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## **T**he Trans-Pacific Strategic Economic Partnership Agreement: a Latin American perspective

Sebastián Herreros



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Sebastián Herreros



Division of International Trade and Integration

Santiago, Chile, March 2011

This document has been prepared by Sebastián Herreros, expert of the International Trade Unit, Division of International Trade and Integration of the Economic Commission for Latin America and the Caribbean (ECLAC). The author wishes to thank Mikio Kuwayama for his valuable comments on an earlier version of this document.

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## Contents

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<b>Abstract .....</b>	<b>5</b>
<b>Introduction .....</b>	<b>7</b>
<b>I. The current TPP members at a glance .....</b>	<b>9</b>
<b>II. Main features of the TPP .....</b>	<b>13</b>
<b>III. The TPP process in the context of Asia Pacific regionalism ...</b>	<b>17</b>
<b>IV. Latin American approaches to Asia Pacific .....</b>	<b>21</b>
<b>V. Opportunities and risks of TPP enlargement for Latin American countries.....</b>	<b>25</b>
A. Opportunities .....	25
1. Improved market access .....	25
2. Reduction of transaction costs .....	26
3. Economic cooperation .....	27
4. Benefits from further TPP expansion .....	28
B. Risks .....	30
1. US trade politics .....	30
2. Difficulty to find an overall balance .....	31
3. Lack of clarity on accession procedures .....	35
<b>VI. Conclusion.....</b>	<b>37</b>
<b>Bibliography.....</b>	<b>39</b>
<b>Serie Comercio internacional: issues published .....</b>	<b>41</b>
 <b>Tables</b>	
TABLE 1 TPP MEMBERS: SOME BASIC ECONOMIC STATISTICS (2009) .....	10
TABLE 2 SHARE OF MAIN PARTNERS IN LATIN AMERICA AND THE CARIBBEAN (LAC)'S TRADE 2000 AND 2006-2009 .....	21

TABLE 3	FREE TRADE AGREEMENTS BETWEEN MEMBERS OF THE LATIN AMERICAN PACIFIC ARC FORUM AND ASIA PACIFIC ECONOMIES (AS OF FEBRUARY 2011) .....	23
---------	--	----

TABLE 4	FTAS LINKING THE PARTICIPANTS IN THE TPP ENLARGEMENT NEGOTIATIONS (AS OF FEBRUARY 2011) .....	27
---------	--	----

### Figures

FIGURE 1	TPP MEMBERS: SIMPLE AVERAGE MOST FAVORED NATION APPLIED AND BOUND TARIFFS (2009) .....	10
----------	---	----

FIGURE 2	MEMBER COUNTRIES OF THE LATIN AMERICAN PACIFIC ARC FORUM: SHARE OF THE ASEAN 3 GROUP IN THEIR TOTAL EXPORTS AND IMPORTS (2009) .....	22
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## Abstract

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In March 2010, negotiations aimed at enlarging the Trans-Pacific Strategic Economic Partnership Agreement (TPP) were launched. Nine countries from Asia, Oceania and the Americas currently participate in them. The United States, which in practice has assumed a leading role, has stated that this process has the ultimate goal of transforming the TPP in a platform for large-scale trans-Pacific economic integration. It has also expressed that the enlarged TPP should be a high-quality, 21<sup>st</sup> century agreement.

For the current two Latin American participants (Chile and Peru), as well as for other prospective candidates, the TPP offers the possibility of strengthening their trade and investment links with Asia Pacific, the world's most economically dynamic region. The TPP could also make a meaningful contribution to "tame the tangle" of preferential trade agreements across Asia Pacific. However, given the current set of participants, the negotiations offer both Chile and Peru little in terms of improved market access. Moreover, they are characterized by uncertainty as to their content, architecture and membership, as well as by risks such as having to make new concessions in sensitive areas like intellectual property and investment. Overall, the success prospects of the TPP negotiations depend largely on how the trade policy environment in the United States evolves during 2011.



## Introduction

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The Trans-Pacific Strategic Economic Partnership Agreement, also known as P4 or TPP, was signed in July 2005 by the Sultanate of Brunei (Brunei Darussalam), Chile, New Zealand and Singapore, entering into force in 2006.<sup>1</sup> It is the first Free Trade Agreement (FTA) linking three continents (South America, Asia and Oceania).

The current four TPP signatories are also members of the Asia Pacific Economic Cooperation (APEC) forum, and both the origin and nature of the TPP have a strong link with APEC. The TPP traces its origins back to 1998, when the United States (US) proposed negotiating an FTA to Australia, Chile, New Zealand and Singapore to prod other APEC members to make progress in trade liberalization (Capling 2009). For different reasons Australia and the US itself did not follow up on this initiative, so New Zealand and Singapore negotiated a Closer Economic Partnership agreement that entered into force in January 2001. Negotiations towards a trilateral agreement including also Chile were launched at the APEC Leaders' Summit in November 2002 in Mexico. Brunei joined afterwards, first as an observer and subsequently as a full member of what became the TPP.

The TPP has as an explicit goal to support the achievement of free trade and investment within APEC by 2020, as agreed by this forum's Leaders in 1994 in Bogor, Indonesia (the so-called Bogor Goals).<sup>2</sup> The prospects that the TPP could become a platform towards

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<sup>1</sup> Henceforth the acronym TPP will be used to avoid the association of the term P4 with the specific agreement between the current four members.

<sup>2</sup> According to the commitment made in Bogor, the goal of free trade and investment was to be met in 2010 by the developed members of APEC (Australia, Canada, Japan, New Zealand and the United States). However, it was left unclear how this would be achieved. The three Latin American members of APEC (Chile, Mexico and Peru), as well as other five developing economies (Hong Kong, China; South Korea; Malaysia; Singapore and Chinese Taipei), also committed to achieve the Bogor Goals by 2010.



freer trade in Asia Pacific<sup>3</sup> have been heightened since November 2009, when President Barack Obama announced in Japan that the US would engage with the TPP countries “with the goal of shaping a regional agreement that will have broad-based membership and the high standards worthy of a 21<sup>st</sup> century trade agreement”.<sup>4</sup> Negotiations to that effect —also including Australia, Peru and Vietnam (the latter initially as an observer)— were launched in March 2010, and as of writing five negotiating rounds have taken place. Malaysia formally joined the negotiations in October 2010, bringing the total number of participants to nine, all of them APEC members. Other countries from Asia and the Americas have expressed an interest in joining the talks or are considering doing so. Although the TPP’s text stipulates that both APEC members and other States can accede to the agreement, in practice eligibility has been confined to the former.

The TPP enlargement negotiations are the Obama administration’s main trade initiative to date. They raise important systemic questions, notably concerning how they will relate to both existing agreements among TPP participants and other economic integration processes currently underway in Asia Pacific. They also pose both opportunities and risks to participating Latin American countries. The main opportunity is to improve their economic and trade links with Asia Pacific, a region that has become the world’s main growth engine. Among the main risks is having to make new concessions in sensitive areas such as intellectual property, investment and labor and environmental standards, which would add up to those they already made in their bilateral FTA negotiations with the US.

This document examines the short- to medium-term prospects of the TPP process and the possible implications for participating Latin American countries. After this Introduction, Section I briefly reviews some features of the current TPP members’ economies. Section II describes the main elements of the TPP agreement. Section III examines how the current TPP process fits within the broader context of Asia Pacific regionalism. Section IV reviews the main initiatives by Latin American countries to establish preferential trade links with Asia Pacific. Section V analyzes the opportunities and risks that the TPP process poses to participating Latin American countries. Section VI concludes.

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<sup>3</sup> The Asia Pacific concept has imprecise geographical boundaries. It is often understood as including the economies of North East and South East Asia plus Australia, New Zealand and in some contexts also India. However, for the US (and APEC) it encompasses both rims of the Pacific Basin, thus also including countries in the Americas. In this article both definitions are used, depending on the specific context.

<sup>4</sup> See <http://www.ustr.gov/about-us/press-office/fact-sheets/2009/december/tpp-statements-and-actions-date>. The launch of negotiations aimed at the US joining the TPP had already been announced towards the end of the Bush administration, in September 2008, by then US Trade Representative Susan Schwab. This decision was ratified by the Obama administration in late 2009, after conducting a review of US trade policy.

## I. The current TPP members at a glance

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The current TPP members share several common features. First, they are all small economies, together accounting for less than 0.5% of world population, less than 1% of world gross domestic product (GDP), and less than 3% of both world exports and imports of goods. Secondly, they have high per capita incomes (with the relative exception of Chile, which nevertheless has one of the highest per capita income levels in Latin America). Thirdly, they are all open economies, as evidenced by their high ratios of exports plus imports to GDP. This is especially the case of Singapore, reflecting the role this city state plays as a main commercial hub for Asia (see Table 1).<sup>5</sup>

The openness of current TPP members' economies is also evident in their low tariff levels. Figure 1 shows that their simple average Most Favored Nation (MFN) applied tariffs —i.e. those charged on imports from non-preferential origins— vary between 0% for Singapore and 6% for Chile.<sup>6</sup> As to their bound tariffs —the maximum levels committed to at the World Trade Organization (WTO)— they are considerably higher for all TPP members. This feature, which is the norm among developing countries, is shared by New Zealand, the only current TPP member classified as a developed country.

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<sup>5</sup> The figures presented in Table 1 underestimate the actual trade openness ratios of TPP members. This is because in 2009, as a consequence of the world economic crisis, trade measured by value fell considerably more than GDP for the world as a whole and for most countries (including the four current TPP members). Therefore, their trade to GDP ratios fell from their 2008 levels.

<sup>6</sup> These figures overestimate actual levels of tariff protection: In all TPP members a sizable share of imports enjoys duty free treatment as a result of preferential trade agreements subscribed with some of their main partners. This share reaches nearly 90% in the case of Chile.

**TABLE 1**  
**TPP MEMBERS: SOME BASIC ECONOMIC STATISTICS (2009)**

	GDP <sup>a</sup>	Population <sup>b</sup>	Per capita GDP <sup>c</sup>	Merchandise exports <sup>d</sup>	Merchandise imports <sup>d</sup>	Trade openness ratio(%) <sup>e</sup>
Brunei Darussalam	10.4	0.4	25 386	6.9	2.5	90.3
Chile	161.6	17.0	9 516	53.7	42.4	59.5
New Zealand	117.8	4.3	27 259	24.9	25.5	42.9
Singapore	182.2	5.0	36 379	269.8	245.8	282.9
Total P4	472.1	26.7	17 664	355.4	316.3	142.3
World	57 843.4	6 776.9	8 535	12 490	12 682	21.8
TPP share (%)	0.8	0.4		2.8	2.5	

Sources: International Monetary Fund, *World Economic Outlook Database*, October 2010 (GDP, population and per capita GDP) and World Trade Organization (exports and imports).

<sup>a</sup> In billion current dollars.

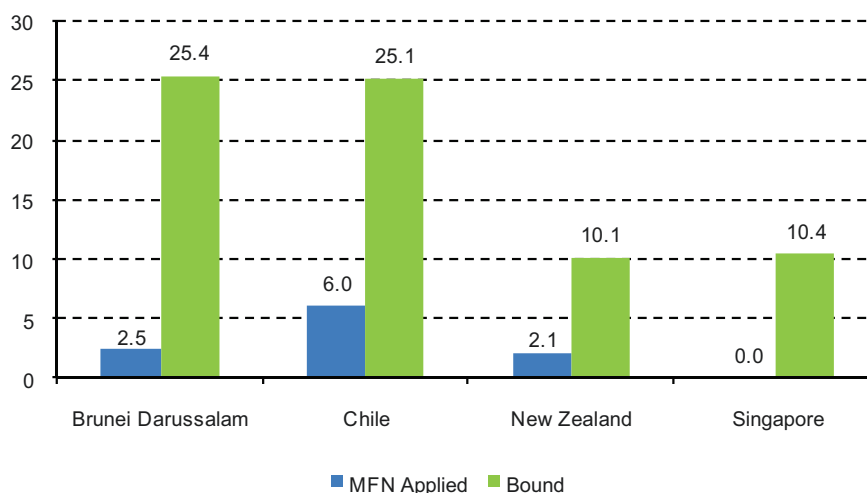
<sup>b</sup> In million inhabitants.

<sup>c</sup> In current dollars.

<sup>d</sup> In billion current dollars. It includes intra-European Union trade. Singapore's exports include re-exports. Brunei's figures are estimates.

<sup>e</sup> Ratio of exports plus imports to GDP.

**FIGURE 1**  
**TPP MEMBERS: SIMPLE AVERAGE MOST FAVORED NATION APPLIED AND BOUND TARIFFS (2009)**  
(In Percentages)



Source: World Trade Organization and International Trade Centre (2010).

The results of the Global Enabling Trade Report 2010, published in May 2010 by the World Economic Forum, provide additional evidence about current TPP members' high levels of trade openness. That publication ranks countries according to the degree to which they provide a favorable environment to trade. To this effect, their policies, institutions and available services are assessed in four areas: market access, border administration, transport and communications infrastructure, and business environment. Out of 125 economies, Singapore topped the list —same as in the 2009 edition of the same study—, New Zealand came 6<sup>th</sup> and Chile 18<sup>th</sup>, while Brunei was not evaluated (Lawrence et al. 2010).

Due to their geographic distance, different productive and export structures and lack of strong historical economic links, the current TPP members trade little with each other. Between 2006 and

2008, intra-TPP trade represented on average 0.8% of total TPP exports of goods. The *sui generis* nature of the TPP becomes thus apparent from the brief characterization of its members presented here. It is a trade agreement among four small economies that present generally very low trade barriers and which trade very little among themselves. This underscores that one of the most usual motivations countries have in negotiating preferential trade agreements (PTAs)<sup>7</sup> —removing barriers to their exports in their main markets (and/or those most protected) was not a key factor in the decision to negotiate the TPP.

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<sup>7</sup> PTAs form a very broad category in terms of their product, sectoral and thematic coverage as well as the depth of the commitments undertaken by their members. They include FTAs as well as more limited agreements. Henceforth the FTA acronym will be used to refer only to agreements specifically described as such by their signatories. No judgment is made on whether such agreements actually meet WTO disciplines on FTAs.



## II. Main features of the TPP<sup>8</sup>

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The TPP provides for the creation of a free trade area among its members, with no product exclusions.<sup>9</sup> For the vast majority of products free trade was achieved as from the agreement's entry into force. Concerning trade remedies, the parties retain their rights and obligations under the WTO Agreements on Safeguards, Anti-Dumping, and Subsidies and Countervailing Measures. Chile was allowed to apply a transitional safeguard to a limited number of sensitive agricultural products (all of them in the dairy sector). This safeguard cannot be invoked prior to or following completion of the scheduled tariff phase-out period of the good concerned.

The TPP includes chapters on trade in services, public procurement, intellectual property and competition policy, among other areas. It also has its own dispute settlement mechanism. The issues of investment and financial services were not originally included in the TPP. However, negotiations to that effect were launched in 2008 and subsequently incorporated into the current enlargement negotiations.

The main substantive obligations applying to trade in services in the TPP are: market access<sup>10</sup>, national treatment<sup>11</sup>, local presence<sup>12</sup>

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<sup>8</sup> This section draws partly on World Trade Organization (2008).

<sup>9</sup> Except for Brunei, which excluded alcohol, tobacco and firearms on grounds of protecting public morals, human health and security.

<sup>10</sup> Pursuant to this obligation, Parties cannot adopt or maintain any of the following types of limitations: on the number of services suppliers, total value of transactions, total number of operations, total number of natural persons employed, and measures that restrict or require specific types of legal entity or joint venture.

<sup>11</sup> Pursuant to this obligation, each Party must accord to services and service suppliers of another Party treatment no less favorable than that it accords, in like circumstances, to its own services and service suppliers.

<sup>12</sup> Pursuant to this obligation, no Party may require a service supplier of another Party to establish or maintain a representative office or any form of enterprise in its territory, or to be resident, as a condition for the supply of a service.

and most favored nation treatment<sup>13</sup>. The Agreement follows a negative-list

approach whereby these obligations apply to all covered services sectors in all modes of supply, except to the extent that reservations for existing non-conforming measures or future measures have been explicitly listed by the Parties. This approach is generally considered more liberalizing and transparent than the positive-list approach used in the WTO's General Agreement on Trade in Services (Elms 2009). Under the latter, parties to an agreement list those sectors and modes of supply to which core obligations apply, it being understood that these do not apply to any other sector or mode of supply.

The TPP also covers procurement of goods and services by specified government agencies for contracts valued above thresholds set out in the agreement. Its core principles in this area are national treatment, non-discrimination and transparency. By virtue of the non-discrimination provisions, suppliers from a Party may bid for contracts tendered by covered entities of the other Party without having first to establish in the Party or establish partnering arrangements with companies of that Party. Parties also commit to treat goods, services and suppliers of the other Parties in the same way as their own domestic goods, services and suppliers.

The TPP also contains an Environment Cooperation Agreement and a Memorandum of Understanding on Labor Cooperation. The former aims to encourage sound environmental policies and improve the Parties' capacity to address environmental matters. To this effect, the Parties commit to pursue high levels of environmental protection, to fulfill their respective multilateral obligations, and to avoid the use of environmental regulations for protectionist purposes or to encourage trade or investment. Within this context, the Parties agree to cooperate on mutually agreed environmental issues; to encourage and facilitate collaborative research; and to exchange information and environmental experts.

The Memorandum of Understanding on Labor Cooperation aims to promote a better understanding of the Parties' labor systems; to encourage and facilitate dialogue on labor matters; and to improve working conditions and quality of work including the development and management of human capital. In it the parties affirm their commitment to the International Labor Organization's Declaration on Fundamental Principles and Rights at Work by ensuring that their national laws, policies and practices are in harmony with those principles. They also recognize that it is inappropriate to set or use their labor laws and practices for protectionist purposes or to encourage trade or investment by weakening protections afforded in domestic labor laws. Cooperation and consultation mechanisms are established on a wide range of issues, including the participation of social actors.

One notable feature of the TPP, as indicated by its name, is that it aims at establishing a strategic association among its members that transcends the trade domain. In its initial provisions it is stated that the agreement covers the commercial, economic, financial, scientific, technological and cooperation fields, and that it may be extended to other areas to be agreed upon by the Parties. It also includes a specific chapter ("Strategic partnership") in which priority cooperation activities are outlined in the areas of education, research, science, technology and primary industries, among others. An example is the proposed cooperation between Chile and New Zealand in biotechnology and exchange of professionals in the dairy, agro industry and forestry sectors (General Directorate for International Economic Relations 2009).

The other defining feature of the TPP is that it has as an explicit goal to support the process to achieve free trade and investment within APEC by 2020. To this effect, its preamble states the commitment of member countries to promote the accession of other economies to the agreement. Article 20.6 states that other APEC economies or other states can join the TPP on terms to be agreed by the parties.

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<sup>13</sup> Pursuant to this obligation, each Party must accord to services and service suppliers of another Party treatment no less favorable than that it accords, in like circumstances, to services and service suppliers of a non-Party.

Summing up, the TPP has been characterized by its members (as well as by the United States) as a “high quality agreement”<sup>14</sup> that could serve as a model for the gradual construction of a trans-Pacific free trade space. In trade policy terminology, the TPP represents a possible “building block” for the convergence of the different preferential initiatives underway within Asia Pacific. It is in this strategic vision that resides its importance, not in its limited current commercial value. However, it is worth noting that such “high quality” was made possible largely by the important commonalities that exist among the current TPP members. The new five participants are much more diverse in terms of a wide range of dimensions, not least income levels.<sup>15</sup> This means that keeping the same “quality level” of the existing TPP —let alone increase it— will be a very challenging task.

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<sup>14</sup> Several authors argue that the TPP contains elements that are not in keeping with this characterization. Among these is the fact that the agreement does not impose any limitation on the application of antidumping measures among its members. This stands in contrast with provisions in other agreements subscribed by the same countries (such as the Chile-Canada FTA and the New Zealand-Singapore Closer Economic Partnership Agreement) that eliminate the use of antidumping measures among signatory countries. These authors also point to the non inclusion in the original TPP agreement of chapters on investment and financial services and to the agreement’s relatively weak provisions on intellectual property (Capling 2009; Elms 2009; Gao 2009).

<sup>15</sup> According to the IMF’s World Economic Outlook (October 2010), the ratio between the per capita GDP of the richest TPP participant (the US) and the poorest one (Vietnam), measured in current dollars, was 43 to 1 in 2009. In the same year, the ratio measured between the richest and the poorest of the original TPP signatories (Singapore and Chile, respectively) was only 3.8 to 1.





### **III. The TPP process in the context of Asia Pacific regionalism**

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Asia Pacific was a relative latecomer to the proliferation of PTAs that took place in other regions since the late 1980s. This was due to several reasons, including a legacy of conflicts and political tensions among some of the main Asian economies; the role of the United States as a central actor in the Asian geopolitical context (especially in security matters); and the primacy accorded by countries such as Australia, Japan, South Korea (henceforth Korea) and Singapore to the multilateral trading system—first under the GATT and since 1995 the WTO—as a forum for trade negotiations.

Since the first decade of the 21<sup>st</sup> century Asia Pacific has enthusiastically embraced regionalism. Today all its main economies are parties to several PTAs, both with intraregional and extra regional partners.<sup>16</sup> Several factors account for this shift. Among them are: the creation of a complex network of industrial value chains, centered around China and which extends across all East and Southeast Asia (the so-called “Factory Asia”); the financial crisis of 1997/98, which increased the perception of a need for stronger intra-Asian cooperation; the lack of progress in the WTO’s Doha Round, launched in 2001; and the need (real or perceived) not to “lose ground” vis-à-vis Europe’s and North America’s regional integration initiatives (Bergsten and Schott 2010; Kawai and Wignaraja 2009). Some authors also stress the political dimension of Asian regionalism, arguing that this process responds to a competition for political and diplomatic influence among

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<sup>16</sup> According to statistics from the Asian Development Bank, by July 2010 China had 10 TPAs in force; India 11; Japan 11; South Korea 6; and Singapore 18 (see <http://www.aric.adb.org/10.php>, consulted on 9 December 2010).

Asia's main powers more than to economic considerations (Barfield and Levy 2009; Ravenhill 2009).

In contrast with the FTAs negotiated by the United States or the Association Agreements negotiated by the European Union, there is no single "Asian model" of PTAs. This is reflected in the great diversity that characterizes the agreements negotiated by Asia Pacific countries. In general those involving Australia, New Zealand and Singapore show a high coverage of liberalized products and commitments that often go beyond multilateral disciplines (i.e. are "WTO-plus") in areas such as trade remedies, government procurement, investment and trade in services. The current TPP broadly fits here. At the opposite end are the agreements negotiated by China, India and ASEAN, which tend to present a lesser coverage of liberalized products, longer implementation periods and less ambitious trade disciplines.<sup>17</sup> As to the agreements negotiated by Japan and Korea, they tend to have ambitious disciplines but also numerous exceptions to liberalization for agricultural products, reflecting the strong defensive sensitivities of both countries in that sector (Ravenhill 2009).

A problem stemming from the proliferation of PTAs in Asia is that of the so-called "spaghetti bowl". This consists in the increase of transaction costs associated to foreign trade operations due to the different, and sometimes overlapping, regimes that a firm trading with several countries must comply with. This effect is potentially more serious in the Asian context, characterized by high levels of intra-industry and intra-firm trade in manufactures, and where the production of a final good is often fragmented across several countries.<sup>18</sup>

The majority of Asian PTAs, both in force and under negotiation, are bilateral. However, in recent years some initiatives have begun to emerge that point at achieving convergence among this complex network of agreements, so as to create larger economic areas and reduce transaction costs. Many of these initiatives are centered on ASEAN, as this group has concluded PTAs with all of its main regional trade partners: China, Japan, Korea, India, Australia and New Zealand. These agreements are generally known as "ASEAN plus one". Of particular relevance because of its size is the ASEAN-China FTA, which entered into effect in January 2010.

The best known among the initiatives described above is the "ASEAN plus three" mechanism, launched in 1997 and under which the ten ASEAN members meet regularly with China, Japan and Korea. An East Asia Free Trade Area (EAFTA), which would encompass all thirteen countries, has been under study within this mechanism since 2002. This initiative enjoys strong backing by China. Another initiative under consideration, proposed by Japan in 2006, is that of a larger agreement (the Comprehensive Economic Partnership in East Asia, CEPEA) which would include India, Australia and New Zealand as well as the "ASEAN plus three" countries. For this reason the CEPEA initiative is informally known as "ASEAN plus six".

It is worth noting that a pan-Asian free trade area, either in the form of EAFTA or of CEPEA, is not a short-term prospect. Although ASEAN already has PTAs in force with China, Japan and Korea, none of these three countries has a PTA in force with the other two.<sup>19</sup> Reaching these agreements would seem a reasonable first step before proceeding with either EAFTA or CEPEA. However, this is a difficult task, especially given the concerns of both Japan and Korea about freeing up trade with China (Kawai and Wignaraja 2009).

<sup>17</sup> For example, within the AFTA, ASEAN members committed only to apply tariffs not exceeding five percent to intra-regional trade, not to eliminate them (see <http://www.aseansec.org/19585.htm>, consulted on 5 June 2010).

<sup>18</sup> Some empirical evidence seems to support this concern. Surveys applied between 2007 and 2008 to 609 firms from Japan, Korea, the Philippines, Singapore and Thailand revealed that on average only 22% of them had taken advantage of tariff preferences negotiated through PTAs. This figure doubled to a still modest 44% when firms were asked if they intended to use those preferences in the future (Kawai and Wignaraja 2009). These low utilization rates probably respond to a large extent to the fact that intra-Asian trade is dominated by manufactures, which tend to be subject to low tariffs in Asia. Accordingly, for many firms the tariff preferences negotiated might not be large enough to justify the cost of complying with the rules of origin and associated administrative procedures required to benefit from them.

<sup>19</sup> Korea and Japan launched negotiations toward an Economic Partnership Agreement in December 2003, which were suspended in November 2004. Since June 2008 several meetings have been held with a view to their resumption. Meanwhile, since October 2009 these two countries and China have been jointly studying the feasibility of a trilateral FTA.

Beyond the strengths and weaknesses of Asian regionalism from a technical standpoint, there are concerns that this process might lead to the creation of a purely Asian bloc (such as EAFTA or even CEPEA).<sup>20</sup> Especially in the US, the possibility that a regional architecture might emerge that “splits down the middle” the Asia Pacific region<sup>21</sup> is seen with great unease. According to several US scholars, the creation of an exclusively Asian bloc —promoted and in practice led by China— would leave the US at a disadvantage in the world economy’s most dynamic region and weaken the strong security links the US has maintained with East Asia since the end of World War Two (Barfield and Levy 2009; Bergsten and Schott 2010).

The most ambitious project of trans-Pacific economic integration suggested thus far is that of a Free Trade Area of the Asia Pacific (FTAAP), which would include all 21 members of APEC. However, materializing this initiative —proposed in 2004 by APEC’s Business Advisory Council (ABAC)— poses formidable challenges, both technical and political. It would involve reaching an agreement on a very ambitious goal among a large group of highly diverse countries, in terms of their development levels, interests, and institutional capacities, among many other dimensions. Launching negotiations aimed directly at a FTAAP is therefore not a viable alternative, at least in the short term.

According to US trade authorities, the TPP, despite its little current economic weight, represents “the most promising path” to a trans-Pacific free trade space (Inside US Trade 2010a). In their view, gradual expansion of the TPP can help build a “trans-Pacific community” that could counterbalance the centripetal tendencies observed today in East Asia (Barfield and Levy 2009; Bergsten and Schott 2010; Capling 2009). This prospect will only be credible, though, if several conditions are met and numerous difficulties overtaken. We return to this subject in Section V.

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<sup>20</sup> For these purposes, both Australia and New Zealand are best described as Asian economies.

<sup>21</sup> Again, this is the US definition of Asia Pacific.



## IV. Latin American approaches to Asia Pacific

In recent years Asia has emerged as a key trade partner for Latin America and the Caribbean (LAC). As table 2 shows, during the last decade Asia's share in LAC exports tripled from 5% to 15%, whereas its share in the region's imports more than doubled from 11% to 25%. This phenomenon has been led by China, which alone represented almost half of both LAC exports to Asia and imports from Asia in 2009. Asia's gains have been mostly at the expense of the US, which nevertheless continues to be the region's main individual trade partner.

**TABLE 2**  
**SHARE OF MAIN PARTNERS IN LATIN AMERICA AND THE**  
**CARIBBEAN (LAC)'S TRADE, 2000 AND 2006-2009**  
*(In percentages)*

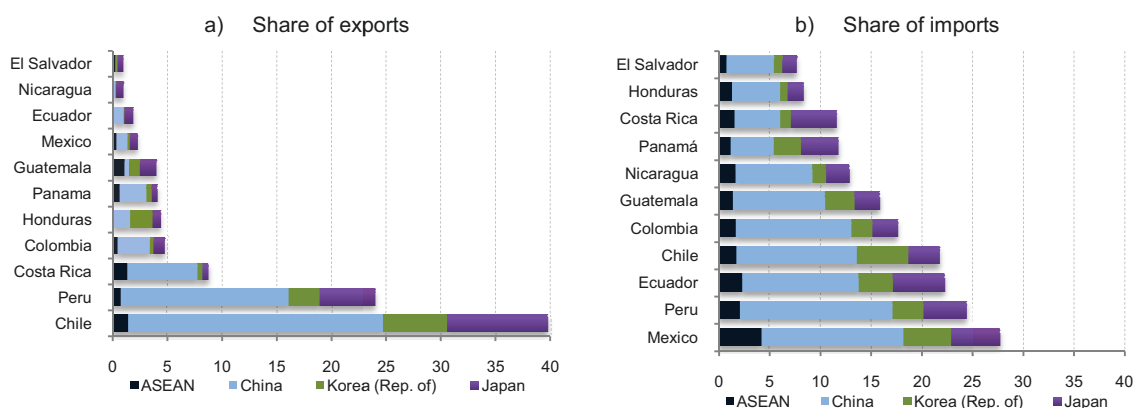
Share in LAC exports					
	2000	2006	2007	2008	2009
LAC	19.0	16.4	17.2	18.4	17.2
Asia	5.0	9.7	11.3	11.8	14.5
<i>China</i>	1.1	3.4	4.6	5.0	6.9
US	61.0	47.6	44.0	41.4	39.8
European Union	11.8	12.8	13.8	13.7	12.8
Share in LAC imports					
	2000	2006	2007	2008	2009
LAC	15.1	18.9	19.1	18.9	18.8
Asia	10.9	22.2	23.0	23.5	24.9
<i>China</i>	1.8	8.4	9.6	10.4	11.8
US	55.0	32.4	30.3	29.0	29.2
European Union	12.1	12.8	13.3	13.5	13.8

Source: Economic Commission for Latin America and the Caribbean 2010b).

In this document it is assumed that the universe of potential Latin American TPP members is not limited to the region's current three APEC members (Chile, Mexico and Peru) but to its eleven countries with coasts on the Pacific Ocean, namely Colombia, Costa Rica, Chile, Ecuador, El Salvador, Guatemala, Honduras, Mexico, Nicaragua, Panama, and Peru. These countries created in 2007 the Latin American Pacific Arc Forum (LAPAF), an informal cooperation forum which has among its main objectives to deepen economic links between its members and Asia Pacific economies.<sup>22</sup> Same as for the rest of LAC, during the past decade Asia Pacific increased significantly its share in the foreign trade of the LAPAF countries (taken as a group). Thus the share of the ASEAN+3 countries (used here as a proxy of Asia Pacific) in total LAPAF exports grew from 4% in 2000 to 9.4% in 2009. In the case of LAPAF imports, the share of the ASEAN+3 countries grew from 9.6% in 2000 to 23.9% in 2009.

Despite the marked increase in Asia Pacific's share in LAPAF foreign trade, the situation varies widely among the group's members. In 2009 the ASEAN+3 countries accounted for 40% of Chile's total exports, almost a quarter of Peru's, 9% of those of Costa Rica and less than 5% of those of all other LAPAF countries (see figure 2.a). There is much less dispersion when it comes to imports, with Asia Pacific's share ranging from 8% for El Salvador to 28% for Mexico (see figure 2.b). Thus on the whole Asia Pacific is much more important for LAPAF countries as a source of imports than as an export market.

**FIGURE 2**  
**MEMBER COUNTRIES OF THE LATIN AMERICAN PACIFIC ARC FORUM: SHARE OF THE ASEAN 3 GROUP IN THEIR TOTAL EXPORTS AND IMPORTS (2009)**  
*(In percentages)*



Source: Economic Commission for Latin America and the Caribbean and Inter American Development Bank (2010).

The asymmetry noted above between exports and imports reflects the existence within LAPAF of two sub-groupings with very different export orientations. At one end there are Chile and Peru, which are important commodity exporters (mainly in the mining sector) to Asia.<sup>23</sup> At the other end are most of the Central American countries and Mexico, whose exports —comprised mainly of low and medium-technology manufactures— are heavily oriented towards the US market and for which Asia is still a marginal export destination (as well as a competitor). Costa Rica is a relative exception

<sup>22</sup> See [www.arcodelapacifico.org](http://www.arcodelapacifico.org) (in Spanish). LAPAF is neither a sub-regional integration body nor a trade agreement. It is based on voluntary cooperation instead of legally binding agreements. Its main trade initiative to date was the launch in late 2009 of negotiations aimed at achieving cumulation of origin among its members. In January 2011, four LAPAF members (Chile, Colombia, Mexico and Peru) agreed to press ahead with a "deep integration" initiative aimed at achieving the free flow of goods, services and capital (as well as at facilitating the movement of persons) among them.

<sup>23</sup> In 2009, primary products and natural resource-based manufactures accounted for 99% of both Chile's and Peru's total exports to Asia Pacific, 98% of those of Ecuador, and 70% of those of Colombia (ECLAC, Interactive Graphic System of International Trade Data, at [http://www.cepal.org/comercio/serieCP/eclactrade/serie\\_spanish\\_110.html](http://www.cepal.org/comercio/serieCP/eclactrade/serie_spanish_110.html), accessed 15 December 2010).

to this pattern, as it sends almost 10% of its exports (mainly integrated circuits and parts of processing machines) to Asia.

Historically, Asian economies have not been large investors in Latin America. Foreign direct investment (FDI) in the region is still largely dominated by the US, European countries and Canada. Thus in 2009 —admittedly a bad year for FDI worldwide— the US accounted for 37% of FDI flows into Latin America and the Caribbean, whereas Japan, the top investor from Asia, accounted for just 5% (Economic Commission for Latin America and the Caribbean 2010a). However, this is changing fast, mostly due to a large increase in Chinese FDI in the region. This investment is mostly in natural resource sectors such as oil, gas and mining which are strategic to the Chinese economy, but has begun to spread into manufactures and services as well.

Those LAPAF countries for which Asia Pacific is an important export destination are also the ones that have been most active in negotiating preferential trade links with partners from that region. Thus Chile and Peru, which are LAPAF's largest exporters to Asia in absolute terms (and its only two members consistently posting trade surpluses with Asia), have the highest number of FTAs with Asia Pacific economies. More recently, Costa Rica has also been very active in this regard. It subscribed in April 2010 FTAs with China and Singapore, both of which are expected to enter into force in 2011, and intends to launch FTA negotiations with Korea during the present year. Finally, Colombia started in December 2009 negotiations toward an FTA with Korea, its first such negotiation with an Asian country (see table 3).

**TABLE 3**  
**FREE TRADE AGREEMENTS BETWEEN MEMBERS OF THE LATIN AMERICAN PACIFIC ARC FORUM**  
**AND ASIA PACIFIC ECONOMIES (AS OF FEBRUARY 2011) <sup>a</sup>**

LAPAF member	Agreements in force	Agreements signed	Agreements under negotiation
Colombia			Korea
Costa Rica		China, Singapore	
Chile <sup>b</sup>	Australia, Korea, China, India <sup>c</sup> , Japan, TPP	Malaysia	Vietnam, Thailand <sup>d</sup>
El Salvador	Chinese Province of Taiwan		
Guatemala	Chinese Province of Taiwan		
Honduras	Chinese Province of Taiwan		
Mexico <sup>b</sup>	Japan		Korea <sup>e</sup>
Nicaragua	Chinese Province of Taiwan		
Panama	Chinese Province of Taiwan, Singapore		
Peru <sup>b</sup>	China, Singapore	Thailand	Korea <sup>f</sup> , Japan <sup>f</sup> , TPP

Source: Author, based on information contained in the Foreign Trade Information System of the Organization of American States ([www.sice.oas.org](http://www.sice.oas.org)).

a FTAs with Canada and the United States are not included.

b APEC member.

c This is not an FTA, as the parties agreed tariff reduction commitments (not elimination) for a limited number of products.

d The decision to launch FTA negotiations between Chile and Thailand was announced by the Presidents of both countries at the APEC Summit in Yokohama, Japan (November 2010).

e Negotiations suspended since June 2008.

f Negotiations were successfully concluded during 2010.



Eight out of the 11 LAPAF countries (Costa Rica, Chile, El Salvador, Guatemala, Honduras, Mexico, Nicaragua and Peru) have FTAs in force with the US, the main driver of TPP expansion.<sup>24</sup> Colombia and Panama have also signed bilateral FTAs with the US, in November 2006 and June 2007, respectively. However, as of early March 2011 neither agreement had been sent to the US Congress for approval, and the Obama administration had not indicated a concrete timetable to do so. In the case of Colombia, this is due to demands for a strengthening of workers' rights made by members of the House of Representatives from the Democratic Party, as well as by US labor organizations and other civil society groups. In the case of Panama, concerns in the US focus primarily on its tax regime and to a lesser extent on its labor laws. Prospects for approval of both agreements during 2011 look stronger following the November 2010 US midterm Congressional elections (see section VI.B.1).

Ecuador, the only LAPAF member that has not signed an FTA with the US, participated in negotiations to that effect between 2004 and 2006, along with fellow Andean Community members Colombia and Peru. However, in May 2006 the US unilaterally interrupted the negotiations in protest against the Ecuadorian government's decision to cancel a contract to exploit its oil fields with the US firm Occidental Petroleum.

As of March 2011, the only Latin American country that has officially requested to join the TPP negotiations is Colombia. Nevertheless, no decision has been made on that request, allegedly because Colombia is not an APEC member (although it has been applying for APEC membership since 1995). Costa Rica has expressed some interest in the TPP but so far has not requested acceding to the talks.

As of writing, Mexico has not expressed an interest in joining the TPP process. Indeed, in recent years Mexico's trade negotiations agenda has slowed down considerably, mostly due to the opposition of its private sector. Thus Mexico's organized business has been able to forestall the conclusion of FTA negotiations with Peru (a current TPP participant) and Korea (a potential one). It has also opposed all unilateral tariff reduction programs undertaken by the Mexican government since 2005 (Zabludovsky and Pasquel 2010). Today the Mexican private sector looks more concerned about increased foreign competition (particularly Asian) in its own market than about seeking new export destinations to reduce its dependence on the US market. Against this background, Mexico's participation in the TPP process looks uncertain, at least in the short term.

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<sup>24</sup> Chile and Peru have bilateral FTAs with the US, in force since January 2004 and February 2009, respectively. Mexico is a member of the North American Free Trade Agreement (NAFTA), in force since January 1994, and the five Central American countries are members, together with the Dominican Republic, of the Dominican Republic-Central America Free Trade Agreement (DR-CAFTA). This pact entered into force between March 2006 and January 2009, depending on the country.

## **V. Opportunities and risks of TPP enlargement for Latin American countries**

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### **A. Opportunities**

#### **1. Improved market access**

In terms of obtaining preferential access to new markets, the TPP negotiations today offer little to the two current Latin American participants. This is especially the case for Chile, which —aside from already being a TPP member— has bilateral FTAs in force with Australia, Peru and the US, signed another with Malaysia in November 2010 and is negotiating one with Vietnam. As to Peru, it has bilateral FTAs in force with Chile, Singapore and the US, while the other five current TPP participants (Australia, Brunei, Malaysia, New Zealand and Vietnam) together accounted for just 0.8% of total Peruvian exports in 2009.

Market access gains would likely be small too for the other Latin American countries that have expressed an interest in joining the TPP negotiations or that have been mentioned as likely candidates to do so. Colombia, for example, already has FTAs in force with Chile and Peru (with the latter within the context of the Andean Community), plus its pending FTA with the US (its top export market). The remaining six TPP participants (Australia, Brunei, Malaysia, New Zealand, Singapore and Vietnam) accounted for barely 0.4% of total Colombian exports in 2009.

Costa Rica already has FTAs in force with the US and Chile, and in April 2010 subscribed one with Singapore. Moreover, in November 2010 it started —together with three other Central American countries and Panama— FTA negotiations with Peru. The other five current TPP participants (Australia, Brunei, Malaysia, New Zealand, and Vietnam) together accounted for just 1.4% of its total exports in 2009. The other Central American countries are in a similar position. They have FTAs in force with the US (by far their most important trade partner) and Chile, and are negotiating one with Peru (with the exception of Nicaragua). While they do not have FTAs in force with Asian economies (other than the Chinese Province of Taiwan, and in the case of Panama also Singapore), Asia remains a marginal destination for their exports.

Finally, in the case of Mexico, the US market (to which it enjoys duty-free access through NAFTA) alone represented 81% of its total exports in 2009. Mexico also has a bilateral FTA with Chile and is negotiating one with Peru. The remaining TPP participants (Australia, Brunei, Malaysia, New Zealand, Singapore and Vietnam) accounted for just 0.6% of total Mexican exports in 2009.

## **2. Reduction of transaction costs**

Of course, the benefits arising from a trade agreement are not necessarily restricted to the removal of tariff barriers. In the case of the TPP, a potentially important source of gains for participant countries would be the reduction of transaction costs associated to trade among them. In effect, the TPP offers —at least theoretically—the possibility of harmonizing in a single agreement the disciplines contained in the numerous agreements already linking the nine current participants (see table 4). A clear example is that of the origin regimes that must be complied with to have access to tariff preferences. An agreement among the nine countries would theoretically allow having a single set of rules of origin applying to trade among them instead of the current multiplicity of regimes, thus simplifying businesses' production decisions.

An enlarged TPP could also expand the range of foreign inputs that producers in every member country could incorporate into their exported products without losing access to tariff preferences. For example, a Peruvian producer could incorporate without limitation inputs of Chilean origin into the final goods that it exports to Australia, while still benefitting from preferential access to that market. This would be so because inputs from any TPP member would be considered as if they had originated in the country exporting the final good for the purposes of determining the origin of that good, a concept known as cumulation of origin. This possibility has less immediate appeal for Latin American economies than for Asian ones, due to the smaller share of manufactures in Latin American exports, especially to Asia. However, cumulation of origin would still provide incentives for Latin American economies to integrate more closely their productive structures, thus promoting intra-industry trade and a gradual upgrading of their exports to more sophisticated products.

The possibilities of convergence among the several agreements currently linking the nine TPP participants are not limited to the origin regime. They also extend —at least theoretically— to the rules applying to trade in services, the treatment of foreign investment, government procurement and technical barriers to trade, among other areas. In short, an overarching agreement would allow “connecting” the existing, smaller preferential spaces, creating gains through increased efficiency and reduction of discrimination.

**TABLE 4**  
**FTAS LINKING THE PARTICIPANTS IN THE TPP ENLARGEMENT NEGOTIATIONS**  
**(AS OF FEBRUARY 2011)<sup>a</sup>**

	Australia	Brunei	Chile	Malaysia	New Zealand	Peru	Singapore	US	Vietnam
Australia									
Brunei	X <sup>b</sup>								
Chile	X	X <sup>c</sup>							
Malaysia	X <sup>b</sup>	X <sup>d</sup>	X <sup>e</sup>						
New Zealand	X	X <sup>c</sup>	X <sup>c</sup>	X <sup>b</sup>					
Peru			X						
Singapore	X	X <sup>d</sup>	X <sup>c</sup>	X <sup>d</sup>	X <sup>g</sup>	X			
US	X		X			X	X		
Vietnam	X <sup>b</sup>	X <sup>d</sup>	X <sup>f</sup>	X <sup>d</sup>	X <sup>b</sup>		X <sup>d</sup>		

Source: Author, based on information contained in the Foreign Trade Information System of the Organization of American States (<http://www.sice.oas.org>) and in the Free Trade Agreement Database for Asia of the Asian Development Bank (<http://aric.adb.org/FTAbCountryAll.php>).

a All agreements are bilateral unless otherwise indicated.

b ASEAN-Australia-New Zealand FTA.

c TPP.

d ASEAN Free Trade Area (AFTA).

e FTA signed, not yet in force.

f Free Trade Negotiations underway.

g The New Zealand – Singapore Closer Economic Partnership (NZSCEP) Agreement, the ASEAN-Australia-New Zealand FTA and the TPP coexist.

To the extent that having a “model agreement” as a reference helps convergence efforts, two blueprints come immediately to mind. Firstly, the original TPP agreement constitutes an obvious starting point for an enlarged -and updated- version. Secondly, the leading role played by the US in the TPP process almost inevitably means that the so-called “NAFTA model” —on which all US FTAs to date have been largely based— will be another important reference. Indeed, most current TPP participants are familiar with the latter model: four of them (Australia, Chile, Peru and Singapore) have bilateral FTAs in force with the US, while New Zealand has expressed in the past its interest to engage in such negotiations and Malaysia was actually involved in them for a number of years. The main challenge thus is how to combine these two models into a new TPP, incorporating as well more recent topics and approaches that are not reflected in either of them.

### 3. Economic cooperation

A common challenge for Latin American countries is to enhance the quality of their trade relations with Asia. The current trade pattern between both regions is fundamentally inter-industrial: Latin America mostly exports natural resources with low processing levels, whereas Asia exports mainly manufactures with different degrees of elaboration. This is largely explained by China’s seemingly inexhaustible demand for commodities such as copper, iron ore, petroleum and soy beans.

FTAs (including the TPP) might contribute to a higher diversification and technological sophistication of Latin American exports to Asia. Nevertheless, making progress in that direction also requires changes in the productive structure of the region that largely exceed what trade policy and negotiations can deliver. Achieving productive (and export) diversification requires action on a wide range of public policies, including those dealing with innovation, science and technology, access to credit, education and foreign investment, among other areas. Moreover, a radical shift in the region’s exporting pattern to Asia looks unlikely, given its strong comparative advantage in natural resources and the Chinese economy’s high demand for them. What looks more feasible (and still desirable) is

increasing the value added and knowledge content of natural resource-based exports. This can be done, for instance, by taking advantage of developments in biotechnology and other life sciences.

As already noted, the original TPP explicitly recognizes the importance of cooperation in a wide range of areas to further the agreement's goals. An enlarged TPP should build on this vision, providing for a strong and adequately funded cooperation agenda. Such agenda could make a significant contribution towards meeting the challenges Latin American countries face as they try to develop their economic links with Asia Pacific. Thus the inclusion in the ongoing talks (under the heading of "horizontal issues") of topics such as how to promote the internationalization of small and medium enterprises and the development of regional value chains seems to be a positive step.

#### **4. Benefits from further TPP expansion**

For Latin American countries, the risks derived from the current TPP negotiations (see section B) must be weighed against two main types of potential benefits: commercial ones and those of a strategic nature. The former refer to the gains already outlined in terms of new market access opportunities and the reduction of transaction costs for trade with other TPP members. The latter would derive from being part of an agreement that could become one important platform for the construction of the trans-Pacific economic architecture for the coming decades, and which could even become a "laboratory" for future WTO disciplines. The magnitude of both types of benefits ultimately depends on other countries joining the current participants.

As noted above, the TPP —given the current set of participants— does not represent an attractive vehicle for Latin American countries to gain access to new key markets. This results from a combination of factors:

- Both the current Latin American TPP participants and the prospective ones already have FTAs in force with the US (their first or second most important individual export market), or have at least signed those agreements, which could reasonably be expected to enter into force in 2012.
- Both the current Latin American TPP participants and the prospective ones either have FTAs in place among themselves or are negotiating them (the latter is the case, for example, of ongoing negotiations between Peru and Mexico, Peru and Central America plus Panama, and Colombia and Panama).
- Chile and Peru already have a large number of FTAs in force, subscribed or under negotiation with Asia Pacific economies (including several current and prospective TPP participants). Other possible Latin American TPP candidates such as Costa Rica, Panama, Mexico and Colombia have also started following this route.
- Among LAPAF members, Asia is today an important export market only for Chile, Peru and —to a lesser extent— Costa Rica and Colombia. The bulk of that trade corresponds to China, Japan and Korea, three countries which are not currently participating in the TPP negotiations.

Thus the TPP's attractiveness from a market access viewpoint depends on the incorporation of new (mainly Asian) economies. The prospects for some key Asian countries to join the TPP are briefly discussed below.

Korea and the US signed a bilateral FTA (the KORUS FTA) in June 2007. It is the most important FTA subscribed by the US since NAFTA, in terms both of the volume of bilateral trade involved and the partner's economic size. However, more than three and a half years after being signed, the KORUS FTA still has not been sent to the US Congress for approval. This is due to allegations that the agreement did not sufficiently address several non-tariff barriers affecting US exports of cars and beef to Korea. This scenario changed when in December 2010 the US and Korea struck a deal supplementing the KORUS FTA, essentially through further Korean regulatory concessions in the automotive sector (Schott 2010).

The December 2010 deal has wide support within the US Congress, which could pave the way for approval of the KORUS FTA in 2011. Indeed, the Obama administration has indicated that it attaches high priority to its early passage, if possible during the first half of 2011. The way this process unfolds has a direct bearing for the TPP negotiations: Although Korean authorities have indicated in the past that the possibility of joining the TPP was being considered, they made it clear that first the US must approve the KORUS FTA (Washington Trade Daily 2010).

Japan's government has expressed an interest in joining the TPP negotiations, indicating that a decision on the matter should be made by June 2011.<sup>25</sup> Approval of the KORUS FTA by the US Congress, whether or not followed by Korea's entry into the TPP talks, could tilt the balance in favor of Japan joining the latter. This is because Japan and Korea compete strongly in the US market in products such as automobiles, electric home appliances and information technology goods. The entry into force of the KORUS FTA would grant Korean exports an advantage over those from Japan in the key US market. This could induce the Japanese government to seek to "level the playing field" by joining the TPP. In doing so, it would have to overcome the resistance of its powerful farming lobby. However, there seems to be a growing awareness among Japanese authorities that reform of the agricultural sector is needed, including by greater exposure to foreign competition (Government of Japan 2010).

China's economic relationship with the United States presents numerous elements of tension. Behind these is the large US trade deficit with China, which in 2010 reached 273,000 million dollars (equivalent to 43% of the total US trade deficit). China has been periodically accused in the US of undervaluing its currency, the Yuan, to maintain its surplus in bilateral trade. It is also often accused of maintaining numerous barriers to US products and investments in areas such as government procurement and intellectual property, and more generally through a wide range of industrial policies.<sup>26</sup> This has resulted in the US starting ten dispute settlement cases against China at the WTO since 2004.<sup>27</sup>

China, for its part, has been critical of both US pressure to revalue the Yuan and what it perceives as a growing protectionism against it, in the US and elsewhere.<sup>28</sup> It also has often clashed with the US in the Doha Round, due to its reluctance to accept demands for Chinese participation in tariff elimination initiatives in sectors such as chemicals, engineering machinery and medical equipment. Moreover, China promotes the formation of a purely Asian trade bloc such as EAFTA, that is, precisely the kind of initiative the TPP is intended to preempt or at least counterbalance. Taken together, all these elements seem to preclude the possibility of China and the US entering free trade negotiations with each other in the near future, be it within the TPP or bilaterally.

Neither does India—which is not even yet an APEC member—appear as a likely candidate to join the TPP. In spite of the reforms started two decades ago, it still has a less open economy than those of China and most East Asian countries. It has also ventured more cautiously than them in the negotiation of PTAs. India has in particular strong defensive sensitivities in agriculture, linked to its large subsistence agriculture sector. This has resulted in frequent clashes with the US in the Doha Round, given the strong exporting interests of US agro industry, especially in the larger emerging economies. Concerning intellectual property, it looks unlikely that India would be willing to accept the strict demands the US often poses to its FTA partners, especially if such demands are seen as potentially restricting the Indian population's access to generic medicines (on the basis of which India has built an internationally successful pharmaceutical industry).

<sup>25</sup> The timing of this decision may obviously be affected by the events following the massive earthquake that affected North Eastern Japan on March 11<sup>th</sup>, 2011.

<sup>26</sup> See "US Statement at the WTO Trade Policy Review of China", May 31, 2010, at <http://geneva.usmission.gov/2010/05/31/tp-r-china/> (consulted on 11 June 2010).

<sup>27</sup> See [http://www.wto.org/english/tratop\\_e/dispu\\_e/dispu\\_by\\_country\\_e.htm](http://www.wto.org/english/tratop_e/dispu_e/dispu_by_country_e.htm) (consulted on 21 December 2010).

<sup>28</sup> The main manifestation of this alleged protectionism is the frequent targeting of Chinese products in antidumping investigations, especially since the onset of the recent global economic crisis (Bown 2010).



Two ASEAN members (Brunei and Singapore) were original TPP signatories, and two more (Malaysia and Vietnam) have joined the enlargement talks. Nevertheless, it is likely that countries such as Thailand, Indonesia and the Philippines will maintain a cautious, “wait and see” approach to the TPP in the coming months. They will probably want to see how the process evolves during 2011, including whether the emerging agreement accommodates the specific needs of relatively less developed countries such as Vietnam. Moreover, ASEAN is becoming the *de facto* hub of the main economic integration initiatives in East Asia, which means that the TPP is to some extent competing with processes such as ASEAN+3.

Summing up, it is unclear at this point whether some of the main Asian economies could be attracted to the TPP negotiating table during 2011. If approval of the KORUS FTA by the US Congress were to result in Korea, Japan or both joining the TPP negotiations, these would become a much more commercially attractive proposition than they are today.<sup>29</sup> Moreover, that could set in motion a domino effect whereby countries such as Thailand, Indonesia and the Philippines would have stronger incentives to follow suit.

## B. Risks

### 1. US trade politics

The US already has FTAs in force with four of its TPP partners (Australia, Chile, Peru and Singapore), and the remaining four (Brunei, Malaysia, New Zealand and Vietnam) represented in 2009 just 1.5% of its total exports. This is why for the US, same as for the participating Latin American countries, the TPP’s commercial payoff rests on bringing larger economies to the negotiating table (Bergsten and Schott 2010). The same can be said about the TPP’s strategic appeal: an agreement limited to the current nine participants would be far from representing a real platform for trans-Pacific integration.

Despite the strategic importance President Obama’s administration attaches to the TPP, doubts remain concerning the United States’ ability to lead this process and bring it to a successful conclusion. In recent years the prevailing attitude towards trade within the US Congress and among the US population at large has been ambivalent at best, and more often openly critical. Increased competition by emerging economies and the recent world economic crisis have strengthened this stance, especially among large segments of the Democratic Party. Accordingly, the Obama administration has generally taken a very cautious approach to trade, especially during its first year in office. Thus the US has not entered new trade negotiations (other than the TPP), passage of the FTAs with Colombia, Panama and Korea remains pending, and the administration has not requested Congress for a new grant of Trade Promotion Authority (TPA), last expired in July 2007.<sup>30</sup>

Perhaps the most tangible expression of discontent with recent US trade policy, especially under the Bush administration, is the Trade Reform, Accountability, Development and Employment (TRADE) Act, introduced in June 2009 by a number of members of the House Representatives from the Democratic Party. The TRADE Act rejects the so-called “NAFTA model” of US trade negotiations, calls for the review (and possible renegotiation) of existing agreements, and sets forth a new set of requirements for future negotiations, in terms of issues that should and should not be included in them. Among the former are increased food and product safety and labor and environmental standards, whereas among the latter are privatization and deregulation requirements in

<sup>29</sup> It is worth noting, however, that Chile already has FTAs in force with Japan and Korea (as well as China). Peru, for its part, has an FTA in force with China, and during 2010 successfully concluded negotiations towards an FTA with Korea and an Economic Partnership Agreement with Japan.

<sup>30</sup> TPA essentially consists in Congress temporarily renouncing its prerogative to amend trade agreements negotiated by the Executive, limiting itself to a yes or no vote on them. It is generally considered that TPA is essential for the approval of trade agreements by Congress.

the service sector, bans on Buy American procurement policies, and new rights and privileges for foreign investors under investor-State dispute settlement mechanisms.<sup>31</sup>

Against the above background, the Obama administration does not seem to have come yet to a firm position on what type of agreement it wants the TPP to be. Various groups, including business coalitions, non-governmental organizations and the two parties in Congress, are closely scrutinizing the TPP process and pulling in different directions. This is arguably a consequence of the expectation that the TPP should somehow set the standard for future US trade negotiations in a “post NAFTA model” era. Meeting the sometimes conflicting expectations of those groups is already proving a challenge for the administration. The ongoing discussions aimed at defining the US position on investment and intellectual property (on which more below) are a case in point.

Secondly, although the US partners in the TPP are all relatively small economies, this does not mean that liberalizing trade with them is going to be free of problems. There are lobbies that actively oppose opening up the US market to agricultural imports from New Zealand, especially in the dairy sector. Similar lobbies have been successful in the past, as evidenced by the exclusion of sugar from tariff reductions in the Australia-US FTA. Trade liberalization should prove even more controversial with Vietnam, which is internationally competitive in textiles and clothing, both politically sensitive sectors in the US. In particular, Vietnam’s low per capita income, poor labor standards and non-market economy status have already given rise to claims of unfair competition.

All the above notwithstanding, there are some encouraging signs. The administration’s initial attitude of relative neglect for trade has been gradually changing, as suggested by President Obama’s stated goal of doubling US exports in five years<sup>32</sup> and by the recent supplementary deal to the KORUS FTA. Prospects for US trade policy also look somewhat brighter following the November 2010 midterm congressional elections in which the Republican Party regained control of the House of Representatives and increased its strength in the Senate. Although at this point it is too early to make any firm predictions, this new correlation of forces could result in more progress on the trade agenda than when the Democratic Party dominated both chambers of Congress. Recent calls by Republican members of Congress for early passage of all three pending FTAs seem to point in that direction.

## **2. Difficulty to find an overall balance**

Ultimately, like any trade negotiation, the TPP will come to fruition only if all participants are able to find a configuration of “gains” and “losses” (i.e. an overall balance) which is both economically attractive and politically saleable. The possible gains for Latin American countries have already been discussed. The issue of the possible costs is examined below. As will become clear, much depends on the position taken by the US on several issues, which in turn is heavily influenced by its domestic trade politics.

TPP participants have already decided that the existing agreements among them will remain in force and will thus coexist with an enlarged TPP. However, the latter most likely will include provisions that effectively amount to a reopening of the existing pacts in several areas. This, depending on the country and the subject, can represent an opportunity or a threat. Some of the most contentious issues are discussed below. Since the US appears as the main driver of the negotiations, particular emphasis is placed on US debates on those issues.

US business groups have called for using the TPP negotiations to set a new, higher standard for protection of intellectual property rights (IPRs), thus raising the protection levels agreed in previous US bilateral FTAs (which already exceed in several aspects those agreed in the WTO’s TRIPs agreement). Intellectual property is an area in constant expansion in a world economy which is increasingly technology—and knowledge—driven. Accordingly, the US—as the world’s largest net

<sup>31</sup> See <http://www.citizen.org/documents/TRADEActFactSheet2009.pdf> (consulted on 1 July 2010).

<sup>32</sup> This goal was mentioned in the President’s State of the Union address to Congress in January 2010. See <http://www.whitehouse.gov/the-press-office/remarks-president-state-union-address>. To this effect, President Obama spoke of strengthening US trade relations in Asia. The TPP would be one vehicle to do that.



exporter of intellectual property— has pursued since the 1980s a policy of continuous upward protection of IPRs in its trade negotiations, in which the last FTA negotiated (in this case the one with Korea) becomes the *de facto* baseline for future talks.

In light of the above, there is ample scope for the US to use the TPP process to push Latin American countries (and other participants) to adopt new commitments on IPRs, both substantive and enforcement-related.<sup>33</sup> A case in point could be language in the KORUS FTA that allows the granting of patents for “any new uses or methods of using a known product”, a provision which goes well beyond TRIPs disciplines. Another possible example concerns copyrights and patents in the digital environment, such as demands by US business groups that the TPP require countries to provide patent protection for computer implemented inventions. Nevertheless, the US has so far not been able to table a full, formal proposal on intellectual property at the TPP. According to press reports, this would be because some business demands clash with previous agreements reached in May 2007 between the Bush administration and the then Democratic majority in the House of Representatives and which somehow relax IPR protection in some US FTAs (Inside US Trade 2011).

The US has been patent conducting since August 2009 an interagency review of its 2004 Model Bilateral Investment Treaty (BIT), on which the investment chapters of most of its FTAs are largely based. The review has extended well beyond its expected completion date in late 2009. This arguably reflects the difficulty of reconciling business demands for increased protection for US investments abroad with calls by civil society groups and parts of Congress to limit what are perceived as extraordinary rights granted to foreign investors in the US (Gantz 2010). A particularly contentious feature of existing US BITs is the investor-state dispute settlement (ISDS) mechanism, which is also part of the investment chapters of all US FTAs (except for the Australia-US FTA).

Against this background, it is unclear how prepared the US may be to depart from its existing model in the investment chapter of an enlarged TPP. Although as of writing the US has not tabled a draft investment chapter, early indications suggest that it will push for the inclusion of ISDS. The US has neither BITs nor FTAs in force with four TPP partners: Brunei, Malaysia, New Zealand and Vietnam. This means that US firms investing in those countries (except for Vietnam<sup>34</sup>) do not have recourse to ISDS, a mechanism whose promoters consider necessary when there are doubts about the reliability of the host country’s domestic courts to settle disputes involving foreign investors. More often than not these will be developing countries such as those mentioned above (except New Zealand) and other prospective TPP candidates like Indonesia, Thailand and the Philippines.<sup>35</sup>

Also concerning investment, it seems that the US is maintaining in the TPP its traditional tough line on capital controls. In all its BIT and FTA negotiations so far the US has sought —and largely achieved— to constrain the ability of governments to deploy such controls, even if done on a temporary basis and for purposes of financial stability (Gallagher 2010). Chile (and later Peru) secured in their bilateral FTAs with the US some limited flexibility to apply capital controls, under the so-called “cooling off” provision.<sup>36</sup> Attempts to restrict that flexibility in the context of the TPP could

<sup>33</sup> It is worth noting that Chile was included in the “Priority Watch List” in the Special 301 Report on the state of intellectual property protection in US trade partners, released by the Office of the United States Trade Representative (USTR) in April 2010. According to the USTR, this category includes countries that do not provide an adequate level of protection or enforcement of intellectual property rights. Brunei, Colombia, Costa Rica, Malaysia, Mexico, Peru and Vietnam, all of them current or potential TPP participants, were included in the lower-level “Watch List” category (see <http://www.ustr.gov/about-us/press-office/press-releases/2010/april/ustr-releases-2010-special-301-report-intellectual-p>, consulted on 27 May 2010).

<sup>34</sup> The US Vietnam Bilateral Trade Agreement, in force since 2001, has an investment chapter that includes ISDS. Moreover, both countries started in 2008 negotiations towards a BIT. Nevertheless, no negotiating rounds have been held since November 2009, arguably in part because of both countries’ involvement in the TPP talks.

<sup>35</sup> Nevertheless, as already noted, there is some opposition to ISDS within the Democratic Party. Thus in December 2010 seven House Democrats stated in a letter to President Obama that ISDS should be excluded from the TPP, or at least substantially constrained, to avoid granting foreign investors greater rights than those afforded to domestic ones. ISDS could be constrained, for example, by requiring a foreign investor to exhaust local administrative and judicial remedies before being able to file an international arbitration claim (Inside US Trade 2010d).

<sup>36</sup> Under this provision, no claims can be filed against Chile or Peru (either state to state or investor-state) in relation with restrictive measures they apply with regard to payments and transfers, for a one-year period following the implementation of those measures. Once the claim is brought, loss or damages shall be limited to the reduction in value of the transfers, thus excluding loss of profits or business and any similar consequential or incidental damages.

prove problematic, not just with Chile but also with other participants such as Malaysia that have often resorted to capital controls. These countries may be especially reluctant to accept further constraints on their ability to apply capital controls given the current context, marked by the recent world financial crisis and by large net capital inflows to developing countries. These inflows, which are often of a short-term nature, push for real appreciation of developing countries' currencies, thus hurting their export competitiveness.

US demands to raise standards above those of previous FTAs may also come in the areas of labor and environment. As part of its May 2007 compromise with the then Democratic majority in the House, the Bush administration agreed to incorporate new environmental and labor provisions in the FTAs with Colombia, Panama, Peru and Korea. Although the new Republican majority in Congress may be less keen to push for raising labor and environmental standards in trade negotiations, the Obama administration will probably still need to deliver results on that front to gain support for the TPP from its own Democratic Party. Probably reflecting the complexity of finding a compromise acceptable to both parties, the US has still not tabled full, formal proposals on labor and environment.

The TPP process also considers horizontal discussions on regulatory coherence. These talks are at an early stage, so it is difficult to speculate on their outcome. Increasing the transparency of regulatory regimes in TPP members would certainly be desirable, same as facilitating the exchange of best regulatory practices among them. However, the discussions may prove problematic if—as it already seems to be the case—they result in calls for regulatory harmonization across TPP members, disregarding their obvious differences in development levels, institutional capacities and legal systems, among other dimensions.

Apprehensions about the inclusion of “TRIPs-plus” provisions and ISDS in trade agreements between developed and developing countries have often been voiced by developing country governments, as well as by academics and civil society organizations in both the developing and developed world. More recently, similar concerns have begun to be raised within the governments of industrialized countries, including TPP participants. Thus in a report released in December 2010 the Australian Government's Productivity Commission recommends that Australia “avoid the inclusion of IP [intellectual property] matters as an ordinary matter of course in future BRTAs [bilateral and regional trade agreements]”, arguing that plurilateral or multilateral fora should be privileged instead (Australian Government Productivity Commission 2010). As to ISDS, the Commission's report states that “Australia should seek to avoid accepting ISDS provisions in trade agreements that confer additional substantive or procedural rights on foreign investors over and above those already provided by the Australian legal system” (ibid., page 277).

Notably, the Commission's arguments against the inclusion of IP and ISDS in preferential trade agreements are based both on an assessment of Australia's national interest and on that of partner countries, especially developing ones. In the case of IP, the report refers openly to the risk of “negative sum game” outcomes, as countries that are net IP exporters—such as the US—experience gains but those that are net IP importers suffer even larger losses. For example, it is argued that the extension in the duration of copyright required by AUSFTA imposed a net cost on Australia, partly reflecting its status as a net IP importer, and that it would likely impose net costs on other countries in a similar position (ibid., pp 259-260). According to press reports, the New Zealand government shares some of these apprehensions. Specifically, it is concerned that overly strong IP protection could actually hamper innovation, especially in relatively less developed countries such as several TPP participants. Therefore, New Zealand would prefer that the IP chapter of an enlarged TPP do not go beyond the protection provided by the TRIPs agreement (Inside US Trade 2010c).

As to ISDS, the Commission's report concludes that “there does not appear to be an underlying economic problem that necessitates the inclusion of ISDS provisions within agreements” (ibid., p 271), as foreign investors already have a number of ways to insure themselves against the risks of investing abroad (including political risk). At the same time, a number of potential risks to host governments are identified. These include the risk of “regulatory chill”, as governments are dissuaded from taking regulatory action for fear of triggering arbitration claims, as well as concerns

relating to the arbitration process such as institutional bias, conflicts of interest, lack of transparency, and excessive sums being awarded to foreign investors, *inter alia* (ibid., pp 271-273).<sup>37</sup> Against this background, the Commission argues that a preferable option could be for developed countries to help developing ones to develop stable and transparent legal and judicial frameworks through capacity building.

Chile and Peru, as well as other Latin American potential TPP candidates, had to make several economically and politically costly concessions in their respective FTAs with the US. Some of those concessions were made even after the formal closure of negotiations, through amendments to the agreed texts.<sup>38</sup> Commitments on intellectual property have been especially contentious, as they often involved going beyond TRIPs provisions. Such is the case, for example, of the increased protection afforded by FTAs to pharmaceutical and agrochemical products, as well as copyrighted matter; of the restrictions placed on certain flexibilities allowed by TRIPs such as mandatory licensing for medicines; and of the strengthening of enforcement provisions beyond TRIPs disciplines (Roffe, 2004; Roffe and Santa Cruz 2010). Renegotiation within the TPP of existing commitments on issues such as IPRs, investment and environment involves for Latin American countries the risk of “paying twice” in areas of great political sensitivity and which relate to a broad range of public policies.

The prospect of new demands in sensitive areas will be more problematic if the US is not inclined to accommodate developing countries’ concerns through flexibilities in a future TPP agreement. Although this is unclear at this point, there already are indications that US negotiators would prefer to limit such flexibilities to extended implementation periods, so as not to have a “two-tier” agreement (Inside US Trade 2010b). This may prove a big challenge, since the “TPP 2.0” would be an agreement with an extremely diverse membership, in terms of their development levels, population’s size, institutional capabilities, and legal and political systems. Although on a smaller scale, the TPP process may end up facing similar challenges to those that plagued the failed negotiations on the Free Trade Area of the Americas, in terms of how to structure a high quality agreement while accommodating the large diversity of interests and capacities among its members.

Disagreements have also emerged on how tariff commitments would apply within an enlarged TPP. The current TPP members and Australia favor aiming immediately for a single market access schedule, common to all TPP members (that is, creating a free trade area among them). By contrast, the US initially tabled bilateral market access offers. These were presented only to those countries with which the US does not have FTAs in force. The US has not made its views known on how TPP members would move from there to a single schedule. Keeping existing schedules closed for a prolonged period is in principle the least ambitious option, as existing carve-outs (for example, that of sugar in the Australia-US FTA) would be locked in. Moreover, such approach would in principle mean that existing bilateral sets of rules of origin would also be kept in place, thus reducing the contribution of an enlarged TPP to addressing the spaghetti bowl problem and to cutting businesses’ administrative and transaction costs. This issue is at the heart of whether an enlarged TPP would become a truly regional agreement or something resembling more an umbrella for existing bilateral agreements among its members.

It is generally recognized that if rules of origin are too difficult to meet, they may end up nullifying the tariff commitments negotiated for the affected products. To the extent that the ongoing negotiations lead to a new set of rules of origin which is more restrictive than those applying under the current TPP, that would diminish the new agreement’s value in terms of trade liberalization. This is a particular concern in sectors such as textiles and clothing, where existing US FTAs impose very stringent origin requirements (the so-called “yarn forward” rule). Moreover, as of writing, little is known publicly about the US position on the possibility of achieving cumulation of origin among TPP members. This would be one of the most important “selling points” for countries such as Chile and Peru, which already enjoy duty free treatment on the bulk of their trade with other TPP participants.

<sup>37</sup> Another set of concerns about ISDS relates to sovereignty and equity issues, as foreign investors may in practice end up having rights exceeding those of domestic ones.

<sup>38</sup> For a detailed analysis of recent trade negotiations between Latin American countries and developed countries (especially the US) in services, investment and intellectual property, see Rosales and Saez (2010).

Aside from the likely US reluctance to fully open up its market in sectors such as dairy, sugar, textiles and clothing, it looks doubtful that the US will be prepared to put on the table at the TPP its agricultural subsidies and antidumping practices. Both are issues of great interest to developing countries but which the US has so far only been prepared to deal with in the Doha Round at the WTO. This could end up providing a justification for other TPP partners to carve out their own sensitive products and sectors, thus diminishing the value of the final deal.

More generally, a key issue for the TPP negotiations will be determining the relationship between an enlarged TPP and the several agreements already linking the current participants. As already noted, the latter are expected to remain in place after the entry into force of an enlarged TPP. This begs the question of what set of rules would prevail in situations where provisions from an existing agreement and the new TPP apply. The contribution that the latter can make to overcome the spaghetti bowl problem depends critically on the answers to these and related questions.<sup>39</sup>

### **3. Lack of clarity on accession procedures**

As already discussed, for Latin American countries the TPP's appeal depends largely on other economies joining the talks. However, following Malaysia's entry there seems to be no consensus among the current TPP participants on whether, and when, to accept new countries into the negotiations. The US in particular appears reluctant to have other countries join the talks at this point, even if they are APEC members. For example, Canada has officially expressed its interest in joining the TPP negotiations. However, despite its being a large developed economy, an APEC member and a traditional US ally and trade partner in NAFTA, it has been told that there is no consensus yet on its acceptance into the talks. According to several reports, one of the reasons is demands by the US and New Zealand for Canada to commit to open up its sensitive supply management system applying to poultry and dairy products.

For its part, Colombia has not yet been accepted into the negotiations despite having the support of the other two Latin American participants, having concluded an FTA with the US and being a key US political ally. The fact that Colombia is not an APEC member should be immaterial, as TPP accession is not a priori confined to APEC members.<sup>40</sup>

Reluctance among some TPP participants to let other countries join at this stage may respond to concerns about the negotiations becoming excessively complicated, or to a desire to reach an agreement on the fundamental parameters and level of ambition among the current members that could later be presented essentially as a "fait accompli" to other interested countries, or both. Be that as it may, the later interested Latin American countries are allowed to join, the lesser their capacity to influence the outcome of the negotiations will be. This in turn may result in decreasing interest in joining the TPP.

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<sup>39</sup> An interesting precedent here is provided by New Zealand and Singapore. Both countries decided that the New Zealand–Singapore Closer Economic Partnership (NZSCEP) Agreement, which had entered into force in 2001, would remain in force along with the TPP. In this way, exporters from both countries are able to choose the better of the treatment afforded under either agreement. Although this arrangement can provide benefits to traders via increased flexibility, it can also be seen as contributing to the spaghetti bowl problem through the overlapping of the two TPAs.

<sup>40</sup> Quite another issue is whether it would be in Colombia's best interest to engage in the TPP talks while its bilateral FTA with the US still has not been approved by the US Congress.



## VI. Conclusion

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The “TPP 2.0” negotiations have attracted considerable interest from policy makers, academics, businesses and civil society groups in many countries. There are several reasons for this, including Asia Pacific’s economic dynamism, which has transformed it in the world’s main growth engine; the development in that region of several competing economic integration initiatives; the uncertain prospects of the Doha Round, after more than nine years of negotiations; and the strategic importance the Obama administration attaches to the TPP project. However, a year after the negotiations were launched, numerous elements of uncertainty still surround this process. Full, formal proposals are still to be tabled in some of the most contentious areas and no draft texts have been released to the public. Key decisions remain to be made, including on the architecture of the future agreement, its thematic coverage, the definitive list of participating countries, and the procedures according to which other countries would be allowed to accede following conclusion of the current negotiations. By now it is widely admitted that the negotiations will not be concluded by the original target of November 2011, when the US will host APEC Leaders in Hawaii.

In light of the above, it is very difficult today to assess with any precision what the TPP process offers Latin American countries. The answer depends crucially on a number of factors which remain unclear, including: whether Latin American countries -other than Chile and Peru- will be allowed to enter the negotiations, and if so, when and on what terms; which other countries —especially Asian— join the negotiations; and how an enlarged TPP will relate to the FTAs Latin American countries already have in force with other TPP participants. Concerning the latter point, a particularly important issue is whether —and to what extent- the “new TPP” will involve renegotiation of



existing FTA commitments in sensitive areas such as intellectual property, investment and labor and environmental standards.

For Latin America, it is imperative to develop stronger links with the main Asian economies, due to the key role these —led by China and India— are acquiring in world production, trade, investment and finance. Doing so through an agreement with a broad membership and whose agenda is not confined to trade but also has a strong cooperation component appears in principle as a more attractive option than the negotiation of bilateral trade agreements with each Asian partner. The TPP has the potential to become such an instrument, as well as to make a significant contribution to “multilateralize regionalism” in Asia Pacific. However, it remains to be seen to what extent it will realize that potential. A particular challenge in this regard will be managing the large diversity that exists among TPP partners. This will require avoiding extreme regulatory harmonization which is neither politically feasible nor desirable from a developmental perspective. It will also require building a robust economic cooperation framework, aimed —inter alia— at increasing the institutional capacities of the least developed TPP partners to gradually assume more demanding commitments.

Given the big challenges facing the TPP process, and the relatively small size of the other partners, the US should naturally exercise a positive leadership in it. Nevertheless, at this point it is not clear what the US can offer its TPP partners in exchange for the likely prospect of being presented with politically difficult demands. An agreement that appears biased towards US interests (both offensive and defensive) would arguably be difficult to sell domestically for the remaining TPP partners. Moreover, it would be of little interest for other Asian (and Latin American) developing countries currently considering whether to join the TPP, thus defeating its stated goal of becoming a platform for gradually building a trans-Pacific free trade area. For Asian nations in particular, the less accommodating of developing country sensitivities and needs the TPP is perceived to be, the more attractive the alternative processes centered on ASEAN will become.

Lastly, it seems clear that US interest in the enlargement of the TPP is at least as much defensive (preempting or building a counterweight to a purely Asian bloc) as it is offensive (gradually moving towards a trans-Pacific free trade area). Latin American countries participating in the TPP negotiations or considering joining them must be fully aware of the strategic backdrop of this process, in which Latin America plays a relatively minor role. Within this context, they should pragmatically decide on their participation and positioning in the talks, according to their own national interests.

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