

Medalla, Erlinda M.; Mantaring, Melalyn C.

Working Paper

On Free Trade Agreements (FTAs): the Philippine Perspective

PIDS Discussion Paper Series, No. 2009-35

Provided in Cooperation with:

Philippine Institute for Development Studies (PIDS), Philippines

Suggested Citation: Medalla, Erlinda M.; Mantaring, Melalyn C. (2009) : On Free Trade Agreements (FTAs): the Philippine Perspective, PIDS Discussion Paper Series, No. 2009-35, Philippine Institute for Development Studies (PIDS), Makati City

This Version is available at:

<https://hdl.handle.net/10419/126793>

Standard-Nutzungsbedingungen:

Die Dokumente auf EconStor dürfen zu eigenen wissenschaftlichen Zwecken und zum Privatgebrauch gespeichert und kopiert werden.

Sie dürfen die Dokumente nicht für öffentliche oder kommerzielle Zwecke vervielfältigen, öffentlich ausstellen, öffentlich zugänglich machen, vertreiben oder anderweitig nutzen.

Sofern die Verfasser die Dokumente unter Open-Content-Lizenzen (insbesondere CC-Lizenzen) zur Verfügung gestellt haben sollten, gelten abweichend von diesen Nutzungsbedingungen die in der dort genannten Lizenz gewährten Nutzungsrechte.

Terms of use:

Documents in EconStor may be saved and copied for your personal and scholarly purposes.

You are not to copy documents for public or commercial purposes, to exhibit the documents publicly, to make them publicly available on the internet, or to distribute or otherwise use the documents in public.

If the documents have been made available under an Open Content Licence (especially Creative Commons Licences), you may exercise further usage rights as specified in the indicated licence.



Philippine Institute for Development Studies
Surian sa mga Pag-aaral Pangkaunlaran ng Pilipinas

On Free Trade Agreements (FTAs): the Philippine Perspective

Erlinda M. Medalla and Melalyn C. Mantaring

DISCUSSION PAPER SERIES NO. 2009-35

The *PIDS Discussion Paper Series* constitutes studies that are preliminary and subject to further revisions. They are being circulated in a limited number of copies only for purposes of soliciting comments and suggestions for further refinements. The studies under the *Series* are unedited and unreviewed.

The views and opinions expressed are those of the author(s) and do not necessarily reflect those of the Institute.

Not for quotation without permission from the author(s) and the Institute.



December 2009

For comments, suggestions or further inquiries please contact:

The Research Information Staff, Philippine Institute for Development Studies

5th Floor, NEDA sa Makati Building, 106 Amorsolo Street, Legaspi Village, Makati City, Philippines

Tel Nos: (63-2) 8942584 and 8935705; Fax No: (63-2) 8939589; E-mail: publications@pids.gov.ph

Or visit our website at <http://www.pids.gov.ph>

On Free Trade Agreements (FTAs): The Philippine Perspective

Abstract

The formation of free trade agreements (FTAs) has been set in motion worldwide and its conclusion does not appear imminent in the near future. In the face of such developments, the Philippines is hard pressed to formulate a more rational FTA policy framework to deal with not just external, but perhaps more importantly, domestic repercussions. Like any other country, it would have to examine closely the motivations and impact, assess capacity needs and balance short-term adjustments with long-term opportunities. It would need to look further ahead and formulate a vision about its regional and global participation. This short paper is an attempt to contribute towards this end. It starts with a brief discussion on current developments in Philippine FTA engagement. A suggested framework for FTA policy follows, with some discussion on the noodle bowl syndrome. The paper concludes with a discussion on the prospects for an East Asian FTA.

Keywords: free trade agreements (FTAs), preferential trading agreements (PTAs), regional trade agreements (RTAs), East Asian integration

On Free Trade Agreements (FTAs): The Philippine Perspective¹

Erlinda M. Medalla and Melalyn C. Mantaring[□]

Introduction

The formation of free trade agreements (FTAs) has been set in motion worldwide and its conclusion does not appear imminent in the near future. This growing phenomenon poses a special challenge not only to the multilateral trading system but also to individual economies, especially developing ones. The world is thus progressively becoming integrated, aided by rapid technological change. As a result, economies, down to industries, firms and households, are facing new sets of parameters to work with. The need for innovation, skills and know-how, and new approaches has never been more urgent. Rich and poor alike, governments have to deal with the need to balance domestic industries' interest vis-à-vis the opportunities from the increased regional and global integration.

The bright side is that new generation FTAs have evolved which include elements for cooperation and mutual development. Increasingly, these newer FTAs cover diverse agenda, encompassing not just trade facilitation and liberalization but other enhanced features of cooperation as well. And hopefully, higher quality FTAs are formed, which would eventually form building blocs rather than stumbling blocs for a global trading order.

For its part, starting in the 1980s, the Philippine strategy shifted from a protectionist to a more open trade policy, with the implementation of various stages of unilateral trade reforms. In addition, it was a party to establishment of the Asia Pacific Economic Cooperation in 1989 as well as the creation of the ASEAN Free Trade Area in 1992. However, the FTA bandwagon and increasing East Asian integration (both formal and market driven) has prompted the Philippines to consider forging FTAs. The Philippines is a late comer but it has started engaging in formal FTA negotiations, mainly *inter-regionally*, as part of ASEAN (e. g. ASEAN-China, ASEAN-Japan and ASEAN-Korea), and *bilaterally* (e. g. with Japan for an economic partnership agreement).

In the face of such developments, the Philippines is hard pressed to formulate a more rational FTA policy framework to deal with not just external, but perhaps more importantly, domestic repercussions. Like any other country, it would have to examine closely the motivations and impact, assess capacity needs and balance short-term adjustments with long-term opportunities. It would need to look further ahead and formulate a vision about its regional and global participation. This short paper is an attempt to contribute towards this end. It starts with a brief discussion on current developments in Philippine FTA engagement. A suggested framework for FTA policy follows, with some discussion on the noodle bowl syndrome. The paper concludes with a discussion on the prospects for an East Asian FTA.

¹ This paper was presented at the "Asian Noodle Bowl Conference" sponsored by Asian Development Bank Institute, held in ADBI, Tokyo, Japan, 17-18 July, 2008.

[□] Senior Research Fellow and Senior Research Assistant respectively, Philippine Institute for Development Studies

Current Situation in Philippine FTA Engagement

Starting in the 1980s, the Philippines implemented trade reforms that have substantially opened up the economy. It has also joined the pursuit of regional cooperation, as member of Asia Pacific Economic Cooperation (APEC) and the ASEAN. This nevertheless has not brought about more FTA initiatives for the Philippines, which has stayed more within the spirit of multilateralism.

However, the proliferation of regional trading arrangements worldwide and the rise of Asian bilateralism have prompted the Philippines to begin thinking about jumping into the FTA bandwagon. During the past decade, the Philippines started engaging in formal FTA negotiations, both *bilaterally* and *regionally* through the ASEAN. Indeed, as explicitly stated in the Philippine Medium Term Development Plan, the current policy is open to “*appropriate international engagements, including Free Trade Agreements (FTAs) and similar arrangements.*” As with other countries, this is motivated primarily by the need to enhance (strategic) or at least maintain (defensive) trade and investment flows. Other motivations include, among others, mutual support on issues of common interest in international fora, a means to achieve global competitiveness, portfolio diversification. It is also seen as a measure to support its engagement in cross-border industrial complementation.

Nonetheless, the Philippine government generally continues to consider these preferential FTAs as complements to the multilateral system and hence, attempts to ensure consistency with existing WTO rules. On the whole, these FTA initiatives manifest the Philippines’ commitment to greater trade liberalization in this era of globalization. Recently however, the Philippine FTA trend has suffered a small setback, with concurrence of Japan-Philippine Economic Partnership Agreement (JPEPA) ratification being stalled in the Senate. It is hoped that this is temporary, as there is no strong indication that the Philippine commitment to openness would change.

Bilateral FTA Agreement and ongoing negotiations

The Japan-Philippine Economic Partnership Agreement (JPEPA) is a historical deal for the Philippines being the first signed bilateral economic agreement. It represents what is known as a “new age” FTA. It is because JPEPA goes beyond traditional FTA’s liberalization of trade in goods and services and includes cooperation measures which formed the strong basis for ratification. JPEPA seeks to promote measures toward a freer trans-border flow of people, capital and information along with areas like investment, competition, government procurement, trade facilitation, as well as cooperation in science and technology (S&T), human resource development (HRD), small and medium enterprises (SMEs), and the environment.

After two and a half years³ of consultation and negotiation process, JPEPA was signed

³ The entire process actually took about four and a half years including the preparation period. It started in January 2002 when Japanese Prime Minister Koizumi proposed the “Initiative for Japan-ASEAN Comprehensive Economic Partnership” to which President Arroyo gave her full support. In May of the same year, PGMA proposed to setup a

on September 9, 2006 at the sidelines of the Summit of the Asia-Europe Meeting (ASEM) in Helsinki. It was expected to take effect before the end of 2007, however, under the Philippine laws, a legislative ratification is necessary to fully implement the agreement. Senate deliberations on this matter created much controversies and debates among various stakeholders regarding the content, conduct and overall impact on the Philippine economy.⁴

There are other Philippine bilateral agreements being proposed and are currently under consultation and study. These include the RP-US Free Trade Agreement, RP-EU Partnership Cooperation Agreement and Pakistan-Philippines Free Trade Agreement.

On the RP-US FTA, a PIDS research study⁵ in 2004 was commissioned by the Department of Trade and Industry (DTI) to look at the prospects for such FTA. The study supports the view that a bilateral FTA may be worth exploring as there are potential gains in establishing an economic partnership with the US. In 2006, a new approach has evolved such that DTI explored the idea of a Trade Enhancement Agreement (TEA) with the US that would practically translate to a phased negotiation of an FTA. However, the US maintained its position that the idea of a phased FTA was not acceptable as it wants a comprehensive FTA. In the meanwhile, the Philippines and the US will continue to engage in discussions to better understand their respective requirements and work towards a future FTA engagement.

A bilateral agreement called Partnership Cooperation Agreement (PCA) with the European Union is in the works to facilitate completion of the comprehensive Free Trade Agreement (FTA) between the EU and member-countries of the ASEAN. PCA covers political issues that have not been covered in any bilateral agreement entered into by the Philippines with other countries. These include human rights, migration, security and political cooperation, transparency and anticorruption measures. As such, the Philippines is facing roadblocks in committing to the proposed PCA with the European Union owing to its problems on extrajudicial killings, undocumented migrant workers in European states as well as perception of rampant corruption. (Q & A Primer: ASEAN for Philippine Business, Philexport 2007)

ASEAN and ASEAN plus Framework

Perhaps the most substantial FTA and regionalization effort by the Philippines is through the ASEAN and the “plus 1,” plus three (APT) and EAS (East Asian Summit) mechanisms.

Within the ASEAN, substantial progress has been made in terms of achieving economic cooperation agreement or economic integration. The first important milestone is the 1992

working group to study possibility of an EPA and subsequently created the Philippine Coordinating Committee under EO 213. Formal negotiations started in early 2004.

⁴ The Philippine Senate finally ratified the Japan-Philippines Economic Partnership Agreement (JPEPA) on 8 October 2008 adopting Resolution 131.

⁵ Research work covered three major areas: (i) Impact analysis on the Philippine economy, (ii) Sectoral studies covering financial services, garments, electronics, business process outsourcing, agriculture and movement of natural persons, and (iii) Special studies dealing with intellectual property rights, government procurement, competition policy, trade remedies, and political and legal issues, among others.

adoption of the Framework Agreement on Enhancing ASEAN Economic Cooperation. The Agreement launched the ASEAN Free Trade Area (AFTA)⁶ and the Common Effective Preferential Tariff (CEPT)⁷ Scheme as the main mechanism for AFTA. The more recent milestone is the adoption of the ASEAN Charter. With regards to the latter, the Philippines is still among the non-signatories, mainly as a consequence of the difficulties in the JPEPA Senate concurrence.

Nonetheless, the Philippines remains an active member of the ASEAN negotiation process and its various endeavors.

To supplement and complement the liberalization of trade, the ASEAN Framework Agreement on Services (1995) and ASEAN Investment Area (1998) were formulated and being carried out to facilitate free flow of services and investments among ASEAN member states.

In November 2004, the Ministers have signed the Framework Agreement⁸ for the Integration of Priority Sectors and its Protocols by 2010. These priority areas which include agro-based products, air travel, automotive products, e-ASEAN, electronics, fisheries, healthcare, rubber-based products, textiles and apparels, tourism, and wood-based products were proved to be cost competitive to which Member countries have a comparative advantage. These are the main instruments that will catalyze the creation of a single market and production base towards the realization of ASEAN Economic Community (AEC) by 2015.⁹

In addition to the ASEAN Free Trade Area, ASEAN as a whole is also engaged with various Dialogue Partners to implement or discuss free trade areas under the ASEAN plus framework. These efforts recognize that ASEAN cannot afford to be complacent especially as competition for global FDIs continues to intensify as countries (including ASEAN's trading partners) forge economic alliances and open-up their markets in order to attract investors.¹⁰

Agreements have been signed with China (ASEAN-China Comprehensive Economic

⁶ One of the objectives is to increase member states international competitiveness by lowering intra-regional tariffs and eventually free flow of goods.

⁷ More than 99 percent of the products in the CEPT Inclusion List (IL) of ASEAN-6, comprising Brunei Darussalam, Indonesia, Malaysia, the Philippines, Singapore and Thailand, have been brought down to the 0-5 percent tariff range. (Overview of the ASEAN Free Trade Area <http://www.aseansec.org/12021.htm>)

⁸ An amendment of the Framework was agreed and signed in December 2006 during the 12th ASEAN Summit in Cebu, Philippines. The revised agreement reflects the necessary changes to move ahead with the integration of the identified 11 Priority Sectors.

⁹ Originally scheduled by 2020 during the Bali Concord II Declaration but ASEAN leaders affirmed their strong commitment to accelerate the establishment of an ASEAN Community by 2015. The Declaration was signed by members' Head of States in December 2006 during the 12th ASEAN Summit in Cebu, Philippines.

¹⁰ Joint Media Statement of the Thirty Seventh ASEAN Economic Ministers' (AEM) Meeting Vientiane, 28 September 2005.

Cooperation Agreement (ACFTA)¹¹ and Korea (ASEAN-Korea Comprehensive Economic Cooperation Agreement (AKFTA)¹² and are currently under implementation (i.e. some provisions of the FTA become effective, e.g. tariff cuts begin). Both agreements cover trade in goods, trade in services, investment, and/or other areas of economic cooperation.

In the ASEAN-China FTA (ACFTA)¹³, the Philippines was the last of the ASEAN member states to seal an agreement for an Early Harvest Program (EHP) with China in 2005. This was primarily because the country's sensitivity was concentrated on the target scope of the EHP that covered raw, unprocessed agricultural products in chapters 1-8 of the Tariff Code. Furthermore, negotiations slowed down as a result of intensive lobbying by affected sectors, particularly sugar, pork and poultry, rice and corn, and vegetable. (Medalla and Balboa, RPS 2007-01) With pressure building up from both sides, the Philippine government was eventually able to come up with a package that sufficiently represented the strategic interest of the agriculture sector, which was, at the same time, acceptable to China. Under the China-Philippines EHP,¹⁴ the government approved the grant of zero tariffs on 214 tariff lines in compliance with the Memorandum of Understanding (MOU)¹⁵ between the two countries.

The liberalization of trade in goods for an ASEAN-Korea FTA is envisioned to be realized by 2010 for ASEAN-6 (flexibility to 2012 for the Philippines and Indonesia) and Korea and by 2016 for Vietnam and 2018 for CLM countries and Korea. For ASEAN-India, trade in goods agreement will be completed by 2011 between ASEAN-5 and India and 2016 for the Philippines and CLMV countries..

With respect to ASEAN and Japan (ASEAN-Japan Comprehensive Economic Partnership),¹⁶ Japan's strategy is to follow a dual track approach of forging bilateral partnership

¹¹ Framework Agreement was signed on November 2002; its initial phase is an early harvest program (EHP), Trade in goods agreement came into force in July 2005. The agreement on trade in services were signed in January 2007 and implemented in July 2007. Discussions on the detailed elements on the Investment Agreement are still on-going

¹² Framework Agreement and the Agreement on Trade in Goods (TIG) were signed during the ASEAN Summit in Kuala Lumpur on 13 December 2005. The TIG, originally scheduled to be implemented beginning July 2006 is delayed due to some ASEAN member countries requiring more time in the preparation of the Legal Enactment to effect the tariff reduction/ elimination. Negotiations on investment and services are on-going and expected to be concluded by end of 2007. (Status of Regional FTA Negotiations, <http://www.miti.gov.my>)

¹³ Within the ACFTA is an Early Harvest Program which will lead to elimination of tariffs on eight categories of agricultural products by 2010 (flexibility to 2012 for the Philippines)

¹⁴ mandatory product coverage of chapters 1-8: live breeding animals and other live animals, meat of sheep, goats, horses, meat of bovine animals, fish (live, chilled or frozen, dried), ornamental fish, crustaceans, mollusks, milk and cream, live plants, fruits and vegetables (including desiccated coconut, bananas, pineapples, mangoes), coconut oil (Chapter 15), and cocoa powder (Chapter 18). Products excluded from chapters 1-8 are placed either in the Normal Track or in the Sensitive Track.

¹⁵ Signed on April 27, 2005 and took effect on January 1, 2006

¹⁶ The general framework was signed in October 2003, negotiation talks started formally in April 2005, with a view to finishing up by 2009. It will be a comprehensive agreement covering trade in goods, services, investments, rules

with individual ASEAN country along side negotiating an agreement with ASEAN as a group. A number of reasons have been cited, including the most practical one of threshing out first the details and difficult areas with specific countries, which would pave the way for a smoother implementation of an ASEAN-Japan partnership¹⁷. The bilateral agreements forged by Japan with individual ASEAN countries¹⁸ are intended to be incorporated (as annexes) in the ASEAN-Japan FTA (AJEPA). While AJCEP could be considered a fallback position for the Philippines in its East Asian regional integration efforts, strategically, the delay in the Senate concurrence for JPEPA ratification places the country at a disadvantage with respect to the other ASEAN countries which have forged an EPA with Japan.

Also under negotiations are potential partnership with other dialogue partners namely: Australia-New Zealand (ASEAN-Australia and New Zealand Closer Economic Relations)¹⁹, India (ASEAN-India Regional Trade and Investment Area)²⁰, and EU (ASEAN-European Union Free Trade Agreement)²¹.

On a broader regional cooperation in Asia, East-Asia-wide initiatives are being proposed and are currently under consultation and study: 1) East Asia Free Trade Area (EAFTA)²² under

of origin, dispute settlement, sanitary and phyto-sanitary regulations, technical barriers to trade, economic cooperation and, on Japan's request, intellectual property rights.

http://www.bilaterals.org/rubrique.php3?id_rubrique=170

¹⁷ Negotiations suppose to be concluded within 2 years (from April 2005) but the progress has been slow due to differences between ASEAN and Japan on the approach and modalities for Trade in Goods. (Status of Regional FTA Negotiations, <http://www.miti.gov.my>)

¹⁸ Five bilateral agreements have been concluded and in force (i.e. with Singapore, Malaysia, Thailand, Indonesia and Brunei). The Japan-Philippine EPA has been signed but as yet to be ratified by the Philippine Senate and Japan's EPA with Vietnam is in the process.

¹⁹ It was launched on November 2004; negotiations are scheduled for completion by mid 2007 and for implementation in January 2008. Negotiations have commenced in the areas of goods, rules of origin, investment, services, cooperation activities and legal and institutional issues. (Status of Regional FTA Negotiations, <http://www.miti.gov.my>)

²⁰ The Framework Agreement was signed on October 2003, negotiations started in 2004 and provides for the establishment of an FTA in Goods (for ASEAN-5 and India by 2011; 2016 for the Philippines and CLMV) and progressive liberalization for trade in services and investments regimes. Both parties agreed to speed up negotiations for the Agreement of Trade in Goods be concluded by July 2007. The conclusion will pave the way for commencement of negotiations on services and investment. (Status of Regional FTA Negotiations, <http://www.miti.gov.my>)

²¹ On May 2007, the two regional blocs agreed to start negotiations for a bilateral agreement. The EU-ASEAN FTA is generally expected to deepen the spread of neoliberalism in Southeast Asia — more privatization and more deregulation — with the goal of improving business opportunities for European TNCs in the region. To do this, the EU will likely push strong reforms in investment, services and intellectual property. ASEAN, on the other hand, will be looking for improved market access for its exports to the EU (http://www.bilaterals.org/rubrique.php3?id_rubrique=151)

²² Feasibility study was conducted by a joint expert group chaired by the Chinese. During the ASEAN+3 Summit in Cebu, Philippines in January 2007, leaders noted to continue studying on the FTA configurations and welcomed

the ASEAN Plus Three (APT) mechanism, consisting of ASEAN+3 (Japan, China and South Korea) being proposed by China; 2) Comprehensive Economic Partnership in East Asia (CEPEA)²³, a multilateral trade agreement that would encompass ASEAN Plus 6 (ASEAN+3 plus India, Australia and New Zealand) proposed by Japan; and 3) Free Trade Area of the Asia-Pacific (FTAAP)²⁴ comprising of 21 APEC economies proposed by the United States. These possible Asian regional FTAs is Asia's undertaking to catch up with the regional integrations in North America and Europe. (How Should We Deal with 3 FTA Proposals in Asia? <http://www.jef.or.jp>)

With all these various economic integration efforts, the Philippines continues to pursue its active role within the ASEAN. Notwithstanding the fact that the United States remains the top trading partner of the country, RP's relation within the region has opened up huge potential for investments as well as cooperation in various areas.

Despite the setback from the delay in the Senate concurrence of the JPEPA, the engagement in FTAs remains a significant trade policy tool for the Philippines. It remains in dialogue with prospective partners, and the government has actually benefitted from lessons from the JPEPA experience. Concerned agencies have become more familiar with the issues and the requirements for capacity building that are needed to deal with the regionalizing world. In a sense, they are learning more negotiating skills in both domestic and foreign fronts. These continuing efforts, despite the difficulties faced, manifest the Philippines' commitment to greater trade liberalization in this era of globalization.

Formulating a Philippine FTA Policy Framework

It goes without saying that the foremost consideration for the Philippines in entering into any bilateral or regional FTAs should be its own national agenda. In a nutshell, this is ultimately guided by the following underlying principles and objectives of reforms: (1) global competitiveness, (2) sustainable growth, (3) efficiency in allocation of resources, and (4) poverty alleviation. If these objectives of reform are workable within the proposed economic partnership, then there should be no impediment to forging such agreement.

Nonetheless, from purely theoretical economic viewpoint, there is general consensus that

South Korea's proposal to conduct a Phase II study involving in-depth sector by sector discussions on details of the EAFTA.

²³ Although the CEPEA proposal had been just taken note of when it was submitted at first to the ASEAN+3 economic ministers' meeting in August 2006, the second East Asia Summit held in Cebu in January 2007 agreed to launch a Track Two study on it and asked the ASEAN Secretariat to prepare a time frame for the study. Study group meetings were already held several times under the chair of Japan and participants have been assigned to report on issues related to CEPEA.

²⁴ Formally proposed at the 14th APEC economic summit held in Hanoi in November 2006. APEC economic leaders instructed officials to undertake studies on ways and means to promote regional economic integration, including an FTAAP as a long-term prospect

multilateralism would be the ideal approach to bring about optimum welfare. There are potential risks (costs) to a preferential (bilateral) approach, specifically *trade diversion*, *resource diversion* (e. g. government resources diverted away from multilateral negotiations), and *political diversion* (could deplete political capital in doing domestic reforms)

However, handicapped with resource, capacity and capability constraints, developing countries like the Philippines are often unable to actively (and pro-actively) negotiate and bring to the table the concerns which are most vital to them. Indeed, there could be practical and possibly compelling reasons for pursuing the bilateral and regional approach. First, there is expected trade creation from the FTA. More importantly, the FTA could be used as a *testing ground*, as a *step to multilateralism* and as a *defensive mechanism*:

As a testing ground. The liberalization process is difficult. If we can do this more gradually with a particular partner first, it could serve as a testing ground and provide demonstration effects on the benefits of liberalization which the country could then adopt more easily as a policy.

As a step to multilateralism. Small countries like the Philippines often find it difficult to deal with issues in a multilateral setting, having little bargaining tools in advancing their interests. The success of bilateral cooperation would encourage regional integration and provide the building blocs for the WTO. This would unify and strengthen the region's position in the multilateral WTO.

As a defensive mechanism. Proliferation of FTAs even in our region is happening. Forging our own partnership is seen by many as a necessary defensive mechanism. An important example is that of Thailand forming JTEPA, our competitive position with Japan is threatened. JPEPA can be used as a protective shield from the necessary consequences of JTEPA and similar FTAs.

Many countries also see such economic partnership agreements as a means to pursue own domestic reforms, especially those where additional help is needed for example in terms of strengthening not just capacities, but also the political will to undertake reforms. Indeed, even in Japan, this is one important motivation viewed by many for forging economic partnerships with other countries: to help pursue its own much needed domestic reforms.

Indeed, regionalism and integration could well serve national interests and reform objectives. The Philippine economy, like most others, has become increasingly integrated with the global economy. With the growing trends in international production sharing and global production networks, major businesses have established greater linkages with the global business communities. The challenge is to negotiate an agreement that would maximize market access and investment opportunities.

However, in formulating such preferential trade agreements, a country should at least be able to have a clear objective with respect to the *elements* of the FTA, its substantive contents and institutional framework, the *criteria for choosing a partner* to the FTA and that the FTA should be more than the FTA *per se* and more of a mechanism towards achieving a stronger

purpose. At the same time, in drafting the country's areas for negotiation and FTA agenda, the country could benefit from the different models of FTAs entered into by the prospective partners. Finally, there should also be an explicit adherence to following consistency with the WTO.

Defining the Elements of FTA

Entering into a FTA provides an avenue for the country to overcome existing and emerging barriers to trade beyond what can be achieved within the multilateral framework. Hence it increases the country's competitiveness, enabling it to compete better in the global economy. (Austria 2003) Although FTAs are very much about market access and investment liberalization in general, the country should look further and consider FTA in terms of investment attraction, trade facilitation, institution- building, technology upgrading and industry competitiveness. Industry –by-industry adjustment and competitiveness strategies must be mapped out by the government with the industry leaders in order to maximize the potentials and manage the challenges of integration of economies. (Intal 2004)

Ideally, the FTA strategy should be seen as a complementary tool in the country's development and competitiveness strategies, with impact on the three (3) pillars of the FTA namely goods, services, and investments. As such, the identification of what provisions can be negotiated in these three pillars, what may be committed and unbound, the conditionalities as well as special issues that need to be addressed should be done within this overall development framework.

Determining the scope

In the context of multilateralism, FTAs serve as exception to the most-favoured nation (MFN) clause. Hence the need for substantial elimination of all trade barriers with respect to goods and substantial sectoral coverage with respect to services.²⁵ These should serve as the minimum for a preferential agreement.

With respect to goods, trade barriers have gone beyond the tariff and quota restrictions. The salient issue now is especially with respect to the use of sanitary and phytosanitary (SPS) measures whether they are indeed regulatory mechanisms or actually non-tariff barriers to trade. As a developing country, the Philippines has a difficulty in complying with the strict requirements of a developed country's SPS measures. If the standards cannot be negotiated then the country should push for the provision on cooperation and support in capability building for compliance with such measures.

²⁵ FTA conditionalities include: ***For trade in goods*** 1. Members of a FTA are not permitted to raise trade barriers (both tariff and nontariff) against non-members; 2. Members of a FTA must eliminate, rather than lower, *substantially* all trade barriers among themselves; and 3. Members must achieve free trade among members by a certain date. ***For trade in services*** 1. The FTA must have substantial sectoral coverage in terms of the number of services sectors and volumes of trade; 2. Members of a FTA must eliminate existing discriminatory measures and/or prohibit new or more discriminatory provisions in these services sectors.

Another important task for the government is the identification not only of what the country wants but specifically what are its priority and sensitive products. Prior to the start of the negotiation, there must already be a classification of what products are negotiable and non-negotiable. This is especially relevant if FTA partners are to adopt a negative listing approach. Otherwise, there will be scenario that a prospective partner or member will make reservations as to all the products covered even reaching a point that as if all these products are to be excluded or protected in that country's perspective. Emphasis is also given with respect to agriculture and services liberalization. For instance, should the FTA stick to the GATS or GATS plus in services liberalization? This is only an example of the many issues that need to be addressed at the national level. On the other hand, the agreement on the mode of liberalization is relatively easier as it could either adopt a WTO-plus approach or the AFTA-like modalities.

FTA plus provisions

Aside from these traditional FTA issues, attention should also be given with respect to the so-called enhancing features of new age FTAs. This would generally include rules on investments, competition policy, government procurement, transparency and trade facilitation measures (otherwise collectively referred to as the "Singapore issues"). Aside from the fact that they facilitate trade, these provisions would also serve as institutional safety nets for each FTA partner or member state. The objectives of the FTA would be better achieved if especially in the case of a developing country, provisions on cooperative undertakings, support and assistance in the areas of technology transfer, human resource development, environment, SMEs and infrastructure development are included.

Choosing a FTA partner

In forming a partnership, the primary question is of course with whom. In this regard, it would be useful to review some criteria in choosing a FTA partner of countries who have engaged or negotiated in various FTAs. The United States requires that a prospective partner must be a member of the WTO and should have an existing Trade and Investment Framework Agreement (TIFA) with it. On the other hand, Japan's criterion in choosing a FTA partner is generally based on (a) economic criteria, (b) geographic criteria, (c) political and diplomatic criteria, (d) feasibility criteria and (e) time-related criteria. (MOFA 2002)

In sum, the general rule is that the bigger the partner (and by induction, the more economies involved), the bigger the potential gains from an FTA. Another important and logical criterion for larger benefits is the proximity of the partner.

Taking into consideration these factors, it can be argued that the Philippines can derive most benefits in bilateral agreements with respect to its major trading partners, specifically US and Japan. In trade data alone, United States remains the most important trade partner of the Philippines, accounting for almost 28 percent of Philippine exports and 16 percent of the latter's imports during the past decade. Meanwhile, Japan is the second largest trading partner of the Philippines after the United States, accounting for 14 percent of Philippines exports and 19 percent of the latter's total imports.

Hence, to obtain benefits from a preferential trading agreement and at the same time manage the risks, the number of these bilateral agreements should be limited to those with greatest positive potential impacts. In this regard, the US, Japan, and an East Asia FTA appear to be the prime candidate for the Philippines.

Aside from these traditional FTA issues, attention should also be given with respect to the so-called enhancing features of new age FTAs. Aside from the fact that they facilitate trade, these provisions would also serve as institutional safety nets for each FTA partner or member state. The objectives of the FTA would be better achieved if especially in the case of a developing country, provisions on cooperative undertakings, support and assistance in the areas of technology transfer, human resource development, environment, SMEs and infrastructure development are included.

In drafting the Philippine FTA policy, a system of the following would prove to be useful:

- Intra and Intergovernmental coordination mechanisms for coordinated policy decision making process;
- Participation of private sector through business advocacy, consultation, observer status in negotiations; and
- Networking of negotiators, academe/experts and business/industry sector as well as civil society

The complication that could arise is the noodle bowl effect coming from the existence of multiple FTAs. This could happen if the different FTAs diverge widely from each other and the ROO regimes become unwieldy. Thus while there may not be a single ideal FTA template, the different economies, at least in the region which would eventually merge, should probably be guided by a template to ensure some consistency. Such template would not need to forge a consolidated FTA, but more workably, a nested type of FTA which would allow for (open) sub-regional grouping for those which can move ahead on certain aspects of integration.

This leads to the future direction for the Philippines within the context of the East Asian Regionalism and the case for an East Asian FTA.

The East Asian Vision

The bottomline is that the Philippines belongs to the increasingly integrating and dynamic East Asian Region. Greater trade and investment liberalization, rising international production sharing through regional/global production networks and deepening economic integration among countries are shaping relationships in the region and the rest of the world. Where is the Philippines in this dynamic international and regional arena? There really is no question. The rational direction for the Philippines is clear. It needs to become an active participant in East Asian Regionalism. It must be in sync especially with the rest of East Asia. The Philippines should be on board the building of an East Asian community and its vision of shared prosperity, peace, and stability.

As earlier noted, an East Asian FTA (EAFTA) is a logical and natural candidate for Philippine partnership. It passes all major criteria for a partner: economic importance, size, geographic proximity. Substantial complementarities that exist between Asian economies have yet to be exploited. To name a few, for example, in the ICT industry, the north East Asia has huge hardware capacity, while less developed countries like the Philippines have the software capacity and the manpower. Japanese and Korean construction and engineering industries have underutilized capacities that could be used to meet the demand of other Asian economies for services from such industries. (Lamberte 2004)

The EAFTA should be of high quality, not just it focusing on the mere liberalization of goods. The various agreements (ASEAN plus) have already provided for substantial liberalization and increasingly wider coverage. It could start with multilateralizing the salient provisions among all East Asian countries, albeit possibly with some flexibility for less developed countries. Development cooperation initiatives that would support industrial upgrading, infrastructure for trade financing, and stable economic and trade policies would help achieve the potential benefits of an EAFTA and bring it that much closer to shared vision of *East Asian community*. It would help overcome the difficulties faced by the Philippines in its effort to forge the partnership with Japan.

Finally, an EAFTA would possibly stem the FTA proliferation. This would benefit the individual countries and the region as a whole, as it should decrease the cost of doing business in the region and would on the whole serve to support its competitiveness. And with explicit adherence to WTO principles, the EAFTA that would be formed could be formulated to become a viable building bloc of wider grouping of economies.

Multilateralism should still be the ultimate goal. Preferential agreements could be entered into, *bilaterally* where benefits can be maximized or specific concerns addressed and *regionally* to serve as catalysts for development and mechanism for a more orderly global trading order. In these endeavors, consistency with WTO in the long-run should always be explicitly articulated. In practice, however, there are risks about where these preferential trade agreements could eventually lead to. Political factors could intrude. Embedded vested interests could be created by the preferential trading arrangement which could become too resistant to overhaul. The “noodle bowl” impact could prove difficult to unravel. And convergence into one single, larger (if not global) bloc may become impeded. To be sure, there will always be failures and successes, but one has to be optimistic that the world should be able to right itself, to achieve long-run growth and integration despite numerous hurdles along the way.

References

- Austria, Myrna (2003). The Philippines in the global trading environment: looking back and the challenges ahead. PIDS Perspective Paper Series No. 3. Makati City: Philippine Institute for Development Studies.
- _____ (2004). The Pattern of Intra-ASEAN Trade in the Priority Goods Sectors. REPSF Project No. 03/006e ASEAN-Australia Development Cooperation Program.
- Hatakeyama, Noboro (2008). How Should We Deal with 3 FTA Proposals in Asia? <http://www.jef.or.jp>
- Hufbauer, Gary Clyde and Yee Wong (2005). Prospects for Regional Free Trade in Asia. IIE Working Paper Series 05-12. October.
- Intal, Ponciano (2004). Towards a framework for an RP-US Free Trade Agreement. Angelo King Institute Quarterly 2 No. 2.
- Kwon Yul (2004) Toward a Comprehensive Partnership: ASEAN-Korea Economic Cooperation *EAST ASIAN REVIEW* · Vol. 16, No. 4, Winter
- Lamberte, Mario (2004). An Overview of Economic Cooperation and Integration in Asia. ADB.
- Medalla, Erlinda and Jenny Balboa (2007). The Impact of ASEAN-China FTA Early Harvest Program: the Case of the Philippines with Focus on Short-run Effects on the Agriculture Sector. Research Paper Series 2007-01. PIDS
- Medalla, Erlinda and Dorothea Lazaro (2003). The Outlook for a Philippine-Japan Economic Partnership. DRN 2003 Vol. XXI No. 6. PIDS.
- _____ (2004). Exploring the Philippine FTA Policy Options. Policy Note 2004-09. PIDS, Makati City.
- _____ (2005). What's Happening in the Philippine Free Trade Agreements Policy Note 2005-05. PIDS, Makati City.
- Ministry of Foreign Affairs (2002). Japan's FTA Strategy (Summary).
- Philippine Exporters Confederation, Inc. (2008). RP Free Trade Areas: Status and Implications. <http://www.philexport.ph/policy/fta.pdf>
- Philippine Exporters Confederation, Inc. (2007). Q & A Primer: ASEAN for Philippine Business. http://www.philexport.ph/jpepa/ASEAN_Business_final.pdf
- Status of Regional FTA negotiations (2007). <http://www.miti.gov.my/>

WTO (2005) Philippines Trade Policy Review. WT/TPR/G/149. June.