minimal. The fact that the economy has been operating close to full employment in the last few years, and the rapid demographic transition that Brazil has been going through (with the total fertility rate now below the replacement level required to assure a stable population), underscore the limits of this approach.

The recipe to unlock an innovation-led growth strategy is well known, but not easy to implement.[2] A competition 'shock', for example, can spark a recovery of productivity levels, but for it to be sustainable, it needs to be flanked by complementary policies (education, tax reform, competition laws, a reorientation of the lending strategy of Brazil's development bank (BNDES) towards areas of the economy that cannot access long-term private financing, etc.). Keeping this in mind, a significant review of Brazilian trade policies is in order and it should be implemented along the following lines:

- First, unilateral trade liberalisation to reduce the anti-export bias implicit in the current development strategy. This should be accomplished not only via gradual liberalisation of the most protected sectors (capital goods, intermediate inputs, automobiles, etc.), but also by improving the predictability of Brazilian trade policies.
- Second, reorientation of the industrial policy, diminishing the prohibitive levels of local content requirements in publicly financed projects, with a view to facilitating an increase in investment in infrastructure and oil exploration, in particular.

1 This section relies on Primo Braga (2014a).

2 See, for example, OECD (2013) and McKinsey Global Institute (2014).

- Third, adoption of a comprehensive national treatment approach, treating imports for tax purposes as local products, independently of local content.

These are necessary steps not only to create market incentives for innovation and productivity growth, but also to allow Brazil to better integrate with dynamic global value chains (GVCs). As already noted, the political economy of such reforms is not easy. The irony is that as time goes by, the resistance to change from vested interests benefiting from the current strategy will become more entrenched since they will fall further back from the technological frontier and will fear even more an increase in competition.[3]

Strategic responses

Given the challenges faced by Brazil to re-energise its economy, it could be argued that unilateral reform combined with 'benign neglect' towards the TTIP and continued emphasis on the WTO constitute the best response at this stage. After all, the unilateral reforms make sense in any case and they would also improve the capacity of Brazilian firms to cope with the implicit discrimination of the TTIP and to better adapt to new regulatory standards.

Such a strategy would align well with the conventional wisdom associated with the official position of the EU and the US vis-à-vis the TTIP. The 'official' narrative is that the TTIP will not generate significant trade diversion simply because most favoured nation (MFN) tariffs are already very low both in the US and the EU. According to this perspective, by focusing on behind-the-border issues and promoting regulatory convergence, the TTIP will not discriminate against non-members. In fact, it will not only contribute to filling gaps in the multilateral trade rulebook, but it will also facilitate

3 For a discussion of the interface between competition, trade and innovation see Primo Braga et al. (2009).

exports from non-member countries to the extent that they will face common standards in these critical markets.

There is, however, a minor problem with this argument. Although on average MFN tariffs are indeed low, there are tariff peaks (e.g. dairy products, sugar, beverages and tobacco) and non-trivial non-tariff barriers (NTBs) on both sides of the Atlantic exactly in some of the areas where Brazil displays significant comparative advantage: the agribusiness sector.

In the last few decades, Brazil has become an agricultural superpower, reflecting its comparative advantage in terms of arable land (the fourth largest endowment in the world), favorable weather conditions and access to water, combined with improvements in the availability of skilled labour and technology. Although agriculture accounts for just 6.5% of Brazil's GDP, it employs roughly 17% of its labour force (OECD 2013). Moreover, the agribusiness sector as a whole (including production, processing and distribution) accounts for roughly 25% of the Brazilian economy and 32% of the country's exports.[4]

Hence, it is not surprising that some analysts have found that the TTIP would generate significant trade diversion for Brazil. Thorstensen and Ferraz (2014), for example, find that in a scenario of full trade liberalisation (full elimination of both tariffs and NTBs) under the TTIP, Brazilian exports would fall by roughly 10% in both markets.

Such a finding suggests that Brazilian 'benign neglect' towards TTIP may be a dangerous option. In other words, Brazil should engage with the EU and the US to promote mutual liberalisation so that the danger of trade diversion could be minimised. Needless to say,

4 Since 1990, average agricultural productivity in grains (including production of cotton, rice, beans, soybeans, wheat, corn, peanuts and sorghum) has increased by more than 100%, and there has also been a dramatic expansion of production of sugar cane and ethanol, as well as meat. Brazil nowadays is a leading exporter/producer of not only coffee and sugar, but also orange juice, soy complex, broiler chickens, beef, corn and pork. With more than 100 million hectares of additional available arable land (excluding rainforest and other conservation areas), Brazil is expected to further increase its strong position in global agricultural trade (see Primo Braga 2014b).

this is easier said than done. After all, the TTIP negotiations are not going to be open to other countries at this stage. Brazil could, however, push for the completion of the FTA negotiations between the EU and Mercosur with a view to softening the impact of the TTIP-related discrimination. It is unlikely, however, that all members of Mercosur would support a significant trade liberalisation deal with the EU in the near future.

This brings us back to the preferred option (unilateral liberalisation, benign neglect, and WTO-related efforts as an avenue to promote multilateral liberalisation in agriculture). Brazil has consistently adopted offensive positions in agricultural trade in the multilateral context – in contrast with defensive positions in non-agricultural market access (NAMA) and services. It played a key role in the formation of the WTO-related G20, a group of developing countries that was formed in reaction to the proposal on agricultural trade put together by the US and the EU in 2003.

The G20, however, includes countries with divergent negotiating interests in agriculture. As long as it was able to focus on distortions introduced by developed countries in terms of subsidies and market access restrictions, there were enough common interests to keep the coalition operational. The moment, however, that the negotiations began to address policy flexibilities in developing countries, the alliance between Brazil (and other Latin American exporters in the G20) and those countries that had defensive interests – in particular, China and India – became fragile.

At the December 2013 WTO Ministerial in Bali, Brazilian negotiators decided to adopt a conciliatory position, given the inflexibility of India and its emphasis on food security concerns. One could argue that the risks to Brazilian agribusiness interests are limited, since the focus of the related programmes in these countries are on products such as rice and wheat, commodities in which Brazil does not have major export interests.

The reality, however, is that the space for multilateral liberalisation is shrinking, not only because coming to an agreement on effective modalities for negotiations is difficult, but also because agricultural trade and production have been going through significant structural transformations since the Doha Development Agenda (DDA) began. As the price of commodities increased in the 2000s and food prices reached new peaks – reflecting crop failures, changes in diet in major developing economies, and the impact of biofuel subsidies – policymakers have increasingly had to deal with a global environment characterised by supply constraints.[5] As a consequence, demands for policy space to protect consumers in net food importing countries have increased. This does not bode well for a negotiating process that is still focused on the distortions introduced by industrialised countries in the past. An 'early harvest' in the DDA focusing on agriculture is unlikely to be agreed upon. After all, the outcome of the agricultural negotiations will inevitably be linked to bargains resulting from the negotiations on NAMA and services. In this context, time is not on Brazil's side, since its ability to engineer a pro-trade outcome in agriculture is inclined to be further eroded by growing food security concerns in key developing nations.

Concluding remarks

Maybe – as indicated in the title of this chapter – the whole concern about the TTIP is a good example of 'much ado about nothing'. It is important to remember that success in the negotiations of the TTIP is by no means assured. In particular, chances that a full liberalisation of NTBs in agricultural trade will occur are, to say the least, not very high. Historic differences, for example, in addressing sanitary and phytosanitary (SPS) matters (the US science-based approach versus the EU's precautionary principle emphasis) conspire against a deal. In any case, the future of the TTIP negotiations and its implications both for non-members and for the multilateral trade system are topics that merit continued attention.

5 See, for example, Meyer and Schmidhuber (2013).

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TTIP and its implications for China

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Since President Obama declared in his 2013 State of the Union address that the US would initiate negotiations with the EU over a Transatlantic Trade and Investment Partnership (TTIP), with the goal of establishing a "high-calibre" free trade area across the Atlantic Ocean, at the time of writing the two sides have undertaken seven rounds of talks. Some progress has been made, although initial discussions were overshadowed by certain events as well as by differences over agricultural and cultural products, financial regulations, and so on.

As the two largest economies in the world, the US and the EU account for approximately half of world output. Their trade volume is nearly 30% of the global total. Moreover, both are the world's most advanced economies with sound market systems, cutting-edge science and technology, established track records of competitiveness, and high living standards. The establishment of a mega-regional trade agreement (RTA) between them is certain to affect the world economy and the making of the future global trade rules. Understanding the impact of TTIP on China is the first step in preparing a proper response by Beijing. However, the negotiations are still ongoing and many of the relevant texts are not yet available, so we can only analyse TTIP's potential impact on China based largely on perceptions on the parties' strategic intentions, in particular those of the US.

Why did the US initiate TTIP?

This is certainly a question of great interest to China. While the WTO will soon reach its 20th anniversary, the US – the founder of the WTO and its predecessor, the General Agreement on Tariffs and Trade – is busy with trade negotiations outside of the organisation. Five years after joining the TPP negotiations in the Asia-Pacific region in 2008, the US launched TTIP with the EU on the other side of the world. Being the global leader of the international trading system for so long, the US now seems to be more obsessed with the regional approach. This dramatic shift of the US from multilateralism to mega-regionalism is reasonably assumed to have deep strategic causes.

Strategic purposes of the US with regard to TTIP

What follows may seem an unfair comment, since the US has worked hard to conclude a deal with India on the Trade Facilitation Agreement and has contributed to a Post-Bali Work Programme for the WTO. Nevertheless, the ultimate priority of the US trade agenda is concluding the Trans-Pacific Partnership (TPP) and TTIP. While some scholars argue that the US is seeking to counter the growing influence in the world trading system of the emerging economies, particularly China, we assume that there are both deeply thought-through intentions as well as passive responses.

In recent years, the rapid growth of developing and emerging economies has led to the rise in their political and economic influence in the world arena. The rapid rise of China in particular, which has attracted the world's attention, is believed by some Westerners to pose challenges to the existing world order and trade rules made by, as it happens, Western governments. Meanwhile, the US and the EU have been weakened by, among others, the two wars in Afghanistan and Iraq in the first decade of this century, the Global Financial Crisis in 2008, and the subsequent sovereign debt crisis in the Eurozone. Many Americans worry about the ability of the US to maintain its position as the world's only superpower.

In order to face the challenges posed by the rise of the emerging economies (especially that of China), to respond to the attendant global power shift, and to continue to maintain its position in the world, the US needs to develop new world trade rules that reflect its own interests and revitalise its own economy. Combined with the North American Free Trade Agreement (NAFTA) and TPP, TTIP has been put on the table as part of the US strategic response to the changes in the current global political and economic situation.

While the US does not have enough power to unilaterally make multilateral rules in the WTO, it is still capable of leading TTIP and TPP negotiations. Although the US will face some difficulties in persuading its negotiating partners, they are largely allies and friends of the country. Once the new trade rules of 21st century are established under TTIP and TPP, covering more than half of the world economy, and given the institutional and technological advantages of its members, the US is expecting to turn these rules into multilateral ones.

Economic considerations and TTIP

The US economy was badly hit by the Global Financial Crisis in 2008. The priority in the second term of Obama's presidency is surely to lift the US out of the mire of financial crisis, to further boost the US economy, and to expand exports in order to create more jobs for American people and more opportunities for American enterprises. The Obama administration has attempted to achieve its goal of doubling exports in five years partly by further regional economic integration, setting new criteria for trade agreements, and speeding up the TTIP and TPP negotiations.

The US is seeking to translate its large domestic buying power into leverage in making a new generation of world trade rules. Due to the vast markets covered by the TTIP and TPP negotiations, other countries may either seek to join regional integration initiatives led by the US, thereby becoming followers of the US and European standards, or develop their own RTAs, which will in turn lead a wider 'spaghetti bowl' and competing sets of international trade rules.

How will TTIP affect China?

China has been left out of the TTIP and TPP clubs, which will weaken the country's influence as the number one trader in the world. The US strategy for mega-RTAs has indeed created some difficulty for China to "close the vast gap between it and the US when it comes to trade policy – and to translate economic power into a seat at the table where the new rules of global commerce are being drafted" (Donnan 2014).

However, every cloud has a silver lining, and so it does in this case. No matter what motivations the US had for TTIP and TPP, their initiation reveals that the US cannot ignore the rise of China. We should not only analyse these negative impact of these mega-RTAs on China, but also recognise the opportunities they have brought China.

How should China respond to TTIP?

Responding to TTIP in a proper way could help China to change its development model, upgrade its industrial structure, and to some degree realise sustainable development. Any trade diversion caused by TTIP may encourage China and its enterprises to attach greater importance to the domestic market, expand the consumption potential of its own people, and thus lead to a change in the development model from an export-oriented to a consumption-led one, and from a resource- and labour-intensive to a capital-, management- and technology-intensive approach. China would upgrade its industrial structure during such a process. Improvements in standards for the environment, technical barriers to trade, sanitary and phytosanitary standards, market access, protection of intellectual property, labour standards and reform of state-owned enterprises could also help enhance public awareness of the drivers of sustainable development.

It is almost universally accepted now that healthy competition is good for every person, every organisation, and every nation. Though we cannot jump to the conclusion that China's initiatives, such as closer cooperation with BRIC partners, building the Silk

Road Economic Belt, the 21st Century Maritime Silk Road and the promotion of FTAAP, are a counter-balance to the US TTIP and TPP, they were indeed good innovations and objectively improve China's influence worldwide. These steps, combined with many other Chinese initiatives around the world, will in turn lead to a reassessment by the US of whether it is a good idea to exclude China from the world trade clubs it is busy setting up. The 2014 APEC summit held in Beijing shows that the US now seems to be emphasising cooperation more than rivalry. If this is the case, a proper response by China to the US mega-RTA strategy might help to further adjust US attitudes and policy.

Conclusions

TTIP is designed to shape global trade flows, set new rules and standards, maintain the leading position of the US, and oblige the rest of the world to accept the new rules the US and EU have made or are making. Accordingly, both China and the rest of the world will come under pressure and need to respond to in a proper way. China has not yet acquired the clout which matches its current weight in world trade and the world economy. TTIP and TPP will further prevent China and other emerging economies from participating in international trade rulemaking, thus keeping them in a rule-taker position for longer. However, no country in this world can really check China's rise.

In responding to TTIP properly, China can channel any pressure into motivation to explore more scientific ways to develop itself, push forward reforms of state-owned enterprises, improve the quality of its economy, accomplish sustainable development, and realise the great rejuvenation of the Chinese nation. On top of that, China will redouble its efforts to promote the Post-Bali Work Program. The future of a prosperous and peaceful world lies in the normal functioning of the WTO.

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TTIP and India: Potential implications and reactions

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The Transatlantic Trade and Investment Partnership (TTIP) has been a wake-up call for those concerned with the proliferation of regional trade agreements. With the two largest markets in the world negotiating TTIP, it will determine the direction and content of international standards across global value chains (GVCs), and its trade rules would be impossible for any multilateral system or commercial activity to ignore. Furthermore, since the US is part of both TTIP and the Trans-Pacific Partnership (TPP), the ramifications of TTIP could be far larger than appears at present.

Reactions to TTIP can be illustrated by two different sentiments expressed by India's senior policymakers. In April 2014, India's commerce secretary talked about TPP and TTIP as potential challenges *and* opportunities, and said that India could not remain an island in the evolving world where many trade policy regulations will reflect those arising from the TPP and TTIP.[1] The Government of India's *Economic Survey 2013-2014* provides another perspective:[2] "*India should also ready itself to face new threats like the Transatlantic Free Trade Agreement (TAFTA) [TTIP] between the US and EU which intends to create the world's largest free trade area, protect investment, and remove unnecessary regulatory barriers*." (page 135; emphasis added)

1 For a summary of this statement, please see http://moneymantra.co.in/detailsPage.php?id=8262&title=News%20Tracks&wrt=MM%20Bureau.

2 http://www.indiabudget.nic.in/survey.asp.

The challenges of and opportunities from TTIP have to be addressed through a package of domestic and trade policies. The new Indian government has begun actively with domestic policy initiatives.[3] India's new Foreign Trade Policy is expected in the near future. The country has already begun to adjust its trade policy regime for the next five years to the potential effects of mega-regionals. We consider below the implications of TTIP for India and the country's possible reactions.

Implications of TTIP for India

TTIP aims to (i) increase market access for goods, services and government procurement; (ii) address non-tariffs barriers; (iii) improve regulatory cooperation and compatibility; (iv) strengthen rules with global relevance, such as those relating to intellectual property rights (IPRs), the environment, labour, digital trade, localisation barriers to trade in the digital environment, and state-owned enterprises; and (v) develop rules, principles or modes of cooperation in several areas such as trade facilitation, competition policy, raw materials and energy, SMEs, and transparency.[4]

The implications of TTIP for India would include a particular focus on loss of market access (trade diversion), IPRs (especially the public health impact of new IP standards), digital trade (data flows and digital privacy), localisation rules, investment, and possible negative or positive impacts of regulations on standards. Four aspects of such implications should be kept in mind:

1. The direct impact of TTIP on India.
2. Implications arising from the links of TTIP to other large negotiations, such as TPP and the Trade in International Services Agreement (TiSA).

3 See for instance the policies announced under the 'Make in India' programme at http://www.makeinindia.com/policies/.

4 See for example, Akhtar and Jones (2014) and Table 1 in Pelkmans et. al. (2014).

3. Positive lessons for India from modes of cooperation and solutions providing convergence on issues.
4. Efforts required to ensure that the final TTIP results are inclusive.

Trade diversion due to tariff cuts

TTIP will lead to the removal of or a major reduction in tariffs. For countries such as India, such tariff declines will imply significant trade diversion in some areas. Table 1 shows EU and US average and peak tariffs for selected industrial product categories. Amongst them, textiles and clothing have the highest average tariffs in both markets, and some of the other categories also have particularly high peak tariffs. The trade diversion effect on textiles and clothing, in particular, would be significant for India: it is third largest exporter of textiles and sixth largest exporter of clothing in the world. This trade diversion effect would be exacerbated by the fact that India would also face trade diversion due to tariff reductions under TPP (of which India is not a member), losing out to its strong competitors in these areas such as Vietnam (a party to TPP negotiations), which would have better access to the US market and through that also to TTIP commercial opportunities.

Table 1 MFN and peak applied tariffs in selected product categories for the EU and US (%)

Product category	EU average tariff	EU peak tariff	US average tariff	US peak tariff
Wood, paper, etc.	1	12	0.5	16
Textiles	6.6	12	7.9	34
Clothing	11.5	12	11.6	32
Leather, footware, etc.	4.2	17	3.7	60
Non-electrical machinery	1.9	10	1.2	10
Electrical machinery	2.8	14	1.4	15
Transport equipment	4.3	22	2.3	25
Manufactures, n.e.s.	2.6	14	2.2	39

Source: WTO (2013).

Other implications

Even stronger overall effects are likely from other areas, such as standards. Regulatory coherence and mutual recognition of standards by the EU and US under TTIP will elevate the higher standards prevailing in these important markets, and provide a stronger basis for them to become incorporated into international value chains. Further, the overall impact of standards regulations would also depend on the inclusiveness of the conformity assessment regime. For instance, if wide-ranging mutual recognition were to be agreed in TTIP with no recognition of third-country bodies, it would create a significant loss of competitive advantage for exporters outside the EU and the US, including from India.

With a generic and cross-product coverage, TTIP-blessed regulations would affect production in several sectors. Additional complexity and difficulty would arise due to the importance of private standards in the extant standards regime of the US. Private standards are periodically upgraded reflecting changes in value systems or competitive pressures faced by producers in these economies. Thus, for sustained access to these markets, the relevant standards regime in India has to be flexible and responsive to such periodic developments.

Furthermore, the high level of discipline/constraint imposed by TTIP in several other areas – for instance, digital trade and localisation – will result in a regime that may not reflect the concerns emphasised by India. With GVCs necessitating smooth cross-border transactions, especially through digital trade, TTIP disciplines in these areas may increasingly become accepted as global trade disciplines. Since these disciplines may not reflect India's present concerns, India's policy space could be constrained in its areas of primary interest. For such eventualities, India would need to prepare a transition mechanism to adapt its domestic regulation to become consistent with TTIP disciplines. In addition, it would need to build strong coalitions with other similarly affected nations to emphasise and explain an alternative viewpoint through discussions and other initiatives involving various stakeholders in the process.

With this background, consider some estimates from two studies showing very different estimates of the likely impact of TTIP on India. According to CEPR (2013), a less ambitious and more ambitious TTIP result would lead to India's GDP increasing by 0.02% and 0.04%, respectively. Felbermayr et al. (2013) show that TTIP will lead to a decrease in India's real per capita GDP of 2.5% in a situation with a tariff-only reduction, and a 1.7% decrease with deep liberalisation including regulatory coherence. Irrespective of the results of simulation studies, a crucial point in this context is that loss from trade diversion could be partially mitigated if India reforms its standards regime to align with the standards prevailing in the EU/US.

Reactions

India's reactions have to be seen in the context of two important considerations. One is the need to adapt trade policy in view of the global trade regime likely to emerge from mega-regionals like TTIP. The second is India's major concern about its trade deficits and emphasis on enhancing domestic production and value added. Policies to achieve both these objectives would overlap, but in the present global situation with rising protection, there may be a temptation to use protectionist trade policies to achieve the second objective.

India has begun addressing the two above-mentioned concerns. On standards, India has developed a standards roadmap to upgrade its policy mechanism and the capacity of domestic business. The roadmap envisages changes in regulations and laws, coordination amongst different agencies/ministries, the identification of best practices, and coordination with business and conformity assessment bodies. Further, India has started focusing on a value chain approach to identify areas that may need more support or provide greater opportunities. This may also bring changes in India's tariffs to encourage links to foreign inputs and GVCs.

Taking account of the changes in TTIP, India may use a two-step process for its trade policy reform to be more consistent with mega-regionals, such as first concluding ongoing FTA negotiations with the EU and then making other policy changes. This would provide India with a basis to move towards a TTIP regulatory regime and enter the TTIP market in a bigger way. India has developed close political links with Japan and the US, and could work with them as well to help transition towards the new trade regime.

India has recognised the important role of FDI and is encouraging it through its 'Make in India' scheme. This scheme could also be used to help India prepare a move towards the trade policy framework emerging from TTIP. Interestingly, India may also consider ways of encouraging outward FDI in markets that are linked to the key economies in mega-regionals.

In a world with an increasing presence of GVCs, India would need policies that enable the country to link up better with these chains through facilitating trade, removing infrastructure constraints to increase operational efficiency, and introducing higher quality consistent with global standards. If tariff increases are used to promote domestic production of any good, they would lead to inefficiencies over time, and also be inconsistent with the regime emerging from TTIP and TPP. Thus, such protectionist policies cannot be used for long; instead, policies focusing on enhancing efficiency and removing operational constraints are more important. India has begun implementing such policies through its programmes for skill improvement, the facilitation of investment, addressing infrastructure and energy constraints, a single window for requisite permissions, a timely response to applications and requests for provision of facilities, a focus on supportive clusters, and the establishment of several modern production and urban centres to link up with better technologies and create higher value-added domestic capacities.

Interestingly, there are some important lessons on promoting industries, particularly SMEs. For instance, TTIP envisages business training sessions and seminars for SMEs, new online programmes to increase and enhance trade information sharing for small businesses, and simplified rules of origin. When pressing the negotiators to build inclusive systems, India could also emphasise that similar rules of origin should be applicable to SMEs from non-member economies.

Conclusions

TTIP has many important implications for India. Its policymakers have begun to respond in many ways through policy reforms and better coordination with business to improve operational efficiency and meet the higher standards emerging from mega-regionals such as TTIP. There is, however, an important issue of the inclusiveness of the emerging trade policy regimes through TTIP and other mega-regionals. Special effort and attention will be needed to address such concerns so that the global market place is not fragmented with different standards and the positive effects of trade creation can be shared widely.

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Potential impact of TTIP: A Korean view

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Introduction

In the wake of the Global Financial Crisis in 2008, the US and the EU implemented massive fiscal and financial interventions in efforts to get their economies out of the Great Recession. Yet, as these economies rebounded slower than expected and, more generally, as economic growth momentum weakened worldwide, the launch of a high-quality transatlantic free trade area (FTA) arose as an alternative option. The Transatlantic Trade and Investment Partnership (TTIP) was deemed by some as the best option for promoting an economic upturn (Kim 2013), recognising the fact that the credibility of the multilateral trading system represented by the WTO has been undermined by the stalemate in the negotiations over the Doha Development Agenda.

Policymakers and trade experts in the US and the EU have showed a keen interest in the TTIP with a focus on regulatory convergence, with the goal of eliminating non-tariff barriers between two of the largest industrialised economies in the world. In this regard, it is worth noting that import tariffs on a substantial range of manufactured goods are already low in the US and the EU.

It is also contended, however, that the TTIP has been initiated not for just to improve global trade rules, but also for a geopolitical reason (Van Ham 2013). According to this view, the US began the TTIP negotiations with the EU in an attempt to suppress China's rising economic power and to retain its dominance over the global economy (Tellis

2014). Even so, some experts view the successful conclusion of these talks as unlikely, arguing that it would be extremely difficult, if not impossible, for the two economic giants in question to agree on the specifics of regulatory convergence.

Nevertheless, the TTIP negotiations between the two giant economies across the Atlantic began in 2013 and the talks are ongoing. This chapter examines the potential impact of TTIP on the Republic of Korea and the East Asian economies, and identifies possible policy responses.

Potential positive effects of TTIP

Above all, TTIP is expected to catalyse other mega-RTA negotiations, such as CJK-FTA (i.e. an FTA between China, Japan and Korea), the Trans-Pacific Partnership (TPP) or the Regional Comprehensive Partnership (RCEP), none of which have been concluded yet (Kim 2013). In turn, the world economy may experience 'competitive liberalisation' effects, leading ultimately towards the creation of super mega-RTAs such as the Free Trade Area of the Asia-Pacific (FTAAP), an integrated form of TPP and RCEP.

As a participant of the RCEP negotiations and an interested candidate in TPP, Korea could accrue economic benefits should these mega-FTAs finally be concluded. Furthermore, in the long term, Korea may secure export markets in the Asia-Pacific region while taking advantage of international value chains within the region to supply global markets, all to the greater commercial benefit of Korean enterprises. Indirectly – i.e. through such value chains – the integrated market between the US and the EU that would be formed under TTIP would benefit East Asian countries, as they are major trading partners of the transatlantic economic powers.

Moreover, if the TTIP were to promote regulatory convergence successfully in various fields, that would be a great outcome in and of itself, serving as a meaningful lesson for the multilateral trading system. Such regulatory convergence, when realised, may allow for cost reductions for those companies that face different regulations and standards when exporting to the US and to EU markets. Korean automobile companies, for example, are expected to enjoy economic gains should differences in technical regulations across the Atlantic be eliminated.

Potential concerns with TTIP

Although it is contested, there also is a risk of momentum being lost in multilateral trade negotiations when TTIP is finally concluded. With the successful emergence of a giant market connecting both sides of the Atlantic, there will be diminished incentives for the US and the EU to actively participate in subsequent multilateral trade negotiations that depend upon consensus-based decision-making. Moreover, if the US and the EU step back from the multilateral trading system, the welfare of the least developed and developing countries, who are also WTO members, may deteriorate.

There are also concerns about trade diversion effects possibly hurting countries that are excluded from TTIP (Kim 2013). Given the prevalence of intra-industry trade and foreign direct investment between the US and the EU, the trade diversion effects are expected to be significant. Should this be the case, at least in the short term, East Asian countries with a heavy trade reliance on the US and the EU will face reductions in their exports to those markets.

From Korea's perspective, in particular, the conclusion of TTIP would mean a reduction in the preferential benefits created by its FTAs with the US and the EU. The comparative advantage that Korean products have enjoyed in the US market will be shared with products from the EU and similarly, the preferences will be shared with the US products in the EU market (Kim 2013). This may lead, at least temporarily, to a reduction in Korea's exports to both markets. Moreover, should China's exports to these markets be affected, it will have negative impacts on Korea, as a leading parts and components supplier to Chinese exporters (Choi and Kim 2013).

If the TTIP is set to become a formal regulatory bloc, then the global trading system will fragment (Lamy 2014). If the regulatory convergence set by the US and the EU fails to evolve into a multilateral regulatory system, it may serve as an additional non-tariff barrier to the integrated market, resulting in further damage to the commercial interests of many countries in East Asia, including Korea. For instance, newly added technical standards for automobiles could harm those automakers in Korea and Japan that export large volumes to the US and the EU markets. Also, East Asian countries' industrial and trade policies may be challenged by new rules, which in turn could lead to new trade disputes (Kim 2013). In this regard, new regulations regarding competition, investment, labour, and environment policies in particular may cause conflicts with non-members' policies.

Of course, non-TTIP signatories would welcome new trade regulations if they were formed on the basis of rationality. Korea, which values the advancement of trading norms, would also willingly accept these new rules and regulations without much complexity. However, if the TTIP intends to exclude and discriminate against certain non-member countries by forming a regulatory bloc, the global trading system will suffer from greater uncertainty.

Recommended responses

When the TTIP will be concluded is unclear at this time, as are the exact contents of any agreement. It is therefore difficult to predict the responses of Korea and other East Asian countries. This is particularly true given that the Doha Round and other mega-RTAs are far from being concluded as well. Moreover, several East Asian countries are now participating in the TPP negotiations, and Korea has also expressed an interest in doing so.[1] As many parties to the TPP talks overlap with those in the RCEP negotiations, some commonality between the two mega-RTAs is expected.

1 Brunei, Singapore, Malaysia and Vietnam are the participants in the TPP negotiations.

In contrast, besides the Korea-EU FTA, trade relations between East Asia and the EU are relatively under-developed. Trade policy matters are not even included on the agenda of the Asia-Europe Meeting (ASEM) held every two years. Under these circumstances, the East Asian economies and the EU should consider initiating a discussion on a possible mega-RTA, tentatively called 'Asia-Europe FTA (AEFTA)', to establish closer trade and investment connections between two regions.

The launch of a new regional trade negotiation between the East Asian economies and the EU would establish a communication channel that connects all the key players of global trade: the EU, the US and the East Asian countries. This channel may help alleviate the concerns that TTIP will become a regulatory bloc. The idea of a mega-RTA between the East Asian economies and the EU could be proposed at the next ASEM Summit and Korea, having FTAs with both the EU and China, might act as a facilitator of future development.

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TTIP: A Russian perspective

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Due to relatively high levels of economic openness, Russia is sensitive to both negative as well as positive external shocks. At this moment, uncertainty regarding the prospects for global economic growth, falling oil prices, exchange rate fluctuations, and Western sanctions are widely perceived as the most significant external factors influencing the Russian economy in the short run, and probably in longer run. Therefore, one could sensibly argue that the launch and conclusion of the Transatlantic Trade and Investment Partnership (TTIP) negotiations will not radically change the international economic environment facing the Russian Federation. Even so, several points are worth mentioning in assessing Russian attitudes towards TTIP.

RTAs as a source of economic isolation

A large fraction of the Russian political, economic, and academic elite shares the view that in many instances, regional trade agreements (RTAs) ultimately facilitate the isolation of their members from the rest of the world, and in so doing damage outsiders and international cooperation overall. It is noteworthy that Russian Federation President Vladimir Putin, in his address to the APEC Economic Leaders' Meeting on 11 November 2014, referred to "the large number of trade agreements in effect within the region that differ both in the degree of liberalisation and in the number of participants" and said that this "creates the potential danger of the region splitting into individual competing associations. Yet the exact opposite is needed". The extremely negative reaction of Russian authorities to the EU-Ukrainian RTA provides another convincing illustration of the same thinking.

Little potential for trade diversion

Despite the current contraction of Russian-EU trade (total trade for January-August of 2014 was equal to 96.8% of that for the comparable period in 2013), the EU is Russia's largest trading partner, accounting for 49.2% of its merchandise foreign trade. Moreover, about 70% of those Russian exports consist of energy resources. Should proposals strongly advocated by European TTIP negotiators to lift the US ban on crude oil exports be accepted, access to American natural gas supplies[1] could result in a reduction of EU imports from Russia. At the same time, one should not overestimate both the speed and scale of this reduction. There are compelling reasons to believe that during the coming years, Europe will continue to rely heavily upon Russian natural gas.

As for Russian Federation (RF) imports from the EU, one can expect little trade diversion to the US market, where buyers are typically more demanding than in Russia. Furthermore, bilateral trade between Russia and the US is not very significant for either country. During 2010-2013, such trade accounted for 2.5–3.8% of Russian and 0.3–0.4% of American foreign trade. In most cases, EU and Russian products do not compete directly in the US market. Similarly, the EU and Russian markets are not alternative destinations for American manufacturers. So, the direct impact of TTIP on Russian-US trade should not be substantial.

Little impact expected on foreign direct investment (FDI)

Foreign investments (especially recently) constitute an important dimension of Russian economic cooperation with its trading partners. In this field, the EU is an even more important partner for Russia than in case of foreign trade. Indeed, the EU share of the

1 On 9 September 2014, then EU trade Commissioner Karel De Gucht, referring to his talks with US Trade Representative Michael Froman, told reporters that he "cannot imagine there will ever be a TTIP" without the inclusion of US energy exports to Europe (http://www.ibtimes.co.uk/eu-trade-commissioner-karel-de-gucht-cannot-imagine-ttip-without-us-oil-exports-1464902).

FDI stock in Russia is about 75%. Russian investors in turn tend to focus on the EU and certain tax havens associated with the EU. According to the Russian Federation's official statistics, by the end of 2013 the British Virgin Islands, Cyprus, and the Netherlands were hosting 74.8% of total Russian outward FDI stock. Against this background, FDI flows between the US and Russia are small. Indeed, Russian outward FDI stock in the US and American inward FDI stock in Russia account for 2.5 and 2.2% of the Russian totals, respectively. Therefore, TTIP will most probably result in neither tangible expansion nor serious contraction of FDI into and out of Russia. Such FDI is mainly influenced by a variety of other factors. In particular, a significant part of FDI into Russia is financed by Russian capital that was taken out of the country beforehand. Also, Russia recently demonstrated impressive achievements in improving its business environment (see Table 1).

Table 1 Substantial improvements in the Russian business environment since 2012

Russia's overall rank in World Bank "Doing Business" rating	
Year	Rank
2012	112
2013	92
2014	62

Enhanced cooperation within the Eurasian Economic Union (EEU) is an option

Being one of the most impressive of the current regional integration initiatives, TTIP makes the 'challenge of integration' posed by the proliferation of RTAs more demanding for the members of the international community, and Russia in particular. Nowadays, participation in these alliances has become imperative for national economies all over the globe. Consequently, TTIP creates additional incentives for Russia to enhance cooperation within the Eurasian Economic Union (EEU), which in recent years has already been one of the top priorities for authorities in the Russian Federation.

Taking into consideration the fact that Russian officials perceive the EEU as being fully compliant with the rules of the WTO, TTIP might also stimulate Russia to take a more active stance in revitalising negotiations in Geneva. According to some experts, this is the attitude that meets both the short-term and long-term objectives of the Russian Federation (Malokostov and Tourdyeva 2014). Yet, TTIP could also encourage Russian trade policymaking in another way. The point is that Russia has not excluded new RTAs from its policy of promoting international economic cooperation, and the possibilities including negotiating Russian/EEU RTAs with the Republic of Korea and Vietnam. At the same time, from the Russian perspective these initiatives will not be in conflict with global trade liberalisation. President Vladimir Putin, in the above-mentioned address, made it quite clear that no regional agreement "should damage multilateral trade within the WTO system".

Promote export diversification

TTIP could provide an additional argument in favour of ongoing attempts to diversify Russian exports geographically. According to the most radical interpretation, "TTIP's standard-setting power would indeed be overwhelming, and even a major competitor like China would almost certainly comply with whatever trade rules and regulations the transatlantic West offered to the world. TTIP would be the best way to beat China (as well as Russia…) at their own economic game".[2] Under these circumstances, the Russian Federation, together with other members of BRICS as well as other countries in Asia and Latin America, could be tempted to retaliate by building a "World without the West".[3] Hopefully this scenario will not materialise. Nevertheless, Russia tends to believe that a multipolar world results in the best pattern of global rule-making and better serves the interests of the international community in general. Therefore,

2 http://www.clingendael.nl/sites/default/files/The%20Geopolitics%20of%20TTIP%20-%20Clingendael%20Policy%20Brief.pdf.

3 http://nationalinterest.org/feature/welcome-the-world-without-the-west-11651.

expanding economic cooperation with countries outside of TTIP, as well as building coalitions with them in leading international economic organisations, might become the preferred policy for the Russian Federation.

TTIP as a stimulant to Russian economic modernisation

Should TTIP be successfully concluded and implemented, it would make the EU and US economies, as well as their companies, stronger and wealthier. According to existing estimates, the TTIP deal would increase the size of the EU economy by around €120 billion (or 0.5% of GDP) and that of the US by €95 billion (or 0.4% of GDP).[4] This should be a matter of concern for the Russian authorities and business community, since this expansion would challenge the future domestic and international competitiveness of Russian products.

Simplifying to a degree, one might imagine two alternatives to support and promote Russian competitiveness. The first is artificial and is through state support, including various trade policy instruments (import duties, subsidies, technical barriers, licensing, etc.). Here, companies would do nothing to upgrade their performance. In the second alternative, business entities would not rely on external assistance, but would undertake deliberate steps (the introduction of new technological solutions, staff skill improvements, organisational development, etc.) which would be likely to improve their market positions. Progress in TTIP, similar to Russian accession to the WTO,[5] might increase the relative attractiveness of the second alternative.

Overall assessment

In most instances, the possible repercussions of TTIP simply add to existing trends and concerns facing Russian decision-makers. On its own, TTIP will most probably have a

4 http://trade.ec.europa.eu/doclib/docs/2013/september/tradoc_151787.pdf.

5 On that issue, see Sutyrin and Trofimenko (2013).

relatively modest impact on the Russian economy, and consequently TTIP will be far from the top of the Russian national political and economic agendas.

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TTIP: Implications for South Africa

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The high level of ambition behind the proposed Transatlantic Trade and Investment Partnership (TTIP) will, if it is concluded, bring about a mega-trade arrangement with important implications for South Africa and other African states. The agreement being negotiated by the EU and the US has a comprehensive agenda that extends some existing WTO disciplines, as well as covering trade-related matters not currently on the WTO agenda. TTIP and other modern preferential trade agreements are charting a new course in international trade and investment governance; paving the way for the dynamic benefits of enhanced competition and competitiveness in the 21st century. Since the EU and the US are still key trade and investment partners for African countries, including South Africa, it is to be expected that TTIP will have implications for Africa, and South Africa in particular.

Unilateral preferential arrangements have historically provided access to the EU and US markets for African countries. These arrangements include a series of Lomé Conventions, the Generalised System of Preferences (GSP) and the Africa Growth and Opportunity Act (AGOA).[1] These unilateral preferential arrangements are not negotiated trade agreements, and hence do not provide the certainty and predictability of typical trade agreements. In the long term, they do not offer a sufficiently strong basis for African integration into the global economy.

1 AGOA has its basis in American legislation, and is expected to be renewed in 2015.

Since 2000, South Africa's trade with European countries has been governed by the Trade and Development Cooperation Agreement (TDCA). On 15 July 2014, South Africa, Botswana, Lesotho, Namibia, Swaziland and Mozambique concluded an Economic Partnership Agreement (EPA) with the EU[2] that will replace the TDCA. This so-called SADC[3] EPA is still at the time of writing (December 2014) in the legal scrubbing phase, with implementation to follow in 2015.

South Africa belongs to the African Customs Union (SACU), is a member of the SADC free trade area (FTA), and is participating in the negotiations to establish a Tripartite Free Trade Area (TFTA) with 26 member states to integrate markets and economies from Cape to Cairo in eastern and southern Africa. In addition, the 54 member states of the African Union have agreed to establish a Continental Free Trade Area (CFTA), with negotiations scheduled to start in mid-2015.

South Africa's trade policy reflects a very specific set of economic and development concerns. Central issues informing its trade policy include job creation and re-industrialisation. The creation of 'decent jobs' underpins South Africa's economic policy endeavours, and specifically its trade policy and regional integration strategy in Africa, while attempts to stem de-industrialisation find expression in a 'strategic' tariff policy.

In short, South Africa espouses a very traditional (20th century) trade policy, with a predominant focus on trade in goods matters and specifically the use of the import tariffs (and, to some extent, anti-dumping) to protect domestic industry. This policy stance reflects a very complex domestic political economy game, with trade unions and industries (such as clothing and textiles and automobiles) lobbying strongly for protection. This inward-looking trade policy is also characterised by the absence of

2 Angola elected not to initial the EPA in July 2014, but its possible future accession is provided for in the text. The negotiations took about ten years.

3 The Southern African Development Community (SADC) comprises 15 countries in southern Africa, including all five SACU member states. Different EPA configurations are foreseen for the various SADC states.

new generation issues such as services, investment and competition policy. These views have had important implications for the scope and coverage of FTAs negotiated by South Africa (and its SACU partners).

In 2002, the US approached SACU to negotiate a comprehensive FTA, including services, investment and intellectual property issues. South Africa declined this approach from the US, indicating its preference for a more focused trade-in-goods agreement. It is no surprise that South Africa also refused to include these issues in the EPA negotiations with the EU. In an African regional context, South Africa also promotes its particular trade policy approach. In the absence of strong countervailing engagement, its proposals for agenda-setting usually carry the day. This means that the regional integration agenda, for initiatives with South African participation, have to date focused predominantly on a trade-in-goods agenda. Invariably too, this means limited tariff liberalisation buttressed by restrictive rules of origin, especially for sensitive products such as clothing and textiles.

Since the aim behind TTIP is to go *"beyond existing WTO commitments"*, new regulatory arrangements will come into place within the EU and the US which will merit careful scrutiny by third parties. African investors and trade policymakers, as well as firms, will not be able to ignore the dynamic effects flowing from this development. Third parties may find that the EU and US have put new standards and procedures in place which will start to affect their trade with these two blocks. Trade facilitation measures could be another area where mutually agreed TTIP practices will become the norm.

It is true that third parties are not under any obligation to give effect to what the EU and US have agreed *inter partes*. Their trade with the US and the EU will, in principle, be governed by multilateral rules or preferential agreements such as the SADC EPA. The reality might be different and will depend on the scope and content of those treaty provisions that go *"beyond existing WTO commitments"*. This feature has more than one dimension. It will mean that disciplines not covered by WTO agreements (e.g. investment and competition), but nevertheless vital for 21st century trade, are on the agenda of the TTIP. In those disciplines that are included in a TTIP accord, the parties may agree on more detailed rules than are currently in the WTO. Emission standards for automobiles provide a good example. If these disciplines are mutually agreed, as in conformity with WTO sanctioned health standards, they could soon set the norm for wider audiences.

The EU/US deal aims at a comprehensive, rules-based pact with regard to issues typically shunned by SACU and SADC states when they negotiate preferential trade agreements. The SADC Economic Partnership Agreement deals with market access for goods only. When one reads again the original European Commission proposals submitted when these negotiations were launched in 2004 (and it is noted that TTIP is also called a "Partnership"), very much the same issues were on the table as presently being discussed as part of the negotiations with the US. It was then the EU vision for global integration and how to deal with 21st century challenges. African nations, and specifically South Africa, did not buy into that agenda.

The SADC EPA text does not include services, competition, investment, procurement and related 'new generation' issues. All of these are mentioned in the TTIP discussions. Article 67 of the SADC EPA provides for the possibility of further negotiations with the EU on trade in services and investment, but there are few signs of Pretoria embarking on any such initiative soon. Article 67 does, however, mention that Botswana, Lesotho, Mozambique, Swaziland and the EU have started and will continue to negotiate trade in services. If this happens, one might see some divergence among African governments with regards to new generation trade agreements and how they will engage third parties such as the EU and US. The African Regional Economic Communities (RECs) generally do not cover these disciplines to any major extent yet; the East African Community (EAC) being the only exception.

The TFTA could not be concluded on schedule (June 2014) and a 'built-in agenda' has now been adopted to complete the negotiations originally earmarked for the first phase. During the second phase, to be launched in 2015, new negotiations on services, the movement of business persons as well as new generation issues should be tackled. SACU (under South African leadership) has shown little appetite for binding arrangements on the free movement of business persons, which was to have been negotiated during the first phase. Industrialisation and infrastructure development are also on the agenda. Tough negotiations are expected, but a TTIP-type partnership is unlikely.

When comparing TTIP and African preferential trade negotiations, it is clear that they are underpinned by very different philosophies. The EU/US initiative is comprehensive and realistic; tackling 21st century issues. In Africa, the approach still tends to be conservative and inward-looking. When the negotiations to establish a continental FTA are launched next June, there might be even more resistance to the comprehensive type of agenda forming part of the TTIP negotiations.

The implementation of TTIP will require changes to domestic legal arrangements and institutions. This will be necessary to secure the high level of regulatory convergence, predictability and certainty aimed for. This type of follow-up action will also be necessary in order to grant treatment for the establishment in their territories of companies, subsidiaries or branches of the other party that is no less favourable than that accorded to their own companies, subsidiaries or branches. Third parties will not benefit from these provisions. How will they respond?

The obvious answer would be to negotiate similar deals with the EU and US respectively. Pretoria has no such plans. The SADC EPA does contain, in Article 28, a 'regional MFN' clause that stipulates that with respect to customs duties, the EC party shall accord to SADC EPA states any more favourable treatment applicable as a result of the EC party becoming party to a preferential trade agreement with third parties after the signature of the agreement. The implication is that the SADC EPA states may, theoretically, benefit from the possibility of better tariff commitments in TTIP. This will be a meagre harvest; tariffs on substantially all trade in goods covered by the EPA will be eliminated over time, anyway. The real multiplier benefit could have been in trade in services and trade-related commitments, which the SADC EPA does not cover. The EPA MFN clause therefore does not apply to the new benefits to be generated by TTIP.

It seems unlikely that South Africa will, in the near future, embark on a new trade policy and broader economic policy trajectory anchored in fundamental reforms in areas such as labour market regulation, education and immigration policy to address the critical skills deficits and mismatches. The development of a comprehensive services agenda does not appear to be an immediate priority either. This is unfortunate, as preferential agreements such as TTIP, entered into by its key trade and investment partners, will mean that South Africa faces a serious risk of being left behind in the economic governance and competitiveness stakes.

There are also signs of trouble ahead regarding bilateral trade with the US. Anti-dumping duties on American poultry imports have become a highly controversial matter. According to recent media reports, the chairman of the African Affairs Subcommittee of the Senate Foreign Relations Committee will do everything in his power "to make sure (the South Africans) do not derive any benefits from AGOA if they do not end the illegal anti-dumping duties against US chicken".[4] It is not the first time that Washington has expressed unhappiness about South African anti-dumping duties; as have other governments. In 2013, Pretoria withdrew anti-dumping duties on Brazilian chicken when Brazil threatened with a dispute under WTO rules.

The bigger picture consequences cannot be ignored, such as growing concerns by South African firms about the possibility of losing AGOA benefits.[5] A critical appraisal of South African trade policy seems unavoidable. When this is undertaken, the wider implications of TTIP should be on the to-do list.

4 *Business Day*, 12 December 2014.

5 The Association of Meat Importers and Exporters of South Africa is reported to be calling on the government to "urgently drop antidumping duties on US poultry as fears grow that SA might be excluded from trade benefits under the African Growth and Opportunity Act" (*Business Day*, 12 December 2014).

Turkey: Implications of TTIP

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For almost a quarter of a century, the streamlining of global trade through sustained liberalisation advocated by the Bretton Woods institutions has proven to be ineffective. Since its foundation, the WTO has engaged in a series of well-defined multilateral trade negotiations, most notably the Doha Development Round, which unfortunately has yielded meagre results. After numerous complications, the Bali Ministerial Meeting resulted mainly in an accord to improve trade facilitation and a promise of progress in certain other areas, such as 'Duty-free Quota-free' treatment for imports from Least Developed Countries.

Stakeholders in global trade have had to endure 19 years of endless negotiations since the Uruguay Round was concluded, the result being the current trading environment. At the same time, the universe of global trade had faced winds of change that ultimately require stakeholders to agree on new rules to maintain a functioning system. The inherent complexities of trade in today's world make this quest even more challenging. The rising influence of the 'emerging economies' put an end to the pre-eminence of the industrialised economies, particularly that of the 'Quad' (the US, the EU, Canada and Japan), in forging rules for trade liberalisation. The development agenda of the Doha Round sought to correct the asymmetries rooted in the Uruguay Round and resulted in the noticeable assertiveness of developing countries. Hence, the Quad alone cannot bring about further liberalisation of multilateral trade.

Yet the overall finding of many recent reports of the IMF, World Bank, OECD and UNCTAD is that of a strong performance by developing countries (Aran 2013). Evidently, the financial crisis of 2008 has accelerated the dispersion of economic power among industrialised and developing countries – implying that the gap between them has started to narrow. The considerable wealth of the industrialised economies, though, is still a reality, even though pressure emanating from the 'emerging economies' has become more visible. The crisis of 2008 in a way accelerated the shift sooner than anticipated. The industrialised economies are not preparing to concede, however, and their strategies towards regional trade agreements, amongst other initiatives, reflect this.

Mega-trade agreements: A challenge or an opportunity for developing countries?

The US responded to these changes by embarking on two major regional trade initiatives: first the Trans-Pacific Partnership (TPP), and later the Transatlantic Trade and Investment Partnership (TTIP). Both initiatives are complementary and should be regarded as the essential parts of a coherent strategy. The EU and many other countries have demonstrated their readiness to join these partnership quests. Of all the industrialised countries, only Norway and Switzerland have not taken part in such mega-regional negotiations.

In these circumstances, the vital interests of key industrialised countries are at stake and hence the prospect of concluding both quests is high. It is safe to assume that both TPP and TTIP, when they come into force, will introduce new rules that will substantially change the way the multilateral system operates today. The economic size of the countries involved in both quests implies that these new rules will be universally implemented. Once concluded, they will *transform* the global trading environment, both in terms of market access and the rules that govern international trade. Hence the frustration on the part of those countries that are not part of the negotiations to shape these new rules.

Upon the completion of the seventh round of TTIP negotiations in Washington, it was declared that "negotiations are now moving smoothly into the textual phase, where discussions are based on specific textual proposals".[1] An advanced phase of the negotiations has been reached. The EU's chief negotiator, Mr. Ignacio Garcia Bercero, highlighted two aspects at a press conference, noting "the regulatory part of the TTIP to have the potential to deliver the most benefits" and the importance of cooperation "if the US and EU wish to play a leading role in developing international regulations and standards based on the highest level of protection".[2]

At present, average applied tariffs on EU-US trade are low. Therefore, tariffs are no longer considered a major issue except for a limited number of sensitive products, which vary from one jurisdiction to the next. The major impact of the TTIP is anticipated to be in 'new rule' making capacity (what some refer to as the 'game changer'). Greater regulatory alignment in competition policy, intellectual property rights, public measures towards small and medium size enterprises, and labour and environment policies is being sought.

TTIP covers a wider range of policies than the existing set of WTO rules. It may result in deeper harmonisation of rules in many policy areas between the world's biggest traders, which will have implications for investors and investment flows that go beyond the formation of a traditional free trade area. We should keep in mind that, as Richard Baldwin has noted, "the heart of 21st century trade is an intertwining of: 1) trade in goods, 2) international investment in production facilities, training, technology and long-term business relationships" (Baldwin 2011).

It is no secret that many third parties are waiting anxiously for the general framework of the TTIP negotiations as they try to predict their possible outcome and to prepare for possible consequences. The level of impact on these countries will depend not only on the business environment that will be established by TTIP, but also on how far third parties are ready to adopt the newly established rules. In other words, how these

1 http://trade.ec.europa.eu/doclib/press/index.cfm?id=1158

2 http://trade.ec.europa.eu/doclib/press/index.cfm?id=1158

countries will adapt to the new trading environment of TTIP is critical for them as well as for the TTIP signatories.

One option for third parties is to unilaterally harmonise their trade policies and practices with those of TTIP. But major transformations of trade policies need well-structured incentives. The question thus arises: What incentives does TTIP generate for third parties to align with its rules?

TTIP and Turkey's transformation ordeal

Turkey, as an integral part of the global economy, will undoubtedly be affected by the changes in the global trade environment arising from the successful negotiation of mega-regional trade deals. Empirical studies reveal serious welfare reductions for Turkey brought about by trade diversion. Turkish exports are estimated to decrease, even if by a limited amount, should TTIP come into force. Turkey, however, cannot stand still. The manner in which the country reacts to the new era is of critical importance. All the indications show that Turkey is prepared to engage seriously with change and embark on a challenging comprehensive programme of transformation. At the highest political level, Turkey's decisions in this regard are communicated clearly and repeatedly to both the US and the EU. Support in business circles is quite vocal too. Recently, the chairman of the Turkish Businessmen and Industrialists Association (TÜSİAD), a prestigious conglomeration of top Turkish companies, declared that they "consider Brussels to be the second capital for Turkey".[3]

On many occasions, official representatives have stated that the exclusion of Turkey from TTIP will eventually force the country to abandon the customs union with the EU. These kinds of statements could be regarded as manifestations of frustration rather

3 "TÜSİAD: Brussels now 2nd capital for Turkey", *Daily News*, 5 December 2014.

than policy intent. However, the annoyance felt on the Turkish side should somehow be addressed.

The reasons why Turkey's situation is *sui generis* are linked to its special trading arrangements with the EU. The customs union with the EU already includes a far-reaching obligation to align Turkish trade policy to that of the EU, including a specific provision "to align itself progressively with the preferential customs regime of the Community i.e. the autonomous regimes and preferential agreements with third countries".[4] The increasing number of EU regional trading agreements with third countries, however, puts Turkey's preferential market access at risk. The situation is aggravated further in the case of the US because Turkey suffers a huge trade deficit. This deficit will be multiplied under TTIP.

The EU-Turkish customs union, being more than a traditional free trade agreement, has led to a substantial level of alignment of rules and independent regulatory bodies with the EU, thus bringing regulatory coherence up to a reasonable level. On issues pertaining to agriculture, however , Turkey has to engage in a serious transformation process. As an active participant of the Trade in Services Agreement (TISA) negotiations, Turkey policies vis-à-vis services are cognisant of where the TTIP negotiations on services are likely to eventually land. Of course, the services section of TTIP is expected to go beyond TISA. Nevertheless, Turkey has a liberal services market, where foreigners have major stakes in telecommunications, mobile telephone services, banking, insurance, retail chains, and so on. Turkey should enact a full range of legislation regarding its service sector and, during implementation, move towards greater uniformity in regulatory application.

Several ways in which Turkey could be integrated into TTIP can be envisaged. The first option could be 'trilateral negotiations' between the US, the EU, and Turkey. However,

4 See *Decision No 1/95 of the EC-Turkey Association Council of 22 December 1995 on implementing the final phase of the Customs Union*, available at http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:21996D0213%2801%29

the feasibility of this option is close to nil considering the fact that negotiations in TTIP have already reached a mature stage and there is no opportunity for a third country to participate at the moment. The second option could be through the so-called 'Turkey clause' enabling automatic access for Turkish exports covered under the customs union with the EU to the latter's FTA partners. But technically this clause is confined to manufactured products and does not cover obligations on beyond-the-border policies.

As of this writing, the TTIP negotiations do not contain 'accession criteria' for eventual membership of third countries. Turkey has no appetite for a wait-and-see approach. The final option is for the country to initiate a separate FTA with the US to cope with the eventual implications of being left out of TTIP (i.e. trade diversion). However, such an agreement faces two significant challenges. First, the political feasibility of it is doubtful because of a lack of enthusiasm on the US side; political contacts through High Level Committee meetings have not proved very forthcoming. Second, any deal with the US should reflect an ambitious approach including the removal of trade barriers, a reduction in non-tariff barriers and direct spillover effects coming from Turkey's adoption of TTIP standards, all of which are projected to raise GDP and exports considerably (Mavuş et.al 2014).

Turkey should undertake substantial legislative changes in several challenging areas, including meeting the aggressive market access requirements from the US in telecommunications, postal, legal, audio-visual and financial services. The list can be extended to calls for opening up Turkey's restrictive public procurement market, and to cover controversial investor-state dispute settlement procedures, sanitary and phytosanitary measures, bio-safety rules, genetically modified organisms (GMOs), the protection of intellectual property rights (especially in the matter of counterfeit goods), and high tariffs for fruits and vegetables and meat products applied by the country (Akman 2014). Meeting these challenges would be an uphill struggle but, at the same time, would be vital for Turkey's transformation under the new trading rules. It should be noted that these challenges can be turned into gains if Turkey manages regulatory convergence and adopts improved standards and common business practices by mobilising domestic forces accordingly.

We must bear in mind that the Customs Union deliberations in the 1990s were also challenging for the Turkish economy. It nevertheless proved to be a worthwhile experience, as Turkey adopted the EU's *acquis communautaire* in many areas. Turkey successfully aligned its domestic regulatory rules, from technical barriers to trade to food safety, environmental legislation, consumer protection, intellectual property rights, customs legislation, and trade policy measures, as well as the setting up of independent regulatory bodies. The transformation induced by the customs union with the EU has been impressive. A recent World Bank report found that "the [Customs Union] has been a major instrument of integration for the Turkish economy into both European and global markets" (World Bank 2014). In addition, Turkey is gaining valuable experience through participating in the ongoing plurilateral negotiations on trade in services (TISA).

Concluding remarks

Overall, any Turkish concerns about TTIP should not be reduced to worries about trade diversion. Turkey's integration into the transatlantic economy not only helps to improve its relations with the US, but also renders the Customs Union with the EU more effective and functional. This engagement is important for Turkey, a country which is both a member of NATO and in the process of acceding to the EU. The third side of this triangle could be established by 'docking' Turkey into TTIP. The latter can be a stable anchor in Turkey's further transformation towards the global economy.

Close relations with the EU and US have motivated Turkey to engage in a real political and economic transformation process over the past three decades. Well-managed transatlantic relations are at a premium at a hectic time where the turbulence in the Middle East has the potential to result in chaos. It would be timely then for all sides to seek better transatlantic relations.

Turkey has relevant previous experience from the 1980s, when it adopted unilateral economic liberalisation measures, and from the 1990s with the Customs Union. The Customs Union with the EU has been an anchor for a Turkish industrial transformation that provided it with a highly competitive edge. TTIP could initiate a third phase, and in so doing give Turkey leverage to become a 'rule-maker' rather than a 'rule-taker' in shaping the global trade architecture. Thus, TTIP could be an 'opportunity' if well-managed by all. TTIP could lay the foundation for a further transformation in Turkish economic prospects.

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By negotiating a far-reaching Transatlantic Trade and Investment Partnership, American and European trade negotiators hope to set the global trade agenda for years to come. But how will the governments of other major trading nations react? Will TTIP be the catalyst that Washington and Brussels are hoping for? The collection of short analyses in this eBook includes assessments – from both systemic and national perspectives – of the likely knock-on effects of TTIP, seen not just in commercial terms but also the steps that the Rest can take to advance their interests as multilateral trade talks languish.

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