The Trans-Pacific Partnership: The U.S. Response to the Rise of China?

ROCKY INTAN

BETWEEN THE EARLY 1960S until 1990s, high growth rates and rapid industrialization of South Korea, Taiwan, Hong Kong, and Singapore earned them the nickname "Four Asian Tigers" or "Asia's Four Little Dragons".[1] The nicknames were partly inspired by Japan's post-war economic success, the perceived 'dragon' at the time. However, perception of such might not be warranted given the recent economic rise of Asia's real 'dragon', China.

Reforms spearheaded by Deng Xiaoping in 1978 have resulted in an unprecedented growth for China's national economy. In 1980, China's Gross Domestic Product based on purchasing power parity—GDP (PPP)—stood at US$ 248 billions. In 2012, its GDP/PPP stood at US$ 12.383 billions, a growth of approximately 300%, with an average annual

1 John Page, "The East Asian Miracle: Four Lessons for Development Policy," *National Bureau of Economic Research Macroeconomics* 9 (1994): 219-282.

Rocky Intan *is a research assistant at the Department of Politics and International Relations, Centre for Strategic and International Studies.*

growth of 9,5%.[2] This means that as of this writing, People's Republic of China's national economy is one of the largest national economies of the world, second only to the United States.

China's newfound economic power has been translated into political influence. China's energy consumption has been rapidly growing as an inevitable consequence of its booming economy. From 2009-2010, its net oil import—now the second largest only to the United States—grew at the rate of 10%. In the same report, it is estimated that in 2011, China's oil consumption growth accounted for half of the global oil consumption growth.[3] This has led Beijing to meddle in the domestic affairs of resource-rich countries. Beijing arms exports to Sudan, Ivory Coast, Democratic Republic of Congo, etc stands as a case in point.[4]

Nowhere is the growth of Chinese political and economic influence felt more than in Asia-Pacific, a region where China itself lies. Strategically, countries in the region have been nervously watching the ever-rising China's military spending over the past decade. China's military spending in 2012 was US$ 106 billion, an 11,2% increase from the previous year. Although only accounted for about 1,3% of its GDP on that fiscal year, it was the second largest national defense budget in the world after the United States, at around US$ 525,4 billion.[5] The concern of U.S. allies such as Taiwan, Japan, and the Philippines seems to be justified after China's recent assertive—confrontational, even—stance on territorial issues in the East and South China Seas, i.e. Senkaku Islands dispute and South China Sea dispute.

It is important to put the rise of China within the context of the waning of the United States, the current global economic superpower. The U.S.—the most powerful nation in the world after the disintegration of the British Empire after World War II and confirmed once more at collapse of the Union of Soviet Socialist Republics (USSR) in 1991—have been in relative decline ever since. Although it has long been the largest national economy in the world, the U.S. economy has been growing slower compared to other large economies, resulting in falling share of

2 International Monetary Fund, "World Economic Outlook Database," October 2012, http://www.imf.org/external/pubs/ft/weo/2012/02/weodata/weorept.aspx?pr.x=66&pr.y=10&sy=1980&ey=2012&scsm=1&ssd=1&sort=country&ds=.&br=1&c=924&s=PPPGDP&grp=0&a=

3 United States Energy Information Administration, "China," 4 September 2012, http://www.eia.gov/countries/analysisbriefs/China/china.pdf

4 "China's Arms Exports Flooding Sub-Saharan Africa". *The Washington Post*, 26 August 2012.

5 Jane Perlez, "Continuing Buildup, China Boosts Military Spending by More Than 11 Percent". *New York Times*, 4 March 2012.

global GDP. Decades of China's economic ascendancy, proven by its (and Asia-Pacific countries') resilience against the 2008-2009 global economic downturn, opened American eyes that the U.S. cannot afford not to focus on the region.

It was against this geopolitical background that the Trans-Pacific Partnership (TPP) emerged as a negotiation for a free trade agreement spanning across the Pacific Rim led by the U.S. The paper explores the TPP from the U.S. perspective, motivated by its insecurity on China's ascendancy.[6] It seeks to answer one central question: Why does the U.S. use the TPP as a policy instrument to balance against China? What is the relationship between the U.S. policy instrument and its international and domestic power structure? Why does the U.S. think that the TPP will benefit it?

Using the realist theory of state action by Mastanduno et al[7], the paper finds that due to its international and domestic power, it is natural for the U.S. to use the TPP to regain and preserve its power in Asia-Pacific vis-à-vis China. It also finds that the TPP is suitable for the U.S. as a future trading system in the region. The first section of this paper shall elaborate upon its theoretical framework, the realist theory of state action. The second shall explain U.S. foreign economic policy using the theory's framework. The third shall explain the content of TPP briefly and why it is suitable for the U.S. as a future regional trading system.

The Realist Theory of State Action

Formulated by Michael Mastanduno, David A. Lake, and G. John Ikenberry, the realist theory of state action seeks to account for the dual realities of international and domestic politics and economics. The authors accounted the failure of both classical and structural realism in doing so, while also incorporating elements from both realist schools of thought. As the name suggests, the theory places the state at the center of analysis, taking into account its power relations with other actors. Afterwards, the theory provides a framework in which a state is most likely to follow given the power constraints it faces in domestic and international politics and economics.

6 For more upon the U.S. motivation, the balance of threat theory by Stephen Walt is illustrative in Stephen M. Walt, "Alliance Formation and the Balance of World Power," *International Security* 9(4): 1985, pp. 3-43.

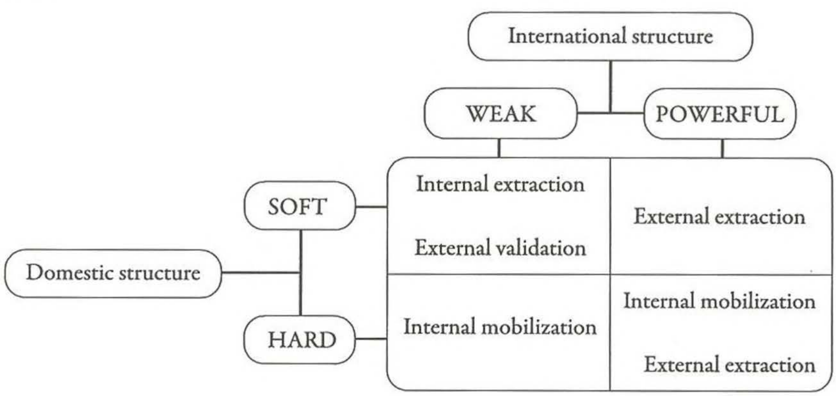
7 Michael Mastanduno, David A. Lake, and G. John Ikenberry. "Towards A Realist Theory of State Action," *International Studies Quarterly* 33: 1989, pp. 457-474.

The theory divides the state into categories based on its strength in both domestic and international realms of politics and economics. Accounting for a state's position in its respective domestic power structure, the theory divides states into two categories: soft and hard.[8] *Soft* states are states whose domestic political and economic structure is decentralized and constrained. *Hard* states are states whose domestic political and economic structure is centralized and autonomous.

Accounting for its international dimensions of strengths politically and economically, the theory divides states into two categories: weak and powerful.[9] *Weak* states are states that are only able to do little more than register the demands of other relatively stronger actors (i.e. most likely other states), or at best resist the demands of actors with similar strengths. *Powerful* states are states that are not only strong enough to resist demands of weaker actors (or at least, those with similar level of strength), but actively shape aspects of international politics and economics.

After considering the two faces of state—domestic and international, the theory puts forward the strategies that states are likely to pursue in the face of their domestic and international positions of power. The graph below presents a summary of the strategies that states will pursue relevant to their strength dimensions internationally and domestically [10].

Figure 1. State Dimensions and Strategies for States by Realist Theory of State Action



Source: Michael Mastanduno, David A. Lake, and G. John Ikenberry. "Towards A Realist Theory of State Action," *International Studies Quarterly* 33: 1989.

8 Ibid, p. 471.

9 Ibid.

10 Ibid., p. 469.

In the domestic realm, soft states will pursue more international strategies, relative to hard states. Conversely, hard states are more likely to pursue domestic strategies to achieve their state goals. As they are less able to implement domestic strategies meaningfully, soft states will be more likely to enact internal extraction while hard states will implement internal mobilization. In the international arena, weak states shall rely more on domestic strategies while strong states will rely more on international strategies. Internationally weak states will implement external validation, while their powerful counterparts will emphasize on external extraction.

Using the Realist Theory of State Action to Analyze the U.S. Strategy

Based on the theory's classification, the United States is a domestically soft state. This classification of U.S. domestic power position is based upon two reasons. First, the U.S. government grants a wide array of freedom to the society that it governs. In 2013, the United States was scored 76,0 in the Index of Economic Freedom by the Heritage Foundation.[11] The Index was calculated based on rule of law (property rights and freedom from corruption), limited government (fiscal freedom and government spending), regulatory efficiency (business, labor, and monetary freedom), and open markets (trade, investment, and financial freedom).[12] The U.S. score in 2013 was slightly lower than year earlier (a 0.3 point decrease) due to worsening situation for government spending, freedom from corruption, and investment freedom. However, it was still above the world's average, ranking 10th globally.[13] As the government allows it much freedom, most economic decisions in the U.S. are undertaken by the private sector, albeit the Foundation noted that this situation has worsened since the arrival of several government regulations post-2008 Financial Crisis.[14]

Second, decision from the top level of government cannot always be translated to an individual level in society due to the government's decentralized nature. The decentralized nature of the U.S. government is mirrored in its division to three levels: federal, state, and local. Although the federal government can exert considerable pressure to other levels

11 Heritage Foundation, "2013 Index of Economic Freedom," http://thf_media.s3.amazonaws.com/index/pdf/2013/Index2013_Highlights.pdf

12 Ibid.

13 Ibid.

14 Ibid.

(e.g. the Federal Reserve system essentially transfers money from a tax surplus state to a deficit one), there exist large policy differences in each level of government. A relevant example for economic activities in the U.S. is different the level and types of taxation on each U.S. state. As a case in point, according to the U.S. Federation of Tax Administrators, Texas has no individual income tax while Massachusetts imposes a flat rate individual income tax of 5.25% as of January 2013.[15]

Based on the theory's classification, the United States is an internationally powerful state. Indeed, by many measurements, it is the most powerful state in the world. The single most relevant economic measurement of the U.S. state's powerful position is the U.S. large and open market. With a GDP—both PPP and nominal—at US$ 15 trillion, the size of the American domestic market is second to none.[16] Even though international trade only makes around 28% of the U.S. GDP, it is one of the top five trading partners for numerous countries, including the five negotiating countries of the Trans-Pacific Partnership analyzed in the previous sub-chapter.[17] For example, the Vietnamese-American trading relationship is asymmetrically crucial for Vietnam. The export and import between U.S. and Vietnam in 2011 was valued at around US$ 22 billion and the Vietnamese GDP (nominal) stood at around US$ 122 billion.[18] This implies that trade with the U.S. made up around 6% of Vietnamese GDP (nominal) and only made up around 0.7% of U.S. GDP (PPP and nominal). The U.S. alone made up around 9% of Vietnam's total export, ranking first of all its export partners.[19] The large size of the U.S. market to other countries' trade renders its importance to others, enhancing the state's bargaining power vis-à-vis other countries.

Additionally, no other large market is as open as the United States (10th). The Index of Economic Freedom supports such assertion, in which other comparatively large national markets like China (136th), India (119th), Brazil (100th), etc were well below the U.S. in terms of openness. This high degree of openness is reflected in high level of foreign direct investment to the United States. Over the years, the U.S. has frequently been the largest national host of FDI globally at around US$ 2.8 trillion

15 United States Federation of Tax Administrators, "State Individual Income Taxes" (2013), http://www.taxadmin.org/fta/rate/ind_inc.pdf

16 World Trade Organization, "Trade Profiles 2012," p.180, http://www.wto.org/english/res_e/booksp_e/anrep_e/trade_profiles12_e.pdf

17 Ibid.

18 Ibid, p. 185

19 *Ibid.*

per annum.[20]

The theory posits that an internationally powerful and domestically soft state will tend to emphasize a strategy of international extraction.[21] International extraction is a policy that seeks to enhance and reinforce the existing power of an actor through rent-seeking activities.[22] An effective free trade agreement acts as an international extraction as it reinforces a country's economic competitive rank by lowering tariff and non-tariff trade barriers, all things equal.[23] As such, the U.S. eagerly used the TPP in order to respond to the economic ascendancy of China because it is constrained to do so domestically and internationally capable to do so.

The Trans-Pacific Partnership as U.S. Strategy

The Trans-Pacific Partnership is a proposed free trade agreement between countries in the region Asia-Pacific. As of April 2014, the negotiating members of the Trans-Pacific Partnership are Malaysia, Vietnam, Singapore, Brunei Darussalam, Australia, New Zealand, Chile, Peru, Canada, Mexico, the United States, and Japan.[24] South Korea has expressed interest in joining the negotiations.[25] The agreement was initially known as the Trans-Pacific Strategic Economic Partnership (TPSEP), an agreement on a framework for a free trade agreement among Brunei Darussalam, Chile, New Zealand, and Singapore in 2005.[26] In 2008, the United States formally announced that it will be joining the negotiations on issues that have not been previously covered such as trade liberalization on financial services.

The proposed agreement is hailed as a "21st century trade deal" as it includes clauses that deal with issues never before dealt with in trade agreements. It needs to be noted that the exact content of TPP in

20 Central Intelligence Agency, "CIA World Factbook: United States," https://www.cia.gov/library/publications/the-world-factbook/geos/us.html

21 Mastanduno, Lake, and Ikenberry, "Towards A Realist Theory of State Action," p. 469.

22 Ibid, p. 470.

23 Ibid.

24 Japan requested to join the negotiations only in March 2013, under the leadership of Prime Minister Shinzo Abe and his reform program of "Abenomics."

25 Sophie Song, "South Korea Is Considering the Trans-Pacific Partnership But Will Prioritize Bilateral Free Trade Agreement with China," *International Business Times*, 13 January 2014, , http://www.ibtimes.com/south-korea-considering-trans-pacific-partnership-tpp-will-prioritize-bilateral-free-trade-agreement

26 "Trans-Pacific Strategic Economic Partnership," Main Agreement, http://www.mfat.govt.nz/downloads/trade-agreement/transpacific/main-agreement.pdf

negotiation is not known. The best glimpse into the TPP's content is the content of TPSEP, in which the TPP is largely based upon as a template. Through this analysis, it can be observed that the TPP will focus on four main areas: 1) trade in services, 2) intellectual property rights, 3) technical barriers to trade, and 4) competition policy and government procurement.

On trade in services, negotiating countries seek to increase and deepen trade in services between member countries on a mutually advantageous basis.[27] For example, by obliging every member to treat services and service suppliers equally as those from their own. On intellectual property rights, the TPP seeks to strengthen the enforcement of their respective intellectual property rights regime while striking the balance between rights holders and users.[28] On technical barriers to trade, negotiating countries aim to reduce costs of compliance among them on their respective technical trading regulations.[29] On competition policy and government procurement, the TPP aims to reduce and remove trade barriers to increase economic efficiency and welfare[30]. To such end, the agreement shall abolish discrimination of government procurement contracts based on national ownership.

Observing such features, one can understand why the U.S. views the TPP as crucial to its interest. The four features described above suit the U.S. as an advanced economy. The World Economic Forum characterized the U.S. as a country in an innovation-driven level of development.[31] In this level, technological innovation and business sophistication make up 50% of a country's competitiveness. The four features of the TPP will benefit countries with better technological innovation and business sophistication such as the U.S. more.

It is important to put the TPP in the context of another Asia-Pacific wide trade agreement under negotiation, Regional Comprehensive Economic Partnership (RCEP). It is a free trade agreement under negotiation between ten Association of Southeast Asian Nations (ASEAN) members and the six states that ASEAN has existing free trade agreements with;

---

27 Ibid, p. 12-2.

28 Ibid, p. 10-1.

29 Ibid.

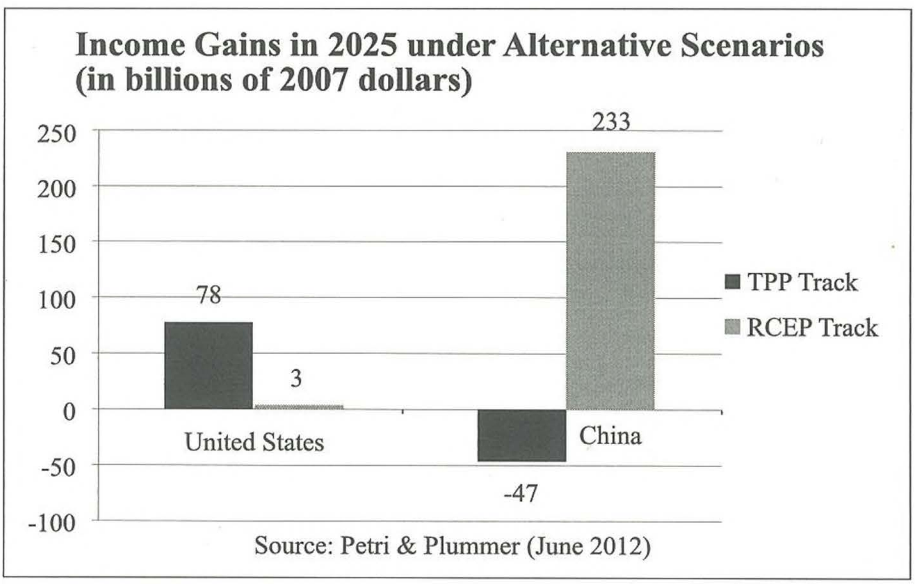
30 Ibid, p. 9-1.

31 World Economic Forum, *The Global Competitiveness Report 2013-2014*, http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2013-14.pdf

namely China, Japan, South Korea, India, Australia, and New Zealand.[32] As an ASEAN-centered agreement, it will mainly focus upon issues such as market access to goods, dispute resolution, and cooperation and capacity building. The content focus on market access to goods of RCEP reflects the interests of emerging countries with comparative advantages in manufacturing vis-à-vis advanced countries.[33] This is in contrast with the TPP content focus on services, investment, and intellectual property rights, which in turn reflects the interests of advanced countries.

A clear difference between the two templates favored by emerging and advanced countries can be observed, with the U.S. on the latter side. It is crucial to understand that this does not imply that the implementation of one template will necessarily translate into loss for countries favoring another template. As a positive-sum game, both implementations will benefit all countries in the region. Countries will benefit more if their favored template becomes the center of future integrated regional template, though. And through the TPP, this is what the U.S. is pursuing.

Figure 2. U.S. and Chinese Income Gains in 2025 under Alternative Scenarios



32 Association of Southeast Asian Nations (ASEAN) Secretariat, *Regional Comprehensive Economic Partnership (RCEP) Joint Statement The First Meeting of Trade Negotiating Committee*, 10 May 2013, http://www.asean.org/news/asean-statement-communiques/item/regional-comprehensive-economic-partnership-rcep-joint-statement-the-first-meeting-of-trade-negotiating-committee

33 Peter A. Petri and Michael G. Plummer. *The Trans-Pacific Partnership and Asian Integration: Policy Implications*, Peterson Institute for International Economics, June 2012, http://www.iie.com/publications/pb/pb12-16.pdf

The figure provides the simulation of income gains for the U.S. and China in 2025 with regards to the implementation of TPP and RCEP. In 2025, the U.S. will gain US$ 78 billion and China will lose US$ 47 billion if only the TPP is implemented. Correspondingly, the U.S. will gain US$ 3 billion and China will gain US$ 233 billion. The full simulation also shows that countries in both agreements stand to gain if TPP and RCEP are integrated into a single agreement with the U.S. gaining more on the condition that the TPP becomes the center of the integrated agreement. The paper by Petri and Plummer also simulates the results for other countries in the region.[34]

Conclusion

It is clear that why the U.S. chose the TPP as its instrument of choice to balance against China. First, American domestic and international position requires it to pursue a strategy of international extraction, which in this case, a free trade agreement. Second, the content of the free trade agreement has to be the one that benefits the U.S., symmetrically if possible. The TPP fits this requirement nicely. Its content focus on services, intellectual property rights, technical trade barriers, and competition policy and government procurement reflects the interests of the U.S. as a country in an advanced level of development.

In the case of the TPP, the U.S. has correctly identified its competitiveness and a free trade agreement that benefits it. As a lesson for policy recommendation, other countries will do well to do the same. Identification of what makes a country's competitive is an essential step before negotiating a free trade agreement. The second policy recommendation concerns the potential effects of the TPP towards other countries in Asia-Pacific and ASEAN. Can Indonesia, Thailand, the Philippines, and other ASEAN countries accept that Malaysia, Singapore, Vietnam and Brunei will acquire preferential market access to the U.S. market through the TPP? Can ASEAN maintain its centrality and cohesiveness when not all of its members are inside the TPP? ASEAN and its member should seriously consider their stance towards the coming agreement.

34 Another paper also explains in detail the model used in the simulation. See Peter A. Petri, Michael G. Plummer, and Fan Zhai, "The Trans-Pacific Partnership and Asia-Pacific Integration: A Quantitative Assessment," East West Center Working Papers Economic Series No. 119, 24 October 2011.