

## PB 17-7 US Trade Policy Options in the Pacific Basin: Bigger Is Better

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One of the first acts carried out by President Donald Trump was to order the United States Trade Representative (USTR) to withdraw formally from the Trans-Pacific Partnership (TPP), as he promised to do throughout the campaign. In place of the TPP, Trump plans to negotiate new bilateral trade deals or recast existing pacts “to promote American industry, protect American workers, and raise American wages.”<sup>1</sup>

Trump’s position on the TPP—a megaregional trade agreement between the United States and 11 other countries that account for almost 40 percent of the world’s economy—is straightforward: It hurts US firms and workers and cannot be fixed. These arguments play well with his grassroots supporters who consider the TPP to be a newer, more virulent North American Free Trade Agreement

(NAFTA), which they claim has wreaked havoc on the US manufacturing sector and employment. Trump’s main objections can be summarized as follows<sup>2</sup>:

- The TPP is typical of bad trade deals that have caused “mounting trade deficits and a devastated manufacturing base.”<sup>3</sup>
- The United States paid too much and got too little from the other TPP countries.
- The TPP contains loopholes (e.g., rules of origin) that allow China and other non-TPP countries to “free ride” on the deal.
- TPP enforcement provisions are too weak.

Is the TPP history? To date there is no indication that the Trump administration would consider revisiting the pact. It had few vocal champions in the 2016 election, and those who supported it kept their profile low. However, many Republicans, representing a vast array of farm and industrial groups, continue to support the TPP and argue instead that Trump should fix the deal rather than deep-six it. They believe that the pact helps level the playing field for US exporters while also reinforcing US strategic interests in the region. Some Republican leaders in Congress already have called on Trump to renegotiate the deal.<sup>4</sup>

This Policy Brief first assesses Trump’s TPP critique and plan to pursue instead new bilateral trade pacts in the Asia-Pacific region. It explains why a regional deal like the

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2. See, for example, comments by Commerce Secretary Wilbur Ross as to why the TPP is a “bad deal.” “CNBC Transcript: Steven Mnuchin and Wilbur Ross Speak with CNBC’s ‘Squawk Box’ Today,” November 30, 2016, [www.cnbc.com/2016/11/30/cnbc-transcript-steven-mnuchin-and-wilbur-ross-speak-with-cnbc-squawk-box-today.html](http://www.cnbc.com/2016/11/30/cnbc-transcript-steven-mnuchin-and-wilbur-ross-speak-with-cnbc-squawk-box-today.html) (accessed on December 5, 2016).

3. “Trade Deals Working for All Americans,” The White House, [www.whitehouse.gov/trade-deals-working-all-americans](http://www.whitehouse.gov/trade-deals-working-all-americans) (accessed on January 26, 2017).

4. Senate Finance Committee Chairman Orrin Hatch has pledged to push the Trump administration to reconsider the TPP and salvage the deal, even if it is kick started as a bilateral deal with Japan, based on the “reality” that “we’re a lot better off if we do free trade agreements.” See “Finance members meet with USTR pick; Hatch pledges to push for TPP,” *Inside US Trade*, January 12, 2017, [www.insidetrade.com](http://www.insidetrade.com) (accessed on January 13, 2017).

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1. “Presidential Memorandum Regarding Withdrawal of the United States from the Trans-Pacific Partnership Negotiations and Agreement,” White House Office of the Press Secretary, January 23, 2017, <https://www.whitehouse.gov/the-press-office/2017/01/23/presidential-memorandum-regarding-withdrawal-united-states-trans-pacific> (accessed on January 26, 2017).

TPP is far more likely to yield gains for all participants than the administration's favored bilateral approach. Second, the paper reexamines the TPP and assesses ways that it could be improved. It concludes that the TPP has flaws that can and should be fixed, in terms of additional liberalization and rulemaking. Finally, the analysis considers options for building a new Asia-Pacific trade pact on the substantial foundation of the TPP.

## The Trump administration may find value in negotiations on a revamped, enlarged, and probably renamed Asia-Pacific pact.

With careful consideration of the alternatives, the Trump administration may find value in negotiations on a revamped, enlarged, and probably renamed Asia-Pacific pact.<sup>5</sup> In this case, USTR officials could find what other trade negotiators have concluded in the past: bigger is better, meaning (1) more countries, including important US trading partners like Korea, Taiwan, and Colombia; and (2) more content, including enforceable obligations on exchange rate policies that protect US manufacturers and workers against damaging currency manipulation and adjustments to investor-state dispute settlement procedures.

### WHAT'S WRONG WITH TRUMP'S VIEW OF THE TPP?<sup>6</sup>

The Trump critique of the TPP echoes populist complaints reminiscent of the anti-NAFTA coalition in the early 1990s that allied the left wing of the Democratic Party with the right wing of the Republicans. What's wrong with this diagnosis?

5. In a recent interview, former Commerce Secretary Penny Pritzker backed the idea of a "name change" for the TPP if it would prevent the United States from throwing out the deal: "It's irrelevant to me what it's called.... I think what's important is to recognize the United States needs to lead economically, and having a significant leadership role in the Asia-Pacific is critical to our economic security and our national security." See Megan Cassella, "Pritzker: Trump tariff threats carry risks," *Politico*, January 6, 2017, [www.politico.com/tipsheets/morning-trade/2017/01/pritzker-trump-tariff-threats-carry-risks-218114](http://www.politico.com/tipsheets/morning-trade/2017/01/pritzker-trump-tariff-threats-carry-risks-218114) (accessed on January 13, 2017).

6. This section draws from Jeffrey J. Schott, "TPP Can Be Fixed If You Know What's Wrong with It," Trade and Investment Policy Watch blog, December 5, 2016, <https://piie.com/blogs/trade-investment-policy-watch/tpp-can-be-fixed-if-you-know-whats-wrong-it> (accessed on December 5, 2016).

### Claim: The TPP is typical of bad trade deals that have caused "mounting trade deficits and a devastated manufacturing base"

Previous trade deals like NAFTA and the Korea-US FTA are criticized as contributing to US trade deficits and job losses in manufacturing.<sup>7</sup> It's a seductive sound bite but too simplistic: Large trade deficits also can coincide with employment gains as they have in recent years, reflecting stronger growth in the United States than in other leading economies. Moreover, the connection between free trade agreements and trade deficits is tenuous: Trade deals may influence the size and composition of the bilateral trade deficit with a specific country, but make little difference to the global US trade deficit because it is largely determined by macroeconomic factors, including domestic levels of private savings and investment and government deficits.<sup>8</sup>

To be sure, the United States does run a cumulative trade deficit with the other 11 TPP signatories. In 2015 the US merchandise trade deficit with these countries totaled about \$175 billion; Japan and Mexico accounted for more than 75 percent of the deficit.<sup>9</sup> Auto imports alone from those two countries plus Canada exceeded \$125 billion. The TPP auto trade deficit (\$93 billion) is more than a third the US deficit in manufactured goods with TPP countries.<sup>10</sup> So the "trade deficit" story with the TPP is in large measure an autos story, and even more a story about the integration of the North American auto industry over the past 50 years since the US-Canada auto pact of 1965.

Regarding the US manufacturing sector, US output is at or near an all-time high, even as US employment in manufacturing has dropped sharply from levels at the turn of the century and now totals about 12.3 million workers, or only 8.5 percent of total US nonfarm employment.<sup>11</sup> But

7. See Donald J. Trump, "Declaring American Economic Independence," June 28, 2016, [https://assets.donaldjtrump.com/DJT\\_DeclaringAmericanEconomicIndependence.pdf](https://assets.donaldjtrump.com/DJT_DeclaringAmericanEconomicIndependence.pdf) (accessed on December 15, 2016).

8. Gary Clyde Hufbauer and Zhiyao (Lucy) Lu, "Free Trade Agreements and Trade Deficits," Trade and Investment Policy Watch blog, March 31, 2016, <https://piie.com/blogs/trade-investment-policy-watch/free-trade-agreements-and-trade-deficits> (accessed on January 13, 2017), and Gary Clyde Hufbauer and Euijin Jung, "Is Our Trade Deficit a Problem?" *PBS NewsHour*, February 2, 2017, <https://piie.com/commentary/op-eds/our-trade-deficit-problem> (accessed on February 8, 2017).

9. Data from UN Comtrade via International Trade Centre, [www.trademap.org/](http://www.trademap.org/).

10. Based on trade in motor vehicles transporting people and goods, tariff lines HS 8702-8704.

11. Establishment data as of December 2016 reported by the Bureau of Labor Statistics, <https://www.bls.gov/ces/>. Interestingly, US manufacturing jobs are up more than

it's worth noting that the overall trend of manufacturing's declining *share* of total US employment was in motion long before NAFTA or other trade deals. The unemploy-

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ment rate in US manufacturing was 4 percent in December 2016, so any significant increase in US jobs would quickly generate wage pressure. In short, fewer US workers are now producing record amounts of goods. Trade and trade agreements are only a small part of the story.

**Claim: The United States paid too much and got too little from other TPP countries.**

The Trump team argues that the United States paid too much because each of the 11 TPP partners demanded something different and additional to what was offered to the others. They believe that one-on-one talks would avoid such cascading demands for more and more US concessions. Instead of multicountry regional accords, Trump wants the United States to pursue bilateral trade deals where US negotiators can use the size of the US market to leverage greater concessions from trading partners. But that's not how it works.

In fact, US concessions in the TPP were very limited. The US market is already largely open to foreign suppliers from all member countries of the World Trade Organization (WTO), and US negotiators did not commit to many significant changes in existing US practices and protection in the TPP. Where the United States maintains barriers, US negotiators grudgingly committed to small or partial reforms—they even postponed cutting the 2.5 percent US auto tariff on Japanese car imports for decades (Oliver 2016). Protections for US dairy and sugar producers were left largely intact. At the same time, US officials achieved in the TPP substantial openings of long-protected Asian markets to benefit US exporters.

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2 million since the global financial crisis 8 years ago. For an overview of the state of the US manufacturing sector, see Lindsay Oldenski and Theodore H. Moran, "Misconceptions on the Campaign Trail: US Manufacturing," Trade and Investment Policy Watch blog, April 11, 2016, <https://piie.com/blogs/trade-investment-policy-watch/misconceptions-campaign-trail-us-manufacturing> (accessed on January 26, 2017).

Sounds like a favorable deal for US interests; in fact, it's even better. The United States got "paid" twice by our TPP partners: first in reciprocal concessions in each of the 11 markets, and then in a bonus payment—more of what we wanted from them in market access and support, *inter alia*, for new investment and intellectual property rules—from many of those countries for helping them get better access via the TPP to the Japanese, Vietnamese, and other markets than they would have been able to get on a bilateral basis.

In sum, negotiating the regional TPP produced large US gains with few US concessions. Without the TPP, foreign access to the US market is substantially the same as before but US firms and workers lose important new opportunities in foreign markets that the TPP would have provided.

**Claim: The TPP contains loopholes that allow China and other non-TPP countries to "free ride" on the deal.**

Critics of the TPP are concerned that TPP rules allow China to supply parts to producers in TPP countries (who then export final goods to the US) and thus indirectly benefit from the TPP tariff preferences without providing new access to the Chinese market. Trump officials specifically cite concerns that TPP origin rules on autos and auto parts allow more imported content than NAFTA and give China a free ride into the US market. They think origin rules for autos and parts should be even more restrictive than those in NAFTA.

From a US perspective, these concerns seem exaggerated. Rules of origin set criteria for qualifying for preferential tariff treatment under the TPP and other free trade pacts. If a good doesn't qualify, it pays the most favored nation (MFN) tariff like other WTO countries. Mexico, Canada, and Japan account for 99 percent of US car imports from TPP countries. The US MFN auto tariff is 2.5 percent regardless of the imported content of those vehicles, and under the TPP the United States does not give a tariff preference to Japan, its primary competitor, for 25 years—not much of a loophole for Chinese parts. Moreover, since Canada and Mexico already receive duty-free treatment under NAFTA, most US car imports are excluded from TPP preferences! It is true that US auto parts tariffs are a bit higher and phased out sooner, but Chinese parts in Japanese and other car exports to the United States are not a significant problem since the existing trade can continue relatively unimpeded simply by paying the small MFN tariffs.

### **Claim: TPP enforcement provisions are too weak.**

The Trump administration is concerned that the United States has not aggressively enforced its rights under FTAs. They commit to “identify all trade violations and to use every tool at the federal government’s disposal” to enforce US rights under trade deals, including possibly government initiated antidumping and countervailing duty cases.<sup>12</sup>

Concerns about TPP enforcement provisions also seem to echo charges by many civil society groups that the pact’s investor-state dispute settlement (ISDS) procedures serve corporate rather than worker interests. US trade agreements and investment treaties include ISDS as a restraint against expropriation or unfair treatment when governments change political direction (Hufbauer 2016). The TPP does improve previous US FTAs like NAFTA with the addition of provisions to safeguard the role of domestic regulation and discourage frivolous cases. Past record shows that the US government has yet to lose a case brought by a foreign investor. But contrary to US business claims, ISDS is not an essential component of the deal; given the TPP controversy and opposition, many TPP countries would be willing to amend the mechanism, as discussed below.

### **BILATERALS ARE NOT THE ANSWER**

In place of the TPP, the Trump administration wants to pursue bilateral FTAs, starting with NAFTA partners Mexico and Canada. But the Trump team has not yet developed a specific agenda of what they would want in a “modernized” NAFTA.

The Trump administration may also revisit the Korea-US FTA, again focusing on the auto sector as well as steel, financial services, and perhaps the controversial exclusion of rice. Since the US Treasury has put Korea on its currency watch list, the issue of disciplines to deter currency manipulation also may be part of the new US agenda.

In addition, they may consider a US-Japan FTA, despite the multitude of political and economic factors that prevented such an initiative in the past and that posed the biggest challenges in the TPP talks.<sup>13</sup> Japanese concessions, especially on access for US farm products, were sustainable politically only because of the added benefits that accrued to Japanese manufacturers and investors in other TPP markets—and

that would not have been achievable without the US-led trade pact. That’s why Japanese negotiators were willing to pay more to the United States in the TPP. In a bilateral deal, the Japanese offer would likely be much less generous. As a practical matter, bilateral negotiations are likely to be engaged in the near future; the Japanese would not say “no” to such an overture. But getting to “yes” on the content of a new bilateral agreement will be much more difficult.

### **In short, the bilateral option is unlikely to bear fruit.**

The Trump administration would also like to strengthen economic ties with Taiwan. The new Taiwanese president, Tsai Ing-wen, had indicated her willingness to strengthen economic ties between the two countries by joining the TPP. But, although Taiwan has instituted some needed economic reforms, it still has a lot to do to meet US standards for FTAs (Schott et al. 2016). While Taiwan would welcome a bilateral FTA with the United States and probably would offer more concessions to secure such a deal, such an initiative would contravene the long-standing “one China” policy and likely cause major ruptures in US-China relations. However, Taiwan also might be willing to offer substantial concessions in a larger regional pact that would open new opportunities for Taiwanese companies in Asia-Pacific markets and reduce the discrimination they face from other FTAs from which they are excluded.

In short, the bilateral option is unlikely to bear fruit. Trump will try to negotiate a better deal with Mexico and Canada and perhaps others, seeking more concessions from abroad and requiring fewer from the United States. But why would these countries do so, when they already have good access to the US market? Of course, Trump threatens to claw back that good access by imposing new tariffs or abrogating the NAFTA pact. The former would violate US international obligations and invite retaliation; the latter is legal (six months after notification) but would be very disruptive to US production and trade. The ensuing damage to US production resulting from disruption of critical North American supply chains would cause a political uproar in Congress and throughout the industrial heartland that gave Trump his electoral victory. So, without additional US concessions, the NAFTA talks may end in a Mexican standoff.

And, even if bilateral talks could be concluded, why would Trump want to expend significant political capital advancing individual FTAs through Congress instead of one comprehensive pact restructured to meet his specifications? As noted above, negotiating the regional pact produces larger US gains with fewer US concessions.

12. “Trade Deals Working for All Americans,” The White House, [www.whitehouse.gov/trade-deals-working-all-americans](http://www.whitehouse.gov/trade-deals-working-all-americans) (accessed on January 26, 2017).

13. See Yoichi Funabashi, “The Trump Effect on Tokyo,” *New York Times*, op-ed, November 15, 2016, [www.nytimes.com/2016/11/16/opinion/the-trump-effect-on-tokyo.html?\\_r=1](http://www.nytimes.com/2016/11/16/opinion/the-trump-effect-on-tokyo.html?_r=1) (accessed on January 12, 2017).



## REVISITING THE REGIONAL APPROACH

The following sections discuss why a new Asia-Pacific pact is needed and how the deal could be structured and rebranded. Would US trading partners agree to a reopening of the TPP? Last year the answer would have been “no” because of concern that the complex, interrelated TPP deal would unravel. But unraveling is now the default position and restructuring the pact is the only promising avenue for US participation. On January 23, 2017, President Trump ordered the USTR not to engage in any TPP negotiations; but the door has not been shut to other Asia-Pacific trade initiatives in the future.

### Negotiating the regional pact produces larger US gains with fewer US concessions.

By the time tax reform initiatives clear Congress and Republican leaders return to trade issues, the climate for dealing with the TPP will likely have changed—for better or worse. Economic stimulus from tax cuts and infrastructure spending should provide at least a short-term boost to US GDP. On the other hand, the stronger dollar likely will contribute to larger trade deficits and thus feed already strong protectionist pressures. Trump could then demand that the other countries return to the negotiating table and redo the deal. In that event, he will discover that most Republicans want to maintain what is already in the trade agreement but would be willing to add, delete, or revise other provisions to address concerns raised by TPP critics. Trump might insist on adding new currency provisions to deter manipulation, drawing on obligations already included in the Joint Declaration of Macroeconomic Policy Officials issued in parallel with the TPP text in November 2015.<sup>14</sup> He also might revise or drop the highly controversial ISDS procedures. And he might try to amend US obligations on pharmaceuticals to satisfy Senator Orrin Hatch, the influential chair of the Senate Finance Committee. These options are expanded on below.

There are several important reasons why the Trump administration may well consider a new trade deal in the Pacific Basin that is bigger and broader than the TPP: (1) Many Republicans in Congress and most business and farm groups want a TPP-style deal; (2) concerns that US competitiveness will be adversely affected as others implement domestic economic reforms and US farm and other interests face increasing discrimination from trade deals in

which the United States is not a participant; and (3) the pact will reinforce strategic interests in the region. Such an initiative should draw heavily on TPP precedents in some areas and augment or revise commitments in others. It could involve more countries than the TPP—increasing the prospective payoff from US participation.

### Political Support

The TPP is strongly supported by a large number of Republicans in Congress because their constituents in agriculture, manufacturing, and service industries would greatly benefit from its provisions. The TPP has been opposed by most Democrats in Congress and US labor unions, among others—only 28 House Democrats voted for Trade Promotion Authority in 2015 and reportedly supported TPP ratification in the previous Congress.

Despite Trump’s directive to withdraw from the TPP, Republican leaders in Congress have argued both publicly and in private conversations with the president that he reconsider and instead renegotiate the deal. Notably, Senate Finance Committee chair Orrin Hatch and House Ways and Means Committee chair Kevin Brady—the committees responsible for all trade legislation—strongly support US participation in the TPP; so, too, do Dave Reichert, chair of the Trade Subcommittee of Ways and Means and many farm belt Republican governors, including Nebraska Governor Pete Ricketts (brother of Todd Ricketts, nominated by Trump to be Deputy Commerce Secretary). And so did several members of Trump’s cabinet, including Commerce Secretary-designate Wilbur Ross and Secretary of State Rex Tillerson, before the election campaign and signing of the final TPP pact.

In short, leading Republicans want the TPP and prefer that Trump try to fix it instead of rejecting it. And almost every major US farm and industry association supports the TPP.

Fixes to specific problems with TPP provisions cited by the pharmaceutical and financial services industries had been substantially completed by President Obama and USTR Michael Froman in anticipation of a vote on TPP implementing legislation during the lame-duck session of Congress after the election. Trump’s election abruptly stopped that legislative effort and the targeted revisions to TPP obligations. A new negotiation would allow improvements to be included in the core treaty text.

14. For full text see [www.treasury.gov/initiatives/Documents/TPP\\_Currency\\_November%202015.pdf](http://www.treasury.gov/initiatives/Documents/TPP_Currency_November%202015.pdf).

## Keeping US Firms Competitive

US farm and other interests will suffer trade discrimination due to existing and new trade preferences accorded in FTAs among TPP countries; the same would apply on a larger scale if the other TPP members applied the pact on a provisional basis among themselves pending US participation. US beef and pork exporters already face loss of market share in Japan due to the Japan-Australia FTA, and that will be replicated in other markets and for other products as TPP countries move forward with FTAs that don't include the United States. This kind of discrimination would expand should Japan and other countries conclude the Regional Comprehensive Economic Partnership (RCEP) with China.<sup>15</sup>

## US withdrawal from the TPP effectively opens the door for China to assert a more pronounced leadership role in the region.

Many of the other TPP countries entered the deal because they wanted to pursue domestic economic reforms required by TPP obligations. Several of them, especially Japan, are continuing to complete their domestic ratification process because the TPP provisions support their own development strategies.<sup>16</sup> They have also discussed moving forward with the TPP or a comparable, high-standard Asia-Pacific pact—including other regional partners like China and Korea—whether or not the United States participates. Such an initiative will take some time to develop, leaving the TPP in suspended animation for the next year or two. This strategy would keep the door open for future US participation; it also maintains the option for a renegotiation of the pact.

## Strategic Interests

The TPP was originally envisioned as the economic arm of the so-called Pivot to Asia, and US participation in the pact was reassurance that the region would remain a priority in US foreign policy. Since the US election, the leaders of Japan, Singapore, Australia, and New Zealand have empha-

sized the strategic importance of the TPP for their countries and for US leadership in the region.<sup>17</sup> Withdrawing from the TPP raises concerns among US allies in the region about the reliability of US support.<sup>18</sup> That's why countries like South Korea and Japan, facing the threat of North Korean missiles and military adventurism, understand and value it very highly. So do other Asia-Pacific nations that depend on open and secure sea lanes for their commercial prosperity.

Furthermore, US withdrawal from the TPP effectively opens the door for China to assert a more pronounced leadership role in the region. China already is a major trade and investment partner for TPP countries—most of which are now pursuing new or enhanced pacts to strengthen bilateral and regional commercial relations. Canada and Mexico are seeking to open talks with China; Chile, Australia, New Zealand, and Malaysia are seeking to expand existing deals; and seven of the original TPP-12 are participating in RCEP negotiations.<sup>19</sup> The Trump administration is worried about giving a free ride to China on auto parts imports; they are actually giving Chinese negotiators new opportunities to expand trade and investment in other TPP markets.

For these reasons, a “bigger and better” deal that builds on the foundations of the TPP would better serve US interests than a limited bilateral approach. The next section discusses how improvements to the content of the deal and the inclusion of new partners could bolster US political support and increase the potential payoff from an Asia-Pacific trade pact.

15. As estimated by the Council of Economic Advisers (2016), if RCEP—involving 16 countries in Asia and Oceania—were successfully concluded, 35 industries in the United States could lose out to Chinese firms that gain tariff preferences in the Japanese market.

16. See Jeffrey J. Schott, “TPP Could Go Forward without the United States,” Trade and Investment Policy Watch blog, November 15, 2016, <https://piie.com/blogs/trade-investment-policy-watch/tpp-could-go-forward-without-united-states> (accessed on December 5, 2016).

17. Japanese officials recently called the TPP pact “meaningless” without US participation. See “Tokyo turns down Australian proposal for TPP without US, vows to keep pushing Trump,” *Japan Times*, January 24, 2017, [www.japan-times.co.jp/news/2017/01/24/national/politics-diplomacy/tokyo-turns-australian-proposal-tpp-without-u-s-vows-keep-pushing-trump/#.WlpYARsrLct](http://www.japan-times.co.jp/news/2017/01/24/national/politics-diplomacy/tokyo-turns-australian-proposal-tpp-without-u-s-vows-keep-pushing-trump/#.WlpYARsrLct) (accessed on January 24, 2017).

18. In his valedictory remarks, former US Trade Representative Michael Froman stated, “From our friends and allies in the region to our own military commanders, we have heard clearly that failure by the U.S. to move forward would be a debilitating blow to U.S. leadership and credibility in the region, one that would create a void that China is all too happy to fill, and one that would leave our closest military allies and partners no choice but to line up behind China.” See Remarks by Ambassador Michael Froman at the Washington International Trade Association, January 10, 2017, <https://ustr.gov/about-us/policy-offices/press-office/speechestranscripts/2017/january/Remarks-Ambassador-Froman-WITA> (accessed on January 13, 2017).

19. See “China FTA Network,” <http://fta.mofcom.gov.cn/english> (accessed on January 27, 2017).

## THE “GO BIG” OPTION

Like Wagner’s music, the TPP isn’t as bad as it sounds or as has been described by Trump and his trade team. To be sure, the TPP has flaws that can and should be fixed in terms of both incomplete liberalization commitments and inadequate or flawed rulemaking. In particular, two concerns of TPP critics merit closer attention: new obligations prohibiting currency manipulation and the controversial ISDS provisions.<sup>20</sup> Reopening the TPP could fix these issues relatively easily and attract bipartisan support in Congress.

### Currency Provisions

Commitments undertaken by TPP countries regarding currency manipulation in a declaration issued in parallel to the TPP text should be incorporated in the TPP and subject to its binding dispute settlement procedures (for detail, see Bergsten and Schott 2016). This amendment would be a major change in the TPP and would address one of the top criticisms of the pact by members of both parties. Such a change should be consistent with new provisions of US law in the Trade Enforcement and Trade Facilitation Act, enacted in February 2016, that are designed to deter the types of predatory practices common among some Asian countries during the past decade. The substance of such currency provisions could be taken off the shelf from the Joint Declaration, with some refinement regarding the definition of currency manipulation drawing on the new US law.

Other TPP countries should accept this major addition—it’s a small price to pay to secure a comprehensive Asia-Pacific pact. Japanese support in particular is critical; while wary of TPP provisions on currencies, the country did already sign the Joint Declaration and has accepted similar commitments in the G-7. Moreover, Japan doesn’t have to change its current policies, assuming the TPP definition of currency manipulation tracks US law and avoids quantitative easing policies (as both the United States and Japan will insist). At the same time, none of the other TPP countries currently engage in currency manipulation, so they too would not have to change existing policies—though they would have to accept constraints on their ability to pursue competitive devaluation or inhibit appreciation of their currencies.

20. This section draws heavily from Jeffrey J. Schott, “TPP Can Be Fixed If You Know What’s Wrong with It,” Trade and Investment Policy Watch blog, December 5, 2016, <https://piie.com/blogs/trade-investment-policy-watch/tpp-can-be-fixed-if-you-know-whats-wrong-it> (accessed on January 11, 2017).

## Investor-State Dispute Settlement

Regarding ISDS, there are two options for TPP fixes: revise the current procedures or drop them entirely. Given that choice, Main Street Republicans and many multinational corporations probably would favor additional procedural reforms. While the TPP already improves significantly on past FTA practice by clarifying the rights of governments to regulate in the public interest (among other reforms), more could be done (Hufbauer 2016). In the financial services sector, the use of ISDS is subject to specific clearances by national authorities before private litigation can proceed (Gelpern 2016). Broadening this precedent, the TPP could be revised to add a requirement that each ISDS petition be reviewed within 30 days of submission by a government legal authority to ensure that the claim is qualified for ISDS proceedings. This review would essentially provide a preclearance to start ISDS litigation; it would constrain abusive litigation but would not deny private investors the right to arbitration panels.

But grassroots Trump supporters may disagree and demand the removal of ISDS altogether. These groups reflect populist concerns, related to past FTA provisions and practice, that ISDS challenges give too much power to multinational corporations and have the potential to undercut regulatory protections or blunt new regulatory proceedings.

Eliminating ISDS entirely was considered and rejected during the TPP negotiations because some developing countries regarded ISDS as helpful in both reinforcing rule of law in their national systems and providing greater predictability for investors—all past US FTAs except the US-Australia trade deal include the mechanism. It does help protect US investment abroad, which is valuable in countries where the rule of law and judicial processes are substandard. But most countries today are trying to attract investment and so have an incentive to avoid indirect expropriations that could harm their reputation and discourage new investors. In short, this useful process may not be worth the political baggage it imposes on trade agreements and could be deleted in a new Asia-Pacific pact.<sup>21</sup>

## FURTHER AREAS OF CONCERN

Significant changes in currency and ISDS would build on several TPP compromises pursued by the Obama administration following the conclusion of the trade deal. Indeed, to build support for a congressional vote, the Obama administration had begun addressing residual concerns of

21. Note, this change would also inadvertently resolve the opposition of some members of Congress to the TPP carveout of specific industries, namely tobacco, from ISDS procedures.

congressional members about the terms of the final deal—specifically the decision to exempt financial services from the TPP’s ban on data localization requirements<sup>22</sup> and the shorter data exclusivity period required for pharmaceutical drugs called biologics<sup>23</sup>—compared with existing US law. In financial services, the compromise was to seek enforceable obligations on data localization in future negotiations, including for potential new entrants to the TPP, and in separate, ongoing plurilateral talks with TPP members.<sup>24</sup> And the Obama administration was working with Senator Orrin Hatch to elicit greater clarification and transparency from TPP country regulatory plans to implement such protections for biologics.<sup>25</sup> Both these changes could be introduced in a restructured Asia-Pacific deal.

To be sure, the TPP also falls short in some other areas in terms of incomplete liberalization and inadequate rules particularly in regards to US concessions (for detail, see Cimino-Isaacs and Schott 2016). The list is not exhaustive but includes

- slow liberalization of autos, including tariffs and origin rules, and no significant changes in certain agricultural sectors, namely US sugar and dairy programs;
- limited new services and procurement liberalization; and
- few disciplines related to energy subsidies and other measures that distort supply and demand for fossil fuels and renewable energy supplies.

Most of these reflect congressional concerns about the TPP’s impact on current US programs, resulting in decisions to make exceptions for US policies. If US negotiators want to elicit more liberalization from Asia-Pacific trading partners in a new deal, no doubt these exceptions would have to be revisited.

22. Data localization mandates require companies to establish local computing and data storage facilities as conditions for doing business.

23. Data exclusivity provisions require confidentiality of “marketing data”—scientific evidence showing that a product is safe and efficacious—for at least five years for pharmaceutical drugs and eight years or at least five years combined with other measures for biologics.

24. “Financial services industry presses Congress to pass TPP this year, touts data fix,” *Inside US Trade*, October 26, 2016, [www.insidetrade.com](http://www.insidetrade.com) (accessed on January 12, 2017).

25. “Sources: Administration close to reaching biologics solution with Hatch,” *Inside US Trade*, November 3, 2016, [www.insidetrade.com](http://www.insidetrade.com) (accessed on January 12, 2017).

## BROADER PARTICIPATION

Reopening trade negotiations also allows the addition of new participants. Those that had been most interested in joining a high-standard Asia-Pacific pact included Korea, Taiwan, and Colombia. Inviting these countries to join the original TPP signatories in a broader Asia-Pacific trade initiative would provide several additional benefits.

First, the cumulative GDP of these countries is almost \$2.5 trillion, so adding them to the pact would open significant new opportunities for US firms and workers.

Second, the inclusion of Korea and Colombia would provide the means to revise and upgrade US bilateral pacts originally signed about a decade ago and to fix problems that have occurred in the implementation and enforcement of those pacts.

Third, broader participation provides a more promising option to reinforce trade ties with Taiwan than pursuing a bilateral deal. And fourth, a broader deal restores and reinforces US economic engagement in the Asia-Pacific and strengthens US strategic alliances with important partners in the region.

## CONCLUSION

The Trump administration has an opportunity to formulate a new policy for trade with Asia-Pacific nations. As suggested above, restructuring the TPP deal designed and developed by the Bush and Obama administrations would remedy key problems with the TPP cited during the campaign and yield important new benefits for the US economy. Recommendations include adding enforceable currency manipulation provisions to the main trade deal and omitting the ISDS provision. A broader, renamed Asia-Pacific deal that includes Korea, Colombia, and Taiwan, among others, would significantly expand the value of the original TPP deal, achieve greater regional integration, and expend less US political capital than a country-by-country bilateral approach.



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