



MEGA FTAS PART 2 OF 2

TPP, the (Secret) Deal of the Century?

HIGHLIGHTS

- This is the second of a two-part series that covers the two leading pathways to the Free Trade Area in the Asia-Pacific (FTAAP).
- The Trans-Pacific Partnership (TPP), currently in its final stages of negotiation, is composed of 12 economies: Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States, and Vietnam. This group has a combined GDP of \$28 trillion, or 40% of world GDP, around \$9 trillion in trade of goods, and \$2 trillion in trade of services.
- The TPP is designed to be a high-ambition, comprehensive free trade agreement that delivers deep liberalization of goods, services, and investment barriers, while also addressing new issues of interest to business in the 21st century, such as intellectual property, environmental protection, regulatory coherence, and electronic commerce.
- This Report also looks into the controversial issues in TPP negotiations particularly on the chapters of investments, agriculture, intellectual property rights, rules of origin, and environment.
- Should the Philippines not join TPP, the country is estimated to incur an opportunity loss of \$500 billion in GDP in 2025.

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The Trans-Pacific Partnership (TPP) agreement, currently in the final stage of extremely secretive negotiations, introduces the start of a highly liberal trade regime. Its comprehensive coverage of issues aims to deliver deep liberalization of goods, services, and investments, while injecting provisions that seek to address 21st century business concerns (see Table 1).

The TPP began as a smaller four-economy bloc called the Trans-Pacific Strategic Economic Partnership or P4, composed of Brunei, Chile, New Zealand, and Singapore. Its goal is to eliminate all tariffs between the parties by 2015. This bloc expanded in 2008 when the United States, Australia, Peru, and Vietnam joined the negotiations, followed by Malaysia in 2010, and Canada and Mexico in 2011, constituting the TPP-11 membership. In March 2013, Japan announced its interest to join the TPP talks and has recently acceded as the 12th member of the TPP negotiating group.

Like the Regional Comprehensive Economic Partnership (RCEP), the TPP also offers a pathway to the envisioned Free Trade Area in the Asia-Pacific (FTAAP) with potential gains of \$1.9 trillion. The 12 TPP economies, including Japan's official accession, have a combined GDP of about \$28 trillion, or 40% of world GDP, around \$9 trillion in trade of goods, and \$2 trillion in trade of services. These make the TPP a formidable trading bloc that can unleash the massive growth potential of lesser-developed member economies, such as Vietnam and Peru, as well as cement the economic leadership of advanced countries, like the US and Japan (see Table 2). TPP negotiations began in 2008 and are scheduled to conclude in October 2013, in time for the APEC Leaders Week in Bali, Indonesia.

This Research Report is the second of a two-part series on the two biggest pathways leading to the FTAAP. Unlike RCEP, which is still in the inception stage, the TPP is close to conclusion, but negotiations have been held with much

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secrecy. As such, majority of the analyses in this report are based on the provisions of existing US FTAs, leaked drafts of TPP chapters, official statements from lawmakers, negotiators and shareholders, and studies that focus on TPP.

Table 1: Comprehensive TPP Coverage

Goods	Competition Policy	Telecommunications
Rules of Origin	Labor	Electronic Commerce
Customs	Environment	Investment
Sanitary and Phytosanitary Standards	Legal and Institutional Issues	Intellectual Property
Technical Barriers to Trade	Cross Border Services	Horizontal Issues: regional economic integration, SME issues, transparency and supply chain issues
Trade Remedies	Business Mobility	
Government Procurement	Financial Services	

Source: USTR website

TRADE IN GOODS

In its 2012 report entitled “Breaking Down 20th Century Barriers,” the Peterson Institute for International Economics (PIIE) notes that much of the TPP negotiations are based on existing high-level FTAs (such as the US-Korea FTA), and, as such, its starting points are closely based on US FTA templates. Because of this, the “sticky points” in the TPP talks also revolve around US-protected sectors which, being mostly agricultural products, are also major sectors protected by other TPP players. In fact, Japan’s ruling Liberal Democratic Party named rice, wheat, beef, pork, and dairy products as sensitive agricultural products that must be excluded from tariff eliminations in the TPP.

Looking at particular agricultural products, liberalization of trade barriers protecting dairy appears to be a difficult goal in the TPP, especially when big players, namely the US and Canada, have regulated their domestic pricing systems which hardly reflect true international market trends. Other dairy importers, such as Mexico and Japan, also impose high tariffs on imported dairy products, whereas top milk exporters, New Zealand and Australia, seek broader liberalization and reduction, if not elimination, of border restrictions to dairy trade. If dairy-producing TPP economies agree to simultaneously liberalize their markets and lower subsidies and protection for domestic producers, they will greatly benefit from expanded market access, not only in Mexico and Japan, but also in Latin American and Asian markets where demand for dairy products is also growing. If there is no agreement, then the sub-chapter on dairy can be excluded in the TPP negotiations, as seen in previous US FTAs.

Sugar is another agricultural product protected by the US and enjoys exemption from existing US FTAs. In the negotiating table, Australia is keen on seeing concrete liberalization commitments from TPP players in order to create opportunities for sugar trading. For the US to agree to

remove the exemption, major reforms such as expanding tariff rate quotas for TPP partners may be required. TPP negotiators should, however, consider the potential expansion in ASEAN markets and the competition posed by ASEAN players. Vietnam, for example, applies a 40% tariff on sugar from non-ASEAN countries, but applies only 5% to its ASEAN neighbors.

With regard to rice, Malaysia and Japan will likely push to retain existing tariffs, while producers of low-cost rice, such as Australia, the US, and Vietnam, are likely to lobby for open rice markets with TPP partners. A study conducted by Alvaro Durant-Morat and Eric Wailes of the University of Arkansas entitled “The Trans-Pacific Partnership and Its Potential Impact on the Rice Market: Implications for Japan and the Partners” may provide insights on the different perspectives of the TPP members regarding rice tariffs. In the study, Japan’s rice imports are estimated to increase by 70% as a result of TPP, benefitting Vietnam’s long grain rice and the US’ medium grain rice, while negatively affecting China and Thailand. With the entry of cheap rice imports from TPP liberalization, Japan’s rice production is projected to eventually shrink by almost 94%, while the US’ medium grain rice production could expand by more than three times its 2009 production levels. Meanwhile, Vietnam’s long grain rice production is seen to expand by 5.2% in this scenario. The study also projects Malaysia’s rice production to dramatically decrease from 672,000 hectares to 276,000 hectares with TPP’s possible rice trade liberalization.

At present, the US applies a fixed tariff ranging from \$18 to \$21 per metric ton, while Australia, Brunei, New Zealand, Peru, and Singapore have open rice markets. The rest of the TPP members either apply steep tariffs or maintain tight controls on rice imports.

Discussions on trade in agricultural commodities are related to the issue of state-owned enterprises (SOE) in the TPP. The

US and Canada are proposing stiff “competitive neutrality” among enterprises to mitigate the market advantages coming from the subsidies and other trade-distorting practices that SOEs and some domestic players enjoy. The possibilities include liquidating large SOEs to “level the playing field” when markets open or retaining SOEs on condition that market shares will be capped and subsidies will be removed. Either way, TPP negotiators will have to define SOEs, identify subsidies and support measures that SOEs can enjoy, and determine how such companies behave in light of competition to avoid firms from escaping classification due to technical ambiguity (e.g., regulatory exemptions for “national security”).

Despite being the primary proponent of the SOE chapter, the United States has several large SOEs and industries that currently benefit from state subsidies and anti-trust exemptions. Other economies, such as Japan, Singapore, and Vietnam, also have a considerable number of large SOEs and government-owned and operated corporations (GOOC). Clearly, strict provisions on SOEs and GOOCs will have a considerable impact on local and global industries.

RULES OF ORIGIN

There are two possible scenarios on how the TPP will treat the rules on origin (ROO). The TPP-11 parties have existing FTAs with each other (e.g., Peru has FTAs with Canada, Chile, Mexico, and Singapore) and can opt to preserve current unique ROO agreements and carve out TPP provisions from these. Similarly, the original P4 members can also adopt ROO rules they have previously endorsed.

The other possibility is to develop a common ROO and tariff schedule for all parties in the TPP. This move, albeit politically challenging, will simplify ease of trading and will expand market access and opportunities for business.

Some of the most controversial sectors in the ROO discussion include textiles, apparel, and footwear—areas where advanced and developing countries alike impose trade restrictions to protect their own domestic manufacturers. The United States, for instance, imposes very strict “yarn forward” requirements in US FTAs, such as those with Mexico and Peru. However, while this rule sits well with current

Table 2: Trade Indicators of TPP member economies, 2012 (in \$ billions)

ECONOMY	GDP	GOODS		SERVICES	
		EXPORTS	IMPORTS	EXPORTS	IMPORTS
Australia	1,542	257	261	53	65
Brunei	17	*14	*3	n/a	n/a
Canada	1,819	455	475	76	105
Chile	268	79	79	13	14
Japan	5,964	799	886	140	174
Malaysia	304	227	197	38	42
Mexico	1,177	371	197	16	25
New Zealand	170	37	38	10	11
Peru	199	46	43	5	7
Singapore	277	409	380	*133	*117
United States	15,685	1,547	2,335	614	406
Viet Nam	138	115	11	*10	*12
WORLD	71,708	18,323	18,567	4,347	4,106
ASEAN (10)	2,306	1,254	1,221	274	277
RCEP (ASEAN+6)	21,189	5,264	5,235	924	1,038
TPP (11+Japan)	27,560	4,342	4,902	1,108	978

Source: WTO Trade statistics, www.wto.org

* WTO Estimates

FTA partners of the US, another TPP member, Vietnam, the second largest exporter of apparel to the US next to China, will most likely push for the “cut and sew” rule that will allow TPP members to import textiles from a third party (non-TPP member) and still receive duty-free treatment for their exports. At present, Vietnam sources its textiles from China and South Korea who are partners in RCEP, but not in the TPP. Critics of the strict “yarn forward” rule argue that such provisions will disrupt existing supply chain systems that already work efficiently for TPP members.

Meanwhile, outside the TPP negotiating room, the Philippines is lobbying for the US Congress to pass the Save Our Industries Act which will allow US-made yarns and fabrics to enter Philippine markets duty-free and, in return, garments from and wholly assembled in the Philippines will gain du-

YARN FORWARD: Yarn used to form the fabric (which may later be used to produce wearing apparel or other textile articles) must originate from an FTA-member country, in this case, a TPP member.

CUT AND SEW: Yarn used to form fabrics may come from non FTA-member countries—in this case, a TPP member—with the product still eligible for duty-free treatment.

ty-free access to US markets provided that the fabrics used are from the US. A similar trade arrangement can be expected in the TPP should negotiators strive for completely open market access.

INVESTMENTS

Perhaps the most controversial chapter in the TPP is the investments chapter, of which a draft was leaked in June 2012. The draft provision contains core investor rights such as the provision of host countries of “fair and equitable treatment” and “full protection and security” to foreign investments and investors. It also prohibits member governments to impose performance requirements that nationalize a covered investment. The prohibited performance requirements include obliging investors’ products to have a certain level of domestic content, to restrict senior management and Board of Directors positions to local nationals, or to transfer technology to the territory or knowledge to a local person, among others.

The most contentious element in the draft texts, however, involves investor-state dispute settlement. The leaked proposal allows foreign investors to bring claims against the government of the host country to an international panel of arbitrators, instead of bringing complaints to the host country’s domestic justice system. In an open letter sent by lawyers to the negotiators of TPP dated 8 May 2012, they

contend that this would “threaten to undermine the justice systems in various countries and fundamentally shift the balance of power between investors, states and other affected parties in a manner that undermines fair resolution of legal disputes.” Australia has also openly rejected the inclusion of this proposed provision in the investments chapter, as it did in its US-Australia FTA.

On the other hand, in a February 2012 statement, business associations in the United States expressed their support in maintaining these provisions in the TPP, noting the weakness of some countries’ legal systems which hinder the progress of cases in domestic courts.

RULEMAKING ON NEXT GENERATION ISSUES

The so-called 21st century, next generation issues are also hitting a roadblock in the TPP talks as some member countries demand stricter and longer protection of patents, copyrights, and intellectual property rights (IPR), while most prefer to adopt the WTO Agreement on Trade Related Aspects of Intellectual Property Rights (TRIPS) framework. The US leads the group that is pushing for stronger provisions similar to the IPR elements in the US-South Korea Trade Agreement (KORUS). The provisions also contain anti-circumvention measures that prohibit tampering of technologies to prevent piracy, impose tougher criminal penalties against copyright piracy and trademark counterfeiting, and empower customs officials to conduct IPR enforcement actions even with the absence of a formal complaint.

A specific contentious area in the TPP regarding intellectual property is patent protection for pharmaceuticals. The controversial “access to medicines” proposal by the US, tabled in September 2011, met strong opposition from other negotiators. The proposal is said to give drug companies extended protection through data exclusivity, patent term extensions, and patent linkage as they apply a product for marketing approval in a TPP country. This would grant an extension of 10 years in addition to the current 20-year patents of existing drugs being modified or renewed for new uses.

Médecins Sans Frontières (Doctors Without Borders), a medical and humanitarian aid organization, claims that such regulations will grant big pharmaceutical companies “a wide-ranging set of legal mechanisms designed to prolong monopoly protection for medicines and delay availability of more affordable generic versions.” A letter issued by over 130 members of the US House of Representatives in 2012 also raised the same concerns on the affordability of medicines in developing countries under the US-proposed provision. Given the secrecy of the ongoing negotiations, it is unclear whether this highly-contested proposal has been revised to address the concerns and fears of its potential impact on the affordability of medicine.

Chapters focusing on the environment are also expected to be heavily discussed in TPP negotiations, judging by

the increasing importance given to this area in free trade agreements in the past decade. In the P4 Agreement between the original four TPP members, general provisions on environmental protection and conservation have already been agreed upon. It recognizes the GATT Articles' exemption provisions which allow the adoption of policies not consistent with the agreement, but are necessary to protect "human, animal or plant life or health," or are related "to the conservation of living and non-living exhaustible natural resources."

Besides these, given that US FTAs are used as models in crafting the TPP, the following environmental provisions in US FTAs may be expected to form part of the TPP's environmental chapters:

- Prohibition on countries from lowering their environmental standards to attract investment
- Access to the same dispute settlement procedures, as used in other obligations in the FTA
- Prohibiting the use of the FTA to undermine obligations of specified multilateral environmental agreements
- Committing to not engage in illegal logging and trade, trade in endangered species, and harmful fishery subsidies.

Aside from commitments to protect and conserve the environment, the TPP is expected to reduce or eliminate tariffs on a specified list of environmental goods and services (EGS). A stronger text will include binding provisions, particularly in logging, wildlife, and fisheries, as currently proposed by the US. Furthermore, cooperation in addressing environmental issues, such as air pollution and waste management, and fostering education to the public will entail dedicated funding and resources from TPP members.

RCEP VS. TPP

Observers following the developments in RCEP and TPP have raised concerns that, instead of being complimentary moves towards a Free Trade Area of Asia-Pacific (FTAAP), the two partnerships appear to be designed to outdo each other by competing for members and agenda. The root of these concerns lie in the presence and influence of the two economic powers behind the developing FTAs: China being part of RCEP, and the US leading the TPP.

RCEP's importance to China is worth considering, bearing in mind that, in the past years, the country failed to secure bilateral trade agreements with Australia, Japan, and India. With RCEP, China would finally gain wider access to these big markets in a single effort. China would also deepen existing commitments in the ASEAN-China Free Trade Agreement, as well as gain access to the Korean and New Zealander markets. Lastly, RCEP can be viewed as a means for China to further solidify its economic position in the world, given its robust growth in the past decades and the difficulties faced by advanced economies in recent years.

The TPP, meanwhile, is the single, biggest trade strategy of the Obama Administration, which may explain why the US is aggressively pushing for a wider membership in TPP and deeper commitments from TPP members. Through this Partnership, the US will simultaneously sign a free trade pact with five new economies—Brunei, Japan, New Zealand, Malaysia, and Vietnam—and broaden commitments from existing trade agreements with Australia, Chile, Singapore, and with Canada and Mexico under the North American Free Trade Agreement (NAFTA). More importantly, this will provide an opportunity for the US to establish new rules on emerging issues at the top of its agenda, such as the movement of electronic information across borders, state-owned enterprises, and regulatory coherence.

Table 3 provides a snapshot of broad demonstrable benefits of TPP, RCEP, and a bigger FTAAP to participating economies, prepared by the Peterson Institute for International Economics. Their analysis shows that there are significant income gains for countries that commit to one or both of these tracks, while an income loss is deemed probable to countries that shy away from these liberalization movements.

In TPP-11 (all TPP members excluding Japan), the US stands to benefit the most with a projected boost of \$23.9 billion in additional income in 2025, as opposed to a non-TPP scenario. This income gain will significantly increase to \$108.2 billion with the addition of Japan to TPP and if Indonesia, Korea, the Philippines, and Thailand decide to join the Partnership as well. Meanwhile, non-TPP economies like China stand to lose \$20.8 billion with TPP-11, and \$82.4 billion with TPP-16.

Interestingly, RCEP's promised gain to Asia (\$627 billion) is much more substantial than gains from TPP-11 (\$26.5 billion) or even TPP-16 (\$299.8 billion). A possible explanation to the potentially large impact may be due to the fact that trade barriers are initially higher between RCEP-members and that RCEP will be the first FTA between its biggest players. With RCEP, China stands to gain the most with an expected income boost of \$249.7 billion.

For the Philippines, the cost of not joining the TPP could result to an opportunity loss of \$500 million in GDP in 2025. This is a low estimation considering that Japan's participation was not incorporated in this TPP-11 scenario. However, if the Philippines, together with Japan, South Korea, Thailand, and Indonesia, join the TPP, the Philippines could post an additional income gain of \$22.1 billion. Similarly, if RCEP is pursued and signed, the Philippines will be expected to reap an additional \$7.6 billion in this ASEAN-led trade agreement.

Going beyond RCEP and TPP, what should be highlighted in the analysis are the notable gains from a wider FTAAP. In this scenario, both the US and China will reap larger benefits if they enter into an agreement as the FTAAP at \$266.5 billion and \$678.1 billion, respectively. According to Petri,

Table 3: Income Gains under Alternative Scenarios

	GDP (\$ BILLION)		INCOME GAIN IN 2025 (\$ 2007 BILLION)			
	2025		TPP-11	TPP-16	RCEP	FTAAP
AMERICAS	24,867		48.8	160.8	2.5	373.3
Canada	1,978		7.0	12.4	-0.1	26.2
Chile	292		2.0	3.5	0.0	6.5
Mexico	2,004		13.1	31.2	2.8	67.7
Peru	320		2.8	5.4	0.0	6.3
United States	20,273		23.9	108.2	-0.1	266.5
ASIA	34,901		26.5	299.8	627.0	1354.3
Brunei	20		0.1	0.4	1.2	1.1
China	17,249		-20.2	-82.4	249.7	678.1
Hong Kong	406		-0.3	-1.3	46.8	84.9
India	5,233		-1.2	-6.9	91.3	-29.5
Indonesia	1,549		-1.1	62.2	17.7	38.0
Japan	5,338		-1.2	128.8	95.8	228.1
Korea	2,117		-0.4	50.2	82.0	129.3
Malaysia	431		20.8	30.1	14.2	38.4
Philippines	322		-0.5	22.1	7.6	15.9
Singapore	415		5.1	12.3	2.4	13.6
Taiwan	840		0.2	-6.4	-16.1	53.0
Thailand	558		-0.7	42.5	15.5	27.4
Vietnam	340		26.2	48.7	17.3	72.9
Other ASEAN	83		-0.3	0.5	1.6	3.1
OCEANIA	1,634		5.7	14.6	21.7	32.1
Australia	1,433		2.8	9.8	19.8	26.4
New Zealand	201		2.9	4.7	1.9	5.8
REST OF THE WORLD	41,820		-6.6	-24.2	-6.8	162.0
WORLD	103,223		74.5	450.9	644.4	1,921.7

Source: Petri, Plummer, Zhai (2012)

Note: TPP-16 includes TPP-11 + Japan, Korea, Indonesia, the Philippines, and Thailand

these gains will be propelled by trade creations rather than trade diversion from non-FTAAP economies. In fact, the world economy is projected to post an additional \$1.9 trillion growth under a comprehensive FTA in the Asia-Pacific region.

FTAS & THE PHILIPPINES: IMPETUS FOR CHANGE

A successful Philippine participation in an FTA should ideally result to an increase in trade activity, foreign investment, technology transfer, knowledge sharing, and massive job creation. The opportunity to compete in existing and new markets should also drive Filipino workers and professionals to acquire higher levels of knowledge and skills for higher productivity. At the same time, it is expected to

accelerate the government's momentum in improving critical infrastructure, and in instilling a culture of integrity and good governance in institutions, both of which are vital in creating a business-friendly environment.

This freer movement in international markets should also strengthen Philippine production and supply chains, since entering into high-level liberalization commitments will provide additional market access for Philippine goods and services and give firms the ability to source international supplies under low or zero tariff rates.

However, a preliminary and necessary question to ask is whether the Philippines can deliver on such high-level liber-

alization commitments. Also worth investigation is whether local businesses and workers can compete if the Philippines will participate in an aggressive trade pact such as the TPP.

At present, the country is one of the region's fastest-growing economies with a strong external profile, moderate inflation, and stable foreign exchange reserves. This year, the Philippines gained investment grade (BBB-) ratings from Fitch Ratings and Standard & Poors—an indication that the Philippines is a safe haven for huge capital investments. These positive macroeconomic signs may show that the Philippines is ready for global players, however, high-standard FTAs would also require local players to be ready for the world.

High-level liberalization on trade, services, and investments entail heavy groundwork for both the private sector and government. For instance, local industries must be competitive enough to take advantage of new opportunities or even to survive when competition enters. This entails that businesses, especially micro and small enterprises, must be operating at optimum efficiency, embrace innovation as part of its growth strategy, and apply good business practices.

Laws and regulations that ensure a level-playing field for both domestic and foreign businesses must also be in place to discourage disputes that will hamper the flow of trade and investments. Equally important is the existence of a national support system and safety nets for businesses and workers that will be negatively affected by the entry of new competition. Since this global market shift will put certain players at a disadvantage, the identification of vulnerable industries will be a significant first step in establishing the right support and safety measures.

Furthermore, the country should be ready to deliver on the requirements that seek to address “next generation issues” which, most likely, will appear in the TPP Agreement. With regard to the Philippines’ enforcement of domestic and international IPR laws, the country remains on the priority watch list in this year’s US Special 301 Report. According to the paper, “internet-based piracy, cable signal piracy, [and] difficulties in prosecuting IPR cases in the judicial system” continues. Among other matters, should the Philippines wish to join TPP, a more aggressive implementation of IPR laws is necessary.

CONSTITUTIONAL BARRIERS

The current administration’s stand against any amendments to the Constitution poses a challenge for the Philippines’ accession into TPP. Some of the TPP provisions are tied to constitutional restrictions, particularly on foreign equity participation, skilled and professional work by foreigners, and land ownership. Filipino economist Gerardo Sicat believes that the restrictive economic provisions in the Constitution reflect a “narrow economic nationalism” of which the end result is the country’s sluggish growth in output and pro-

ductivity in the past decades. He argues that Filipino capital is not in great abundance to take over large public utilities and, as such, with the 60-40 ownership provision, the economy is suffering from undercapitalization of public utilities, resulting in the high cost of utility services. This, coupled with substandard quality of service, translates into high production costs as experienced by industries in the country.

Certain economic laws embedded in the Constitution are also cited as factors that discourage the entry of foreign investments into the country. In 2012, FDI that flowed into the Philippines breached the \$2 billion mark—the first time

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since 2006 when the economy attracted \$3 billion worth of FDI. While this milestone may be the beginning of a promising trend, the Philippines still has much to improve on in order to capture a large and significant chunk of FDI entering Asia.

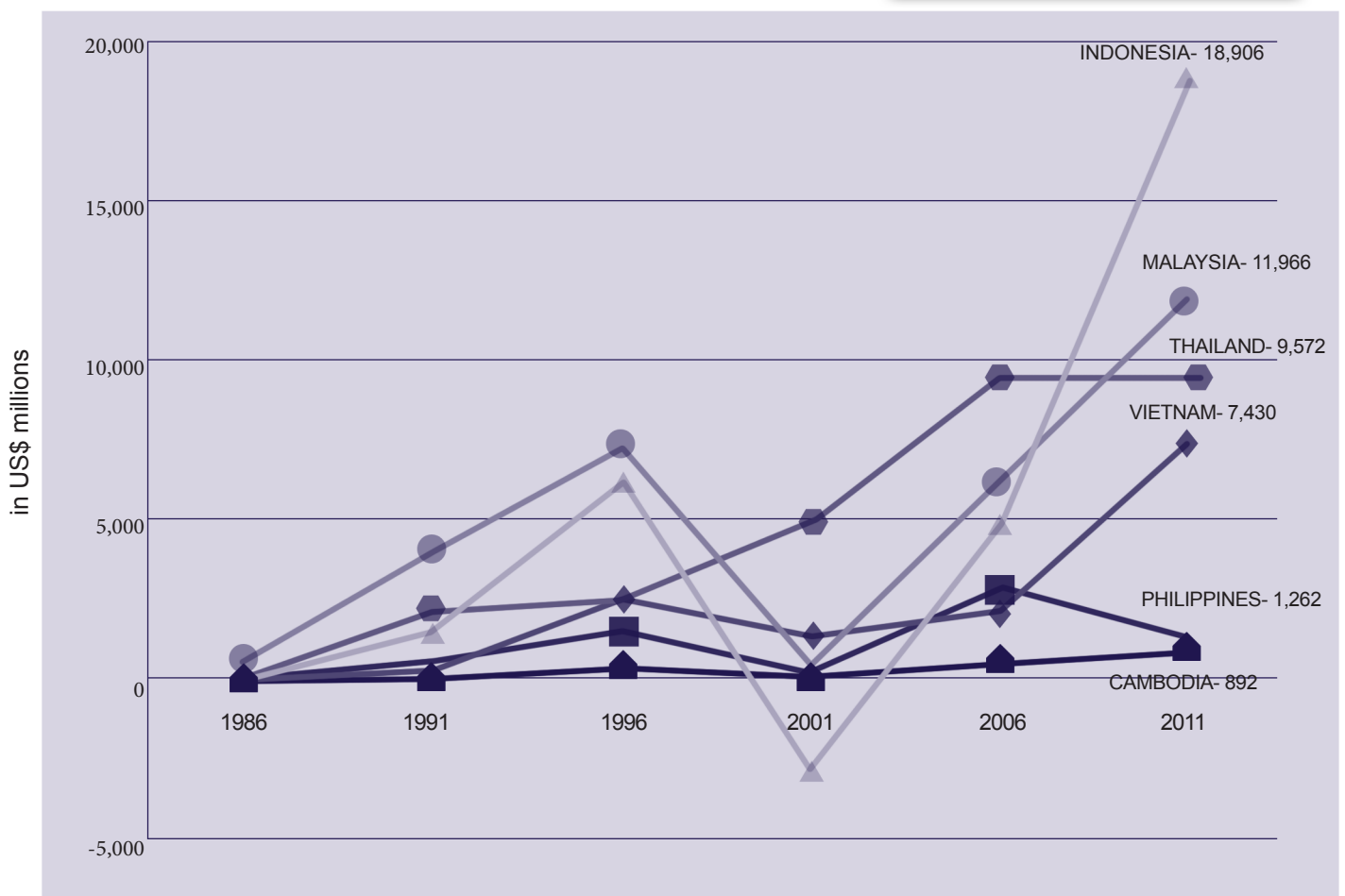
Looking at five-year intervals, net FDI inflows to Southeast Asia, particularly Vietnam, Indonesia, and Thailand, grew substantially and consistently, while the Philippines’ net FDI growth remained low and erratic. The widening of this gap is significant when we trace the FDI flows of select ASEAN countries beginning in 1986 when almost all Southeast Asian economies, except Singapore, were attracting about the same level of FDI.

While it is valid that there are many other factors which affect foreign direct investments—in particular, availability of labor and skills, immobile factor endowments (natural resources and land), government policy, political stability and bureaucracy, incentives, good governance, and peace and stability, among others—several studies by local and international think tanks converge on common issues.

An example is the 2011 comprehensive paper entitled “The Evolving Role of Southeast Asia in Global FDI Flows” prepared by Stephen Thomsen of the IFRI Center for Asian Studies. The study points out the perception of high lev-

- INDONESIA
- MALAYSIA
- THAILAND
- VIETNAM
- PHILIPPINES
- CAMBODIA

Chart 1: Net FDI inflows to selected ASEAN Countries



Source: World Bank website

Table 4: Restrictions to Foreign Investment in Philippine Laws

RA 7042: Foreign Investments Act of 1991 (as amended by RA 8179)

SME Capitalization for Foreign Nationals: Section 8

“Small and medium-sized domestic market enterprises, with paid-in equity capital less than the equivalent two hundred thousand US dollars (US\$200,000) are reserved to Philippine nationals, Provided that if: (1) they involve advanced technology as determined by the Department of Science and Technology or (2) they employ at least fifty (50) direct employees, then a minimum paid-in capital of one hundred thousand US dollars (US\$100,000.00) shall be allowed to non-Philippine nationals.”

Foreign ownership limitations in an SEC registered enterprise: Section 3

“Provided, That where a corporation and its non-Filipino stockholders own stocks in a Securities and Exchange Commission (SEC) registered enterprise, at least sixty percent (60%) of the capital stock outstanding and entitled to vote of each of both corporations must be owned and held by citizens of the Philippines and at least sixty percent (60%) of the members of the Board of Directors of each of both corporations must be citizens of the Philippines, in order that the corporation shall be considered a Philippine national.”

Foreign ownership limitations in business: Section 3

“Foreign Investments Negative List’ or ‘Negative List’ shall mean a list of areas of economic activity whose foreign ownership is limited to a maximum of forty percent (40%) of the equity capital of the enterprises engaged therein.”

1987 Constitution, Article XII: National Economy and Patrimony

Ownership of Lands: Section 2

“All lands of the public domain, waters, minerals, coal, petroleum, and other mineral oils, all forces of potential energy, fisheries, forests or timber, wild life, flora and fauna, and other natural resources are owned by the State. With the exception of agricultural lands, all other natural resources shall not be alienated. The exploration, development, and utilization of natural resources shall be under the full control and supervision of the State. The State may directly undertake such activities, or it may enter into co-production, joint venture, or production-sharing agreements with Filipino citizens, or corporations or associations at least sixty per centum of whose capital is owned by such citizens”

60/40 Limitation of Foreign Ownership: Section 10

“The Congress shall, upon recommendation of the economic and planning agency, when the national interest dictates, reserve to citizens of the Philippines or to corporations or associations at least sixty per centum of whose capital is owned by such citizens, or such higher percentage as Congress may prescribe, certain areas of investments.”

“The State shall regulate and exercise authority over foreign investments within its national jurisdiction and in accordance with its national goals and priorities.”

Operation of Public Utilities: Section 11

“No franchise, certificate, or any other form of authorization for the operation of a public utility shall be granted except to citizens of the Philippines or to corporations or associations organized under the laws of the Philippines, at least sixty per centum of whose capital is owned by such citizens; nor shall such franchise, certificate, or authorization be exclusive in character or for a longer period than fifty years. Neither shall any such franchise or right be granted except under the condition that it shall be subject to amendment, alteration, or repeal by the Congress when the common good so requires. The State shall encourage equity participation in public utilities by the general public. The participation of foreign investors in the governing body of any public utility enterprise shall be limited to their proportionate share in its capital, and all the executive and managing officers of such corporation or association must be citizens of the Philippines.”

Practice of Professions: Section 14

“The sustained development of a reservoir of national talents consisting of Filipino scientists, entrepreneurs, professionals, managers, high-level technical manpower and skilled workers and craftsmen in all fields shall be promoted by the State. The State shall encourage appropriate technology and regulate its transfer for the national benefit.

The practice of all professions in the Philippines shall be limited to Filipino citizens, save in cases prescribed by law.”

1987 Constitution, Article XIV: Education, Science and Technology, Arts, Culture, and Sports

Foreign ownership of schools and foreign enrolment: Section 4

“(2) Educational institutions, other than those established by religious groups and mission boards, shall be owned solely by citizens of the Philippines or corporations or associations at least sixty per centum of the capital of which is owned by such citizens. The Congress may, however, require increased Filipino equity participation in all educational institutions.

The control and administration of educational institutions shall be vested in citizens of the Philippines. No educational institution shall be established exclusively for aliens and no group of aliens shall comprise more than one-third of the enrolment in any school.”

1987 Constitution, Article XVI: General Provisions

Ownership of Mass Media: Section 11

“(1) The ownership and management of mass media shall be limited to citizens of the Philippines, or to corporations, cooperatives or associations, wholly-owned and managed by such citizens.”

“Only Filipino citizens or corporations or associations at least seventy per centum of the capital of which is owned by such citizens shall be allowed to engage in the advertising industry.

The participation of foreign investors in the governing body of entities in such industry shall be limited to their proportionate share in the capital thereof, and all the executive and managing officers of such entities must be citizens of the Philippines.”

els of corruption, restrictive foreign ownership rules, and uncompetitive labor compliance costs as the major impediments in the Philippines’ FDI growth. These are the same issues raised by various Philippine business organizations (the Makati Business Club included), as well as the Joint Foreign Chambers of the Philippines.

The root causes of the problem lies with the unusual setting of specific economic policies in the Philippine Constitution, going beyond basic economic principles and general guidelines (See Table 4). Economic policies should ideally be dynamic and be subject to legislation to meet the evolving global economic landscape. As discussed earlier, the leaked draft of the TPP Investments chapter demands national treatment for foreign investors and eliminates certain performance requirements required of them. These provisions run against existing Philippine laws, but will have to be accommodated if the country decides to join the TPP.

Another important issue in both the TPP and RCEP agenda is the promotion of healthy competition and a level playing field in TPP markets. Currently, Philippine lawmakers are still in the process of passing an anti-trust law. This absence of a comprehensive competition law and a central competition authority weakens the country’s ability to curb anti-competitive practices. Therefore, it is vital for the country to enact a comprehensive competition law, most especially in light of the oncoming ASEAN Economic Integration in 2015.

governed by a high-level of liberalization. Institutional and regulatory reforms are required to meet the standard requirements envisioned in the TPP agreement and to address obstacles concerning constitutionally-enshrined restrictive provisions, particularly on foreign investment and employment.

The government is carefully studying and considering the implications of joining, as well as not joining, the TPP trading bloc. It is reportedly taking steps to consult the public through various fora led by the Department of Trade and Industry, in partnership with universities and some foreign embassies. These stakeholder consultations form part of the overall preparations for the trade department to lead in implementing a unified trade strategy which rests on three pillars: (1) Stakeholder engagement in trade policy making; (2) Trade policy research network and capacity building; and (3) Enhanced inter-agency cooperation.

The TPP negotiations are reaching its end, thus, it is unlikely that the Philippines can join and still negotiate its own terms and conditions with the group. In the end, whether the Philippines will join or not, the creation of this formidable bloc will impact the local economy, as it will for the rest of the world. Moving forward, the country should, nevertheless, continue to monitor the progress of the negotiations, while simultaneously preparing the local economy for the arrival of stronger competition. ■

MOVING FORWARD

The Philippines has to work towards efficient systems and aligned regulations in order to compete in a single market

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