Mega Trading Blocs and New Regional Trade Architectures: Implications for Small States and LDCs

Amitendu Palit*

**Background**

Several large regional trade agreements (RTAs) are being negotiated in world trade. These are distinct by their size, varied membership and new approach to trade governance. The Trans-Pacific Partnership (TPP), Regional Comprehensive Economic Partnership (RCEP), the Trans-Atlantic Trade and Investment Partnership (TTIP), and the Pacific Alliance are some examples of these emerging mega trading blocs. All are negotiating tariffs, standards, goods, services and dispute settlement as composite packages, emphasising on removing ‘behind the border’ barriers affecting market access and transparency in member country rules on trade. Apart from the USA, and the European Union (EU), large emerging markets like China and India are also negotiating the RTAs. Till now, these largely exclude least developed countries (LDCs) and small states. The latter also appear unprepared for tackling various implications of the RTAs ranging from potential loss of market access from trade preference erosion and growth of new standards to trade governance.

This issue of Commonwealth Trade Hot Topics highlights the likely implications of the new RTAs for LDCs and small states in the specific context of the TPP and the RCEP. It identifies specific market access issues and discusses the key elements of future strategic negotiations of LDCs and small states along with the policy imperatives. The paper also discusses the political economy of world trade in the context of the RTAs and the possibility of LDCs and small states integrating deeper into world trade.

**TPP and RCEP**

The TPP currently includes 12 countries: Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the USA, and Vietnam. Australia, Brunei, Japan, Malaysia, New Zealand, Singapore and Vietnam are also negotiating the RCEP, along with Cambodia, Lao PDR, Myanmar, Indonesia, Philippines, Thailand, and China, India and South Korea. Both groups have sizeable shares in global GDP and trade (see Table 1). The TPP, which is till now a collective of the APEC (Asia-Pacific Economic Cooperation) member economies, is at an advanced stage of negotiations. The RCEP has begun as a collective of the countries with which the ASEAN (Association of Southeast Asian Nations) has bilateral trade agreements and is at a relatively early stage.

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Both agreements are seeking market access commitments well above the World Trade Organization (WTO). The TPP’s coverage ranges from tariffs, SPS (sanitary and phytosanitary), TBT (technical barriers to trade), cross-border trade in services and dispute settlement to IP (intellectual property), government procurement, labour and environment standards, competition policy and treatment of SOEs (state-owned enterprises). The RCEP is also negotiating many of these issues. Both are expected to institutionalise new levels of market access commitments and trade governance in their domains.

**Trade linkages of LDCs and small states with TPP and RCEP**

Several LDCs and small states have strong trade linkages with the TPP and RCEP as identified from presence of members of the two agreements among the top five export destinations and/or import sources of the LDCs and small states. Poor and small economies with shares of 10 per cent (or more) of merchandise trades with the TPP and RCEP blocs are shown in Table 2: the implications of the two upcoming RTAs are expected to be particularly significant for these economies.

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<th>Table 1: TPP and RCEP: Shares (%) in World GDP, Population and Trade</th>
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<td><strong>TPP</strong></td>
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<tr>
<td>World GDP (nominal)</td>
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<td>World GDP (PPP)</td>
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<tr>
<td>World population</td>
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<tr>
<td>World merchandise trade</td>
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<td>World commercial services trade</td>
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</table>

Source: Computed from World Bank and WTO publications

More LDCs have greater links with the RCEP and more small states with the TPP (Table 2). Eight LDCs have 10 per cent (or more) of their trades with the TPP in contrast to 18 small states with similar shares. The RCEP absorbs 10 per cent (or more) trade of 26 LDCs, compared with six small states. Asian LDCs like Bangladesh and Cambodia have strong trade links with both blocs, as do small states like Fiji and Maldives. Trade dependences of poor and small economies on key TPP and RCEP members (USA and Canada; China and India) and large Asia-Pacific economies common to both (Australia, Japan, New Zealand and Singapore) influence their trade linkages with the two RTAs. The linkages are also influenced by non-reciprocal preferential accesses extended by the mentioned TPP and RCEP members (and South Korea). Furthermore, geographical factors impact trade links of several SSA (Sub-Saharan Africa) and Asian LDCs with China, India, and the RCEP, as they do for trade links of several small states from the Caribbean and Central America with the USA, and the TPP.

**Market access implications of TPP and RCEP for LDCs and small states**

*Preference erosion*

Potential tariff preference erosion from the TPP and the RCEP are significant since several members of the two RTAs (Australia, Canada, China, India, Japan, New Zealand, South Korea and the USA) grant non-reciprocal preferences to LDCs and small states. Many of the latter are already identified as vulnerable to preference erosion from multilateral tariff reductions (Milner et al, 2010).¹ Many of these have strong trade links with the TPP and RCEP and can suffer greater erosion with several tariff lines becoming MFN (most favoured nation) duty-free

<table>
<thead>
<tr>
<th>LDC</th>
<th>Bangladesh, Cambodia, Lesotho, Myanmar, Samoa, Solomon Islands, Sudan, Vanuatu</th>
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<tr>
<td>RCEP</td>
<td>Afghanistan, Bangladesh, Benin, Bhutan, Burundi, Cambodia, Central African Republic, Eritrea, Guinea-Bissau, Madagascar, Malawi, Mauritania, Myanmar, Nepal, Niger, Rwanda, Samoa, Senegal, Solomon Islands, Sudan, Tanzania, Togo, Uganda, Vanuatu, Yemen, Zambia</td>
</tr>
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<tr>
<th>SVE</th>
<th>Antigua and Barbuda, Barbados, Bolivia, Dominica, Dominican Republic, El Salvador, Fiji, Grenada, Guatemala, Honduras, Jamaica, Maldives, Nicaragua, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, Tonga, Trinidad and Tobago</th>
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<tr>
<td>RCEP</td>
<td>Fiji, Maldives, Mauritius, Mongolia, Paraguay, Tonga</td>
</tr>
</tbody>
</table>

Source: Computed by author from WTO (2013)
under the two RTAs. Eliminating tariffs on around 5,000 items on which the LDCs and the AGOA (African Growth and Opportunity Act) and CBERA (Caribbean Basin Economic Recovery Act) beneficiaries enjoy preferential access in the US market would imply significant preference erosion for the latter. The AGOA beneficiaries would be worried over preference erosion for apparel exports, as would the sugar-exporting small states (e.g. Fiji, St Kitts and Nevis). Market access can cramp further for the Asian apparel-exporting LDCs like Bangladesh, Cambodia and Nepal. Generic concerns on preference erosion from the RCEP are for the preferential tariff lines in the Australian, Japanese and South Korean markets as well as the Chinese and Indian markets. Erosion possibilities from the latter are strong for Afghanistan, Bhutan, Guinea-Bissau, Mauritania, Mongolia, Nepal, Solomon Islands, Sudan and Yemen.

Rules of origin

Restrictive rules of origin (ROOs) have often blocked access for LDC and SVE (small vulnerable economy) exports in markets that extend them non-reciprocal tariff preferences. The possibility can increase if ROOs in the TPP and RCEP confine preferential tariff benefits only to products manufactured or assembled entirely within their geographical domains. LDC and SVE exports would suffer if TPP and RCEP members cannot avail preferential benefits on externally sourced inputs. ROOs imposing such restrictions would also prevent LDCs and small states from entering the TPP and RCEP’s value chains, particularly in fragmented production networks like apparels, footwear and processed food. Liberal ROOs in the TPP can facilitate entry of Asian LDCs like Bangladesh and Nepal in the TPP’s value chains. The RCEP is likely to find it difficult to fix common ROOs as the ASEAN FTAs (free trade agreements) vary widely in this regard. Whether it ends up affecting export prospects of LDCs and small states depends on its eventual conditions on minimum threshold levels of regional value addition and product transformation in its ROOs.

SPS and TBTs

The TPP, RCEP, TTIP and other mega-RTAs are expected to institutionalise rigorous quality standards through SPS and TBTs. These can adversely affect exports from poor and small economies. Several TPP and RCEP members have been proactively initiating SPSs and TBTs in recent years (Figure 1). The USA has initiated the maximum, followed by China, Canada, South Korea, Japan and Mexico. The US and Canadian SPSs, as well as those by Japan, Australia and South Korea aim to restrict presence of harmful chemicals in imports affecting major exports from many LDCs and small states. China also has several SPSs specifying technical

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1 The vulnerable economies include Angola, Bangladesh, Cambodia, Democratic Republic of Congo, Dominica, Dominican Republic, Fiji, The Gambia, Guinea-Bissau, Honduras, Jamaica, Lesotho, Madagascar, Malawi, Maldives, Mauritania, Mauritius, Mozambique, Myanmar, Niger, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, Senegal, Solomon Islands, Tanzania, Togo, Uganda and Zambia.

2 Measures pertain to HS Codes 01-24 covering live animals and animal products, vegetable products, animal or vegetable fats and oils and prepared foodstuffs, beverages, tobacco.
requirements and testing methods for use of food additives and standards for food packaging and quality requirements in plant and animal food products. China’s TBTs, as well as those of the USA, Canada and South Korea specify technical standards for several resource, metal and manufactured imports.

Many recent SPSs by the TPP and RCEP members have specifically affected LDC and SVE exports. These include Chile’s quality measures on import of grains and seeds and rambutan fruits from Paraguay and Guatemala, South Korea’s prohibition measures on import of fresh pineapples from many LDCs and small states (e.g. Angola, Benin, Central African Republic, Democratic Republic of Congo, Ethiopia, Madagascar, Malawi, Mauritius, Mozambique, Niger, Senegal, Sudan, Togo, Uganda), New Zealand’s SPS measures on import of cabbage leaves from Fiji, Samoa, Tonga and Vanuatu, Peru’s measures on import of bell pepper seeds and groundnut from Guatemala and Nicaragua, and the USA’s quarantine orders on rice shipments from Afghanistan, Bangladesh, Burkina Faso, Mali, Mauritania, Myanmar, Niger, Senegal and Sudan. Stiffer quality and safety standards in the TPP, RCEP and TTIP might result in greater incidence of both generic and specific NTBs (non-tariff barriers).

**Services**

LDCs and small states are liberalising market access in domestic services at varying paces. The calibrated commitments are taking place in line with the existing GATS (General Agreement on Trade in Services) disciplines. The TPP aims to secure substantive GATS plus commitments. This would involve major regulatory reforms in large and core services like finance, telecommunications and distribution. By scaling up market access commitments well above the GATS, the gaps between liberalisation trajectories of the TPP and RCEP members would expand significantly from those of the LDCs and small states.

Both the TPP and the RCEP are expected to facilitate temporary movement of service suppliers within their geographical spaces through inter-agency cooperation between members on key issues like mutual acceptance of technical qualifications. This might confine short-term labour flows within the geographies of the RTAs and affecting labour movements to the RTA members from excluded LDCs and small states. Migration of semi-skilled workers from Bhutan and Nepal, for example, to India and Thailand might suffer, as might migration from the Caribbean countries to the NAFTA (North American Free Trade Agreement) countries. The long-term effect could be on inflows of inward remittances from migrant workers essential for economic sustenance of several LDCs.

**Intellectual property**

The IP rules of the TPP and TTIP would be more advanced than those in the TRIPS (Trade-Related Aspects of Intellectual Property Rights) in protecting proprietary knowledge and sanctifying enforcement. The RCEP will also aim for TRIPS plus commitments. The IP rule-making in these RTAs will be influenced by members that are large players in global commercial services trade with comparative advantages in export of IP-intensive services. Measures entailing stronger IP protection like longer patent lives and data exclusivity, lower patentability standards, and empowering patent holders to act against introduction of similar products on suspected infringements have far-reaching implications. These include the impact on introduction and production of generic drugs and their supplies to several LDCs, particularly in the SSA. Longer protection of copyrighted material can affect prospects of parallel trade in such material impacting availability of cheap textbooks and educational resources in poor economies.Stronger provisions on electronic reproduction of copyrighted material and rules on use and governance of the internet can also affect access to knowledge for users in LDCs (Palit, 2013). And finally, the increasing distance between IP rules of the new RTAs and the TRIPS has implications for LDCs and small states developing national IP frameworks on the basis of the TRIPS.

**Government procurement, competition policy, labour and environment**

The TPP is negotiating several ‘new generation’ WTO plus and WTO extra trade issues like government procurement, labour and environment. The WTO has been discussing market access in government procurement in its plurilateral GPA (Government Procurement Agreement). Though the GPA has S&D (special and differential) provisions for LDCs, given that government procurement in many developing countries serves specific goals like helping local industries, few developing countries have annexed to the GPA. Nonetheless, market access talks on public procurement are progressing gradually at the WTO and rapidly in the mega-RTAs. Procurement would also figure in the EPAs (Economic Partnership Agreements) negotiated by LDCs with the EU. The
lack of negotiating experience of the LDCs might be a significant obstacle in this respect. The same limitation would handicap their negotiations in competition policy, labour and environment. As these issues get embedded in the new RTAs, LDCs and small states must accept the imminent possibility of their figuring in future multilateral trade talks and bilateral negotiations with mega-RTA members.

An immediate short-term implication of upcoming labour and environment standards in the new RTAs is the rise of fresh NTBs. The TBTs standardised for protecting environment in host countries might proliferate and exports from LDCs and small states can face greater surveillance. Labour-intensive LDC exports can also come under similar scrutiny. Failure to ratify major international conventions on labour and environment by LDCs and small states is likely to intensify such surveillance.

**Strategic negotiations and policy imperatives**

The new RTAs are aiming ‘deep’ integration by minimising ‘behind the border’ obstacles to movement of goods and services by harmonising standards and rules for maximising efficiency gains from regional value chains (WTO, 2013). LDCs and small states are new to this game dominated by Organisation for Economic Co-operation and Development (OECD) countries and large emerging market economies with aggressive interests in global and regional value chains. But it is essential for the LDCs and small states to integrate closely with the new RTAs and their value chains for maximising export-driven growth given their small domestic markets. This requires dedicated efforts for negotiating with the RTA members.

Tariff preference erosion from the new RTAs is irreversible. The RTAs are likely to liberalise tariffs faster than the WTO since they work on reciprocal preferences and also because it is easier to fix common tariff schedules among smaller number of members. Additional erosion might arise from specific S&D treatment for RTA members. Both the TPP and RCEP are likely to have ‘negative lists’ of exports with zero or phased tariff eliminations for accommodating domestic sensitivities of members. These new tariff barriers (or continuation of old non-preferential tariffs), if applicable to major exports from LDCs and small states to the RTA members, might accentuate loss of market space. LDCs need to negotiate this with RTA members for preventing preferential balance from becoming more skewed.

The core negotiating thrust of LDCs and small states should shift from tariffs and preference erosion to non-tariff issues, particularly ROOs, SPSs, TBTs and access for service suppliers. The 2013 Bali Ministerial Conference’s decision on preferential ROOs for LDCs can be the benchmark in future negotiations. The emphasis on lower threshold for domestic value addition and change in tariff classification and granting of cumulation benefits can be stressed in future negotiations with the TPP and RCEP members. Complying with quality standards will require building domestic capacities. This can strategically feature in future negotiations by linking the commitment to maintaining such standards in exports in bilateral agreements with the RTA members (including interim EPAs with the EU) to funding commitments from the latter for building capacities. The funding can materialise as Aft (Aid for Trade) for addressing specific trade-related constraints (Calì et al, 2011). The Bali Ministerial’s endorsement of preferential access for LDC service suppliers can be utilised in negotiations by identifying possible mode 3 interests, particularly by relatively high- and middle-income small economies from the Caribbean and the Pacific, in members of the new RTAs looking to enlarge their own capacities.

The specific long-term policy objectives of LDCs and small states in the context of the implications of the new RTAs should be as follows:

1. **Build competitiveness by strengthening trade-related infrastructure influencing movement of goods at borders.**
2. **Work towards efficient implementation of the trade facilitation package adopted by the Bali Ministerial.**
3. **Lower domestic tariffs for obtaining cheap primary and intermediate inputs for further processing and re-export and consequent integration in RTA-based value chains.**
4. **Focus on conforming to international quality standards by building capacities secured through Aft.**
5. **Indicate awareness and recognition of new generation trade issues by examining possibilities of ratifying global IP, labour and environment treaties.**

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New RTAs and the political economy of world trade

The ability of LDCs and small states to preserve trade linkages with the new RTAs and integrate in their value chains will be conditioned by the political economy of world trade. The USA, EU and several OECD economies are focusing heavily on these RTAs due to their cynicism about the ability of the WTO to deliver more trade reforms. Some large emerging market and developing economies are also investing in these due to their disappointment over slow progress on the DDA (Doha Development Agenda). The OECD countries consider the new RTAs ideal frameworks for institutionalising preferred trade issues and regulations and pushing them well beyond the WTO’s mandate. Emerging market economies, while not ‘giving up’ on the WTO, are seized of the importance of staying rooted to the value chains of large RTAs.

LDCs and small states hardly feature in the mega-RTAs and the reconfigured balance of power in world trade. The balance has shifted from the Quad towards emerging market economies. But it has not impacted the entire ‘South’. Some of the larger South economies with greater stakes in world trade and strategic influence have participated more actively in multilateral and regional trade negotiations for reciprocal exchange of preferences. Most poor and small countries have hardly done so. As countries receiving non-reciprocal trade preferences, they have been avoided by the new RTAs largely on the assumption that they would be either unwilling or incapable of meeting the exacting standards of these agreements.

Notwithstanding limited influence, LDCs and small states should negotiate with RTA members with an open approach to reciprocal references. They should convey the political willingness to engage in reciprocity-based negotiations in areas where they perceive long-term benefits, particularly for diversifying export-oriented production and entering value chains. While the WTO’s consensus-based mechanism is accommodating for LDCs and small states, they must try creating negotiating spaces in extra-WTO RTA negotiations. This can be done by discussing standards and regulations – core thrusts in the new RTAs – and efforts for improving their quality, transparency and enforceability in LDCs and small states. Very often, negative perceptions about the latter’s ability to implement transparent rules and standards arise from doubts over the willingness of their political establishments to overcome rent-seeking objectives of deeply entrenched domestic cartels and interest groups. Some decisive domestic measures in this regard can serve as effective examples.

Outlook

The Bali Ministerial has reinforced the scope of non-reciprocal preferential treatment for LDCs. But it has not done much for increasing the interest of major global traders in multilateralism. They would continue to prioritise the mega-RTAs. They might also visualise the WTO as a forum for defending the narrow needs of LDCs rather than global trade as a whole. This hardly makes LDCs and small states ‘like minded’ partners for the 21st century agreements like the TPP.

Preserving existing space and securing new room in the world trade order are essential for LDCs and small states for avoiding further marginalisation. They must aim to benefit from the growth of new RTAs. Key to achieving the benefits are policies for integrating deeper into the value chains of the RTAs. This would require building domestic capacities and participating in negotiations with larger economies on a reciprocal basis. After all, S&D treatment and non-reciprocal preferences can only be interim, not permanent measures.

References


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- 24-25 April 2014: Regional meeting on WTO & Post-Bali Trade Agenda for Africa held in Nairobi, Kenya
- 10-11 December 2013: Regional Workshop on South-South Trade and Regional Value Chains in Sub-Saharan Africa held in Nairobi, Kenya
- 4 December 2013: WTO 9th Ministerial event: Discussion Session on the Future of Aid for Trade held in Bali, Indonesia
- 3 December 2013: WTO 9th Ministerial event: Reflections on Global Trade: From Doha to Bali and Beyond held in Bali, Indonesia
- 25-27 October 2013: International Conference on Upcoming Ninth WTO Ministerial in Bali: Securing the LDCs Deliverables held in Dhaka, Bangladesh
- 25-26 September 2013: ACP Brainstorming Meeting on the 9th WTO Ministerial Conference and the Post-Bali Framework held in Geneva, Switzerland
- 2-4 September 2013: 6th South Asia Economic Summit (VI SAES) held in Colombo, Sri Lanka
- 25-26 June 2013: Commonwealth Workshop on Multilateral Trade Issues: Development perspectives for Small Vulnerable Economies (SVEs) and Least Developed Countries (LDCs) held in Geneva, Switzerland
- 2-3 May 2013: International Conference on Regional Trade and Economic Cooperation in South Asia: Trends, Challenges and Prospects held in Delhi, India
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