United States Senate Committee on Finance
Subcommittee on International Trade, Customs, and Global Competitiveness

Hearings on the
Strategic Benefits of a Multilateral Approach to Trade Policy in the Asia-Pacific Region

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Chairman Carper, Ranking Member Cornyn, distinguished Members of the Subcommittee. Thank you for this opportunity to testify, and thank you especially for addressing a critical challenge—the need for a multilateral approach to trade policy in the Asia-Pacific region.

As a researcher specializing in international trade, I have studied this region's development and relationships with the United States for nearly fifty years. Over the last decade, in collaboration with Professor Michael Plummer of Johns Hopkins University and other colleagues, I also undertook extensive studies of actual and proposed trade agreements in the Asia Pacific, and their variants with additional members. These multilateral agreements are summarized in Table 1; I will report some results from our research below.[2]

As you know, the United States has long supported East Asia's political stability and access to world markets, at times at great cost. The region translated this support—through remarkable national success stories—into unprecedented prosperity and poverty reduction. The United States stayed on the job, promoting further progress through regional agreements and institutions as recently as five years ago. In the words of former Secretary of State James Baker, we refused to draw "a line down the middle of the Pacific."[3]

So it's disappointing to see US economic ties with the Asia-Pacific weaken in recent years. While the United States has retained, and indeed intensified, its focus on Indo-Pacific security, it withdrew political

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[2] Most results reported in this testimony will appear shortly in Cyn-Young Park, Peter A. Petri, and Michael Plummer, "The Economic Effects of the Regional Comprehensive Economic Partnership and Recent Trade Policy Developments in Asia and the Pacific," Asian Development Bank Working Paper (forthcoming). Our earlier publications on Asia-Pacific trade agreements are listed and linked on: http://asiapacifictrade.org/
[3] James A. Baker III, *The Politics of Diplomacy.* New York: Putnam and Sons, 1995.

support for deeper economic integration across the Pacific and in East Asia itself, and reduced its participation in Asia's multilateral institutions. Its disengagement is striking relative to increased efforts by other countries, not least China.

The new decade offers a chance to review our engagement in the Asia Pacific. In the past, the United States played an important role in the region's multilateral mechanisms. It should do so again. America's efforts to enhance the competitiveness of our economy will hopefully build confidence and resources for launching new trade initiatives. The US economy is complementary to Asian economies, and the United States is respected in Asia for its historical role and economic prospects. It is uniquely positioned to benefit from the dynamism and prosperity of the Asia-Pacific, the fastest growing world region in the last half century.

Table 1. Multilateral trade agreements in the Asia-Pacific (actual and proposed)

Acronym	TPP	CPTPP	RCEP	RCEP16
Formal name	Trans-Pacific Partnership	Comprehensive and Progressive Agreement for Trans-Pacific Partnership	Regional Comprehensive Economic Partnership	As RCEP
Members	Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, Vietnam	As TPP, except without United States	Australia, Brunei, Cambodia, China, Indonesia, Japan, Lao, Malaysia, Myanmar, New Zealand, Philippines, Singapore, South Korea, Thailand, Vietnam	As RCEP, except with India
Year in force	Abandoned	2018	Expected 2022	Unknown
Description	High-quality, comprehensive agreement with innovative provisions on digital economy and intellectual property	Uses TPP text but suspends 22 provisions including some on investment dispute resolution and intellectual property	Unusually diverse membership, lower-quality agreement, favorable rules of origin, no labor or environment chapters	As RCEP

Source: author.

Fraying trans-Pacific ties

To help assess multilateral cooperation across the Pacific, consider five factors that currently shape these connections. Each of these trends has recently contributed to the erosion of trans-Pacific ties and limits what the United States might achieve in future Asia-Pacific agreements. But the list should not be read pessimistically. Appropriate US policies can change some factors and find better ways to accommodate those beyond our control.

- *China's growing economic influence in East Asia.* In the decade ending in 2019, Chinese trade with East Asian partners excluding China expanded by 7.0 percent annually, compared to 5.6 percent for the United States.[4] China is now the largest trading partner of all 11 major East Asian countries,[5] and the United States is among the top two partners of only 3 countries (Japan, Korea, and Vietnam). These economic interests explain why East Asian countries prefer regional arrangements that are potentially open to China, but also incentivize it to conform to clear international standards.

- *Concerns about trade policy in the United States*. The TPP, which the United States abandoned in 2017, met many objectives for healthy Asia-Pacific relationships: it was a large, high-quality, innovative, multilateral arrangement. The US withdrawal was a flawed decision, but in fact the politics of the TPP had turned very divisive by the time the agreement was signed. Opposition emerged across various political lines, fueled by the frustrations of American workers whose wages were not rising sufficiently fast, and who could not find alternatives to disappearing manufacturing jobs. Trade barriers emerged as plausible (though ultimately ineffective) remedies for unacceptable trends. In fact, our research suggests that agreements like the TPP can benefit workers by expanding markets for productive firms, causing wages to rise faster than profits, and thus also create additional jobs.[6] New trade initiatives will require political support, and current US policy innovations should give workers skills and confidence to pursue opportunities through trade.

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[4] Trade is measured as imports plus exports. Comparisons for the decade ending in 2020 are available but are distorted by the effects of Covid-19. Data are from the World Bank's WITS data base, extracted June 20, 2021.

[5] These are Australia, Cambodia, Indonesia, Japan, South Korea, Malaysia, New Zealand, Philippines, Singapore, Thailand, and Vietnam.

[6] A close review of the TPP's labor market effects suggests positive implications, including increases in the returns to labor compared to capital (Peter Petri and Michael Plummer, "Economics of the Trans-Pacific Partnership: Distributional Impact," *VoxEU*, 30 April 2016. https://voxeu.org/article/economics-tpp-winners-and-losers). Also, we recently added endogeneous labor supply mechanisms to our model, which project job gains from agreements like the TPP that increase real wages (Park, Petri and Plummer, forthcoming, op. cit.).

- *Declining US role in East Asia's cooperative mechanisms.* The key inter-governmental mechanisms operating in East Asia include the Association of Southeast Asian Nations (ASEAN), the 18-member East Asian Summit, which includes ASEAN, the United States and other partners, and the 21-member Asia Pacific Economic Cooperation forum (APEC). Each conducts annual leaders' summits, arranged to minimize related travel, and offers opportunities for high-level dialogue. Although US presidents played important roles in these institutions in the past, during his term President Trump participated in only one of four ASEAN meetings, none of four East Asian Summits, and two of three APEC meetings. These are tables where the United States should be present.

- *Growing East Asian confidence in leading economic integration.* Filling the vacuum left by America's absence, East Asia reoriented its economic integration efforts toward regional and other partners, including Europe and even Russia. The 11 signatories of the TPP remaining after the exit of the United States, led by Japan, concluded a replacement agreement within one year after losing their dominant partner. That breakthrough served to accelerate the negotiations on RCEP, which were concluded in 2020. RCEP is a large agreement with an unusually diverse membership, spanning countries that differ widely in population and development. The United States should welcome and support these trends in collaboration with Asian partners.

- *Deepening intra-Asian, rather than trans-Pacific, economic ties.* Over time, intra-Asian business ties and agreements are becoming more important than trans-Pacific relationships. When the TPP was in negotiation, we estimated that its global benefits would be 72 percent larger than those offered by RCEP (then expected to include India), because the TPP provided a more modern and rigorous template.[7] In contrast, we now estimate that RCEP (without India) would be 40 percent more valuable than the CPTPP, which has become smaller and less productive without the United States. Moreover, the CPTPP is now also likely to add other East Asian economies.

Compared to the final years of the TPP negotiations, the East Asian economy has greater regional focus. The United States remains an important partner, but trends argue for recognizing East Asia's maturing economy. The return of the United States to meaningful regional agreements would be welcomed, for

[7] Peter A. Petri, Michael G. Plummer, Shujiro Urata and Fan Zhai, "Going it Alone in the Asia-Pacific: Regional Trade Agreements Without the United States," Peterson Institute for International Economics, Working Paper 17-10, October 2017.

the large opportunities provided by US markets and technology, and for diversifying regional risks. Many countries, moreover, also want sustained US engagement as a foundation for a rules-based regional system and political stability.

Consequences of East Asia "going it alone"

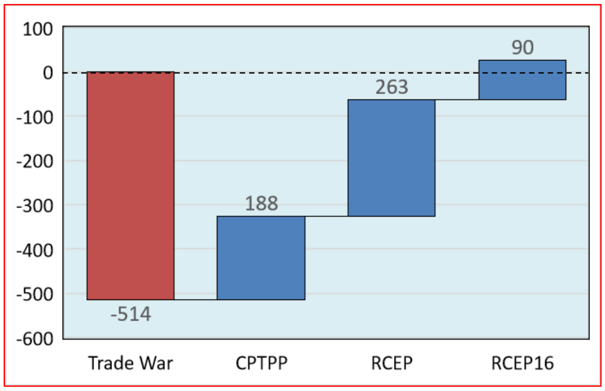
In recent research, colleagues and I have applied quantitative models to examine the consequences of these trends, including the shift from trans-Pacific to East Asia-centered trade agreements. We use a state-of-the-art computable general equilibrium (CGE) model, similar to those used by other researchers including the US International Trade Commission. The model is not designed to make forecasts—rather, it answers "what if" questions about the effects of new policies such as trade agreements. It produces aggregate results, say, on changes in national real incomes, as well as detailed results, say, on bilateral trade flows of motor vehicles. We analyze these changes for the world economy divided into 19 sectors in 29 regions, over the 2015-2030 period.

We recently applied the model to examine four key trade policy developments: the US-China trade war, the implementation of the CPTPP agreement, and the ramp-up of the new RCEP agreement (without Indian membership), and a potential RCEP16 agreement that would also include India. We represented these policy changes with announced details when available, say on tariffs, and with judgments about the effects of unquantified measures, say import, export, and investment restrictions applied to US-China trade.

The results suggest large changes in real incomes as illustrated in Figures 1 and 2 below. These figures track the incremental effects of the policy scenarios. Each starts at zero on the left (the dotted line near the top) and then successively adds bars to show the effects of the trade war and the trade agreements.

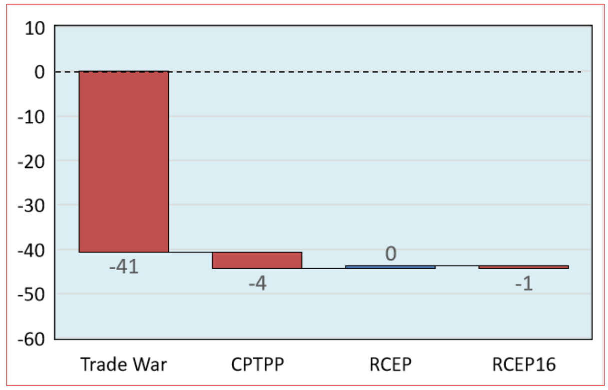
Figure 1 shows global real income effects. The trade war has a large negative effect, reducing world incomes by $514 billion dollars (all values mentioned are annual estimates for 2030, representing also similar effects in later years). The trade agreements all have positive effects, each increasing global incomes from the levels reached under previous scenarios. Thus, the CPTPP will increase world incomes annually by $188 billion, RCEP by a further $263 billion, and RCEP16—RCEP with the addition of India—by a final $90 billion. Together, the three agreements are projected to add $541 billion to world incomes, enough to end up above zero, that is, to offset the costs of the US-China trade war. However, these costs are not fully offset in all countries, including especially in China and the United States.

Figure 1. Effects on global real income, 2030 ($b)



Source: author's simulations.

Figure 2. Effects on US real income, 2030 ($b)



Source: author's simulation.

Figure 2 shows the effects of the same scenarios for real income in the United States. These follow a different pattern: the trade war and the new regional trade agreements all have negative or insignificant income effects (negative bars are shown in red). To be sure, US losses are not large—for example, they represent less than 10 percent of the global losses associated with the trade war, with China bearing a far larger share—but the four scenarios together reduce US incomes by $45 billion annually. These losses reflect trade lost due to the new trade barriers introduced by the trade war as well as new preferences that America's competitors receive (but US producers don't) under the CPTPP and RCEP.

Moreover, the direct losses from the CPTPP agreement shown in Figure 2 do not include what the United States would leave on the table by *not benefiting from joining* the CPTPP. If the United States did join, it would get preferential market access within the agreement—for example, US exports would be subject to lower tariffs. In a 2016 study we estimated these gains at $131 billion annually.[8] We have not re-estimated them since, but changes in our model suggest that updated results would be perhaps 25 percent larger. In other words, benefits foregone by not joining the CPTPP would be several times as large as direct US losses estimated above.

More granular analysis shows that, all else equal, each of the four policy scenarios—the trade war and the new East Asian agreements—will reduce America's Asia-Pacific economic ties. This is because the trade war has raised barriers to US-China trade, and because the new agreements will offer advantages to imports from partners that are members, over imports from the United States. In addition, the new

[8] Peter A. Petri and Michael G. Plummer, "The Economic Effects of the Trans-Pacific Partnership: New Estimates." *Assessing the Trans-Pacific Partnership, Volume 1: Market Access and Sectoral Issues*. Ed. Kimberly Ann Elliott et al. Washington, D.C.: Peterson Institute for International Economics, 2016. 6-30.

agreements, especially RCEP, will create incentives for regional supply chains, enhancing East Asia's competitiveness in manufacturing. RCEP is the first trade agreement among China, Japan, and South Korea, reducing barriers among their firms and with producers in other RCEP countries. RCEP's rules-of-origin provisions will be especially useful for incentivizing such regionwide collaborations.

It would be tempting to see East Asia's trade agreements as beggar-thy-neighbor initiatives, or as concessions to a powerful China. But their evident goal is economic integration; they will create far greater gains for members than losses for outsiders like the United States. As a member of RCEP, China is likely become its biggest beneficiary, given its outsized economic role. But perhaps because this was expected, China did not appear to dominate the negotiations, according to key ASEAN officials.[9] The negotiations demanded exceptional patience; they were repeatedly stuck on the sensitivities of one or more smaller countries.

Building on America's strengths

For better or worse, East Asia is now following policies more focused on the region's own integration than on trans-Pacific relations. One reason is that its trans-Pacific options have narrowed. Reversing, or at least slowing, this trend will require US actions: increasing the priority of America's economic ties with East Asian partners, and participating more fully in regional mechanisms of cooperation, such as ASEAN, APEC and the East Asia Summit.

From an economic perspective, the United States can best address these challenges by joining the CPTPP agreement, or an appropriate successor agreement. This would raise US incomes and send the clear message that America's commitments to the region are aligned across our economic and security interests. This will enhance the credibility of both pillars of the relationship.

Moreover, the value of the CPTPP is bound to expand through the "domino effect"—as new members join, benefits increase for current members as well as further entrants. The United Kingdom is already negotiating membership, while China, Colombia, Indonesia, the Philippines, South Korea, Taiwan, and

[9] ASEAN Secretary General Lim Jock Hoi and others close to the negotiations have widely argued this point. See for example Lim's description of the signing of RCEP as "a historic event as it underpins Asean's role in leading a multilateral trade agreement of this magnitude, despite global and regional challenges and eight years of negotiations" (*The National*, "The RCEP trade deal proves Asia need not be led by the US or China," November 17, 2020).

Thailand have all expressed interest in joining. Nothing would accelerate the domino effect more than US entry. An expanding CPTPP would amplify strategic benefits for the United States.

Still, in my view, America's withdrawal from the TPP will not be quickly reversed. US political divisions on trade remain acute. In the short term, the US government is unlikely to prioritize relations with East Asia above other challenges at home and abroad. Nevertheless, promising signs are on the horizon: the US economy is recovering rapidly from the Covid-19 crisis and Congress is engaging with difficult economic issues. With the American Rescue Plan and a Senate version of the United States Innovation and Competition Act behind it, Congress is poised to tackle legislation on infrastructure and human capital. Each of these bills establishes clear links between America's prosperity and security and its international competitiveness. If successful, they will enhance US leverage and give workers and businesses the tools to embrace international challenges.

As the United States gains confidence in its economic recovery, opportunities in the Asia-Pacific will again come into sharper focus. In the meantime, much needs to be done to build support, abroad and at home, for future agreements. Abroad, the United States could initiate agendas on shared policy challenges in APEC, ASEAN, and the East Asia Summit, to explore zones for potential collaboration. It could scale up contributions to East Asia's people, through investments in public goods and initiatives centered on America's remarkable assets in education, science, and culture. At home, it could encourage diverse communities—in business, technology, health care and other sectors—to reinvigorate partnerships across the Pacific, and to develop joint strategies for renewed trans-Pacific engagement. Clear definitions of America's long-term interests, based on wide political foundations, will be essential for renewing Asia-Pacific ties.