

The importance of TPP for Taiwan

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A. INTRODUCTION

1. The TPP is of critical importance to Taiwan. Its importance and implications are reflected in three major aspects. First is the economic implication if Taiwan joins (or failed to join) the TPP bandwagon. Second is the implication on domestic reforms, i.e. using TPP as a driving force for Taiwan to undertake reform initiatives. Last but not least is the political implication for Taiwan as a policy 'insurance' in dealing with cross-strait relationship with mainland China.
2. TPP is a Preferential Trade Agreement (PTA) in nature. PTAs provide more favorable market access treatments for participating members, thus offering competitive advantages over those non-members. For a heavily trade-dependent economy like Taiwan, it has to date only a handful of PTAs that covers less than 6% of total trade. With major competitors such as Korea, Japan, Singapore, Malaysia, Vietnam and even China mainland that are all accelerating their PTA undertakings, the lagging behind in PTAs obviously create a genuine anxiety among government and industries in Taiwan to join the TPP, especially the number of countries joining the TPP is growing over time.
3. In addition, one of the salient features of TPP and other recent PTAs is that they tend to go beyond traditional tariff and services trade liberalizations to include new trade regimes addressing barriers created by Non-Tariff Measures (NTM) and harmonization of domestic regulations. These so-called 'deep integration' elements offer longer-term benefits for TPP members that are perhaps even larger than tariff concession. This is because deep integration elements reduce costs and uncertainty in cross border transactions in a consistent manner, make

investments less risky, and more importantly improve the efficiency of the reforming countries. This is the under-estimated long term impact and disadvantage if Taiwan fails to join the TPP. Certainly Taiwan can unilaterally undertake reform initiatives that mimic TPP obligations, yet experiences in the past (e.g. WTO membership) demonstrate that external pressure such as TPP negotiations and obligations tends to be a more effective way to push for domestic reforms.

4. As for political importance, many in Taiwan felt uncomfortable if Taiwan is only engaged (and thus locked-in) in PTAs with mainland China. This is reflected in the economic security concern voiced during the debate over the cross-Strait services trade agreement in recent months, with many oppose the agreement and any further advancement without participating at the same time in TPP and other regional integration mechanism. This indicates that TPP membership can also play as a safety buffer that facilitates further development of cross-Strait trade relationship.

B. THE ECONOMIC IMPORTANCE OF THE TPP

5. Taiwan's economy is heavily dependent on trade, with the exportation of manufactured goods and services equivalent to an average of 65% and 11 % of the GDP respectively in the last decade. As indicated in Table 1, around 64 % of Taiwan's total trade value (and 72 % of export) takes place within TPP members and mainland China (including Hong Kong).
6. With trade barriers between Taiwan and mainland China can (hopefully) now be addressed by the ECFA and agreements on services and goods, this warrants that the participation of Taiwan in the TPP will bring significant benefits for Taiwan's trade performance. This is also to address the threat arises from Japan and Korea's active involvement in the regional integration process. Taiwan faces strong competition from them in most major markets, with over 50% of the export items overlaps with the two countries (CIER, 2011).
7. Export to the U.S., which is Taiwan's second largest export destination, also shows signs of reduction in light of the Korea-U.S. FTA. Already 33.5% of the manufactured products that Taiwan exports to the U.S., including textile, electronics, machinery, auto parts and steel products, are subject to different

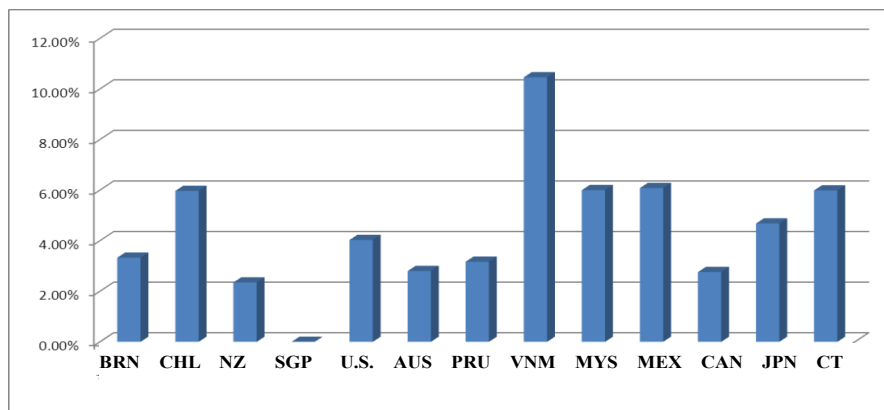
levels of tariffs. The tariff rates for about half of these products are between 2.5% to 5%, and a quarter of them faces tariff rates between 5% and 10%. According to U.S.'s schedule of tariff reduction under the Korea-U.S. FTA, almost all of these affected products will be tariff-free for Korean products by 2014 (Ku, 2011).

Table 1 Taiwan's trade relationship with TPP countries and China

	% of Taiwan's total trade value			% of Taiwan's export		
	2011	2010	2009	2011	2010	2009
TPP (TPP-12)	35.55	36.27	36.15	31.26	30.12	30.65
China +Hong Kong	28.71	28.97	27.89	40.24	41.79	41.09
Sub-total	64.26	65.24	64.04	71.5	71.91	71.74

Sources: Taiwan Ministry of Economic Affairs (MOEA).

8. Trade benefits derive not only from tariff reductions under the TPP, where tariff remains high for some of the participating TPP counties (Fig 1). It is also to ensure Taiwan's position in the Asian Pacific supply chain. Taking for example, if 'yarn forward' is adopted in the TPP as the rule for origin (RoO) for textiles, then it would have a negative impact on Taiwanese textile manufactures, with many of them currently supplying textile products to Vietman and Malaysia. Taiwan's TPP membership would benefit others in the group such that they do not have to look for second-best alternative suppliers.



Sources: WTO Tariff Analysis Online(TAO)

Figure 1 Average tariff for TPP countries and Taiwan

9. To this end, Petri *et al* (2012) estimates using the GTAP modeling that Taiwan will suffer a -0.3% reduction in real DGP and -1% in export value if not being able to join the TPP by 2025. The GDP and export reductions will be worsened to -1.9% and -5.3% respectively if Taiwan is excluded from the “C-J-K FTA plus ASEAN+3(CJK)” integration. To the contrary, our own estimates shows that if Taiwan is able to join the TPP, GDP will increase by 1.95%, and export will increase 6.57%.
10. In addition, RTAs such as TPP also enhances investment and therefore industrial collaborations. To this date TPP countries, especially the U.S., Singapore, Vietnam and Malaysia, remains to be the most important destination of Taiwan’s outbound investment outside China (Fig 2). Therefore from investment and industry interaction perspective, the benefit of joining the TPP exceeds RCEP or any other regional integration mechanism. Finally TPP membership for Taiwan is more likely to initiate a domino effect for Taiwan’s participation on other regional integrations, including the RCEP.

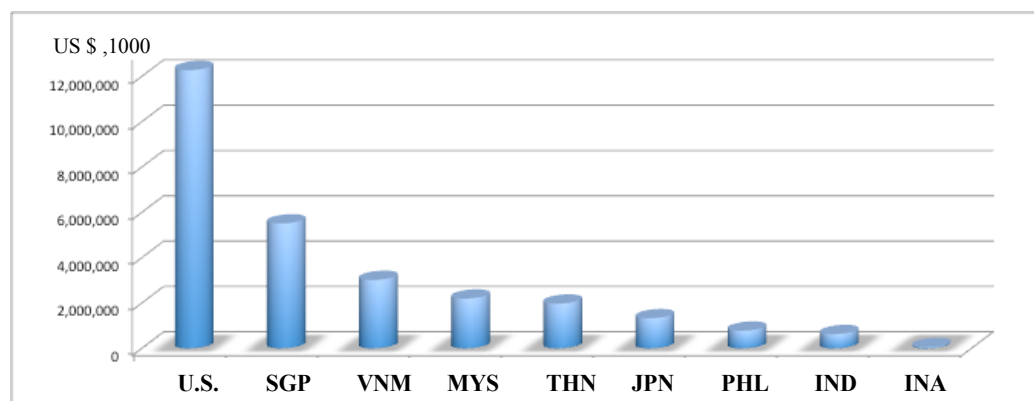


Figure 2 Destinations of Taiwan’s outbound investments (1951-2012; excl China)

C. TPP AS THE DRIVING FORCE FOR DOMESTIC REFORM

11. One of the unique features of TPP and other recent PTAs is the coverage of WTO-plus disciplines on Non-Tariff Measures (NTMs), in particular the reduction and harmonization of regulations that restrict trade and investment post market entry (WTO, 2010). Transparency and streamlining of financial and telecom regulations, for instance, has been one of the core elements in the Korea-U.S. and Korea-EU FTAs. Harmonization of technical regulations and conformity assessment procedures for mandatory product testing through the use

of mutual recognition mechanism and the Suppliers Declaration of Conformity (SDoC) regime are other typical examples. New international trade rules are also introduced for new and emerging services provisions, including rules on the liberalization of electronic commerce and ICT related services and the cross-border transfer of data and information. Another area of reform in TPP is structure reform in public utilities and State-Owned Enterprises (SOEs)

12. Certainly majority of these new disciplines on NTMs are included in TPP and other PTAs mainly to maximize the trade interests of especially economically advanced countries, yet domestic industries will be the primary recipient of the reform benefits if the regulatory system becomes more transparent and predictable, and competition becomes more feasible in markets that are dominated by SOEs.
13. As identified in numerous studies and positions papers by foreign chambers of commerce in Taiwan, Taiwan's lack of regulatory reform has become a major obstacle in economic efficiency, national competitiveness and attraction for foreign investment.¹ It has in fact been argued that Taiwan took a 'ten-year holiday' in (not pursuing) regulatory reform and elimination of unnecessary NTMs since acceded to the WTO in 2002. This is concurred by Taiwan's last WTO Trade Policy Report (WTO, 2010), which concludes that, *inter alia*, lack of foreign investment and the stranded privatization progress of SOEs are the major structural issues in Taiwan.
14. Reviews of the regulatory regimes in Taiwan identified the following primary areas that require further liberalization in Taiwan. First and foremost is the refinement in transparency of administrative procedures. Timeframe allowed for public comment on draft regulations, for instance, is in most cases 7 days, which offers only a nominal opportunity for the public and industries to express different views. Informal administrative measures in the form of Administrative Guidance that is legally non-binding but often produces a strong de facto effect is widely used by regulators across the board. In addition, liberalization of investments in professional (lawyers, accountants, architect etc.), healthcare and education services, as well as the reform of postal services, are also discussed.

¹ A summary of the documents is available at Taiwan's Council for Economic Planning and Development website at: <http://www.cepd.gov.tw/m1.aspx?sNo=0017289> (in Chinese)

15. Yet the progress of unilateral liberalization has been slow in Taiwan, and reform in these areas often proves to be more difficult than tariff elimination and services liberalization. This is because firstly it involves the removal of protectionism in a different form, i.e. the protection of regulators from public scrutiny and accountability. Secondly the groups of affected stakeholders in many of the areas identified (e.g. lawyers, state-owned banks) often have strong political connections.
16. Despite the fact that some of the NTM disciplines included in the TPP are contentious, in particular WTO-plus rules on intellectual rights protection, majority of them still serve as effective means of introducing international best practices in regulatory reform through binding obligations. This lock-in effect on reform is another often under-valued but equally important factor for countries like Taiwan to participate in TPP.

D. TPP AS A POLITICAL SOLUTION

17. Similar to many of its Asian peers, Taiwan's trade and investment is highly concentrated with China. For the last decade, in spite of various government restrictions in the past, China plus Hong Kong accounts for nearly 40% of Taiwan's export, and around 65% of total outbound investment. This indicates that any change in export performance in the Chinese market will undoubtedly have significant impacts on Taiwan's economy.
18. The high concentration of trade with China is also the source of non-economic concerns for many in Taiwan. The anxiety is underpinned by mainly political reasons. In particular relationship between Taiwan and the Mainland has not always been smooth and has been in fact subject to volatile fluctuations in recent years; it is thus argued that trade dependency would make Taiwan vulnerable to Cross-Strait political dispute in the future (Hong, 2010). Diversification of trading structure is therefore of critical importance to Taiwan
19. Such views once again resurged in the debate over recently concluded cross-Strait services trade agreement between Taiwan and mainland. Some challenged that the agreement would further exacerbate the economic locked-in effect and thus should be harmful for Taiwan.

20. TPP, with its U.S. leadership and large number of APEC economies now involved, is considered by many as the preferred platform in serving as an ‘insurance’ for Taiwan’s economic security. TPP can serve as a safety buffer that would facilitate further development of cross-Strait trade and investment relationship. As such, joining the TPP for Taiwan could provide a solution in addressing the internal divergence towards Taiwan-China economic relationship.

E. THE WAY FORWARD

21. Despite all the benefits of joining (and disadvantages of not joining), Taiwan’s participation in the TPP is still overshadowed by several uncertainties. First and foremost is the ‘China factor’. China’s position towards TPP has become clearer in recent months. Open discussion about China’s strategy in TPP has been disallowed until early this year and is now widely available. There is increasing a number of comments that took a positive perspective for China’s TPP participation. As a matter of fact, China explicitly includes the possible TPP membership as one of the policy rationales for the creation of the Shanghai Pilot Free Trade Zone.
22. Yet China’s own estimation suggests that it requires at least 10 years or more for China to match the requirements under TPP. Thus if China insists that the implicit principle of “China first, Taiwan next “ (as applied in the WTO accession process) must be observed, it means that Taiwan also needs 10 year of waiting. Unfortunately Taiwan does not have another 10 years. Possibility for China to adopt a more flexible approach will be one of the major factors affecting Taiwan’s TPP participation.
23. Second uncertainty is the level of determination to push for domestic reform. Reforms that would qualify Taiwan for TPP membership came in two categories. First category is the so-called ‘confidence building measures’ that Taiwan needs to adhere to before winning support from the U.S. and other TPP members. Japan’s commitments in re-opening U.S. beef, expanding auto vehicles quotas and reforming the Japan Post Insurance prior to receiving U.S. endorsement early this year provide some of the examples for Taiwan’s ‘down payments’. Second category of reform commitments is those regulatory obligations addressing behind the border issues in the TPP chapters.

24. The difficulty and thus uncertainty arise in this context is the resistance from *within* the government. Many of the reform agendas require competent authorities to collaborate and take initiatives in the process, yet they tend to at the same time bring fundamental changes to the way these authorities have been operating for a long time. Enhanced transparency in decision-making, for instance, increases the accountability of the government, which might not be able to gain support from the grassroots without strong political mandate from the top.
25. That said, as the government itself becomes a major stakeholder in the preparation of Taiwan's TPP application, a new form of protectionism, i.e. the protection of regulatory regimes to be able to stay in the 'good-old-days', also need to be addressed.