

FROM EAST ASIAN FTAS TO AN EAFTA

Typology of East Asian FTAs and Implications for an EAFTA

Chang Jae Lee, Hyung-Gon Jeong,
HanSung Kim, and Ho Kyung Bang

EAFTA

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Preface

Although functional economic integration in terms of trade and investment proceeded quite rapidly among East Asian economies, it was only recently that institutionalization of regional economic integration was started among East Asia countries. The first ASEAN+3 (China, Japan, and Korea) Summit Meeting was held in Kuala Lumpur in 1997, and the first bilateral Free Trade Agreement (FTA) between East Asian countries was signed between Japan and Singapore in 2002.

Since then, however, some East Asian countries adopted active FTA policies and concluded many FTAs. As a result, there are several FTAs between East Asian countries and regions, such as the Korea-Singapore FTA, the Japan-Malaysia Economic Partnership Agreement (EPA), the Japan-Philippines EPA, ASEAN-China Trade in Goods Agreement, the Korea-ASEAN Trade in Goods Agreement, China-Hong Kong Closer Economic Partnership Arrangement (CEPA), and the China-Macao CEPA, in addition to the Japan-Singapore EPA. In addition, there exist many ongoing FTA negotiations between East Asian countries, including ASEAN-Japan FTA.

The FTAs among East Asian countries proliferate with such a speed that there is a growing concern that increasing FTA webs may hinder producing “spaghetti bowl” phenomenon rather than facilitate intraregional trade in East Asia. Therefore, the need for a region-wide FTA seems to be emerging in East Asia.

Compared to Europe and North America, East Asia is the only major economic region in the world without any region-wide FTA. Furthermore, given the growing interdependence of East Asian economies in terms of trade and investment, the rationales for an East Asia FTA (EAFTA) seem to be evident. However, there exist also serious obstacles to an EAFTA such as diversity of economic development levels among East Asian countries and the lack of regional awareness.

Under these circumstances, this study aims to contribute to the debate on the formation of an EAFTA. In order to do that, it analyzes the contents of existing FTAs between East Asian countries, focusing their tariff concession structure, rules of origin and service and investment treatment, and on the basis of these analyses, it proposes a feasible and desirable type of an EAFTA. In

addition, this study also suggests the prospects for an EAFTA, as well as the future tasks needed for East Asian countries and Korea, in particular, to facilitate its formation.

This study was conducted by Dr. Chang Jae Lee, Dr. Hyung-gon Jeong, Dr. HanSung Kim, and Mr. Ho Kyung Bang, all of them from KIEP. The authors want to express their sincere gratitude to Mr. Chang Sang Cho, Dr. Sijoong Kim, Dr. Yanghee Kim, Mr. Yungmoo Kim, Dr. Jun Sung Ko, and Dr. Inwon Park for their helpful comments made in the process of this study.

I hope that this study can be used as a reference to those researchers and policy makers, who feel the need for a region-wide FTA in East Asia, and want to find ways to achieve it.

Kyung Tae Lee

President, Korea Institute for International Economic Policy

Executive Summary

As the number of Free Trade Agreements (FTAs) between East Asian countries continues to increase, the need for a region-wide FTA is emerging in East Asia. The main objective of this study is to develop the current study on the East Asia FTA (EAFTA) by suggesting likely options of an EAFTA that will both be feasible and desirable.

To search for an optimal EAFTA, this study analyzes the characteristics of six FTAs between East Asian countries, i.e. the ASEAN Free Trade Area (AFTA), the ASEAN-China FTA (ACFTA), the Korea-ASEAN FTA (KAFTA), the Japan-Singapore Economic Partnership Agreement (JSEPA), the Korea-Singapore FTA (KSFTA), and the Japan-Malaysia EPA (JMEPA). Although the policies and instruments in existing FTAs cannot be directly transposed to an EAFTA, they are quite likely to serve as reference points in the future.

Chapter II examines the tariff concession structure of the six FTAs. The tariff concession structure of these FTAs can be grouped into two categories: an ASEAN-type approach and item-by-item approach. The ASEAN-type approach divides tariff items first according to their sensitivity in the Normal Track and Sensitive Track. For those tariff items belonging to the Normal Track, they can be further divided into i) tariffs that will be eliminated when the FTA comes into force and ii) tariffs that will be eliminated within predefined years. Those items belonging to the Sensitive Track will be further divided into the Sensitive List and the Highly Sensitive List, depending on their degree of sensitivity. AFTA, ACFTA and KAFTA belong to this ASEAN-type approach. ACFTA differs from other agreements in having an Early Harvest Program.

The other type is the item-by-item approach, which sets tariff elimination schedules for each tariff item. KSFTA, JSEPA, and JMEPA have adopted this approach. This approach can produce a number of different tariff concession structures depending on partner countries, as we see in JSEPA and JMEPA.

This chapter also attempts to assess the quality of existing FTAs among East Asian countries in terms of trade liberalization in goods by analyzing the share of tariff lines in the Highly Sensitive List or the tariff lines of excluded items, in terms of both the number of tariffs and share of imports. Our results indicate that the quality of trade liberalization varies significantly among the FTAs. First, those FTAs involving ASEAN countries show relative overall weaknesses, mainly due to the CLMV countries (Cambodia, Laos, Myanmar,

and Vietnam). Our analysis also reveals that within an FTA, there often exist asymmetrical situations in terms of trade liberalization among participant countries. However, it was difficult to conduct a more rigorous comparison among these FTAs due to the different use of classification systems in East Asian countries. For instance, Korea uses HS 10-digit codes, Japan and Malaysia use HS 9-digit codes, and China and the Philippines use HS 8 digit codes, whereas for some sectors, only HS 6-digit data were available.

From our analysis, we also identify the sensitive sectors in a select number of countries. In particular, agriculture and fishery are the most sensitive sectors for both Korea and Japan. However, a more detailed comparison was once again difficult to make because of the use of different classification systems in East Asia.

Overall, although Korea and China show much more willingness in terms of trade liberalization in goods compared to the CLMV countries, the level of trade liberalization is also limited due to the existence of sensitive sectors. Japan is also quite reluctant to open its market, especially for agricultural and fishery products. It is, therefore, difficult to make a strong case that existing FTAs between East Asian countries are of high quality in terms of market access for goods.

Chapter III investigates the rules of origin in East Asian FTAs. Rules of origin are laws and administrative practices used to identify the country of origin of internationally traded goods. They are needed to limit the trade gains from FTAs within participating countries. However, they are sometimes looked upon as necessary evils because they may distort markets and can be used as instruments to protect domestic industries.

Examining the six intra-regional FTAs, we observe that the AFTA and ACFTA have simple and compact rules of origin; for most products which are not wholly obtained and produced, rules of origin requires that non-originating import contents not exceed 60% or that the originating content is more than 40% of the FOB price of the product. On the other hand, rules of origin for KAFTA, KSFTA and those between Japan and two ASEAN member countries are based on product specific. These FTAs adopt changes in tariff classifications and use the percentage criteria as the main decision instrument. However, at the product specific level, the criteria of conferring originating status varies and there are situations in which a country imposes different rules of origin for an identical product in different FTAs.

The “rules of origin” clause reflects the bilateral (or multilateral) relationship between participating countries. What Country A adopts with Country B in one

agreement can be a rule that Country A wants to avoid with Country C in another. This may cause complexities in the rules of origin in East Asia and it will become a critical factor that deters improving economic integrity in East Asia.

As a measure to mitigate the problem of rules of origin in East Asia, we look at the possibility of introducing diagonal cumulation. Given the web of bilateral FTAs in East Asia, diagonal cumulation may be the best way to integrate the East Asian economies into one single territory, at least in terms of the production side of the economy. However, each country may have a different perspective on this matter and introducing diagonal cumulation to East Asia may not be as easy as it seems. However, if countries in the East Asian region acknowledge the need for regional integration and regard the EAFTA as a common goal, diagonal cumulation will not be impossible to achieve. Furthermore, diagonal cumulation can be considered as an intermediate target for the EAFTA. By reaching this intermediate target, we can reduce the market distortion effects of rules of origin in the region, increasing integrity in the region as a single production market and creating a better position to move forward with the EAFTA.

Chapter IV analyzes the characteristics of FTAs related to service and investment in East Asia. In the FTA between Korea and Singapore, a negative list method has been adopted to expand service and investment liberalization. With leading competitiveness in services, Singapore has a higher degree of market opening for its service sector (95.6% vis-à-vis Korea) than Korea (72.3% vis-à-vis Singapore).

The opening ratio for Japan's service sector is 68.4% vis-à-vis Singapore, while Singapore's opening ratio is 66.2% vis-à-vis Japan. By adopting mechanisms like the positive list method, etc., Japan has chosen to contract a defensive EPA with Singapore. In its EPA with Malaysia, Japan has restricted the liberalization of its service sector by stipulating that certain commitments can be modified or cancelled in the schedule of specific commitments. In its EPAs with Singapore and Malaysia, Japan has especially focused on intellectual property rights. Due to the weak competitiveness of its service industry, Malaysia has a low degree of service market opening at 27.7% vis-à-vis Japan.

Trade and investment facilitation is generally not an important item when dealing with FTAs. However, in East Asia, where there exist large gaps in economic development levels among countries, trade and investment facilitation is of particular importance. AFTA, JSEPA and JMEPA ensure a higher level of trade and investment facilitation than KSFTA. This is because both AFTA and

Japan's EPAs are approached as a form of economic cooperation. With regard to development cooperation, there has not been any significant measure in the East Asian FTAs we examined, even those it would be important element for an EAFTA given the disparity in economic development levels among East Asian countries.

The last chapter suggests likely prospects for an EAFTA and proposes possible options of an EAFTA based on the analyses in the previous chapters. In addition, it also provides policy implications regarding the formation of an EAFTA for the governments of East Asia, with special regard to the Korean government.

As for the prospects of an EAFTA, after having examined rationales and obstacles, three plausible scenarios to an EAFTA are presented. The issues of membership and schedule are also discussed. With regard to the possible types of EAFTA, if East Asian countries choose to form an EAFTA that is to co-exist with other East Asian FTAs, this will result in a complex, multi-layered FTA web in East Asia. One advantage of this type of EAFTA is that it will be relatively easy to negotiate politically. However, since such an EAFTA would not prevent the "spaghetti bowl" phenomenon, one may question the rationality of creating a region-wide FTA that would only serve symbolic purposes. Another option would be to pursue a high quality EAFTA that would replace the majority of FTAs among East Asian countries. However, our analysis of existing FTAs in East Asia shows that given the diversity of East Asian economies, it would be rather difficult to agree upon a high-quality EAFTA in the near future. Nevertheless, it is precisely this sort of EAFTA that would maximize economic benefits, preventing the further proliferation of bilateral FTAs in the area.

One way of avoiding this dilemma altogether is by developing an EAFTA with i) a relatively flexible tariff concession structure, ii) simple and liberal rules of origin, iii) strengthened trade and investment measures, and iv) a concrete development cooperation mechanism. This type of EAFTA would probably not replace existing FTAs in high numbers, but it would be more than symbolic and palpably contribute to creating freer trade and investment in East Asia.

Furthermore, the last chapter also provides policy implications regarding the formation of an EAFTA. In particular, this study proposes that the Korean government take the initiative and continue feasibility studies on an EAFTA, such as those conducted by the Joint Expert Group. Another important task to successfully realize an EAFTA is related to Northeast Asian countries. Since an

EAFTA cannot be realized until the establishment of a de facto China-Japan-Korea FTA, the three Northeast Asian countries must not neglect the importance of a CJK FTA in the establishment of an EAFTA. In this regard, it is suggested that the Korean government act as a facilitator persuading both China and Japan of the importance of a CJK FTA in achieving an EAFTA. As an alternative, the Korean government can also facilitate the formation of a CJK FTA and the EAFTA by concluding a Korea-Japan FTA and a Korea-China FTA as a first order.

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I. Introduction

Along with globalization, regionalism has become a global phenomenon in the world today. However, it was only after the outbreak of the Asian financial crisis in 1997 that really prompted East Asia to seriously consider economic regionalism. The first ASEAN+3 (China, Japan, and Korea) Summit Meeting was held in Kuala Lumpur in December 1997; since then, the summit has become an annual event. In addition, various ASEAN+3 Ministerial Meetings and Senior Officials Meetings have taken place regularly since 2000 to complement the Summit Meetings. Thus, in the wake of the Asian financial crisis, a basic institutional framework for regional economic cooperation was established in East Asia.¹⁾

Furthermore, other East Asian countries belatedly jumped on the Free Trade Agreement (FTA)²⁾ bandwagon in the early 2000s.³⁾ Among these countries, Singapore has by far the most active FTA policy. Singapore signed the Closer Economic Partnership Agreement with New Zealand in November 2000 and the Economic Partnership Agreement (EPA) with Japan in January 2002, which was then the first bilateral FTA between two East Asian countries. Since that time, Singapore has concluded bilateral FTAs with countries, such as the European Free Trade Association (EFTA),⁴⁾ Australia, the United States, Jordan, India, Korea, and Panama, and has formed the Trans-Pacific Strategic Economic Partnership Agreement (SEP) with Brunei, New Zealand, and Chile.

1) East Asia includes Northeast Asia and Southeast Asia. However, when it comes to institutional economic integration, the East Asia countries will often be used in this study as a synonym for the ASEAN+3 countries.

2) In this study, the term "FTA" will also be used synonymously with "RTA (Regional Trade Agreement)," which includes (1) customs unions and FTAs (in the strict sense of the word) reported under GATT Article XXIV, (2) preferential arrangements under the enabling clause, and (3) service agreement under GATS Article V.

3) Before these new waves of FTAs, the ASEAN Free Trade Area (AFTA) and three other preferential arrangements (Bangkok Agreement, Bangkok Agreement- Accession of China, and Laos-Thailand Preferential Arrangement), all of them reported under the enabling clause, were the only RTAs in East Asia (http://www.wto.org/english/tratop_e/region_e/region_e.htm).

4) Switzerland, Iceland, Liechtenstein, and Norway are the members of the EFTA.

Another country that has actively pursued FTAs in recent years is Thailand, which has signed FTAs with Australia, New Zealand, Peru, India, and the BIMSTEC (Bangladesh India Myanmar Sri Lanka Thailand Economic Cooperation).

The three Northeast Asian countries—Japan, Korea, and China—have also shown great interest in bilateral FTAs. Japan has signed EPAs with Singapore, Mexico, Malaysia, and the Philippines. Korea has signed FTAs with Chile, Singapore, and the EFTA, as well as a Trade in Goods Agreement with ASEAN (excluding Thailand). As for China, it has signed Closer Economic Partnership Arrangements (CEPA) with Hong Kong and Macao, a Trade in Goods Agreement with ASEAN, and two FTAs with Chile and Pakistan.

Among the FTAs in Table I-1, 16 have been notified to the GAT/WTO and have been in force as of September 15, 2006. Moreover, there now exist several FTAs between East Asian countries, such as the Japan-Singapore EPA,

Table I-1. FTAs concluded or under negotiation by East Asian countries (as of November 2006)

| | Korea | China | Japan | Singapore | Thailand | ASEAN |
|-------------------|---|---|---|--|--|-------------------------|
| Concluded | Chile* Singapore* EFTA* ASEAN | ASEAN* Hong Kong* Macao* Chile Pakistan | Singapore* Mexico* Malaysia* Philippines | AFTA*, New Zealand*, Japan*, EFTA*, Australia*, USA*, Jordan*, Chile, Korea*, India, Panama, Trans-Pacific SEP | AFTA, Australia*, New Zealand*, Peru, India, BIMSTEC | AFTA*, China*, Korea |
| Under Negotiation | Japan Canada Mexico India USA | New Zealand GCC Australia Singapore | Korea Thailand ASEAN Indonesia Chile Brunei GCC | Bahrain, Canada China, Egypt, Mexico, Pakistan, Peru Sri Lanka Kuwait, Qatar, UAE | USA, Bahrain | CER, Japan, India |

Note: * Notified to GATT/WTO and in force as of September 15, 2006;

GCC (Gulf Cooperation Council: Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and UAE); CER (Closer Economic Relations: Australia and New Zealand).

Source: Compiled by authors based on data from documents and official websites of East Asian countries, ASEAN and the WTO.

the Korea-Singapore FTA, the ASEAN-China FTA, the Korea-ASEAN FTA, the Japan-Malaysia EPA, the Japan-Philippines EPA, the China-Hong Kong CEPA, and the China-Macao CEPA.

In addition, there are also a number of ongoing FTA negotiations between East Asian countries. For instance, out of the 25 FTAs currently under negotiation in East Asia, 6 are intra-regional FTAs between East Asian countries.

With the rapid rise of bilateral FTAs in reaction to the Asian financial crisis, there were increasing calls for the establishment of an East Asia FTA (EAFTA). On October 31, 2001, the East Asia Vision Group (EAVG) made an official recommendation in a report submitted to the leaders of ASEAN+3 pertaining to the formation of an "East Asia Free Trade Area." Moreover, on November 4, 2002, the East Asia Study Group (EASG) also proposed the pursuit of an EAFTA.

However, no serious efforts were made until the 8th ASEAN+3 Summit in Vientiane on November 29, 2004, which welcomed the decision by the ASEAN+3 Economic Ministers to set up an expert group to conduct a feasibility study regarding the EAFTA. Following four workshops, the Joint Expert Group on EAFTA Feasibility Study submitted its report to the ASEAN+3 Economic Ministers on August 23, 2006. However, despite these efforts, the EAFTA failed to make it on the economic cooperation agenda at the 10th ASEAN+3 Summit in 2006.

Objectives and Structure

To date, numerous studies have touched upon various topics, including functional economic integration among East Asian countries and regions, recent developments in the institutionalization of East Asian economic integration (including its prospects), and the economic effects of an EAFTA.⁵⁾

Based on the findings of these studies, as well as of the Joint Expert Group Report, this study deepens the ongoing debate on the EAFTA by examining the type of EAFTA that would be most feasible and desirable. In order to advance discussions on the EAFTA, it is necessary to go beyond abstract prospects of

5) See Lee (2005) and Urata (2004) for functional economic integration and recent developments in regionalism in East Asia. See also Chirathivat (2004) and Urata et al. (2003) for the economic effects of an EAFTA. See Kwon et al. (2005), which deals with all issues mentioned above.

an EAFTA and examine concrete models, as the effects will be significantly different depending on the type of EAFTA concluded.

In developing feasible concrete models, we turn to existing FTAs between East Asian countries for insight: the ASEAN Free Trade Area (AFTA), the China-ASEAN Trade in Goods Agreement, the Korea-ASEAN Trade in Goods Agreement, the Japan-Singapore FTA, the Korea-Singapore FTA, and the Japan-Malaysia FTA.⁶⁾ Although an EAFTA cannot be formed directly from these existing FTAs, they serve as useful reference points. Analyzing these FTAs will allow us to identify common characteristics as well as differences. It is also expected that the limitations of existing East Asian FTAs will be revealed.

Since market access for goods constitutes one of the main elements of any FTA, we start off by analyzing the tariff concession structure of existing FTAs in the following chapter. This will reveal the quality of these FTAs in terms of coverage, the degree of trade liberalization, and the sensitive sectors in the East Asian economies.

The proliferation of bilateral FTAs between East Asian countries has raised concern regarding the so-called spaghetti bowl phenomenon,⁷⁾ a direct result of the diverse rules of origin adopted in East Asia. The third chapter compares the rules of origin in existing FTAs building a rationale, as well as drawing policy implications, for the formation of an EAFTA.

In the fourth chapter, service and investment liberalization and other issues, such as trade and investment facilitation measures and elements related to development cooperation, are addressed.

Finally, in the last chapter, we suggest likely prospects for an EAFTA. After examining rationales and obstacles, we present plausible scenarios, discuss membership issues, and draft a schedule for the EAFTA. We then propose possible EAFTA options based on the analyses in previous chapters, highlighting the relationship between the EAFTA options and bilateral FTAs—existing and forthcoming. This chapter ends with policy implications regarding the formation of an EAFTA for the governments of East Asian countries, with special regard to the Korean government.

6) Due to their specific nature, the Bangkok Agreement and the Laos-Thailand Preferential Arrangement will not be examined, whereas the Japan-Philippines EPA, which was concluded on September 9, 2006, cannot be covered due to a lack of detailed information so far.

7) Bhagwati and Panagariya (1999), p. 77.

Six Existing FTAs between East Asian Countries

Before conducting detailed analyses of the tariff concession structure, rules of origin, service and investment liberalization, and other issues, let us take a brief look at the basic framework of the six existing FTAs.

ASEAN has promoted economic integration since the early 1990s and the earliest realization of intraregional FTAs among East Asian countries was the AFTA. The AFTA was one of the first endeavors to achieve a closer economic relationship among member countries and was later developed into the AFTA-plus, which included the ASEAN Framework Agreement on Services (AFAS), the ASEAN Investment Area (AIA), the ASEAN Industrial Cooperation (AICO), and other program initiatives.

ASEAN has tried to achieve economic integration through two major instruments: the Agreement on a Common Effective Preferential Tariff (CEPT), which covers the elimination or reduction of tariffs imposed on goods; and, the AFAS, which is concerned with removing trade barriers in services among ASEAN member countries. The CEPT has set its target year for removing tariffs by 2010 for the ASEAN-6⁸⁾ countries and by 2015 for the CLMV countries.⁹⁾ On the other hand, AFAS has already conducted three rounds of negotiations, with the fourth concluding at the end of 2006. Each round sets Schedules of Specific Commitments for each country, which forces countries to open more service markets more as each round goes by.

The ASEAN-China FTA and the Korea-ASEAN FTA are similar in the sense that they both deal with liberalization in trade and services separately. Both FTAs have concluded agreements on trade in goods, but negotiations on trade in services and investment are still underway. It is reported that one of the major reasons for taking a separate approach toward trade in goods and services is to expedite the negotiation process. As ASEAN countries are reluctant to open their service markets to China or Korea, it would be very difficult to finalize the deal if both goods and services were included in the agreement.

In contrast, goods and services are covered simultaneously in the Korea-Singapore FTA. Reaching a final agreement was deemed relatively easier in this case as both countries have similar stages of economic development.

Japan, on the other hand, has ratified two EPAs with ASEAN member countries—Singapore and Malaysia. The FTAs between Japan and Singapore, as well as between Japan and Malaysia, use the terminology EPA rather than FTA.

8) Brunei Darussalam, Indonesia, Malaysia, the Philippines, Singapore, and Thailand.

9) Cambodia, Lao PDR, Myanmar, and Vietnam.

According to Japanese explanations, EPAs are different from FTAs in the sense that they focus more on mutual economic cooperation.¹⁰⁾ In addition, EPAs cover the liberalization of both trade in goods and services and include contents regarding bilateral economic cooperation.

10) Ministry of Economy, Trade and Industry (2003).

II. Market Access for Goods in East Asian FTAs

1. ASEAN Free Trade Area (AFTA)

The main characteristics of the AFTA in terms of tariff reductions for goods seem to be flexibility and gradualism. The tariff reduction schedule differs for the ASEAN-6 and CLMV countries and it also varies, sometimes significantly, between members of the two groups. Its other key characteristic is that its tariff concession structure consists of an Inclusion List and a Sensitive Track, with some products in the latter gradually transferring to the former.

The Agreement on a Common Effective Preferential Tariff (CEPT) Scheme for the AFTA was signed on January 28, 1992. As illustrated in Figure II-1, the CEPT consists of products in the Fast Track and those in the Normal Track. In addition, there are products not yet included in the CEPT, i.e. products in the Temporary Exclusion List (TEL), the Sensitive List (SL), and the General Exception List (GE), with corresponding MFN tariff rates.¹¹⁾

The ending years of the tariff reduction schedules differ from country to country based on the date that the CEPT Agreement was implemented. The final year for the six initial signatories to the CEPT Agreement (ASEAN-6) was 2003. Fast Track products were to have had their tariffs reduced to 0-5 percent by the year 2000 at the latest, whereas Normal Track products were to have their tariffs reduced to 0-5 percent by 2003. The ending year for Vietnam is 2006, 2008 for Lao PDR and Myanmar, and 2010 for Cambodia.¹²⁾

Products in TEL were to be phased into the Inclusion List on specified dates, namely by 2000 for most manufactured products (2003 for Vietnam, 2005 for Lao PDR and Myanmar, and 2007 for Cambodia) and by 2003 for unprocessed agricultural products (2006 for Vietnam, 2008 for Lao PDR and Myanmar, and 2010 for Cambodia).¹³⁾

11) *Agreement on the Common Effective Preferential Tariff Scheme for the ASEAN Free Trade Area; Protocol on the Special Arrangement for Sensitive and Highly Sensitive Products.*

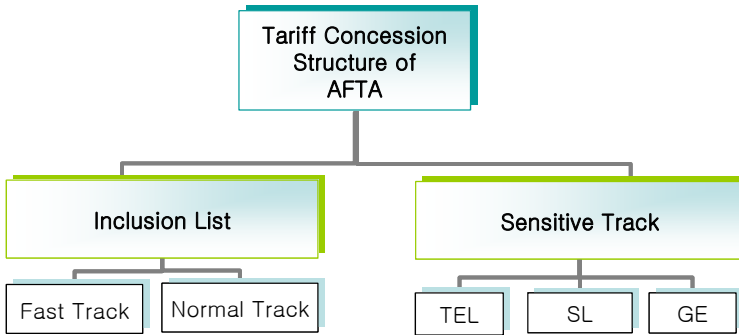
12) *Agreement on the Common Effective Preferential Tariff Scheme for the ASEAN Free Trade Area.*

13) *Protocol Regarding the Implementation of the CEPT Scheme Temporary Exclusion*

Products in SL are mainly unprocessed agricultural products that are granted a more flexible arrangement for phasing into the Inclusion List: i.e., beginning in 2001-2003 and ending in 2010 (2013 for Vietnam, 2015 for Laos and Myanmar, and 2017 for Cambodia).

Products under General Exception are those permanently excluded from the scheme for reasons of national security, protection of public morals, protection of human, animal, or plant life, health, and the protection of articles of artistic, historic, and archaeological value.

Figure II-1. Tariff Concession Structure of AFTA, 2001



The decision to eliminate import duties on all products by the year 2015 for the ASEAN-6 members by 2018 for the new ASEAN members (CLMV) was made on September 29, 1999 at the Thirteenth AFTA Council Meeting.¹⁴⁾

On January 31, 2003, the agreement was amended as follows: 1) the ASEAN-6 members shall eliminate import duties on at least 60 percent of the products in the Inclusion List by January 1, 2003, while tariffs on the remaining 40 percent of the Inclusion List shall be eliminated not later than January 1, 2010; 2) the CLMV shall eliminate import duties on products in the Inclusion List by January 1, 2015. However, flexibility to defer the elimination of duties to January 2018 for some products in the Inclusion List deemed sensitive shall be allowed for all ASEAN countries.¹⁵⁾

List.

14) Protocol to Amend the Agreement on the Common Effective Preferential Tariff (CEPT) Scheme for the ASEAN FTA for the Elimination of Import Duties.

15) *Ibid.*

Table II-1 shows the tariff structure of major ASEAN countries. In terms of the number of tariff lines, the share of products belonging to the Sensitive Track is slightly higher in Malaysia (3.4 percent) and Brunei (3.3 percent) compared to the other ASEAN-6 countries in 2001, while Vietnam's share is noticeably higher (22 percent). As shown in Table II-2, in terms of the size of imports from the world, the share of products belonging to the Sensitive Track is quite substantial in Indonesia (9.8 percent), while it is very small in Thailand (0 percent).

Table II-1. The Tariff Structures of Major ASEAN Countries, 2001

(number, percent)

| | Number of Tariffs | FT | NT | TEL | SL | GE |
|-------------|-------------------|-----------------|-----------------|-----------------|-------------|--------------|
| Malaysia | 10,393 | 3,192 (30.7) | 6,847 (65.9) | 218 (2.1) | 83 (0.8) | 53 (0.5) |
| Brunei | 6,492 | 2,495 (38.4) | 3,781 (58.2) | 0 (0) | 14 (0.2) | 202 (3.1) |
| Singapore | 5,859 | 0 (0) | 100 (100) | 0 (0) | 0 (0) | 0 (0) |
| Philippines | 5,658 | 1,029 (18.2) | 4,547 (80.4) | 6 (0.1) | 60 (1.1) | 16 (0.3) |
| Thailand | 9,111 | 2,969 (32.6) | 6,135 (67.3) | 0 (0) | 7 (0.1) | 0 (0) |
| Indonesia | 7,285 | 2,108 (28.9) | 5,084 (69.8) | 21 (0.3) | 4 (0.1) | 68 (0.9) |
| Vietnam | 6,391 | 0 (0) | 4,984 (78.0) | 1,217 (19.0) | 51 (0.8) | 139 (2.2) |

Source: Calculated by authors from the *Consolidated 2001 CEPT Package*.

Each year ASEAN countries report their tariff concession schedules to the ASEAN Secretariat. The tariff concession structure of the AFTA based on the Consolidated 2006 CEPT Package is presented in Figure II-2. This figure shows that the 2006 tariff concession structure of AFTA has been simplified compared to its 2001 version. It now consists of an Inclusion List and a Sensitive Track and the latter includes a Highly Sensitive List (HSL) and a General Exception List (GE).¹⁶⁾

Table II-2. Share of Major ASEAN Countries' Imports from the World by Tariff Structure, 2001

| | (percent) | | | | |
|-------------|-----------|------|-----|-----|-----|
| | FT | NT | TEL | SL | GE |
| Malaysia | 57.5 | 39.5 | 1.6 | 1.3 | 0.1 |
| Philippines | 42.0 | 55.4 | 0.2 | 2.4 | 0 |
| Thailand | 22.3 | 77.7 | 0 | 0 | 0 |
| Indonesia | 22.0 | 68.2 | 3.2 | 6.5 | 0.1 |

Source: Calculated by authors from Table II-1 and data from *COMTRADE*.

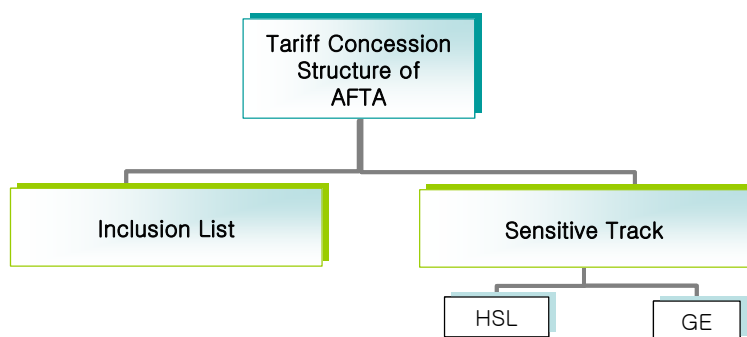
Figure II-2. Tariff Concession Structure of AFTA, 2006

Table II-3 shows the tariff structure of ASEAN-6 in 2006. Among the ASEAN-6, only Singapore and Thailand do not have any products belonging to the Sensitive Track. On the other hand, Indonesia and the Philippines have products in both the HSL and GE List, while Malaysia and Brunei only have products in the GE List. Compared to 2001, the share of products belonging to the Sensitive Track has generally decreased. However, in terms of tariff lines, the share of products in the GE List increased in Malaysia (from 0.5 percent to 0.7 percent) and Brunei (from 3.1 percent to 7.3 percent), while it remained the same in Indonesia. In terms of the size of global imports, the share of products belonging to the Sensitive Track also shows a decrease (see Tables II-2 and II-4).

Table II-3. The Tariff Structure of ASEAN-6, 2006

| (number, percent) | | | | |
|-------------------|--------------|------------------|-------------|--------------|
| | Tariff Items | IL (percent) | HSL | GE |
| Singapore | 10,705 | 10,705 (100) | 0 | 0 |
| Malaysia | 12,591 | 12,502 (99.3) | 0 | 89 (0.7) |
| Brunei | 10,702 | 9,924 (92.7) | 0 | 778 (7.3) |
| Philippines | 11,091 | 11,045 (99.6) | 19 (0.2) | 27 (0.2) |
| Thailand | 11,030 | 11,030 (100) | 0 | 0 |
| Indonesia | 11,153 | 11,028 (98.9) | 25 (0.2) | 100 (0.9) |

Source: Calculated by authors from the *Consolidated 2006 CEPT Package*.

Table II-4. Share of Major ASEAN Countries' Imports from the World by Tariff Structure, 2006

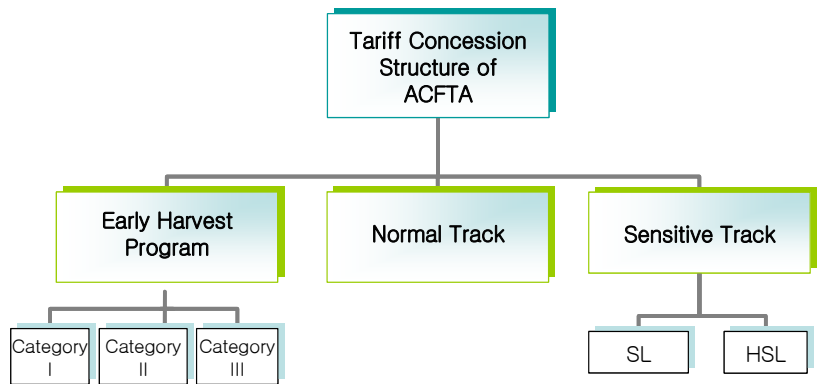
| (percent) | | | |
|-------------|------|-----|-----|
| | IL | HSL | GE |
| Malaysia | 99.8 | 0 | 0.2 |
| Philippines | 98.8 | 1.2 | 0 |
| Thailand | 100 | - | - |
| Indonesia | 98.4 | 1.1 | 0.4 |

Source: Calculated by authors from Table II-3 and data from *COMTRADE*.

2. ASEAN-China FTA

The ASEAN-China FTA (ACFTA) has a similar tariff concession structure as the AFTA. It consists of a Normal Track and a Sensitive Track. Its main difference from the AFTA is that, in addition to the two pillars, it also includes an Early Harvest Program.¹⁷⁾

Figure II-3. Tariff Concession Structure of ACFTA



2.1. Early Harvest Program

All products in the following chapters at the 8 or 9 digit level (HS Code) are covered by the Early Harvest Program, unless otherwise excluded by a party in its Exclusion List as set out in Annex 1 of the Framework Agreement on Comprehensive Economic Cooperation between ASEAN and China.¹⁷⁾

The specific products set out in Annex 2 of the agreement are also covered by the Early Harvest Program and the tariff concessions are applied only to the

| Chapter | Description |
|---------|----------------------------|
| 01 | Live animals |
| 02 | Meat and edible meat offal |
| 03 | Fish |
| 04 | Dairy produce |
| 05 | Other animal products |
| 06 | Live trees |
| 07 | Edible vegetables |
| 08 | Edible fruits and nuts |

17) Framework Agreement on Comprehensive Economic Co-operation between the Association of South East Asian Nations and the People's Republic of China.
18) Ibid., Part 1, Article 6.

parties indicated in Annex 2. All products covered under the Early Harvest Program are divided into three product categories for tariff reduction and elimination. The following is an excerpt from the agreement:¹⁹⁾

(1) Category 1

For China and ASEAN 6, this refers to all products with applied MFN tariff rates higher than 15%, while for the CLMV countries, this refers to all products with applied MFN tariff rates of 30% or higher.

(2) Category2

For China and ASEAN 6, this refers to all products with applied MFN tariff rates between 5% (inclusive) and 15% (inclusive), while for the CLMV countries, this refers to all products with applied MFN tariff rates between 15% (inclusive) and 30% (exclusive).

(3) Category 3

For China and ASEAN 6, this refers to all products with applied MFN tariff rates lower than 5%, while for the CLMV countries, this refers to all products with applied MFN tariff rates lower than 15%.

The Early Harvest Program is to be implemented according to the agreed timetables, which is between January 1, 2004 and January 1, 2010 (see Annex Table II-1).

2.2. Normal Track

Products listed in the Normal Track by each party is to have their respective applied MFN tariff rates gradually reduced or eliminated in accordance with specified schedules and rates (to be mutually agreed on by the parties) over a period from January 1, 2005 to 2010 for ASEAN-6 and China and, in the case of the CLMV countries, the period is to be from January 1, 2005 to 2015 with higher starting tariff rates and different staging. In respect of those tariffs which have been reduced but have not been eliminated, they are to be progressively eliminated within timeframes to be mutually agreed between the parties.²⁰⁾

Tariff lines in the Normal Track for China and ASEAN-6 are to have their respective applied MFN tariff rates gradually reduced and eliminated according to the schedule shown in Table II-5.

19) *Ibid.*

20) *Modality for Tariff Reduction and Elimination for Tariff Lines Placed in the Normal Track*, Annex 1.

Table II-5. Tariff Reduction and Elimination Schedule in the Normal Track for China and ASEAN-6

| | 2005* | 2007 | 2009 | 2010 |
|------------------|------------|------------|------|------|
| $20 \leq X$ | 20 | 12 | 5 | 0 |
| $15 \leq X < 20$ | 15 | 8 | 5 | 0 |
| $10 \leq X < 15$ | 10 | 8 | 5 | 0 |
| $5 \leq X < 10$ | 5 | 5 | 0 | 0 |
| $X \leq 5$ | Standstill | Standstill | 0 | 0 |

Note: * The first date of implementation is July 1, 2005.

Source: *Modality for Tariff Reduction and Elimination for Tariff Lines Placed in the Normal Track*, Annex 1.

Each country is also committed to undertake further tariff reduction and/or elimination in accordance with the following thresholds:²¹⁾

(a) ASEAN 6 and China

- (i) Each Party shall reduce to 0-5% not later than July 1, 2005 the tariff rates for at least 40% of its tariff lines placed in the Normal Track.
- (ii) Each Party shall reduce to 0-5% not later than January 1, 2007 the tariff rates for at least 60% of its tariff lines placed in the Normal Track.
- (iii) Each Party shall eliminate all its tariffs for tariff lines placed in the Normal Track not later than January 1, 2010, with flexibility to have tariffs on some tariff lines, not exceeding 150 tariff lines, eliminated not later than January 1, 2012.
- (iv) Each Party shall eliminate all its tariffs for tariff lines placed in the Normal Track not later than January 1, 2012.

(b) CLMV countries

- (i) Each Party shall reduce to 0-5% not later than January 1, 2009 for Vietnam; January 1, 2010 for Lao PDR and Myanmar; and January 1, 2012 for Cambodia the tariff rates for at least 50% of its tariff lines placed in the Normal Track.

21) *Ibid.*

- (ii) Cambodia, Lao PDR and Myanmar shall eliminate their respective tariffs not later than January 1, 2013 on 40% of its tariff lines placed in the Normal Track.
- (iii) For Vietnam, the percentage of Normal Track tariff lines to have their tariffs eliminated not later than January 1, 2013 shall be determined not later than December 31, 2004.
- (iv) Each Party shall eliminate all its tariffs for tariff lines placed in the Normal Track not later than January 1, 2015, with flexibility to have tariffs on some tariff lines, not exceeding 250 tariff lines, eliminated not later than January 1, 2018.
- (v) Each Party shall eliminate all its tariffs for tariff lines placed in the Normal Track not later than January 1, 2018.

2.3. *Sensitive Track*

Products listed in the Sensitive Track by a party on its own accord are to have their respective applied MFN tariff rates reduced in accordance with mutually agreed end rates and end dates and, where applicable, have their respective applied MFN tariff rates progressively eliminated within timeframes to be mutually agreed between the parties.²²⁾ The number of products listed in the Sensitive Track is subject to a maximum ceiling to be mutually agreed among the parties.

For the products listed in the Sensitive List, tariffs are to be reduced to 0-5 percent by 2018 for China and ASEAN 6, and by 2020 for the CLMV countries. For those listed in the Highly Sensitive List, tariffs are to be reduced to below 50 percent by 2015 for China and ASEAN 6, and by 2018 for the CLMV countries.

2.4. *Assessment of the ACFTA*

In order to evaluate the level of market access for goods in the ACFTA, we first examine China's tariff concession schedule. As shown in Table II-6, in terms of the number of tariff lines, the share of Chinese products belonging to the Early Harvest Program, Normal Track, and Sensitive Track are 6.6 percent, 89.2 percent, and 4.2 percent, respectively. The ratio of these tariff lists in terms of China's share of imports from ASEAN are 1.1 percent, 90.3 percent, 8.6 percent; on the other hand, in terms of China's total share of imports, they are,

22) *Framework Agreement on Comprehensive Economic Co-operation between the Association of South East Asian Nations and the People's Republic of China*, Part 1, Article 3.

and 0.9 percent, 91.8 percent, 7.3 percent, respectively.

In other words, 6.6 percent of China's total tariff lines representing 1.1 percent of China's total imports and 0.9 percent of China's imports from ASEAN are to be eliminated no later than January 1, 2006, and 95.8 percent of China's total tariff lines representing 91.4 percent of China's total imports and 92.7 percent of China's imports from ASEAN are to be eliminated no later than January 1, 2012. Therefore, the level of market access of the ACFTA, evaluated from China's perspective, can be regarded as reasonably good.

However, it is difficult to be as positive about ASEAN countries. First, as mentioned earlier, the target date of tariff elimination for products placed in the Normal Track for the CLMV countries is set much later on January 1, 2018.

Second, Tables II-7 and II-8 reveal that the shares of tariff lines placed in Indonesia and Cambodia's Sensitive Tracks are greater than that of China. In particular, 6.7 percent of Cambodia's total tariff lines—representing 63.9 percent of Cambodia's imports from China and 38.5 percent of Cambodia's total imports in 2004—are on the Sensitive List, whereas 2.6 percent of Cambodia's total tariff lines—representing 3.4 percent of Cambodia's imports from China and 7.4 percent of Cambodia's total imports in 2004—are on the Highly

Table II-6. China's Tariff Concession Structure, ACFTA

| | | Number of tariff lines | Share of China's total tariff lines (percent) | Share of China's imports from ASEAN in 2004 (percent) | Share of China's total imports in 2004 (percent) |
|--------------------------|---------|---------------------------|---|--|---|
| Early Harvest List | | 348 | 6.6 | 1.1 | 0.9 |
| Normal Track List | general | 4,533 | 86.5 | 84 | 87.5 |
| | 2012 | 139 | 2.7 | 6.3 | 4.3 |
| Sensitive List | | 138 | 2.6 | 1.9 | 4.7 |
| Highly Sensitive List | | 81 | 1.6 | 6.7 | 2.6 |

Note: * HS 6-digit. Due to code changes from HS 1996 to HS 2002, the number of tariff lines could change.

Source: Calculated by authors from the *KITA Trade Research Institute's Database*.

Table II-7. Indonesia's Tariff Concession Structure, ACFTA

| | | Number of tariff lines | Share of Indonesia's total tariff lines (percent) | Share of Indonesia's imports from China in 2004 (percent) | Share of Indonesia's total imports in 2004 (percent) |
|--------------------------|---------|---------------------------|---|--|--|
| Early Harvest List | | 355 | 6.8 | 5.0 | 2.7 |
| Normal Track List | general | 4,087 | 78.2 | 76.7 | 75.4 |
| | 2012 | 393 | 7.5 | 5.9 | 6.2 |
| Sensitive List | | 340 | 6.5 | 10.7 | 11.2 |
| Highly Sensitive List | | 49 | 0.9 | 1.7 | 4.5 |

Note: * HS 6-digit. Due to code changes from HS 1996 to HS 2002, the number of tariff lines could change.

Source: Calculated by authors from the *KITA Trade Research Institute's Database*.

Table II-8. Cambodia's Tariff Concession Structure, ACFTA

| | | Number of tariff lines | Share of Cambodia's total tariff lines (percent) | Share of Cambodia's imports from China in 2004 (percent) | Share of Cambodia's total imports in 2004 (percent) |
|--------------------------|---------|---------------------------|--|--|---|
| Early Harvest List | | 302 | 5.9 | 2.6 | 0.8 |
| Normal Track List | general | 4,105 | 80.1 | 26.7 | 44.0 |
| | 2012 | 241 | 4.70 | 3.4 | 9.3 |
| Sensitive List | | 343 | 6.7 | 63.9 | 38.5 |
| Highly Sensitive List | | 134 | 2.6 | 3.4 | 7.4 |

Note: * HS 6-digit. Due to code changes from HS 1996 to HS 2002, the number of tariff lines could change.

Source: Calculated by authors from the *KITA Trade Research Institute's Database*.

Sensitive List. So, in terms of the share of tariff lines, while only 9.3 percent of items are on the Sensitive and Highly Sensitive Lists, these items represent 67.3 percent of Cambodia's imports from China in 2004.

Third, as we noticed in the case of the AFTA, some ASEAN-6 countries did not always stick to pledged targets. So, it is also possible that some countries may not respect their market access targets in the future.

Table II-9 shows the Chinese tariff items placed on the Sensitive List and the Highly Sensitive List. There are 138 tariff lines in the Sensitive List: half of them are chemical products, 19 are textile tariff items, and 11 automobile tariff items. Out of the 81 tariff lines in the Highly Sensitive List, there are 38 chemical items and 15 agricultural products.

Table II-9. China's Sensitive and Highly Sensitive List Tariff Items by Industry, ACFTA

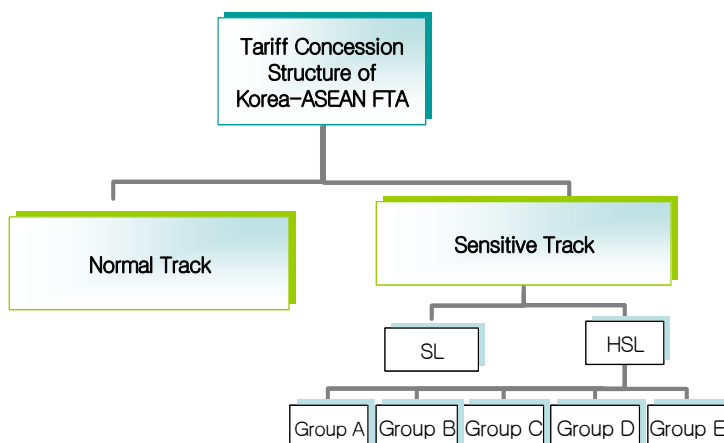
| Industry | Number of Sensitive List | Highly Sensitive List |
|---------------------|--------------------------|-----------------------|
| Agriculture | 26 | 10 |
| Forestry | 17 | 6 |
| Minerals | 8 | - |
| Chemicals | 15 | 69 |
| Textiles | 8 | 19 |
| Steel and metals | 3 | - |
| General machinery | 11 | 3 |
| Electronics | 25 | 4 |
| Automobiles | 10 | 11 |
| Precision machinery | 1 | - |
| Ships | 3 | 3 |
| Others | 12 | 13 |
| Total | 139 | 138 |

Source: *Framework Agreement on Comprehensive Economic Co-operation between the Association of South East Asian Nations and the People's Republic of China*; KITA Trade Research Institute's Database.

3. Korea-ASEAN FTA

The tariff concession structure of the Korea-ASEAN FTA (Trade in Goods Agreement) is basically similar to those of the AFTA and ACFTA in that it consists of a Normal Track and a Sensitive Track.

Figure II-4. Tariff Concession Structure of Korea-ASEAN FTA



3.1. Normal Track²³⁾

The tariff lines in the Normal Track are to have their applied MFN tariff rates gradually reduced and eliminated according to the schedule shown in Table II-10.²⁴⁾

Korea is to eliminate its tariffs for at least 70 percent of the tariff lines placed in the Normal Track upon entry into force of the Trade in Goods Agreement. It is also required to eliminate its tariffs for at least 95 percent of the tariff lines in the Normal Track not later than January 1, 2008 and eliminate all tariffs placed in the Normal Track by no later than January 1, 2010.

For ASEAN-6, each party is to reduce its tariff rates for at least 50 percent of the tariff lines in the Normal Track to 0-5 percent not later than January 1,

23) *Agreement on Trade in Goods under the Framework Agreement on Comprehensive Economic Cooperation among the Governments of the Republic of Korea and the Member Countries of the ASEAN*, Annex 1.

24) The schedules for Vietnam, Cambodia, Lao PDR and Myanmar are on Annex I (ii), (iii).

Table II-10. Tariff Reduction and Elimination Schedule in the Normal Track for Korea and ASEAN-6

| | (percent) | | | | |
|------------------|------------|------------|------------|------|------|
| | 2006 | 2007 | 2008 | 2009 | 2010 |
| $20 \leq X$ | 20 | 13 | 10 | 5 | 0 |
| $15 \leq X < 20$ | 15 | 10 | 8 | 5 | 0 |
| $10 \leq X < 15$ | 10 | 8 | 5 | 3 | 0 |
| $5 \leq X < 10$ | 5 | 5 | 3 | 0 | 0 |
| $X \leq 5$ | Standstill | Standstill | Standstill | 0 | 0 |

Source: *Agreement on Trade in Goods under the Framework Agreement on Comprehensive Economic Cooperation among the Governments of the Republic of Korea and the Member Countries of the ASEAN*, Annex 1.

2007. Each party is to eliminate its tariffs for at least 90 percent of the tariff lines not later than January 1, 2009 and eliminate its tariffs for all tariff lines not later than January 1, 2010, with the flexibility to have tariff lines not exceeding 5 percent of all the tariff lines, or as listed in an agreed schedule eliminated not later than January 2012.

Vietnam is to reduce its tariff rates for at least 50 percent of the tariff lines in the Normal Track to 0-5 percent not later than January 1, 2013. It is also to eliminate its tariffs for at least 90 percent of the tariff lines not later than January 1, 2015 and eliminate its tariffs for all tariff lines not later than January 1, 2016, with flexibility to have tariff lines not exceeding 5 percent of all the tariff lines, or as listed in an agreed Schedule eliminated not later than January 2018.

For Cambodia, Lao PDR, and Myanmar, each party is to reduce its tariff rates for at least 50 percent of the tariff lines in the Normal Track to 0 - 5 percent not later than January 1, 2015. Each party is to eliminate its tariffs for at least 90 percent of the tariff lines not later than January 1, 2017, and eliminate its tariffs for all tariff lines not later than January 1, 2018, with flexibility to have tariff lines not exceeding 5 percent of all the tariff lines, or as listed in an agreed schedule eliminated not later than January 2020.

3.2. Sensitive Track²⁵⁾

The number of tariff lines which each party can place in the Sensitive

25) *Agreement on Trade in Goods under the Framework Agreement on Comprehensive Economic Cooperation among the Governments of the Republic of Korea and the Member Countries of the ASEAN*, Annex 2.

Track is subject to a maximum ceiling: for Korea and ASEAN-6, 10 percent of all tariff lines and 10 percent of the total value of imports from Korea or from ASEAN member countries as a whole based on 2004 trade statistics; for Vietnam, 10 percent of all tariff lines and 25 percent of the total value of imports from Korea based on 2004 trade statistics; and, for Cambodia, Lao PDR, and Myanmar, 10 percent of all tariff lines.

Tariff lines placed by each party in the Sensitive Track are to be further classified in the Sensitive List and the Highly Sensitive List. The number of tariff lines which each party can place in the Highly Sensitive List is to be subject to a well defined maximum ceiling: for Korea and ASEAN-6, 200 tariff lines at the HS 6-digit level or 3 percent of all tariff lines at the HS digit level of each party's own choice and 3 percent of the total value of imports from Korea or from the ASEAN member countries as a whole based on 2004 statistics; for Cambodia, Lao PDR, Myanmar, and Vietnam, 200 tariff lines at the HS 6-digit level or 3 percent of all tariff lines at the HS digit level of each party's own choice.

The schedules to reduce and eliminate tariff rates of the tariff lines placed in the Sensitive List are also given. For instance, Korea and ASEAN-6 are to reduce tariff rates to 20 percent not later than January 1, 2012 and these tariff rates are to be subsequently reduced to 0-5 percent not later than January 2016. For Vietnam, they are to be reduced to 20 percent not later than January 1, 2017 and subsequently reduced to 0-5 percent not later than January 1, 2021. For Cambodia, Lao PDR, and Myanmar, they are to be reduced to 20 percent not later than January 1, 2020 and subsequently reduced to 0-5 percent not later than January 2024.

The tariff lines placed in a party's Highly Sensitive List are categorized into five groups. For Group A, tariff lines are subject to a 50 percent tariff rate cap; for Group B, tariff lines are subject to tariff reduction by 20 percent; for Group C, tariff lines are subject to tariff reduction by 50 percent; for Group D, tariff lines are subject to tariff rate quotas (TRQs); while for Group E, tariff lines are exempted from tariff concession. For each group, the parties are to undertake defined commitments. For instance, Korea and ASEAN-6 are to reduce the tariffs rates of tariff lines placed in Group A by not more than 50 percent and not later than January 1, 2016, and the number of tariff lines, which each party can place in Group E, is subject to a maximum ceiling of 40 tariff lines at the HS 6-digit level.

3.3. Assessment of the Korea-ASEAN FTA

Table II-11 shows Korea's proposed tariff concession structure in the Korea-ASEAN FTA. Of Korea's total tariff lines, 92.4 percent belong to the Normal Track, while 7.6 percent are in the Sensitive Track. The tariff lines placed in the Sensitive List and the Highly Sensitive List represent 4.3 percent and 3.3 percent, respectively, of Korea's total tariff lines and 98 tariff lines (0.87 percent) are exempted from tariff concession.

In terms of the share of imports in 2004, tariff items under the Normal Track and those under the Sensitive Track represent 91.6 percent and 8.4 percent, respectively, of Korea's imports from ASEAN countries, while their shares of Korea's total imports amount to 94.8 percent and 5.2 percent, respectively. The excluded items represent 0.8 percent and 0.9 percent, respectively,

Table II-11. Korea's Tariff Concession Structure in the Korea-ASEAN FTA

| | | Number of tariff lines | Share of Korea's total tariff lines (percent) | Share of Korea's imports from ASEAN in 2004 (percent) | Share of Korea's total imports in 2004 (percent) |
|--------------------------|--------|---------------------------|--|---|---|
| Normal Track | Year 0 | - | 70 | 91.6 | 94.8 |
| | Others | - | 22.4 | | |
| Sensitive List | | 481 | 4.27 | 5.6 | 3.2 |
| Highly Sensitive List | A | 6 | 0.05 | 0.04 | 0.1 |
| | B | 224 | 1.99 | 1.2 | 0.7 |
| | C | 36 | 0.32 | 0.06 | 0.2 |
| | D | 11 | 0.1 | 0.6 | 0.1 |
| | E | 98 | 0.87 | 0.8 | 0.9 |
| | B+D | 2 | 0.02 | 0.1 | 0.01 |

Note: HS 10-digit (Total tariff lines: 11,261).

Source: Calculated by authors from *Agreement on Trade in Goods under the Framework Agreement on Comprehensive Economic Cooperation among the Governments of the Republic of Korea and the Member Countries of the ASEAN, Appendix 1 & KOTIS Database*.

Table II-12. Indonesia's Tariff Concession Structure in the Korea-ASEAN FTA

| | | Number of tariff lines | Share (percent) | Share of Indonesia's imports from Korea in 2004 (percent) | Share of Indonesia's total imports in 2004 (percent) |
|-----------------------------|---|---------------------------|--------------------|---|---|
| Normal Track | | 9,745 | 87.28 | 80.1 | 86.5 |
| Sensitive List | | 884 | 7.92 | 10.1 | 7.7 |
| Highly Sensitive List | A | 21 | 0.19 | 0.5 | 0.3 |
| | B | 382 | 3.42 | 7.8 | 4.3 |
| | C | 0 | 0 | 0 | 0 |
| | D | 0 | 0 | 0 | 0 |
| | E | 133 | 1.19 | 1.5 | 1.2 |

Note: HS 10-digit level (Total tariff lines: 11,165): share of imports were calculated using HS 6-digit level data.

Source: Calculated by authors from *Agreement on Trade in Goods under the Framework Agreement on Comprehensive Economic Cooperation among the Governments of the Republic of Korea and the Member Countries of the ASEAN*, Appendix 1, 2 & COMTRADE Database.

Table II-13. Malaysia's Tariff Concession Structure in the Korea-ASEAN FTA

| | | Number of tariff lines | Share (percent) | Share of Cambodia's imports from Korea in 2004 (percent) | Share of Cambodia's total imports In 2004 (percent) |
|--------------------------|---|---------------------------|--------------------|--|--|
| Normal Track | | 4,848 | 91.2 | 20.8 | 45.7 |
| Sensitive List | | 265 | 5.0 | 1.2 | 7.0 |
| Highly Sensitive List | A | 5 | 0.1 | 0.6 | 0.7 |
| | B | 155 | 2.9 | 6.8 | 13.1 |
| | C | 0 | 0 | 0 | 0 |
| | D | 0 | 0 | 0 | 0 |
| | E | 40 | 0.8 | 70.6 | 33.5 |

Note: HS 9-digit level (Total tariff lines: 10,592): share of imports were calculated using HS 6-digit level data.

Source: Calculated by authors from *Agreement on Trade in Goods under the Framework Agreement on Comprehensive Economic Cooperation among the Governments of the Republic of Korea and the Member Countries of the ASEAN*, Appendix 1, 2 & COMTRADE Database.

of Korea's imports from ASEAN and Korea's total imports.

Tables II-12, II-13 and II-14 show the proposed tariff concession structures of Indonesia, Malaysia, and Cambodia. Compared to the Korean tariff concession structure, the shares of products placed in Indonesia, Malaysia, and Cambodia's Normal Track are smaller both in terms of tariff lines and in importance of imports, while their shares of items placed in the Sensitive List and the Highly Sensitive List are in general larger than those of Korea. The share of items placed in Indonesia's Highly Sensitive List is 4.8 percent in terms of the number of tariff lines, but makes up 9.8 percent of Indonesia's share of imports from Korea in 2004. For Malaysia, the shares of tariff lines and imports from Korea are 3.0 percent and 7.1 percent, respectively. For Cambodia, the tariff items in the Highly Sensitive List represent 3.8 percent of the total number of tariff lines and 78.0 percent of the imports from Korea. Moreover, while

<Table II-14> Cambodia's Tariff Concession Structure in the Korea-ASEAN FTA

| | | Number of tariff lines | Share (percent) | Share of Malaysia's imports from Korea in 2004 (percent) | Share of Malaysia's total imports in 2004 (percent) |
|--------------------------|---|---------------------------|--------------------|--|--|
| Normal Track | | 9,221 | 87.06 | 80.7 | 89.6 |
| Sensitive List | | 1,048 | 9.89 | 12.2 | 8.1 |
| Highly Sensitive List | A | 28 | 0.26 | 0.2 | 0.1 |
| | B | 190 | 1.79 | 6.9 | 1.8 |
| | C | 0 | 0 | 0 | 0 |
| | D | 24 | 0.23 | 0 | 0.1 |
| | E | 81 | 0.76 | 0 | 0.3 |

Note: HS 6-digit level (Total tariff lines: 5,313); share of imports were calculated using HS 6-digit level data.

Source: Calculated by the authors from *Agreement on Trade in Goods under the Framework Agreement on Comprehensive Economic Cooperation among the Governments of the Republic of Korea and the Member Countries of the ASEAN*, Appendix 1, 2 & COMTRADE Database.

Cambodia's excluded items represent only 0.8 percent of the total number of tariff lines, their share of imports from Korea in 2004 amounted to 70.6 percent.

As shown in Table II-15, mostly agricultural and fishery products are placed in Korea's Highly Sensitive List, while its Sensitive List mainly consists of agricultural, chemical, textile, forestry, and fishery products.

Table II-15. Number of Items on Korea's Sensitive and Highly Sensitive List, Korea-ASEAN FTA

| Industry | Number of Sensitive List | Number of Highly Sensitive List |
|---------------------------|--------------------------|---------------------------------|
| Agriculture | 136 | 272 |
| Fishery | 49 | 82 |
| Prepared food and tobacco | 16 | 6 |
| Forestry | 66 | 9 |
| Minerals | 17 | - |
| Chemicals | 83 | 8 |
| Textiles | 80 | - |
| Metals | 1 | - |
| General machinery | 8 | - |
| Electronics | 5 | - |
| Automobiles | 19 | - |
| Others | 1 | - |
| Total | 481 | 377 |

Source: *Agreement on Trade in Goods under the Framework Agreement on Comprehensive Economic Cooperation among the Governments of the Republic of Korea and the Member Countries of the ASEAN*, Appendix 1, 2.

4. Korea-Singapore FTA

The tariff concession structure of the Korea-Singapore FTA is fairly simple. It consists of four tariff line categories: i) tariff lines whose tariff rates are to be eliminated upon the entry into force of the Agreement, ii) tariff lines whose tariff rates are to be eliminated within five years, iii) tariff lines whose tariff rates are to be eliminated within ten years, and iv) tariff lines that are exempted

from tariff concession.

About 60 percent of Korea's total tariff items, which represent 70.9 percent of Korea's total imports and 80.3 percent of Korea's imports from Singapore in 2004, is to be eliminated upon the entry into force of the Agreement (see Table

Table II-16. Korea's Tariff Elimination Schedule, Korea-Singapore FTA

| | Number of tariff lines | Share of total tariff lines (percent) | Share of Korea's total imports in 2004 (percent) | Share of imports from Singapore in 2004 (percent) |
|-----------|---------------------------|---|--|--|
| Year 0 | 6,724 | 59.7 | 70.9 | 80.3 |
| Year 5 | 2,004 | 17.8 | 9.6 | 3.0 |
| Year 10 | 1,587 | 14.1 | 12 | 7.3 |
| Exclusion | 946 | 8.4 | 7.4 | 9.4 |

Note: Out of 11,261 total tariff items. Share of imports were calculated using HS 6-digit level data.

Source: Calculated by authors from *Free Trade Agreement between Korea and Singapore*, Annex 3A & KOTIS Database.

Table II-17. Annual Tariff Reduction Schedule, Korea-Singapore FTA
(percent)

| | "Year 0" items | "Year 5" items | "Year 10" items |
|---------|----------------|----------------|-----------------|
| Year 0 | 100 | 16.7 | 9.1 |
| Year 1 | - | 33.3 | 18.2 |
| Year 2 | - | 50.0 | 27.3 |
| Year 3 | - | 66.7 | 36.4 |
| Year 4 | - | 83.3 | 45.5 |
| Year 5 | - | 100 | 54.5 |
| Year 6 | - | - | 63.6 |
| Year 7 | - | - | 72.7 |
| Year 8 | - | - | 81.8 |
| Year 9 | - | - | 90.9 |
| Year 10 | - | - | 100 |

Source: *Free Trade Agreement between Korea and Singapore*, Annex 3A.

II-16). On the other hand, 946 tariff items (8.4 percent of Korea's total tariff lines) are excluded from tariff concession. They represent 7.4 percent of Korea's total imports and 9.4 percent of Korea's imports from Singapore in 2004.

Table II-17 shows Korea's tariff reduction schedule. For "Year 5" items, the tariff rate will be reduced by about 16.7 percent each year, while the tariff rate will be reduced by about 9.1 percent each year for "Year 10" items.

Agricultural, fishery, and chemical products mainly constitute excluded items for Korea, while many textile, chemical and agricultural items belong to Korea's tariff lines that are to be eliminated within 10 years (see Table II-18).

Table II-18. Korea's Excluded Tariff Items by Industry, Korea-Singapore FTA

| Industry | Number of excluded tariff items | Number of "Year 10" tariff items |
|---------------------------|---------------------------------|----------------------------------|
| Agriculture | 427 | 316 |
| Fishery | 190 | 43 |
| Prepared food and tobacco | 35 | 42 |
| Forestry | 42 | 43 |
| Minerals | 48 | 15 |
| Chemicals | 166 | 421 |
| Textiles | 3 | 440 |
| Steel and metals | - | 18 |
| General machinery | 1 | 103 |
| Electronics | 31 | 75 |
| Automobiles | - | 10 |
| Precision machinery | 3 | 46 |
| Others | - | 15 |
| Total | 946 | 1,587 |

Source: *Free Trade Agreement between Korea and Singapore*, Annex 3A.

5. Japan-Singapore EPA

Japan's tariff elimination schedule under the Japan-Singapore EPA consists of six parts:²⁶⁾

26) *Agreement between the Republic of Singapore and Japan for a New Age Economic*

- A: Customs duties shall be eliminated as from the date of entry into force of the Agreement;
- B: Customs duties shall be eliminated as of 1 April 2006;
- C1: The rate of customs duties shall be 2.8 percent as from the date of entry into force of the Agreement and shall be reduced annually in eight equal installments from 2.8 percent to zero percent. This annual reduction shall take place on 1 January of each year from 2003 to 2010;
- C2: The rate of customs duties shall be 3.1 percent as from the date of entry into force of the Agreement and shall be reduced annually in eight equal installments from 3.1 percent to zero percent. This annual reduction shall take place on 1 January of each year from 2003 to 2010;
- C3: The rate of customs duties shall be 3.9 percent as from the date of entry into force of the Agreement and shall be reduced annually in eight equal installments from 3.9 percent to zero percent. This annual reduction shall take place on 1 January of each year from 2003 to 2010;

Table II-19. Japan's Tariff Elimination Schedule, Japan-Singapore EPA

| | Number of tariff lines | Share of total tariff lines (percent) | Share of Japan's imports from Singapore in 2004 (percent) | Share of Japan's total imports in 2004 (percent) |
|----|------------------------|---------------------------------------|---|--|
| A | 7,045 | 76.1 | 91.5 | 86.0 |
| B | 3 | 0.0 | 3.8 | 1.8 |
| C1 | 10 | 0.1 | 0.3 | 0.0 |
| C2 | 2 | 0.0 | 0.0 | 0.0 |
| C3 | 2 | 0.0 | 0.0 | 0.0 |
| D | 4 | 0.0 | 0.0 | 0.0 |

Note: The total number of Japan's tariff lines at the HS 9-digit level amounts to 9,261.

However, the total number of tariff lines included in this schedule amounts to 7,066.

There is no mention of the exempted tariff lines in the agreement.

Source: Calculated by authors from *Agreement between Japan and Singapore for a New-age Economic Partnership*, Annex I & KOTIS Database.

D: The rate of customs duties shall be 6.5 percent as from 1 January 2004 and shall be reduced annually in six equal installments from 6.5 percent to zero percent. This annual reduction shall take place on 1 January of each year from 2005 to 2010.

As shown in Table II-19, of the 7,066 total tariff lines, 7,045 are subject to the agreement and belong to Category A. Only 21 tariff items (0.3 percent)—all petrochemical products—do not belong to Category A.

6. Japan-Malaysia EPA

The tariff concession structure of the Japan-Malaysia EPA is quite complex. It consists of 15 different categories:²⁷⁾

A: customs duties classified under the tariff lines indicated with “A” shall be eliminated as from the date of entry into force of the Agreement;

B3: customs duties classified under the tariff lines indicated with “B3” shall be eliminated in 4 equal annual installments from the Base Rate to free, as from the date of entry into force of the Agreement;

B4, B5, B6, B7, B9, B10, B15: same formula as B3 (For instance, customs duties classified under the tariff lines indicated with “B10” shall be eliminated in 11 equal annual installments from the Base Rate to free);

B4*: customs duties classified under the tariff lines indicated with “B4*” shall be eliminated in equal annual installments from the Base Rate to free, as from the date of entry into force of the Agreement, the final reduction taking place on January 1, 2010.

B9*: same formula as B4* (the final reduction taking place on January 1, 2015).

P: customs duties classified under the tariff lines indicated with “P” shall be as provided for in the terms and conditions set out in the note indicated in Column 5 in each Country’s Schedule;

Q: customs duties classified under the tariff lines indicated with “Q” shall be as provided for in the terms and conditions set out in the note indicated in Column 5 in each Country’s Schedule;

R: customs duties classified under the tariff lines indicated with “R” shall

27) *Agreement between the Government of Japan and the Government of Malaysia for an Economic Partnership*. Annex 1. Japan’s tariff elimination schedule has 10 categories, while Malaysia’s one contains 13 categories (see Tables II-20 and II-21).

be subjected to negotiation provided for in the terms and conditions set out in the note indicated in Column 5 in the Schedule of Japan; and

X: goods classified under the tariff lines indicated with “X” shall be excluded.

As shown in Table II-20, 81.2 percent of Japan’s tariff lines, representing 93.2 percent of Japan’s imports from Malaysia and 88.5 percent of Japan’s total imports in 2004, are to be eliminated from the date of entry into force of the agreement. On the other hand, 9.3 percent of Japan’s tariff lines, representing 0.5 percent of Japan’s imports from Malaysia and 5.7 percent of Japan’s total imports in 2004, are to be excluded, while the tariff rates of 1.8 percent of Japan’s tariff lines, representing 6.1 percent of Japan’s imports from Malaysia and 1.6 percent of Japan’s total imports in 2004, are subject to further negotiation.

For Malaysia, 74.3 percent of tariff lines, representing 67.0 percent of its imports from Japan and 79.2 percent of total imports in 2004, are to be eliminated as from the date of entry into force of the agreement. On the other

Table II-20. Japan’s Tariff Elimination Schedule, Japan-Malaysia EPA

| | Number of tariff lines | Share of total tariff items (percent) | Share of Japan’s imports from Malaysia in 2004 (percent) | Share of Japan’s total imports in 2004 (percent) |
|--------------|------------------------|---------------------------------------|--|--|
| A: Year 0 | 7,519 | 81.2 | 93.2 | 88.5 |
| B5: Year 6 | 98 | 1.1 | 0.0 | 0.9 |
| B6: Year 7 | 5 | 0.1 | 0.0 | 0.0 |
| B7: Year 8 | 210 | 2.3 | 0.0 | 1.9 |
| B9: Year 10 | 3 | 0.0 | 0.0 | 0.0 |
| B10: Year 11 | 259 | 2.8 | 0.2 | 1.1 |
| B15: Year 16 | 135 | 1.5 | 0.0 | 0.3 |
| P | 6 | 0.1 | 0.0 | 0.0 |
| R | 167 | 1.8 | 6.1 | 1.6 |
| X: Exclusion | 859 | 9.3 | 0.5 | 5.7 |

Note: HS 9-digit level. Imports are calculated based on HS 9-digit data.

Source: Calculated by authors from *Agreement between the Government of Japan and the Government of Malaysia for an Economic Partnership*. Annex 1 & KOTIS Database.

hand, 1.1 percent of its tariff lines, representing 0.0 percent of its imports from Japan and 0.5 percent of its total imports in 2004, are to be excluded, while the tariff rates of a substantial number of tariff lines, representing 28.5 percent of its imports from Japan in 2004, have a phase-out period of 5 to 10 years (see Table II-21).

Table II-22 reveals that agricultural and fishery products constitute almost 90 percent of Japan's excluded items, while also representing more than half of Malaysia's excluded items.

Table II-21. Malaysia's Tariff Elimination Schedule, Japan-Malaysia EPA

| | Number of tariff lines | Share of total tariff items (percent) | Share of Malaysia's imports from Japan in 2004 (percent) | Share of Malaysia's total imports in 2004 (percent) |
|--------------|------------------------|---------------------------------------|--|---|
| A: Year 0 | 7,867 | 74.3 | 67.0 | 79.2 |
| B3: Year 4 | 21 | 0.2 | 0.3 | 0.1 |
| B4: Year 5 | 24 | 0.2 | 0.2 | 0.1 |
| B4*: 2010 | 47 | 0.4 | 1.8 | 0.7 |
| B5: Year 6 | 395 | 3.7 | 1.5 | 3.2 |
| B6: Year 7 | 46 | 0.4 | 3.1 | 1.0 |
| B7: Year 8 | 1373 | 13 | 12.1 | 8.6 |
| B9: Year 10 | 57 | 0.5 | 0.4 | 0.3 |
| B9*: 2015 | 89 | 0.8 | 6.2 | 1.6 |
| B10: Year 11 | 466 | 4.4 | 5.2 | 3.0 |
| B15: Year 16 | 0 | 0 | 0 | 0 |
| P | 86 | 0.8 | 2.1 | 1.7 |
| Q | 1 | 0.0 | 0.0 | 0.0 |
| R | 0 | 0 | 0 | 0 |
| X: Exclusion | 120 | 1.1 | 0.0 | 0.5 |

Note: HS 9-digit level (total tariff lines: 10,592). Imports are calculated based on HS 6-digit data.

Source: Calculated by authors from *Agreement between the Government of Japan and the Government of Malaysia for an Economic Partnership*. Annex 1 & KOTIS Database.

Table II-22. Number of Excluded Items by Industry in the Japan-Malaysia EPA

| Industry | Japan's number of excluded items | Malaysia's number of excluded items |
|---------------------------|----------------------------------|-------------------------------------|
| Agriculture | 602 | 28 |
| Fishery | 157 | 51 |
| Prepared food and tobacco | 20 | - |
| Minerals | 1 | - |
| Chemicals | 35 | 14 |
| Textiles | 11 | - |
| Others | 33 | 27 |
| Total | 859 | 120 |

Source: Agreement between the Government of Japan and the Government of Malaysia for an Economic Partnership. Annex 1.

7. Overall Assessment and Limitations

The tariff concession structure of the six FTAs between East Asian countries discussed above can be grouped into two categories: an ASEAN-type approach and an item-by-item approach. The ASEAN-type approach divides tariff items according to their sensitivity in the Normal Track and Sensitive Track. For those tariff items belonging to the Normal Track, they are again divided into 1) a category in which tariff rates are to be eliminated when the FTA comes into force and 2) other categories in which tariffs are to be eliminated within predefined years. Those items belonging to the Sensitive Track are also further divided into the Sensitive List and the Highly Sensitive List, depending on their degree of sensitivity. The AFTA, the ASEAN-China FTA and Korea-ASEAN FTA belong to this ASEAN-type approach. However, the ASEAN- China FTA differs from other agreements in that it adopts an Early Harvest Program and the Korea-ASEAN FTA differs by including exempted items in the Highly Sensitive List.

The other FTA category is the item-by-item approach, which sets tariff elimination schedules for each tariff item. The Korea-Singapore FTA, the Japan-Singapore EPA, and the Japan-Malaysia EPA all adopt this approach. As we

can see with the Japan-Singapore EPA and the Japan-Malaysia EPA, this approach produces a number of different tariff concession structures that accommodates different partner countries.

In this chapter, we have assessed the quality of existing FTAs among East Asian countries in terms of trade liberalization in goods by examining the tariff lines in the Highly Sensitive List and Exclusion List in terms of their number and share of imports. Our results conclude that the quality of FTAs in East Asia varies significantly. In particular, the FTAs involving ASEAN countries show relative overall weaknesses, which are mainly due to the CLMV countries. Our analysis also reveals that even within a single FTA, there often exist asymmetrical situations in the trade liberalization of goods among partner countries. However, it has been difficult to conduct a more detailed comparison among the FTAs and among participating countries due to the different use of classification systems: Korea uses HS 10-digit codes, Japan and Malaysia use HS 9-digit codes, and China and the Philippines use HS 8 digit codes; oftentimes, only HS 6-digit data were available for some countries.

From our analysis, we have also been able to identify the sensitive sectors in some of the countries. For example, in both Korea and Japan, agriculture and fishery have been identified as the most sensitive industries. However, a more detailed comparison was again difficult to make due to differing classification systems.

In terms of the disposition toward trade liberalization in goods, Korea and China show much more willingness than the CLMV countries, but the level of trade liberalization in Korea and China is limited due to the existence of sensitive sectors. Japan has also shown reluctance to open its market, especially for agricultural and fishery products. Therefore, it is difficult to make the case that existing FTAs between East Asian countries are of high quality in terms of market access for goods.

III. Rules of Origin in East Asian FTAs

Rules of origin are laws and administrative practices used to identify the country of origin of internationally traded goods. They are used to ensure that importing goods receive appropriate treatments, such as tariff rates and quotas, when such treatments are different depending on exporting countries.

If a good is wholly produced and obtained in one country, the country of origin is evident. However, the widespread fragmentation of production in the world makes it hard to confer originating country and due to such global fragmentation, rules of origin become increasingly complex. Also, the increase in preferential trade diversifies region-specific rules of origin and the growth of overlapping and intersecting rules of origin produces what Bhagwati has referred to as the “spaghetti bowl” problem.

Our objective in this section is to investigate the rules of origin of bilateral trade agreements in which East Asian countries are involved and make suggestions that can ease the market distorting effect of rules of the origin in the East Asian region. For this purpose, we start with a brief overview of rules of origin: the criteria to determine originating country and how rules of origin might affect the regional integration process. Then, we look at the specific properties of each intra-regional FTA in East Asia, focusing on similarities and differences, and how they have evolved as more FTAs have been introduced in the region. Lastly, we focus on the cumulation provision and see how it may help to alleviate the market distorting effect of rules of origin in East Asia.

1. Overview of Rules of Origin

1.1. Determination of Originating Country

The determination of the country of origin is, in general, divided into two categories: (i) goods wholly obtained and produced in one country and (ii) goods whose production involves more than one country. For goods wholly produced or obtained in one country, it is obvious that the country of production is the originating country. On the other hand, for goods that involve more than one country of production, importing countries have to set clear, specific and transparent rules to determine their origination so that exporters can recognize

the rules and follow. The dominant principle underlying determination of origin is that the country of origin is the last country in which a “substantial transformation” or “sufficient working or processing” takes place.

The wording of “substantial transformation,” however, is too abstract. It cannot be used as a criterion to determine the country of origin in itself. In non-preferential rules of origin, the substantial transformation principle is often stated in abstract terminology. However, for preferential rules of origin, substantial transformation needs to be clearly defined and this is a key difference between non-preferential and preferential rules of origin. In the context of preferential rules of origin, three main methods are used to test whether “substantial transformation” occurs. These are the change in tariff classification, the percentage criteria, and the technical test method.²⁸⁾ There does not exist one unique rule that applies for all products to test substantial transformation. Each method complements the other and they are sometimes used in combination.

In addition to the main criteria, most FTAs employ supplementary criteria for rules of origin, such as a *de minimis* or tolerance rule, cumulation rule, minimal process, or roll-up/roll-down provision. Some are to loosen the restrictiveness of rules of origin and others are to improve the transparency of determining the originating country.²⁹⁾

1.2. How Rules of Origin Affect Economic Integration

Setting the rules to determine originating country is an unavoidable means to limit economic benefits from the free trade agreement to the participating countries and prevent others from free-riding. It is usually considered as a ‘necessary evil’ of free trade agreements because it may distort markets, resulting in the limited flow of goods and services between participating countries. In this section, we investigate the economic impact of rules of origin.

First of all, rules of origin may act as trade barriers and distort the market because they impose administrative costs on exporters. To receive originating status for exporting goods, exporters need to provide proof by preparing all paper work required, which adds additional costs to production.

Also, rules of origin may induce exporting firms to switch suppliers from countries who do not participate in the FTA to participating countries in order to meet the rules of origin. This is a classical example of the trade diverting effect of preferential liberalization. The traditional trade diversion effect of FTAs

28) For the definition of each method, see WTO (2002), WT/REG/W/45, pp. 4-5.

29) For the definition of each method, see WTO (2002), WT/REG/W/45, pp. 6-7.

involves the replacement of the most cost-efficient non-partner country products by less cost-efficient partner country products due to the differences in tariff rates. Such trade diversion effects due to rules of origin may occur because, in order to meet rules of origin requirements, the exporting country changes its imports of intermediate inputs from firms in a third country to domestic firms or firms in an FTA partner country (in case bilateral cumulation applies). This implies a welfare reduction in an importing country because the country has to pay higher prices for the same products.

Rules of origin may also be used to protect the domestic industry from foreign imported products. Due to such characteristics of protectionism, rules of origin are sometimes referred to as 'hidden non tariff barriers.' One of the most notorious examples is the rules of origin regarding textile and garments in NAFTA. The US led rules of origin in NAFTA, as well as other FTAs in which the US is involved, adopt what are called yarn forward or fibre forward rules for textile and garment products. This is to protect the domestic textile and garment industry by setting strict rules of origin and it has been indeed quite successful in terms of limiting imports from FTA partner countries.

Lastly, rules of origin may hamper the efficient allocation of resources by inducing more inter-regional investments in the long run. For producers who supply intermediate goods from a third country to exporters in the region, rules of origin may give them an incentive to move their production line into the region because it would then allow their intermediate goods to be counted as regional material, increasing the chance that the final products which incorporate these intermediate goods will receive preferential tariff rates when they are exported. This is more likely to be observable in large countries with low MFN tariff rates; for example, in a country like the US under NAFTA. By relocating production facilities to such countries, producers can enjoy preferential tariff rates when they export products to "spoke" countries, as well as low tariff rates on imported intermediate inputs that were used to produce exporting goods.

Rules of origin have both a positive and negative impact on the economy; the positive side of rules of origin is that they make it possible to limit the economic benefit of FTAs to the participating countries, while the negative aspect is that due to this limiting, they may distort the market and/or be used as tools to protect domestic industries. However, the most serious problems of rules of origin are their complexities and incompatibilities: the growth of overlapping and intersecting preference trade deals and specific rules of origin in each FTA cause what Bhagwati has referred to as a 'spaghetti bowl' problem. He warned that 'preferences like noodles criss-crossing all over the

place' would distort world trade and it would make multilateral liberalization more difficult to achieve.

In the following section, we compare the rules of origin of six intra-regional FTAs in East Asia. Each FTA has different ways of defining rules of origin and we examine the similarities, as well as the differences, among them.

2. Preferential Rules of Origin for Intra-regional FTAs in East Asia

In this section, we focus on the rules of origin in the intra-regional FTAs of East Asia. We consider all FTAs currently established in the region: the Korea-ASEAN FTA, the Korea-Singapore FTA, the ASEAN-China FTA, the Japan-Singapore EPA, the Japan-Malaysia EPA, and the AFTA. Each FTA specifies the method of determining the country of origin of goods in its agreement text. All adopt a wholly produced criterion and a substantial transformation criterion. The main methods of determining substantial transformation are used solely or in combination with three main methods and some supplementary methods are adopted to loosen or clarify the determination process. Our objective in this section is to investigate the rules of origin in each FTA and look at the differences as well as similarities. This process will give us an idea on what we need to do for East Asian economic integration in terms of the rules of origin.

2.1. AFTA

In order to receive preferential concessions, products have to meet eligibility requirements for the CEPT Scheme under the Agreement on the CEPT.

First, ASEAN defines wholly produced or obtained goods as follows:

- (a) Mineral products extracted from its soil, its water or its seabed;
- (b) Agricultural products harvested there;
- (c) Animals born and raised there;
- (d) Products obtained from animals referred to in paragraph (c) above;
- (e) Products obtained by hunting or fishing conducted there;
- (f) Products of sea fishing and other marine products taken from the sea by its vessels;
- (g) Products processed and/or made on board its factory ships exclusively from products referred to in paragraph (f) above;

- (h) Used articles collected here, fit only for the recovery of raw materials;
- (i) Waste and scrap resulting from manufacturing operations conducted there; and
- (j) Goods produced there exclusively from the products referred to in paragraph (a) to (i) above.

This is similar to the definition of wholly produced criterion used in other FTAs. However, a slight difference can be found in defining the recognition of the nationality of a vessel. For example, compared to the KSFTA and the KAFTA, which set clear conditions in order to receive recognition as an exporting country's vessel, AFTA's way of defining the recognition of the nationality of a vessel is not clear.

A product that is not wholly produced or obtained in one country is regarded as originating from an ASEAN member country, if at least 40 percent of its content originates from any member country³⁰⁾ and the final process of manufacturing is performed in the exporting country.³¹⁾ The formula for calculating 40 percent ASEAN content is as follows:

$$\frac{\left(\text{Value of imported Non-ASEAN} \right) - \left(\text{Value of Undetermined Origin} \right)}{\text{Materials, Parts or Produce}} \div \text{FOB price} \times 100\% \leq 60\%$$

The CIF value or the earliest ascertained price paid is applied to determine the value of non-originating materials, parts, or products.

In applying this percentage criteria, a member country chooses either a direct or indirect calculation method. The direct method is used to prove that the value of local contents exceeds 40 percent of the FOB price. Indonesia, Laos, Myanmar, and Singapore use this method. On the other hand, the indirect method is used to show that the value of non-originating materials does not exceed 60 percent of the FOB price. This is exactly the method that uses the above formula; the remaining six countries adopt this method.

40 percent local content (or a 60 percent import content requirement) is deemed as a quite loose application of the percentage criteria. There are only a few preferential rules of origin that allow such low (or high) local (or import) content in conferring originating status. One example is the Common Market for

30) Rules of Origin for the CEPT Scheme for AFTA, Rule 3 (a) (i).

31) Rules of Origin for the CEPT Scheme for AFTA, Rule 3 (a) (iii).

Eastern and Southern Africa (COMESA) in which import content limitation is 60 percent, based on the CIF value. Also, the FTA between Mexico and Israel allows 35-45 percent of domestic content. Other than these exceptions, the threshold for import content is in general higher than the AFTA case.

In addition to the percentage criteria, ASEAN sets technical test criteria for textile and garment products, wood-based products, and wheat flour. It specifies working or processing carried out on non-originating materials that confers originating status (for textile and textile products), uses the change in tariff classification method (for wood-based products), and identifies specific processing (for wheat flour) in order to be considered as originating from ASEAN.

The most notable feature of the rules of origin in the CEPT Scheme is their simplicity: a product imported is eligible for preferential concessions if it is wholly produced or obtained in exporting member states or, in case the product is not wholly produced or obtained, if it contains a local content of at least 40 percent of the FOB price. The way of conferring originating status is simple: by comparing the various measures other countries adopt and using a combination of those measures in the final consideration. Also, other intra-regional FTAs in East Asia usually contain a long list of product specific rules of origin; ASEAN rules of origin have only few exceptions.

2.2. *Korea-ASEAN and Korea-Singapore FTAs*

Both the KSFTA and the KAFTA specify the way of determining the country of origin of goods within the agreement text or in a separate annex. They adopt a wholly produced criterion and a substantial transformation criterion. All major criteria of determining the originating country (i.e. the change in tariff classification, the percentage criterion, and the technical test method) are used to define substantial transformation.

2.2.1. Wholly Obtained or Produced Goods

In terms of the definition of wholly obtained or produced goods, both the KSFTA and the KAFTA use similar language. According to Annex III of the KAFTA, wholly obtained products are defined as³²⁾

- (a) plants and plant products harvested, picked or gathered after being grown there;
- ...

32) KSFTA Annex III, Rule 3.

- (f) products of sea-fishing taken by vessels registered with the Party and entitled to fly its flag, and other products taken by the Party or a person of that Party, from the waters, seabed or beneath the seabed outside the territorial waters of the Party, provided that the Party has the rights to exploit the natural resources of such waters, seabed and beneath the seabed under international law;
- (g) products of sea-fishing and other marine products taken from the high seas by vessels registered with the Party and entitled to fly its flag;
- (h) goods produced and/or made on board factory ships registered with a Party and entitled to fly its flag, exclusively from products referred to in sub-paragraph (g);
- ...
- (l) goods obtained or produced in the territory of the Party solely from goods referred to in sub-paragraphs (a) through (k)."

Wholly produced products are defined in an almost identical way in the KSFTA.

2.2.2. Not Wholly Obtained or Produced Goods

For not wholly obtained or produced goods, the change in tariff classification and the percentage criteria are the main methods of determining substantial transformation. The third method, the technical test method, is also used, but it is limited to specific products, such as textile and garment products.

The change in tariff classification is used in both FTAs and its degree of restrictiveness, i.e. change in tariff classification in 2, 4, or 6 digit HS nomenclature varies depending on the industrial structure, competitiveness, investment and trade relationships among Parties. However, due to the limitation of HS nomenclature, the change in tariff classification method is complemented by the other two methods: the percentage criteria methods and the technical test method.

The percentage criteria, or the value added criteria, are also widely used in FTAs. However, rather than being used independently, they are usually adopted in combination with the change in tariff classification method or used as an optional test. The basis on which the percentage of origination/non-origination materials is to be calculated is an important element. Valuation of non-origination materials may be based on the FOB, CIF, ex-work, or into-factory prices. In terms of calculating the value added in the exporting country, the percentage criteria may be formulated in terms of built-up, built-down, or import content.

In the KAFTA, calculating the Regional Value Content (RVC) of a good is based either on the built-up or built-down method.³³⁾ The formulas of each method are

(i) built-down method

$$RVC = \frac{VOM}{FOB} \times 100\%$$

(ii) built-up method

$$RVC = \frac{FOB - VNM}{FOB} \times 100\%$$

where VOM and VNM means the value of originating and non-originating materials, respectively. The threshold of RVC ranges between 40-50 percent, depending on products, but in most cases it is required to be not less than 60 percent of the FOB value. The Parties are given the flexibility to choose the method of calculating RVC; however, each Party has to adhere to one method.

In the KSFTA, only the built-down method is adopted and the required regional value content of a good to obtain origination status lies in the 45-55 percent range. The regional value content in the KSFTA is stricter than in the KAFTA. This reflects Korea's concern about preventing countries around Singapore from exporting products to Korea using Singapore as intermediation.

In the FTAs in which Korea is involved, the technical test criteria is used in combination with the change in tariff classification or as optional criteria for some specific products, such as textiles (HS Ch50-60) and garments (HS Ch 61-62).

2.2.3. Supplementary Criteria

In order to complement the limitations that the main criteria has, most preferential rules of origin adopt supplementary criteria in determining the originating country of a product. Widely used supplementary criteria are, as mentioned in the previous section, the de minimis (or tolerance rule), cumulation, and the roll-up/roll-down provisions. Other than these methods, provisions regarding intermediate materials, unassembled or disassembled goods, accessories, spare

33) See KSFTA Annex 3, Rule 4.

parts and tools, packaging materials, non-qualifying operations, and/or outward processing are used in FTAs in which Korea is involved

(i) De Minimis/Tolerance Rules

Both the KSFTA and the KAFTA provide a de minimis or tolerance test to alleviate the rigidity inherent in the test of change in tariff classification. The level of tolerance each FTA allows differs among the FTAs. According to the KAFTA, for general products except textiles (HS50-63), a good that does not undergo a change in tariff classification requirement is considered originating, if the value of all non-originating materials used in its production that do not undergo a change in tariff classification does not exceed 10 percent of the adjusted value (based on FOB) of the good.³⁴⁾ The same rule applies for agricultural and fishery products (HS 1-24). For textile products (HS 50-63), it allows the non-originating material to use up to 10 percent in terms of total weight.

A similar tolerance provision is applied in the KSFTA. For general products, other than HS 1-24 and 50-62, the tolerance level is up to 10 percent based on the FOB price. The difference is that the tolerance level for textile and garment products in the KSFTA is 8 percent of the total weight and there is no tolerance provision allowed for agricultural/fishery products in HS 1-14. In addition, for products within HS 15-24 of the KSFTA, it imposes the additional requirement of a change in chapter sub-heading. The properties of the tolerance provision in each FTA are shown in Table III-1.

Table III-1. Application of Tolerance Provision in Each FTA

| | | KSFTA | KAFTA |
|--|---------|---------------------------------|--------------------------------|
| General Products (other than specified below) | | Up to 10 % (FOB price based) | Up to 10% (FOB price based) |
| Textile (in terms of the share of total weight) | | Up to 8% | Up to 10% |
| Agricultural and Fishery Products | HS1~14 | No tolerance | Up to 10% |
| | HS15~24 | Up to 10% + CTSH* | Up to 10% |

Note: * CTSH stands for change in tariff sub-heading.

Source: Modified from Cheong (2005).

34) KSFTA Annex 3, Rule 10.

(ii) Outward Processing and the Gaesong Industrial Complex (GIC)

One of the most prominent features of preferential rules of origin for Korea is the dealing of the Gaesong Industrial Complex. GIC is very important to the Korean government for political stability on the Korean peninsula. In order to provide an incentive for Korean entrepreneurs, securing the market to sell products must precede investments. For such reasons, the Korean government has tried very hard to realize its objective regarding the GIC, which is reflected in the FTAs that Korea has concluded.³⁵⁾ Both the KSFTA and KAFTA deal with the GIC. The GIC is referred in either outward processing provisions or a specific provision added to the text.

Paragraph 1 of Article 4.3 (Treatment of Certain Goods) of Chapter 4 in the KSFTA text reads that the “goods listed in Annex 4B shall be originating goods when the goods are imported into the territory of Singapore from the territory of Korea. The goods shall also be originating material for purposes of satisfying the requirements specified in this Chapter.” In Section 1 of Annex 4B, originating goods referred to in Article 4.3 are listed and in Section 2 of Annex 4B, it specifies that “... goods in Section 1 are produced in the Gaesong Industrial Complex and other industrial zones on the Korean Peninsula.” What this implies is that exporting goods to Singapore listed in Section 1 of Annex 4B and produced on the Korean Peninsula, including industrial zones in North Korea, are considered as originating in Korea, if they are directly shipped from Korea to Singapore. Without a doubt, Article 4.3 of Chapter 4 is a special provision for the GIC.

On the other hand, in the KAFTA, the related provision regarding the GIC is Rule 6 in Annex 3 of the Agreement on Trade in Goods. Rule 6 reads that

“Notwithstanding Rules 2, 4, and 5, certain goods shall be considered to be originating even if the production process or operation has been undertaken in an area outside the territories of Korea and ASEAN Member Countries (i.e. industrial zone) on materials exported from a Party and subsequently re-imported to that Party. The application of this Rule, including the list of products and the specific procedures related to this application shall be mutually agreed upon by the Parties.”

35) Among the FTAs that Korea concluded so far, only the Korea-Chile FTA excludes the GIC and all others have a GIC provision.

Even though it does not explicitly mention the GIC, Rule 6 targets the GIC and further explanations and conditions are specified in the exchange notes. The individual lists of products from ASEAN member countries (except Thailand, who has still not signed the KAFTA, as of November 2006), containing a total of one hundred products at HS six digits, are also provided. Products from the GIC are deemed to be originating if the total value of non-originating input does not exceed 40 percent of the FOB price of the final good and the value of originating materials exported from a Party is not less than 60 percent of the total value of materials used in manufacturing the final good. Also, some safety devices are provided for ASEAN member countries, including special safeguard and annual review provisions.

The economic benefits Korea can expect from the provision regarding the GIC does not seem to be substantial. However, it has important meaning in the sense that it establishes the basis of international recognition regarding the GIC and can be used as a precedent for other FTAs in the future. Also, it has symbolic meaning and is expected to promote peace on the Korean peninsula.

(iii) Other Supplementary Criteria

There are other supplementary criteria in conferring originating status, such as provisions regarding insufficient working or processing operations, accessories, spare parts and tools, neutral elements, sets and/or direct transport. Most of these supplementary criteria are used in similar ways in both the KAFTA and the KSFTA.

2.3. ASEAN-China FTA

Rules of origin in the ACFTA are compact and straightforward, as is the case with AFTA rules of origin. The ACFTA's rules of origin seem to be influenced by the AFTA, which mostly uses the percentage criteria method in determining whether non-originating materials have undergone a substantial transformation.

Defining wholly obtained or produced products in the ACFTA is similar to other FTAs we have looked at so far. A slight difference is with regard to recognizing vessels of a Country: in the ACFTA, a vessel is considered as a vessel of a Country if it is either registered with a Party or entitled to fly the flag of that Party. This is according to Rule 3(f) of Annex 3 of the ACFTA, which recognizes "(p)roducts of sea fishing and other(s) ... by vessels registered with a Party or entitled to fly the flag of that Party." It is a looser requirement compared to other FTAs, such as the KAFTA and the KSFTA. In both the

KAFTA and the KSFTA, it is required that a vessel has to be registered (or recorded) with a Party and fly its flag to be recognized as a vessel from participating parties. Rather than adopting stricter dual requirements, the ACFTA accepts that satisfying one condition is enough to be recognized as a vessel from participating parties.

For not wholly produced or obtained products, the basic rule of determination is the percentage criteria. The way of calculating the ACFTA content is as following;

$$\frac{\left(\begin{array}{c} \text{Value of Non - ACFTA} \\ \text{Materials} \end{array} \right) + \left(\begin{array}{c} \text{Value of Materials of} \\ \text{Undetermined Origin} \end{array} \right)}{\text{FOB price}} \times 100\% \leq 60\%$$

According to the Rule 4 of Annex 3 of the ACFTA, a product is deemed to be originating if

- (i) Not less than 40 percent of its content originates for any Party; or
- (ii) If the total value of the territory of a Party (i.e. non-ACFTA) does not exceed 60 percent of the FOB value of the product of the product so produced or obtained provided that the final process of the manufacture is performed within the territory of the Party.

The percentage criteria, or the 40 percent ACFTA content rule, applies to basically all products which are not wholly obtained or produced, except products specified in the product specific rules in Attachment B. The product specific rules include exclusive rules for some wool products in HS chapter 51 and adopt the change in tariff classification method for 42 products (in HS 6 digits). It also specifies specific rules for textile and garment products.

One of the distinguished features in the ACFTA is the cumulation provision. Rule 5 of Annex 3 of the ACFTA refers to cumulative rules of origin, which says,

“Unless otherwise provided for, products which comply with origin requirements provided for in Rule 2 and which are used in the territory of a Party as materials for a finished product eligible for preferential treatment under the Agreement shall be considered as products originating in the territory of the Party where working or

processing of the finished product has taken place provided that the aggregate ACFTA content (i.e., full cumulation, applicable among all Parties) on the final product is not less than 40 percent.”

Among the six FTAs we consider here, only the ACFTA and the AFTA adopt the full cumulation provision. Applying full cumulation has advantages in terms of increasing trade and enhancing economic integrity among participating countries. We will further discuss the cumulation provision in the following section.

2.4. Japan-Singapore and Japan-Malaysia EPAs

Japan has two FTAs with two ASEAN member countries, Singapore and Malaysia. The FTAs Japan has with Singapore and Malaysia use the terminology EPA rather than FTA, insisting that they are different from other FTAs in the sense that the agreements give emphasis to bilateral cooperation in the field of mutual interest.

2.4.1. Wholly Obtained or Produced Goods

Article 23 of Chapter 3 in the JSEPA and Article 28-1 of Chapter 3 in the JMEPA define goods that are wholly obtained or produced. They contain similar contents; however, the difference lies on how factory ships of a Country are defined. In the JSEPA, goods from the sea, seabed, or beneath the seabed are required to be taken by vessels of that Party and flying the flag of that Party is enough to be considered as “a vessel of that Party.” On the other hand, in the JMFTA, Article 27(d) says that

“the terms “factory ships of the Country” and “vessels of the Country” respectively mean factory ships and vessels:

- (i) which are **registered** in the Country;
- (ii) which sail under the **flag** of the Country;
- (iii) which are **owned** to an extent of at least 51 percent by nationals of the Country, or by a juridical person with its head office in the territory of the Country, or which the representatives, chairman of the board of directors, and the majority of the members of such board are nationals of the Country, and of which at least 51 percent of the equity interest is owned by nationals or juridical persons of the Country; and
- (iv) of which at least 75 percent of the total of the master, officers and crew are nationals of the Countries or third State which are member

countries of the ASEAN;”

Unlike the JSEPA case, it has stronger requirements to be considered as a vessel of a Country and it seems to reflect Japanese concerns regarding the importation of fishery products.

2.4.2. Not Wholly Obtained or Produced Goods

Goods that are not wholly obtained or produced in a Country are treated as originating goods of a Party if goods have undergone sufficient transformation in the Party. The criteria of determining whether a good has undergone sufficient transformation are defined in the Annexes as product specific rules. The product specific rules are expressed by either the change in tariff classification, the value added, or by a combination of these two.

In the JSEPA, most goods have one corresponding product-specific rules of origin based on the change in tariff classification. The percentage criteria method is used as an alternative choice for some products. The qualifying value content of a good is calculated as follows:

$$QVC = \frac{FOB - NQM}{FOB} \times 100,$$

where NQM is the non-qualifying value of materials used by the producer in the production of a good. 264 products are specified by two alternative rules. For those products, they qualify for preferential tariff treatment, if

- (i) it has undergone a change in tariff heading (change in HS 4 digits), or
- (ii) the qualifying value content is no less than 60 percent.

In the JMEPA, product specific rules are defined in a similar way: for substantial transformation of non-originating materials, products need to qualify for both the change in tariff classification and the percentage criteria. Also, the JMEPA adopts the technical test method for some textiles and garments. For example, for HS 55.12-55.16, it requires either

- (i) A change to heading 55.12 through 55.16 from any heading outside that group, provided that, where non-originating materials of heading 55.8 through 55.11 are used, each of the non-originating materials is spun, or dyed or printed entirely in the territory of either Country or a third

- State which is a member country of the ASEAN; or
- (ii) No required change in tariff classification to heading 55.12 through 55.16, provided that the good is dyed or printed and that the non-originating material of that group is woven in the territory of either Country or a third State which is a member of country of the ASEAN.

Different from the JSEPA, the threshold level of the percentage criteria in the JMEPA ranges from 40 to 60 percent, depending on the product. It is less restrictive than the JSEPA and reflects the country specific characteristics of Singapore, which specializes in intermediate trade.

By comparing product specific rules between the JSEPA and JMEPA, we can conclude that they are similar in terms of the methods and/or criteria on which substantial transformation is determined; however, they are different on a product by product basis. This shows the different situations and concerns of participating countries in each EPA.

2.5. Problem of Increased Complexity of Rules of Origin in East Asia

So far, we have looked at the rules of origin in the intra-regional FTAs of East Asia. They share similarities in terms of methods adopted by each FTA; however, they are quite different at the product-specific description level. Some specify originating status in a long and tedious way, while others have a relatively simple way of determining the country of origin.

The AFTA and the ACFTA have simple and compact rules of origin. For most products which are not wholly obtained and produced, rules of origin require that non-originating import content does not exceed 60 percent or originating content is more than 40 percent of the FOB price of the product. The percentage criteria method, which is the main method to determine originating country, is the most efficient because it is simple and straightforward and applicable to all goods. However, this method requires that participating countries have advanced and transparent accounting systems; to prove that domestic content exceeds 40 percent of the FOB price of the product, the exporting country or firm needs to have clear accounting system. Otherwise, the exporting country may cheat the importing country or disputes may arise regarding the proof of origin. For such reasons, some countries are hesitant to use the percentage criteria as a dominant method. This is especially true in East Asia where there is differing levels of development among countries. Thus, it does not seem to be a universally applicable option for East Asian FTAs yet.

On the other hand, rules of origin for the KAFTA, the KSFTA, and those

between Japan and two ASEAN member countries are based on product specific rules of origin. All of these FTAs adopt a change in tariff classification and the percentage criteria as main decision mechanisms. However, at the product-specific level, the criteria of conferring originating status is quite different and there even exist products that apply to different rules of origin in the different FTAs concluded by a single country.

Difficulties arise when one product faces different rules of origin for customs purposes in various markets.³⁶⁾ For example, it is possible for producers to have multiple sets of supply schedules for intermediate inputs in order to export their outputs to different countries, only to meet differing rules of origin requirements. These difficulties force some firms to give up receiving preferential tariff treatment. This is not what each FTA is aiming for. Also, these situations increase the complexity of production and limit the gains from having numerous FTAs. Rules of origin are designed to prevent the problem of free-riding and should have a neutral and minimal impact on trade flows. However, as more and more rules of origin enter into the region and increase the complexity and administrative costs, it forces exporters to limit their exports to certain countries/region in which they can meet rules of origin requirements. If such specialization processes become aggravated, it will weaken the incentive to form an integrated market in the region.

Rules of origin reflect the bilateral (or multilateral) relationship between participating countries. What a country adopts with one country can be a rule that the same country wants to avoid with another country. This causes all sorts of complexities in the rules of origin in East Asia and it will become an important factor that possibly deters East Asia from improving its economic integrity.

3. Improving Rules of Origin in East Asia

Since 2000, the proliferation of FTAs has become a new trend in East Asia. The complete web of FTAs in East Asia may be accomplished soon, considering all the FTAs currently under negotiation and the number of feasibility studies that have been initiated. It is obvious that economic integration and closeness between East Asian countries increase with FTAs, but it does not necessarily imply that the region is heading toward a single economic

36) Brenton (2003), pp. 13.

community. The web of bilateral FTAs may cause many economic obstacles for East Asian economic integration or further, it may even disturb multilateral negotiations.

Rules of origin is at the center of such pessimism; each of the rules of origin in the bilateral FTAs, which inherently reflect participating countries' interests and concerns, use unique product specific methods to confer originating status. This brings inefficient results in terms of production and the flow of trading goods. Given that forming one regional trade bloc, like the EU or NAFTA, in East Asia is hard to achieve or, at least, not eminent, one way to get around the limitation of the web of multi-bilateral FTAs in East Asia and reduce the negative impact of rules of origin is to modify the cumulation provision. In this section, we turn our attention to the cumulation provision and look at the possibility of introducing diagonal cumulation to the intra-regional FTAs in East Asia.

3.1. Cumulation Provision

The cumulation provision sets the conditions under which inputs imported from certain sources may be counted as domestically supplied in the (preference-receiving) exporting country.³⁷⁾ It has recently received greater attention as a sensible means of overcoming the limitations of rules of origin. There are three types of cumulation provisions: bilateral cumulation, diagonal cumulation, and full cumulation.

Bilateral cumulation is the lowest level of cumulation in terms of supply coverage of input resources and is applied among the participating parties to a given FTA. It counts materials supplied by any participating country of the FTA as domestic materials when the regional value content is calculated. On the other hand, under diagonal cumulation, materials originating from one country are considered as originating in all other countries. Such a cumulation provision exists between the EU, EFTA countries, the countries of Central and Eastern Europe, and Turkey, which are usually referred to as the Pan European Cumulation System (PECS). Lastly, full cumulation alleviates the property of 'all-or-nothing' that the bilateral cumulation has. It allows intermediate processing to be split when calculating regional value content. The FTA between China and ASEAN and agreements between the EC and the countries of the Maghreb adopt full cumulation, as well as the FTA between the EU and the countries of the European Economic Area (EEA), which adopts a full cumulation provision.

37) Cited from the WTO, WT/REG/W/45.

If a unified East Asia FTA, which comprehensively includes all East Asian countries, is not a plausible option or not imminent, applying diagonal cumulation may be considered as an intermediate step to East Asian economic integration. There is no FTA in which diagonal cumulation has been introduced so far in East Asia. Out of the six inter-regional FTAs that we have looked at in previous sections, the KAFTA, the KSFTA, the JSEPA, and the JMEPA apply bilateral cumulation, while the AFTA and the ACFTA adopt full cumulation with minimal content conditions.³⁸⁾

The most notable economic impact of diagonal cumulation is that it can mitigate the trade diversion effect of rules of origin which usually gives producers in the exporting country an incentive to import intermediate goods from the trading partner country to meet rules of origin, even though the trading partner is not the most efficient producer of those intermediate goods. That is, rules of origin hamper cost efficient production leading to market distortion. If diagonal cumulation is introduced, producers in the exporting country have more choice in terms of selecting their supply of intermediate goods or resources and their incentive to buy intermediate products from the bilateral trading partner country reduces. As long as those materials or intermediate goods used to produce exporting goods are supplied from the region that is covered by diagonal cumulation, such materials count as domestic content when calculating regional content. Therefore, diagonal cumulation can reduce the trade diversion effect of rules of origin and facilitate trade in the region.

Empirical evidence can be found in the PECS. The PECS was introduced in 1997 among the EU 15, EFTA4, then 10, and applicant-nations in Central Europe. The PECS shows the expansion of the diagonal cumulation system that was adopted by the EU to other neighboring countries. Augier et al. compare the imports of the EFTA from other non-EU countries that joined the PECS and the EU, as well as the rest of the world. Their results show that, before 1997

38) The way of defining cumulation type is based on bilateral agreements. The KAFTA and the ACFTA are free trade agreements which are bilateral in the sense that the negotiating parties are Korea and ASEAN; China and ASEAN. On the other hand, it can be viewed as multilateral since a total of 11 countries (in both the KAFTA and the ACFTA) are involved. For this reason, some researchers define the cumulation provision in the ACFTA as bilateral cumulation and the provision in the KAFTA as full cumulation. However, considering that the ACFTA cumulation provision has some modified properties of full cumulation, we classify it as full cumulation, while that in the KAFTA as bilateral cumulation. (In addition, the ACFTA text clearly states that its cumulation provision adopts "full cumulation.")

(when the PECS was adopted), imports of the EFTA from non-EU, EU, and the countries from rest of the world increased at similar rates. However, after 1997, the rate of increase in the imports from non-EU countries who entered the PECS exceeded that from the EU and the rest of the world.³⁹⁾ This result shows that the change in the cumulation provision from bilateral to diagonal cumulation facilitates trade within a region, especially between spoke countries.

We can expect similar results: if we introduce diagonal cumulation in East Asia, it will increase trade among countries in East Asia. Also, as anything produced in East Asia will be considered a domestic product, it will virtually establish one huge production market. That is, simply adopting the bilateral cumulation will allow us to initiate a single production market in the region even without an agreement on the EAFTA.

3.2. *Applying Diagonal Cumulation in East Asia*

We have shown how diagonal cumulation positively impacts trade and economic integration in the region. However, introducing diagonal cumulation has several prerequisites: (i) there exist FTAs between the countries involved in the acquisition of originating status and the country of destination, (ii) identical rules of origin apply for all participating countries, and (iii) there should be 'no drawback' provision.⁴⁰⁾

First, applying diagonal cumulation requires all countries to be connected to bilateral FTAs. At this moment, only the KAFTA and the ACFTA have been concluded and Japan has separate FTAs with two ASEAN member countries. FTA negotiations between Korea and Japan are ongoing; however, it has been at stalemate since June 2005 due to economic and political reasons. The Korea-China FTA negotiations are expected to launch soon, but there is still no movement toward an FTA between China and Japan.

The next, and probably the most challenging, problem is harmonizing the rules of origin in each FTA. Harmonizing rules of origin is unavoidable for multilateral economic integration. In the East Asian region, where multilateral negotiations among East Asian countries are not imminent, harmonizing rules of origin will be a great help for improving economic integration and intra-regional trade by getting rid of complexities due to different rules of origin.

However, it will not be easy to achieve. European countries have successfully

39) See Augier *et al.* (2005) pp. 583-584.

40) See Augier *et al.* (2002) and European Economic Area in Protocol 4, Article 5 and 14 for detailed information.

harmonized rules of origin by launching the PECS in 1997. The harmonizing process was relatively simple in the European case: first of all, the EU, which dominates the regional economy, took the leading role and non-EU countries were forced to adopt the EU's rules of origin. Also, by the mid-1990s, 10 out of 13 non-EU PECS members were expected to be members of the EU within a decade in any case. Therefore, for those countries, the PECS simply meant adopting the EU rules of origin a few years in advance.⁴¹⁾

Contrary to the PECS, the problem in East Asia is that there is no leading country, or hub country. Harmonizing and negotiating the rules of origin that were already concluded in each FTA with the participation of all countries will be an extremely hard process, if not impossible. Rather than trying to harmonize the existing rules of origin in each agreement, it may be more plausible to establish new rules of origin, proposed by a country or a group of countries who can force others to adopt these new rules. ASEAN already has two major FTAs in the region with Korea and China, but it is hard to expect ASEAN to take a leading role because of its economic power in the region. On the other hand, if one of three Northeast Asian countries takes a dominant role, it may not be an ideal situation for the other two Northeast Asian countries.

The alternative is to achieve harmonization in a gradual way. Instead of introducing diagonal cumulation for all East Asian countries simultaneously, it may be more realistic to adopt it partially and expand its coverage area later on. The Korea-China FTA, if negotiations successfully launch, may be a great opportunity to do this. Both countries have FTAs with ASEAN and they can take leading roles together. Because of its size and economic impact, the Korea-China FTA may induce ASEAN to replace the rules of origin in previous FTAs with Korea and China with new rules that contain a diagonal cumulation provision covering Korea, China, and ASEAN. It will give stronger incentive for Japan to participate in the system and if it starts or resumes free trade negotiations with East Asian countries, it may make it easier for Japan to adopt diagonal cumulation.

For these reasons, we need to harmonize rules of origin and consider contents that are to be included in such harmonized rules of origin. There is no best way of determining the originating country and each East Asian FTA has different rules of origin that use different methods and criteria. When thinking of harmonization, the key principle should be to keep it simple, transparent, and flexible so that it can minimize the negative effects that rules of origin

41) Augier *et al.* (2005).

inherently contain.

In this section, we looked at the rules of origin in the intra-regional FTAs in East Asia. The major problem with respect to rules of origin in the region is its complexity and diversification, which can lead to market distortion and hamper incentives for regional integration. Diagonal cumulation offers the possibility of mitigating the market distorting effect of rules of origin in East Asia. Given the web of bilateral FTAs in East Asia, diagonal cumulation is a way to virtually integrate the East Asian economies into one single territory, at least in terms of the production side of the economy.

However, introducing diagonal cumulation requires harmonized rules of origin within participating countries. As is mentioned above, reaching an agreement on a unified rules of origin for all 13 countries in the region will be hard to achieve. What we argue in this paper is that if countries in the East Asian region acknowledge the need for regional integration and an EAFTA is a common goal, having harmonized rules of origin will not be as difficult to reach as we imagine at this moment. If an EAFTA is what we are trying to achieve as a common goal, agreeing on a single rules of origin is what we have to agree on first. As observed in the PECS, harmonization will simply mean adopting rules of origin, which will be in effect under an EAFTA anyway, a few years in advance.

In this regard, diagonal cumulation can be considered as an intermediate target for the EAFTA. By reaching this intermediate target, we can reduce the market distorting impact of rules of origin in the region, increasing the integrity of the region as a single production market, and have a better position to go forward toward an EAFTA.

IV. Services, Investment and Other Issues in East Asian FTAs

This chapter will analyze the service sector, investment sector, facilitation in trade and investment, and development cooperation. The FTAs that have been contracted in East Asia include: the Korea-Singapore FTA, the Japan-Singapore FTA, the Japan-Malaysia FTA, and the AFTA. However, as stated earlier, negotiations related to the service and investment sectors are currently underway for two agreements and, thus, analysis of service and investment will be limited to the remaining three FTAs.

Trade and investment facilitation is in itself not a hugely important issue. However, facilitation has a great deal of meaning in East Asia where high-quality FTAs are generally difficult to contract due to gaps in economic power and level of industry. Thus, in this situation, facilitation of this sort could lead to greater promotion of trade and investment among East Asian countries. Analysis of facilitation in trade and investment is covered in section 2.

Development cooperation is also not considered to be an important part of FTAs overall; however, it has significance for FTAs among countries with large gaps in economic power, like the EAFTA. We, therefore, analyze development cooperation as method of solving gaps in economic power in section 3.

1. Liberalization in Services and Investment

1.1. AFTA

1.1.1. Contents for Service and Investment

The endeavor to open the service market between ASEAN member countries started from the Fifth ASEAN Summit in 1995, when ASEAN countries signed the ASEAN Framework Agreement on Services (AFAS). The agreement specifies the objective of AFAS as the enhancement of cooperation, elimination of substantial restrictions and liberalization of trade in services among member states.⁴²⁾ It was to complement the establishment of the ASEAN Free Trade Agreement (AFTA) and to strengthen ASEAN's service sector.

AFAS adopts the structure and approach of GATS in the WTO, using the positive request-offer method, sometimes called the hybrid method. It is based on the GATS-plus principle; for WTO members, it means that they are eligible for commitments that are better than GATS or can be offered new service sectors not covered by GATS. On the other hand, for non-WTO members, commitments cannot go below what a member country has at the time of signing.

Three rounds of negotiations have been completed and four Packages of Commitments have been signed by the ASEAN Economic Ministers. The first round produced the First and Second Package, which were signed in 1997 and 1998, and the Third and Fourth Package of Commitments were agreed to in 2001 and 2004. The current fourth round is expected to conclude by the end of 2006.

Due to the different stages of development, some ASEAN countries were reluctant to open their service markets, resulting in slow negotiations. To get around this problem, new methods, such as a common subsector approach and an ASEAN Formula-X have been adopted to accelerate the opening up of ASEAN service markets. Under the (modified) common subsector approach, a particular subsector would be identified as a common subsector if three or more member countries made commitments in this particular sector under the GATS or the AFAS. The identified common subsector would be subjected to the removal of all restrictions for modes 1 and 2, and the gradual removal of barriers for modes 3 and 4. On the other hand, the ASEAN-X formula allows two or more member countries to conduct negotiations and agree to liberalize trade in services for specific sectors or subsectors, while others may join whenever they are ready. Both of these methods are to expand and deepen negotiations among the ASEAN member countries; however, there have been no reports of an open service market using the ASEAN Formula-X so far.

The new approach, called formula approach, is being discussed in the fourth round of negotiations as an alternative to the request-offer approach. This approach was used in the GATT/WTO system for negotiations on trade in goods; the member countries set a target year by which each country is obliged to remove service market barriers according to the schedule set for each year. It is reported that they consider a sector or subsector open if modes 1 and 2 are unbound and if it satisfies a specific requirement set for mode 3. Since it is currently under negotiation, detailed information regarding the formula

42) ASEAN Framework Agreement on Services (1995).

approach is still limited.

The ASEAN financial crisis prompted ASEAN member countries to launch the “Bold Measures” policy. In response to the rapid drop in FDI to the ASEAN region, Bold Measures were implemented to promote the wider use of AIA. Short-term measures include income tax exemption, corporate investment tax allowance, duty free imports of capital goods, freer domestic market access, allowing 100 percent foreign equity ownership, and so forth. These measures applied to all investors, ASEAN or non-ASEAN and each ASEAN member country announced specific measures to allow for greater liberalization of the investment market and to attract more FDI into the region.

In addition to the Bold Measures, ASEAN member countries agreed on the Framework Agreement for the AIA at the Fifth ASEAN Summit on October 1998. The objective of AIA is to attract more FDI into the region and its contents go beyond those in Bold Measures. The agreement binds member countries to “progressively reduce or eliminate investment regulations and conditions, which may impede investment flows and the operation of investment projects in ASEAN.”⁴³⁾

To achieve liberal investment in the region, the AIA calls for the immediate opening up of all industries except for certain exempted industries. It also calls for ASEAN countries to immediately grant national treatment to all investors, with certain exceptions. There are three categories of exclusions that are subject to immediate liberalization: the Temporary Exclusion List, the Sensitive List, and the General Exclusion List. The Temporary Exclusion List contains industries and investment measures that are temporarily closed to investment and not granted national treatment, but will open up within a specified timeframe. The Sensitive List covers industries and investment measures that are not subject to phasing out, but will be reviewed by the AIA Council in 2003 and at subsequent intervals thereafter, and the General Exclusion List consists of industries and investment measures that will not open up for investment or be granted national treatment for reasons such as national security, public health, public morals, and environmental protection.

Exclusions included either in the Temporary Exclusion List or the Sensitive List will be opened by 2010 for ASEAN investors and by 2020 for non-ASEAN investors. Also, national treatment will be given to the industries in the Temporary Exclusion and Sensitive Lists by 2010 for ASEAN investors and by 2020 for non-ASEAN investors.

43) Framework Agreement on the ASEAN Investment Area, Article 3 (iv).

The AIA is the realization of economic integration and regional cooperation and views the ASEAN region as a single investment area. The facilitation of cost-effective industrial and production activities in ASEAN is expected by providing firms with greater synergy and services. Unlike other bilateral investment agreements, which limit application to participating countries, the AIA will eventually open up its investment market to all investors and investments. The AIA is an attempt to integrate the regional investment market and attract more FDI into the region.

1.1.2. Characteristics and Assessment of AFTA

AFAS service negotiations are limited to seven sectors (out of twelve) in the WTO CPC classification system. They include air transportation, business, construction finance, maritime, telecommunications, and tourism services. Since the negotiations were limited from the beginning, it is hard to judge which sectors are sensitive and which are not in each country.

Following the hybrid method that is used in GATS, AFAS has positive lists of schedules of specific commitments. Through four packages, each country submitted its own list of sub-sectors that are at least partially opened. What country opens which sector is shown in Annex Table -IV-1. Since AFAS adopts a positive system, sub-sectors that are listed in the schedules of specific commitments show the corresponding country's willingness to open those sectors. The fact that a certain sector is included in the specific commitments schedule does not necessarily mean the corresponding service sector is completely open. Still there may exist restrictions such as the limitation on foreign equity and/or movement of natural persons. However, counting and investigating such sub-sectors, we can derive the coverage of service market opening.

On the other hand, Table IV-1 summarizes the depth of commitments under GATS and AFAS 1, 2, 3, and 4 and the Hoekman Score.⁴⁴⁾ The first thing we notice is that all ASEAN member countries are expanding service market liberalization through AFAS. The number of sub-sectors committed under GATS+AFAS 1, 2, 3, and 4 is larger than that under GATS only. In addition, restrictiveness scores (or Hoekman scores) are lower under GATS+AFAS 1, 2, 3, and 4 than under GATS only, except Laos and Vietnam.⁴⁵⁾

44) The Hoekman score measures the restrictiveness of the commitments reported in terms of percentage. The score ranges from 0 percent, the least restrictive, to 100 percent, the most restrictive.

45) Laos is not a member of the WTO and so does not have GATS commitments. The

In terms of coverage, Cambodia has the most number of sub-sectors committed under both GATS and GATS+AFAS 1, 2, 3, and 4, while Brunei has the least number of sub-sectors. In terms of the depth of liberalization in these service markets (as measured by the Hoekman score) Cambodia's scores are again the lowest (meaning it has the least amount of restrictions), followed by Thailand, Singapore, and Malaysia.

Table IV-1 reveals that the openness of each service market and the degree of economic development are not exactly correlated. Cambodia and Vietnam, who are members of the so-called CLMV countries, sustain higher service market openness than other ASEAN-6 member countries. Also, for countries such as Singapore and Malaysia, who have the most developed service markets among ASEAN countries, the opening of their service markets under AFAS is

Table IV-1. Coverage of Commitments and the Hoekman Score

| | The number of subsectors committed under GATS | The number of subsectors committed under GATS+AFAS 1, 2, 3, and 4 | Restrictiveness score under GATS | Restrictiveness score under GATS+AFAS 1, 2, 3, and 4 |
|-------------|---|---|----------------------------------|--|
| Brunei | 26 | 88 | 95.11 | 86.77 |
| Cambodia | 146 | 177 | 68.31 | 62.31 |
| Indonesia | 61 | 95 | 93.17 | 80.67 |
| Laos* | | 90 | | 81.54 |
| Malaysia | 122 | 154 | 80.04 | 76.26 |
| Myanmar | 36 | 108 | 93.02 | 85.22 |
| Philippines | 36 | 109 | 90.07 | 77.03 |
| Singapore | 102 | 111 | 73.35 | 71.17 |
| Thailand | 127 | 172 | 77.76 | 63.71 |
| Vietnam** | 139 | 151 | 77.47 | 77.57 |

Note: * Laos is not a WTO member.

** The GATS schedule for Vietnam is in its WTO entrance paper.

Source: Modified from Thanh and Bartlett (2006).

Hoekman score under GATS+AFAS 1, 2, 3, and 4 is higher than that under GATS only. This is due to Vietnam's recent endeavors to enter the WTO.

quite marginal. It reflects their intention to deal with service market liberalization in multilateral, global negotiations, rather than regional negotiations.

1.2. Korea-Singapore FTA

1.2.1. Contents of Services and Investment

Korea concluded an FTA with Singapore in August 2005, which went into effect on March 2, 2006. The Korea-Singapore FTA has a comprehensive scope covering: goods, service and investment, rules of origin, sanitary and phytosanitary measures, technical barriers to trade, telecommunications, financial services, competition, government procurement, intellectual property rights, cooperation, as well as trade remedies and dispute settlement.

As shown in Table IV-2, there will not be any delays in liberalizing the service sectors in the Korea-Singapore FTA, except for those fields proscribed in the agreement in accordance with the negative list method. Korea has excluded a total of 322 items (188 current reservations and 134 future reservations) related to the service sector, while Singapore has reserved 79 items (30 current reservations, 49 future reservations). A simple comparison of the figures reveals that the extent of opening in Singapore is higher than that of Korea. The present degree of opening in the Korean service sector is 72.3 percent (= 100 percent – 27.7 percent) and that of Singapore is 95.6 percent (= 100 percent – 4.4 percent).

Table IV-2. Korea-Singapore Service Sector Reservations

| | Korea | | Singapore | |
|-----------------------------------|--------|--------|-----------|-------|
| | Number | Ratio | Number | Ratio |
| Reservation for existing measures | 188 | 27.7 % | 30 | 4.4% |
| Reservation for future measures | 134 | 19.7% | 49 | 7.1% |

Source: Calculated by authors from the Annexes of the Korea-Singapore FTA

Tables IV-3 and IV-4 reveals the present status of reservations in the service sectors of each country. These tables include the major sub-sectors with regard to services. In Korea, environment service sectors have the greatest importance; on the other hand, in Singapore, the business service sector is given the most weight in the short-term and transport service has greater importance among future reservations.

In principle, investment is liberalized, with some exceptions like business

Table IV-3. Summary of Reservations for Existing Measures in the Service Sectors

| Sector | Major Sub-sectors |
|---|---|
| Business Services | Professional Services, Industrial Safety and Health Institution (K), Private Investigation Services (S), Consulting (K) Technical testing and analysis services (K) |
| Distribution Services | Retailing Services (K), sales on a animals (K), Wholesale trade services of agricultural raw materials and live animals (K) |
| Environmental Services | Air Quality Control, Waste Water (Sewage) Treatment (K), Composition and purity testing and analysis services (K), Nature and landscape protection services (K) |
| Health Related and Social Services | Veterinary services (K), Medical/Pharmacy Services (S) |
| Transport Services | Road transportation service, Road/Water Transportation, Air transportation service (K), Maritime Transport Service (S) |

Note: S: applies only to Singapore, K: applies only to Korea

and transport services. In addition, it prohibits maintaining or adopting market restriction measures with regard to market access (e.g. quota systems, monopoly, exclusive service providers).⁴⁶⁾ Also, it contains future liberalization provisions to reduce and abolish the restrictions reserved at the time of agreement for market expansion.⁴⁷⁾

To promote investments and to create a liberal, facilitative, transparent, and competitive investment regime, Korea and Singapore agreed to enter into negotiations in order to progressively liberalize the investment regime. They also agreed to strengthen cooperation in investment, facilitate investment and improve the transparency of investment rules and regulations, and provide for the protection of investments. To facilitate investment, Korea and Singapore guarantee national treatment in their FTAs.⁴⁸⁾ Both countries agreed to prohibit

46) FTA between Korea and Singapore, Art. 9.5. Market Access.

47) FTA between Korea and Singapore, Art. 9.8. Future Liberalization.

48) Art. 3.3 National Treatment: "Each Party are to accord national treatment to the goods of the other Party in accordance with article III of GATT, including its interpretative notes, and to this end, Art. III of GATT and its interpretative notes, or any equivalent provision of a successor agreement to which both Parties are Party, are incorporated into and made part of this agreement."

trade restrictions in investment.⁴⁹⁾ In accordance with investments, Korea and Singapore may “impose or enforce any requirements, or enforce any commitment or undertaking, in connection with the establishment, acquisition, expansion, management, conduct, operation, or sale or other disposition of an investment of an investor of a Party or of a non-Party in its territory.”⁵⁰⁾

Table IV-4. Summary of Reservations for Future Measures in the Service Sectors

| Sector | Major Sub-sectors |
|---|---|
| Business Services | Agricultural and manufacturing services (K), Credit Reporting Services (K), Fishing-Related Activities (K), Professional Services(Legal Services-K), Professional Engineering services (S), Financial Auditing services (S), Private Investigation Services (S) |
| Communication Services | Broadcasting, Postal Services (K) |
| Education Services | Primary Education Services, Secondary Education Services, Secondary Education Services, higher education services |
| Environmental Services | Transportation of other goods (K), sewage service (K), refuse disposal service (K) |
| Health Related and Social Services | Services furnished by trade unions (S), social services (S), medical service (S), pharmacy service (S) |
| Transport Services | Transportation by non-sea-going vessels and transportation via space (K), Air Transport Services—Computer Reservation Systems (S), Public Transport Services (S), Land Transport Services Services (S), Maritime Transport Services (S) |

Note: S: applies only to Singapore, K: applies only to Korea

To promote Investment between Korea and Singapore, the two countries are to “accord to investments of investors of the other Party treatment in accordance with the customary international law minimum standard of treatment,”⁵¹⁾

49) Art. 11.3 National Treatment: “Each Party are to accord to services and service providers of the other Party treatment no less favorable than that it accords, in like circumstances, to its own services and service providers.”

50) Art. 10.7 Performance requirements, Korea-Singapore FTA.

including fair and equitable treatment and full protection and security.”⁵²⁾ Each country is to permit all transfers relating to an investment of an investor of the other country to be made freely and without delay into and out of its territory.

Regarding domestic regulations, it guarantees the reasonable, objective, and fair enforcement of all measures affecting the trade of services. In case of issues affecting the trade of services, it prescribes rapid legal examination when a service provider requires it.⁵³⁾

Regarding payment and remittance regulations, there are no restrictions on international payments and remittances for current transactions with related countries. However, if a counterpart country suffers from a serious international

Table IV-5. Summary of Reservations for Existing Measures in the Investment Sector

| Sector | Major Sub-sectors |
|--|--|
| Business Services | Advertising, Research services, Professional Services, Technical testing and analysis services (K), Manufacture of Chemical Products (K), Private Investigation Services (S), Manufacturing (S), |
| Communication Services | Basic Telecommunications Services, Audio visual services, Courier services (S), entertainment services (S) Real estate services (S) |
| Construction and Related Engineering Services | Construction Services, Renting, Maintenance & Repair, Sales and Disassembly of Construction Equipment (S) |
| Distribution Services | Sales on a fee or contract basis of agricultural raw materials and live animals (K), Retailing Services (S) |
| Education Services | Higher education services (K), Adult education services n.e.c. (K) |
| Recreational, Cultural and Sporting Services | News Agency services, entertainment services (S) |
| Transport Services | Freight Transportation by Air, Water Transportation, Air Transport Services |

51) Art. 10.11 Transfer, Korea-Singapore FTA.

52) Art. 10.5 Minimum Standard of Treatment, Korea-Singapore FTA.

53) FTA between Korea and Singapore, Art. 9.11. Domestic Regulation.

payment balance, financial difficulties, or a crisis, limitations on the service trade may be adopted or maintained according to Articles 11 and 12 of GATS.⁵⁴⁾

Table IV-5 and IV-6 indicate the present status of reservations with regard to investment sectors between Korea and Singapore. These tables include the major sub-sectors in each sector and full coverage is summarized in Annex Table IV-2 to Annex Table IV-9.

Table IV-6. Summary of Reservations for Future Measures in the Investment Sector

| Sector | Major Sub-sectors |
|---|---|
| Business Services | Credit reporting services, Agricultural and manufacturing services (K), Professional Services (legal services-K), Betting and Gambling Services (S) |
| Communication Services | Broadcasting services (K), Postal services, Courier Services (S) |
| Distribution Services | Commission agents' services, Wholesale trade services |
| Education Services | Primary education services, Secondary education services, Higher education services (K), Adult education services n.e.c. (K) |
| Environmental Services | Sewage Services, Refuse disposal services, Sanitation and similar services, Nature and landscape protection services |
| Health Related and Social Services | Social Services, Services provided by health-related professionals (S) |
| Transport Services | Transportation by non-sea-going vessels and transportation via space (K), Air transport service (S), Land Transport Services (S) |

1.2.2. Characteristics and Assessment of Korea-Singapore FTA

When comparing the list of reservations, the extent of opening in Singapore is greater than that of Korea in the service and investment sector.⁵⁵⁾ We can assess from the disparity in the number of reservations that Korea has not taken an active part in market opening. The characteristics of the FTA between Korea and Singapore are that Korea has more reservations on opening its environmental

54) FTA between Korea and Singapore, Art. 9.16. Balance of Payments Exception.

55) See Table IV-16: comparison of Opening degree in service sector.

sectors, while Singapore is more open to liberalizing that specific sector. With regard to current and future reservations, the tourism and travel related service sectors have not been included yet.

The liberalization of the service sector with Singapore created momentum for Korea to strengthen its service sector competitiveness. Korea and Singapore agreed to open the entire service and investment sectors, but specified some exceptions by proscribing environment services, business services, gas industry and transport services. Singapore also excluded the gas industry, transport services and environment services.

Korea has not lifted the ban on professional services like accounting, industrial safety, health institutions, technical testing and analysis services in the service sectors. With regard to professional services, Korea requires professional licenses in each applicable field, registration licenses from the head of the applicable authority or minister, and the obligatory provision of local residency as well. Singapore also reserved the opening of the professional business service, such as legal services. In addition, Korea has not opened its environment services.

In relation to distribution services, unprocessed agricultural products, animal brokerage, and wholesale services do not have preferential treatment for domestic citizens. There are also restrictions on market access, as well as a requirement for local residency by receiving a license from the mayor or governor of a locality when opening a private wholesale market.

For Singapore, the distribution, issuance, and printing of newspapers have limitations, while trade services, such as distribution services, commission agent's services, wholesale trade services, retailing services, franchising, and others also reserve opening.

Communications services limit the stock ownership of foreigners. Securities of key communications businesses are regulated so as not to have shares of foreign governments and foreigners exceed 49 percent of total outstanding shares. In addition, those without Korean nationality, foreign governments, and representatives of foreign governments, foreign corporations, or foreign organizations are to not open up a cable station under the Electronic Frequency Act.

Korea reserves the right to adopt or maintain any measure with respect to electric energy, especially electric power generation other than nuclear power generation, electric power transmission, distribution and sales, electric work, and inspection of electrical facilities. The gas industry is not open to foreign investment. In the FTA with Singapore, transportation services related to inland transportation (passengers and cargoes), transportation support and incidental services were not opened.

1.3. *Japan-Singapore EPA*

1.3.1. Contents for Service and Investment

Japan concluded its first EPA (Japan-Singapore New Age Economic Partnership Agreement: JSEPA, effective from November 2002) with Singapore. The JSEPA was the first case in which Japan converted its multilateral liberalization policy into an economic liberalization method under a dualistic policy.

The Japan-Singapore EPA is quite comprehensive. It covers rules of origin, customs procedures, cross-border trade in services, investment, final services, competition, government procurement, intellectual property rights, trade in goods, paperless trading, mutual recognition, movement of natural persons, information and communication technology, science technology, trade and investment promotion, small and medium size enterprises, broadcasting, tourism, and dispute settlement.

Table IV-7. Coverage of JSEPA in the Service Sectors

| Sector | Major Sub-sectors |
|--|---|
| Business Services | Professional Services, Rental and Leasing Services without Operators, Computer and Related Services |
| Communication Services | Audiovisual Services, telecommunications services |
| Construction and Related Engineering Services | Installation and Assembly Work |
| Distribution Services | Retailing Services, Wholesale Trade Services, Franchising (S) |
| Education Services | Primary, Secondary, Higher Education Services |
| Environmental Services | Sewage Services |
| Financial Services | Banking and other financial services |
| Health Related and Social Services | Social, Hospital Services |
| Tourism and Travel Related Services | Hotels and Restaurants |
| Recreational, Cultural and Sporting Services | Libraries, Archives, Museums and Other Cultural Services |
| Transport Services | Air, Rail, Road Transport Services, Maritime Auxiliary Transport Services |

Japan followed the positive list method for services in its FTA with Singapore. Table IV-7 shows the coverage of JSEPA in service sector, which includes the major sub-sectors in services (full coverage is summarized in Annex Tables IV-10 and IV-11). As we can see from the Table IV-7, Japan and Singapore have agreed to open their service sectors using similar standards.

On the other hand, investment liberalization is negotiated using the negative list method. The sectors that are included in the list are summarized in Table IV-8.

Under the Japan-Singapore EPA, both countries define those fields in which market access is permitted; in other words, there are no limitations on the number of service providers irrespective of existing quotas, exclusives, monopolistic services, or economic demand reviews. In addition, both countries stated that neither the total production volume of services nor the number of service operations will be limited by quotas or economic demand reviews.⁵⁶⁾

Table IV-8. List of exceptions in the Area of Investment

| Matter | Coverage | | Sector | Coverage | |
|--------------------------------------|----------|----------|---|----------|----------|
| | Japan | Malaysia | | Japan | Malaysia |
| Land Transaction | ✓ | ✓ | Agriculture, plant Breeder right | ✓ | |
| Money Transaction | | ✓ | Mining Industry including Oil and Natural Gas Exploration and Development | ✓ | |
| Privatization | | ✓ | Water Transport Industry | ✓ | |
| Prior Notification | ✓ | | Telecommunications Industry | ✓ | |
| Formalities | ✓ | ✓ | Financial Services | ✓ | |
| Public Monopoly and State Enterprise | ✓ | | Investments in Services | | ✓ |
| Subsidies/incentive | ✓ | ✓ | Investment in specific sectors | ✓ | |
| Permanent Residents | ✓ | | Arms and Explosives Sector | | |
| | | | Manufacturing Sector | | ✓ |

56) JSEPA, Art. 59 Market Access.

For domestic regulations, Japan and Singapore guaranteed the implementation of all actions that influence service trade using reasonable, objective, and fair methods.⁵⁷⁾ Furthermore, both countries decided to establish a conflict resolution body or the procedures required to enable the above system for prompt review of administrative decisions impacting service trade, providing appropriate relief for administrative decisions.

In relation to monopolies and exclusive service suppliers, both countries guaranteed that they will not act in ways that are inconsistent with the commitment of both parties in supplying monopolistic services by monopolistic service providers.⁵⁸⁾ Under the EPA of Japan and Singapore, with the express exclusion of airline services and domestic marine services,⁵⁹⁾ there are no special regulations on other specific services. However, it does have regulations on co-operation in financial services and information and communication technology fields.⁶⁰⁾ The Japan-Singapore EPA is more comprehensive than the Japan-Malaysia EPA.

1.3.2. Characteristics and Assessment of Japan-Singapore EPA

Singapore restricts the entry of foreigners for its architectural design services. In order to provide architectural design services, a license has to be obtained from the Construction Commission and the service provider must reside in Singapore.⁶¹⁾ Higher education services related to train doctors is defined in a way such that only the higher education institutions of Singapore can operate undergraduate or graduate programs to educate doctors.

In relation to health and social services, nurses, physical therapists, quasi-medical services (limited to nursing and baby delivery services), medical services, pharmacy services and the like are provided by persons who are registered to the respective committee or association and reside in Singapore only.

The key facility service providers in communications service have to be organized under Article 50 of the Singapore Corporation Act, regulated in the aspect of market accessibility and preferential treatment of domestic citizens, and comply with the obligations of the local presence. Power supply, power

57) JSEPA, Art. 64 Domestic Regulation.

58) JSEPA, Art. 65 Monopolies and Exclusive Service Suppliers.

59) EPA between Japan-Singapore Article 58.

60) JSEPA Art. 13 Financial Service Cooperation, Art.14 Information and Communication Technology.

61) The requirement of residency in Singapore was abolished in April 2005.

transmission and distribution are restricted for market accessibility and preferential treatment of domestic citizens.

In the event of retail services related to medical products or wholesale trade services, only the service providers that are designated by the local agent may be allowed to provide medical and health related products and substances for the purpose of medical treatment, moderation, prevention or diagnosis, as well as providing wholesale, retail, and distribution services.

In the transportation services, it reserved the opening of air transportation services, inland transportation services, railway cargo transportation and transportation support services, and marine services. In terms of air transportation services, it discriminates for preferential treatment of domestic citizens; in marine transportation services, cargo processing services, and others, only the service providers who are licensed from the Singapore Marine Port Authority may provide cargo processing services. In addition, all marine transportation service providers may only operate in cruise and passenger terminals owned by the service providers who are licensed from the Singapore Marine Port Authority.

Singapore also regulates the movement of natural persons in entire fields. For airport management, disposition of operation authority, services supplied by the medical institutions under the government's control, or ownership, opening has been postponed.

The opening of the professional service businesses, such as legal services, has also reserved opening. Distribution, issuance, and printing of newspapers have limitations while trade services, such as distribution services, commission agent's services, wholesale trade services, retailing services, franchising, and others also reserve opening.

Singapore has postponed the opening of elementary education, pre-mid-level education, post mid-level education (limited to junior college and preliminary college under the Singapore education system). In medical services, the opening of pharmacy, health, and social services is reserved.

For postal and communication services, opening is postponed and the food and beverage market is also postponed. As a result of the Japan-Singapore FTA, the two countries can create more attractive markets. They can also provide stimulation for economic reforms in both countries, as well as revitalize the economies of the two countries. Moreover, they can complement and reinforce the multilateral trading system and develop closer political and diplomatic relations between the two countries. They can also promote greater mutual understanding between their respective citizens.

1.4. Japan-Malaysia EPA

1.4.1. Contents for the Service and Investment

Under the Japan-Malaysia EPA, air services and domestic marine services were specifically excluded, as was the case with the JSEPA. In addition, the Japan-Malaysia EPA Addendum states that there are to be no limitations on the number of service providers, including a quota or monopolistic or exclusive services.

Unlike the Japan-Singapore EPA, the Japan-Malaysia EPA allows for modifications to the schedule therein. According to this provision, in relation to the schedule of specific commitments under Annex 6, both countries stated that any of the commitments can be modified or cancelled. The country that wishes to modify or cancel the schedule has to explain its reasons to the other country

Table IV-9. Coverage of JMEPA in the Service Sector

| Sector | Major Sub-sectors |
|--|---|
| Business Services | Accounting, auditing and bookkeeping service, Taxation Service, Computer related services (J), Real estate services (J), Rental/leasing services without operation. |
| Communication Services | Voice telephone services (J), Basic telephone services (M), Value-added services (M), Audiovisual services (J) |
| Construction and Related Engineering Services | General construction work for buildings, General construction work for civil engineering, Building completion and finishing work |
| Distribution Services | Commission agents' services (J), Retailing services (J) |
| Education Services | Primary education services (J), Higher education service |
| Environmental Services | In most sub-sectors (J) |
| Health Related and Social Services | Hospital services, Other human health services (J) |
| Tourism and Travel Related Services | Hotel and restaurants, Travel agencies and tour operator services |
| Recreational, Cultural and Sporting Services | Entertainment services, Sporting and other recreational services, New agency services (J) |
| Transport Services | Maritime cargo handling (J), Maritime passenger transportation & freight transportation |
| Other Services Not Included | Skills and training services (M), Laundry collection services (J), Hairdressing and other beauty services (J) |

Note: (J) stands for sub-sectors that only Japan has offered to open and (M) stands for sub-sectors opened by Malaysia.

and, thereafter, a negotiation is to take place pursuant to Article 21(2)(a).

The Japan-Malaysia EPA (JMEPA) also guarantees most favored nation status. Under the mutual recognition provision, a country may recognize the education or experience obtained, requirements met, licenses, or certifications granted in the other country for the purpose of the fulfillment, in whole or in part, of its standard or criteria for the authorization, licensing, or certification of service suppliers of the other country.⁶²⁾

According to the transparency provision, each country is obligated to provide information on laws, regulations, and so on at the request of the other country.⁶³⁾ As in the EPA with Singapore, Japan has a provision for monopolies and exclusive service suppliers under the FTA with Malaysia that guarantees that the monopolistic service providers within its territory will not act in ways inconsistent with the commitments reached by both countries.⁶⁴⁾ In addition, under the

Table IV-10. Coverage of JMEPA in Investment Sector

| Sector | Major Sub-sectors |
|--|--|
| Agriculture, Forestry, Fisheries and Mining, and related services | Agriculture, Forestry, Fisheries, Aquaculture, Exclusive Economic Zone and Continental Shelf (J) |
| Finance | Banking (J) |
| Information and Communications | Telecommunications and Internet Based Services (J), Broadcasting Industry (J) |
| Manufacturing | Leather and Leather Products Manufacturing (J), Wood-based Products Utilizing Local Logs (M), Optical Discs, Fabrics and Apparels of Batik (M) |
| Oil&Gas Industry | Oil Industry |
| Transport | Air, Railway, Road Transport, Freight Forwarding Business (J) |
| Aerospace Industry | Aircraft/Space Industry (J) |
| Arms and Explosives Industry | Arms/Explosives Manufacturing Industry (J) |
| Energy | Electricity/Gas Utility Industry, Nuclear Energy Industry (J) |

Note: (J) stands for sub-sectors that only Japan has offered to open and (M) stands for sub-sectors opened by Malaysia.

62) FTA between Japan and Malaysia, Art. 103 Mutual Recognition.

63) FTA between Japan and Malaysia, Art. 104 Transparency.

64) FTA between Japan and Malaysia, Art. 105 Monopolies and Exclusive Service Suppliers.

Japan-Malaysia FTA, a substantial part of the content was on intellectual property.

Under this positive system, both countries have provided a specific commitment schedule. Table IV-9 shows the coverage of JMEPA in the service sectors. The categories of sub-sectors listed on the Schedule for Specific Commitments according to CPC classifications show the number of service sub-sectors that are referred to in the JMEPA. Table IV-9 includes the major sub-sectors in each sector and full coverage is summarized in Annex Tables IV-13 and IV-14.

On the other hand, liberalization in investment is negotiated using a negative list method. The sectors that are included in the list are summarized in Table IV-10. And as is expected, the list of restrictions reflects each country's priorities and concerns. For example, Malaysia imposes restrictions on wood-based product industries. This is to secure its comparative advantage in that sector by limiting the entry of foreign companies. Coverage-wise, Japan seems to be more restrictive overall. However, the table simply reflects the number of industries included in the negative list and the degree of restrictiveness cannot be accurately measured.

1.4.2. Characteristics and Assessment of the Japan-Malaysia EPA

Japan failed to make concessions in sectors such as medical, dentistry science, nursing, physical therapist services in the business service sector, and veterinary services. In the R&D sector, natural sciences and joint R&D remain unopened. It has also yet to open agriculture, hunting, forests, fishing, mining, manufacturing-related services, and energy-related distribution services. In the audio-visual service sector, it has refused to make concessions in radio and TV services. Regarding health and medical services, it has only conceded hospital-related services—however, this excludes other health-related services and social services. In terms of investment liberalization, Japan's concern seems to lie mainly in agriculture, forestry, fishery and mining related service sectors. Also, it has put several restrictions on energy related services and transportation services.

It is also worth noting that Malaysia wants to keep its distribution and environmental service sectors closed. Malaysia's wishes are, in part, understandable in the sense that it wants to leave sectors with properties of public services, such as the distribution service and environmental service sector, for domestic businesses, rather than allow foreign companies to occupy them. Regarding the investment market, Malaysia has taken greater steps than its negotiation partner in terms of liberalization. While it puts some investment restrictions on manufacturing, agricultural, forestry, and fishery, other than these sectors, the Malaysian investment market is virtually open to its negotiation partner.

2. Trade and Investment Facilitation

This section analyzes the subject of facilitation in trade and investment. All countries that have concluded FTAs are obligated to promote the facilitation of trade in services and investment through greater transparency, conformity of standards, and enhanced information exchange, etc. Typically, the areas of facilitation apply to trade in goods, trade in services, the movement of natural persons, and the flow of capital and information. In the following section, we investigate various methods of trade and investment facilitation.

Facilitating Trade in Goods

FTAs have always included rules of origin as they prevent the circumvention of goods from third countries. Table IV-11 lists the agreements on trade facilitation in goods adopted by the 4 FTAs; while the 4 FTAs are essentially different, all 4 have rules of origin as a common denominator. A brief description of the facilitation agreements follows. Simplified customs procedures are used to increase conformity to international standards, while mutual recognition provides easier customs clearance. As we can see, simplified customs procedures and mutual recognition have similar characteristics in that they both facilitate trade in goods through agreements on customs. The AFTA, KSFTA and JSEPA are unique in that they adopt both methods. Paperless trading, on the other hand, contributes to the promotion of trade in goods by significantly reducing transaction costs. Parties of FTAs should, thus, make greater efforts to realize and promote paperless trading. They should also exchange views and information to study the development of paperless trading to create electronic business environments that would enable cross-border transactions. Of the 4 FTAs, the Japan-Singapore EPA is the only agreement that has a chapter on paperless trading.

Table IV-11. Facilitating Trade in Goods

| Chapters/Agreements | A | K-S | J-S | J-M |
|-------------------------------|---|-----|-----|-----|
| Rules of origin | ✓ | ✓ | ✓ | ✓ |
| Simplified customs procedures | ✓ | ✓ | ✓ | ✓ |
| Mutual recognition | ✓ | ✓ | ✓ | |
| Paperless trading | | | ✓ | |

Facilitating Trade in Services

Table IV-12 compares the scope of facilitation in services of 4 FTAs. The labels on the table are taken from the ASEAN FTA's chapters on trade in service and investment. First, in terms of making additional commitments to liberalizing trade in services (in addition to those stipulated in the WTO), all FTAs in the table include trade in services, except the AFTA.

Table IV-12. Scope of Facilitation in the Service Sector

| Chapters/Agreements | A | K-S | J-S | J-M |
|---|---|-----|-----|-----|
| Market access | | ✓ | ✓ | ✓ |
| National treatment | | ✓ | ✓ | ✓ |
| Local presence | | ✓ | | |
| Additional commitments | | ✓ | ✓ | ✓ |
| Future liberalization | ✓ | ✓ | | |
| Mutual recognition | ✓ | ✓ | | ✓ |
| Schedule of specific commitments | | | ✓ | ✓ |
| Modification schedule | | | | ✓ |
| Most favored nation treatment | | | | ✓ |
| Authorizations, licensing or qualification | | | | ✓ |
| Transparency | | | | ✓ |
| Domestic regulation | | ✓ | | |
| Monopolies and exclusive service suppliers | | ✓ | | ✓ |
| Emergency safeguard measures | | | | ✓ |
| Payment and transfers | | ✓ | | ✓ |
| Restrictions to safeguard the balance of payments | | ✓ | | ✓ |
| Review of commitments | | | | ✓ |
| Modification or addition of reservations | | ✓ | | |
| Settlement of dispute | ✓ | | | ✓ |

Moreover, the scope of facilitation in the AFTA is limited to only three items: future liberalization, mutual recognition, and settlement of disputes. On the other hand, Japan's EPA with Malaysia, includes nearly all facilitation items. It is, however, interesting to note that while Japan is open to facilitating trade with Malaysia, it has chosen to include only a small number of items in its FTA with Singapore. From this, it can be interpreted that Japan has taken a much more defensive position in its service agreement with Singapore.

Facilitating Movement of Natural Persons

Facilitating the movement of natural persons between the two countries is mostly for business purposes and requires the mutual recognition of professional qualifications. With the exception of Japan-Singapore EPA, all other FTAs in Table IV-13 restrict the movement of natural persons.

However, human resources development is becoming an increasingly important issue as the exchange of students, scholars and teachers, and government officials promotes bilateral trade between the two countries in the long run. In addition, it also has the potential to increase tourism between the two countries and develop the science and technology sectors by promoting the exchange of high-skilled scientists and professionals.

Table IV-13. Facilitating the Movement of Natural Persons

| Chapters/agreements | A | K-S | J-S | J-M |
|-----------------------------|---|-----|-----|-----|
| Movement of natural persons | | | ✓ | |
| Human resource development | | | | |
| Tourism | ✓ | | ✓ | |
| Science and technology | | | ✓ | |

As we can see in the table, the Japan-Singapore FTA is more progressive than the other FTAs in terms of movement of natural persons. The transfer of manpower was one of the key issues in the Japan-Singapore EPA. With this agreement, Japan set a precedent in East Asia by accepting foreign workers through the opening of its labor market and measures, such as providing immigration for nurses and social workers with certain qualifications.

Facilitating the Flow of Capital and Information

The benefits of the capital and information-related clauses listed in Table

IV-14 are as follows. First, investment clauses create an environment that make it easier for investors in one country to invest in another by, protecting investors and investments, conferring national treatment to foreign investors and investments (in principle), ensuring appropriate compensation in the event of expropriation, and securing the free transfer of payments. All FTAs in Table IV-14 have investment clauses, except the Korea-ASEAN FTA. Furthermore, having an agreement on intellectual property is useful in facilitating the patent process between two countries. For example, the intellectual property clause in the JSEPA allows the Intellectual Property Office of Singapore to receive examination reports directly from the National Patent Office in Japan. On the other hand, financial service cooperation facilitates the development of capital markets in both partner countries and strengthens the infrastructure of the financial market. Next, information and communication technology clauses promote the development of industry as well as ICT-related services. Trade and investment promotion is pretty much self-explanatory: it is an agreement to increase trade and investment. Finally, the agreement on small and medium enterprises promotes cooperation among small and medium enterprises between the two countries to realize synergy effects.

Table IV-14. Facilitating the Flow of Capital and Information

| Chapters/agreements | A | K-S | J-S | J-M |
|--|---|-----|-----|-----|
| Investment | ✓ | ✓ | ✓ | ✓ |
| Intellectual property | ✓ | ✓ | ✓ | ✓ |
| Financial services cooperation | ✓ | ✓ | ✓ | |
| Information and communication technology | ✓ | | ✓ | |
| Trade and investment promotion | ✓ | | ✓ | |
| Small and medium-sized enterprises | ✓ | | ✓ | |

3. Development Cooperation

Development cooperation and other types of economic cooperation are important methods to promote trade among countries. Development cooperation, for example, has many valuable implications for East Asian countries, which

need to reduce the wide disparity in economic power to further develop FTAs. In fact, development collaboration among Asian countries is expected to increase much more in the future as countries in the region are starting to realize the benefits of cooperation. While we analyze development cooperation in the East Asian countries, the extent of the analysis is limited due to the lack of in-depth data. The following section examines development cooperation specifically looking the ‘development cooperation clause’ as found in the FTAs between Korea-Singapore, ASEAN-China, and Japan-Malaysia.

Table IV-15. Development cooperation

| Chapters/agreements | K-S | J-S | J-M | A |
|---------------------|-----|-----|-----|---|
| Cooperation | ✓ | | ✓ | |

Korea-Singapore FTA

Korea and Singapore agreed to strengthen their cooperation in the fields of “Information and Communications Technology, Electronic Commerce, Science & Technology, Financial Services, Trade and Investment Promotion, Paperless Trading, Broadcasting, Environment, Human Resources Management and Development, Maritime Transport, Energy, Film Production and Gaming and Animation.”⁶⁵⁾

In the case of information and communications technology, in recognition of rapid development led by the private sector of information and communications technology (ICT) and of business practices concerning ICT-related services both in domestic and international contexts, both countries have agreed to promote the development of ICT and ICT-related services with a view to maximize potential benefits. In the field of electronic commerce, the two countries agreed to cooperate in research and training activities to enhance the development of electronic commerce, including the sharing of best practices in electronic commerce development.

In the case of science and technology in their respective economies, they are to develop and promote co-operative activities in the field of science and technology.⁶⁶⁾ They are to encourage, where appropriate, the co-operative activities between the private sectors of the Parties in the field of science and technology. The co-operation may include

65) Korea-Singapore FTA Chapter 18 Co-operation.

66) Article 18.4: Science & Technology.

- “(a) exchange of scientists, researchers, technicians and experts,
- (b) exchange of documentation and information of a scientific and technological nature,
- (c) joint organization of seminars, symposia, conferences and other scientific and technological meetings,
- (d) implementation of joint research and development activities in fields of mutual interest as well as exchange of the results of such research and development activities,
- (e) co-operation in the commercialization of the results of scientific and technological activities and
- (f) any other form of scientific and technological co-operation agreed upon by the Parties.”

Co-operation may also include biotechnology, nano-technology, electronics, micro-electronics, new materials, information technology, manufacturing technology, environmental technology, science and technology (“S&T”) policies and research and development (“R&D”) systems. Desiring to promote closer co- operation between interested organizations and industries of the Parties in the field of CNG technologies and applications to environmental protection, the Parties have concluded a Memorandum of Understanding to facilitate such co- operation.⁶⁷⁾

Recognizing that sustainable economic growth and prosperity depend largely on people’s knowledge and skills, Korea and Singapore are to increase cooperation between the Parties and encourage mutually beneficial cooperation between parties, one or both of whom are entities in their respective territories other than the governments of the Parties, in the field of human resource development.⁶⁸⁾ Such co-operation activities may include exchange of government officials, co-operation between educational institutions, third country training programs, ageing populations and people developers.

Korea and Singapore, recognizing the importance of energy in the respective economies, are to develop and promote co-operative activities in the field of energy. The co-operation may include

- “(a) facilitation of co-operation between the private sectors of both Parties for the purpose of oil/gas exploration,
- (b) facilitation of co-operation between research institutes, and universities

67) Article 18.9. Environment.

68) Article 18.10. Human Resources Management and Development.

- of both Parties for the purpose of engaging in joint R&D projects, and
 (c) exchange of information and sharing experiences in the fields of electricity and gas restructuring efforts, through study visits or such other activities as mutually agreed upon by the implementing authorities.”⁶⁹⁾

China-ASEAN FTA

China and ASEAN agreed on an FTA to strengthen their cooperation in agriculture, information and communications technology, human resources development, investment, and development on the Mekong River basin.⁷⁰⁾ They also agreed to extend to other areas, including banking, finance, tourism, industrial cooperation, transport, telecommunications, intellectual property rights, small and medium enterprises, environment, biotechnology, fishery, forestry and forestry products, mining, energy and sub regional development.

Measures to strengthen cooperation are to include promotion and facilitation of trade in goods and services and investment, such as standards and conformity assessment, technical barriers to trade/non-tariff measures, and customs co-operation. Besides, measures to strengthen cooperation are to include increasing the competitiveness of small and medium size enterprises, promotion of electronic commerce, capacity building, and technology transfer. China and ASEAN agreed to implement capacity building programs and technical assistance, particularly for the newer ASEAN Member States in order to adjust their economic structures and expand trade and investment with China.

Japan-Malaysia FTA

Japan and Malaysia agreed to promote liberalization, trade facilitation and investment between the countries, as well as the welfare of their peoples. The respective governments have thus included agriculture, forestry, fisheries and plantation, education and human resource development, information and technology, science and technology, small and medium enterprises, tourism, and the environment in their agreement.

4. Overall Evaluation

The characteristics of FTAs related to service and investment in East Asia

69) Article 18.13. Energy.

70) China-ASEAN FTA, Art. 7 Other Areas of Economic Cooperation.

are as follows.

The negative list method was adopted in the FTA between South Korea and Singapore and signifies attempts to expand service and investment. The degree of market opening in Singapore, which has greater competitiveness in service sectors, is higher than in Korea.

Japan's contracting, on the other hand, is rather on the defensive, adopting a positive list method in its EPA with Singapore due to the weak competitiveness of its service industry. In addition, it has also restricted the liberalization of its service sector with Malaysia by regulating certain commitments to be modified or cancelled. As we can see Table IV-16, the opening degree of Japan's service sector is relatively low among the four countries.

Japan seems to consider the benefits of trade liberalization in the service sector to be relatively smaller than those of trade liberalization in goods. Accordingly, Japan has concentrated its efforts on trade in goods and investment by supporting domestic manufacturers and easing restrictions on investments in the service industry and, as a result, has made inroads into the Southeast Asian market. Japan has especially focused on intellectual property rights in its EPAs with Singapore and Malaysia.

Table IV-16. Comparison of Opening Degree in the Service Sector

| FTA | Korea-Singapore Existing measures | | Korea-Singapore Future measures | | Japan- Singapore | | Japan- Malaysia | |
|-------------------------|--------------------------------------|------|------------------------------------|------|---------------------|------|--------------------|------|
| | K | S | K | S | J | S | J | M |
| Opening ratio (%) | 72.3 | 95.6 | 80.3 | 92.9 | 68.4 | 66.2 | 65.2 | 27.7 |
| Number of opening items | 488 | 646 | 542 | 627 | 462 | 447 | 440 | 187 |

Source: Calculated by authors from the K-S, J-S, J-M FTAs (Annexes)

Malaysia's opening ratio for its service sector is also low at 27.7 percent (versus Japan) due to the weak competitiveness of its service industry. Among the four countries, Malaysia has the lowest degree of service market opening.

From these results we find that Korea, Japan, Singapore and Malaysia have three reservation items and sixty-two concession items in common.

Table IV-17. List of Reservation Items for All Four Countries

| CPC code | Description |
|----------|---|
| 74510 | Port and waterway operation services (excl. cargo handling) |
| 74520 | Pilot age and berthing services |
| 74530 | Navigation aid services |

Source: Calculated by the authors from Annexes of K-S, J-S, J-M FTA

Table IV-18. Table List of Concession Items for All Four countries

| CPC code | Description |
|----------|---|
| 64110 | Hotel lodging services |
| 64120 | Motel lodging services |
| 64194 | Youth hostel and mountain shelter services |
| 64320 | Beverage serving services with entertainment |
| 74710 | Travel agency and tour operator services |
| 83103 | Leasing or rental services concerning vessels without operator |
| 83104 | Leasing or rental services concerning aircraft without operator |
| 83109 | Leasing or rental services concerning other machinery and equipment without operator |
| 84100 | Consultancy services related to the installation of computer hardware |
| 84210 | Systems and software consulting services |
| 84220 | Systems analysis services |
| 84230 | Systems design services |
| 84240 | Programming services |
| 84250 | Systems maintenance services |
| 84310 | Input preparation services |
| 84320 | Data processing and tabulation services |
| 84330 | Time sharing services |
| 84390 | Other data processing services |
| 84400 | Data base services |
| 84500 | Maintenance and repair services of office machinery and equipment including computers |
| 85201 | Research and experimental development services on cultural sciences, sociology and psychology |

Table IV-18. Continued

| | |
|-------|---|
| 85202 | Research and experimental development services on economics |
| 85209 | Research and experimental development services on other social sciences and humanities |
| 86401 | Market research services |
| 86402 | Public opinion polling services |
| 86501 | General management consulting services |
| 86502 | Financial management consulting services (except business tax) |
| 86503 | Marketing management consulting services |
| 86504 | Human resources management consulting services |
| 86505 | Production management consulting services |
| 86506 | Public relations services |
| 86509 | Other management consulting services |
| 86764 | Technical inspection services |
| 87110 | Sale or leasing services of advertising space or time |
| 87120 | Planning, creating and placement services of advertising |
| 87190 | Other advertising services |
| 88411 | Manufacture of food and beverages, on a fee or contract basis |
| 88412 | Manufacture of tobacco on a fee or contract basis |
| 88421 | Manufacture of textiles on a fee or contract basis |
| 88422 | Manufacture of wearing apparel on a fee or contract basis |
| 88423 | Manufacture of leather products on a fee or contract basis |
| 88430 | Manufacture of wood and of products of wood and cork, except furniture; |
| 88441 | Manufacture of paper and paper products, on a fee or contract basis |
| 88450 | Manufacture of coke, refined petroleum products and nuclear fuel, on a fee or contact basis |
| 88460 | Manufacture of chemicals and chemical products, on a fee or contract basis |
| 88470 | Manufacture of rubber and plastics products, on a fee or contract basis |
| 88480 | Manufacture of other non-metallic mineral products, on a fee or contract basis |
| 88491 | Manufacture of furniture on a fee or contract basis |
| 88492 | Manufacture of other articles n.e.c., on a fee or contract basis |
| 88493 | Recycling on a fee or contract basis |

Table IV-18. Continued

| | |
|-------|---|
| 88510 | Manufacture of basic metals on a fee or contract basis |
| 88520 | Manufacture of fabricated metal products, except machinery and equipment on a contract basis |
| 88530 | Manufacture of machinery and equipment n.e.c., on a fee or contract basis |
| 88540 | Manufacture of office, accounting and computing machinery, on a fee or contact basis |
| 88550 | Manufacture of electrical machinery and apparatus n.e.c., on a fee or contact basis |
| 88560 | Manufacture of radio, television and communication equipment and apparatus on a fee or contact basis |
| 88570 | Manufacture of medical precision and optical instruments, watches and clocks, on a fee or contact basis |
| 88580 | Manufacture of motor vehicles, trailers and semi-trailers, on a fee or contact basis |
| 88590 | Manufacture of other transport equipment, on a fee or contract basis |
| 93110 | Hospital services |
| 96411 | Sports event promotion services |
| 96412 | Sports event organization services |

Source: Calculated by the authors from Annexes of K-S, J-S, J-M FTA

As we see in section 2, trade and investment facilitation is generally not an important issue. However, the facilitation for trade and investment does have important meaning when there exists a large gap in economic power and the level of industry. Moreover, from the analyses in section 2, we see that the measures implemented in the AFTA, JSEPA, and JMEPA ensure a higher level of facilitation of cross-border trade and services than in the KSFTA. This is because these parties regard their agreements as forms of economic cooperation: both the AFTA and Japan contracted their FTAs as economic partnership agreements and regard their FTA counterparts as partners in economic cooperation. Thus, efforts to expand and facilitate trade and investment are required for the promotion EAFTAs in the future.

With regard to development cooperation as analyzed in section 3, there is

very little to say as East Asian countries—which are the main subjects of analysis in this study—have yet to reach an agreement on development cooperation. Nevertheless, the reason why section 3 is included is that development cooperation in FTAs is very important, especially among countries with large gaps in competitiveness. Greater research needs to be carried out regarding FTA contracts among East Asian countries. It is hoped that the analysis included in this study will help to raise awareness on the importance of this issue.

Finally, we end with a note on the method of approach used in this study. Detailed investigations were carried out regarding the reservations prescribed in the annex of each agreement for the service and investment sector. The reservation items in the service sector were counted in detail based on CPC codes for all five digits and searches were run comparing reservations in Korea, Japan, Singapore, and Malaysia. The purpose of this analysis is to figure out the extent of opening of reservation items in these countries. However, we did not conduct a similar analysis for the investment sector because of the inconsistent use of CPC classification marks. As it turns out, the industrial classification symbols for the investment sector are different in each country. While some countries observe CPC classification marks, Japan uses its own industrial classification symbols; thus, making a comparative analysis of this sector difficult. This situation is regretful, but it also reveals the additional steps we need to take in order to promote greater cooperation: namely, the standardization of classification tables for industry sectors in all countries in order to further investigate and analyze EAFTAs for the future.

V. Prospects, Options and Future Tasks for the East Asia FTA (EAFTA)

1. Prospects for the EAFTA

In this section, we will first examine the rationales and obstacles for an EAFTA to clarify objectives, as well as assess the possibilities. We will then present our views on the possible paths toward an EAFTA, as well as membership issues, and finally propose a time schedule.

1.1. Rationales for the EAFTA

Why is there growing interest in a region-wide FTA among East Asian countries? In our view, the continuing proliferation of bilateral FTAs and growing interdependence in the East Asian region have provided several rationales for forming an EAFTA, which are as follows.

Defensive Reaction to the Worldwide Rise of Regionalism

Regionalism became a worldwide phenomenon in the 1990s and continues to expand in the first decade of the 21st century. It is quite likely that we will see the emergence of two mega-trade blocs in the near future: one in Europe and the other in the Americas. In Europe, the European Union (EU) welcomed 10 new member countries on May 1, 2004, thereby becoming a 25-member union. Encouraged by the success of the North American Free Trade Agreement (NAFTA), 34 countries in the Americas have been pursuing the Free Trade Area of the Americas (FTAA).

While Europe and the Americas are quickly developing regionalism, East Asia is clearly lagging behind.⁷¹⁾ In fact, among the major economic regions in the world, East Asia remains the only region that does not have a region-wide RTA.

71) As of September, 15, 2006, out of the 211 RTAs in force and notified to the GATT/WTO, only 35 RTAs involve an East Asian country (http://www.wto.org/english/tratop_e/region_e/region_e.htm).

The argument for an EAFTA by East Asian countries can, thus, be regarded as defensive response rather than a proactive initiative. Nevertheless, in the same way that the early phases of East Asian regionalism have been motivated by the rise of worldwide regionalism, the external environment can serve an important factor in the formation of an EAFTA, especially given the low level of regional awareness in East Asia.

Technical Reasons to Prevent the "Spaghetti Bowl" Phenomenon

In the wake of the Asian financial crisis, a number of East Asian countries belatedly hopped aboard the FTA bandwagon. Many bilateral FTAs were concluded in East Asia within a relatively short period of time, including an increasing number of FTAs between East Asian countries. Furthermore, since a growing number of countries have joined the wave and are pursuing active FTA policies, the proliferation of FTAs is likely to continue in the coming years.

Given the current trend of uncoordinated bilateral FTA proliferation, there exists a real risk that East Asian countries may face a spaghetti bowl phenomenon in the near future. In other words, the complexity of rules of origin resulting from the increasing number of bilateral FTAs between East Asian countries may become a barrier to intraregional trade. Therefore, instead of having various bilateral FTAs with a large number of different rules of origin, an EAFTA encompassing all East Asian countries is more desirable.

Deepening Interdependence

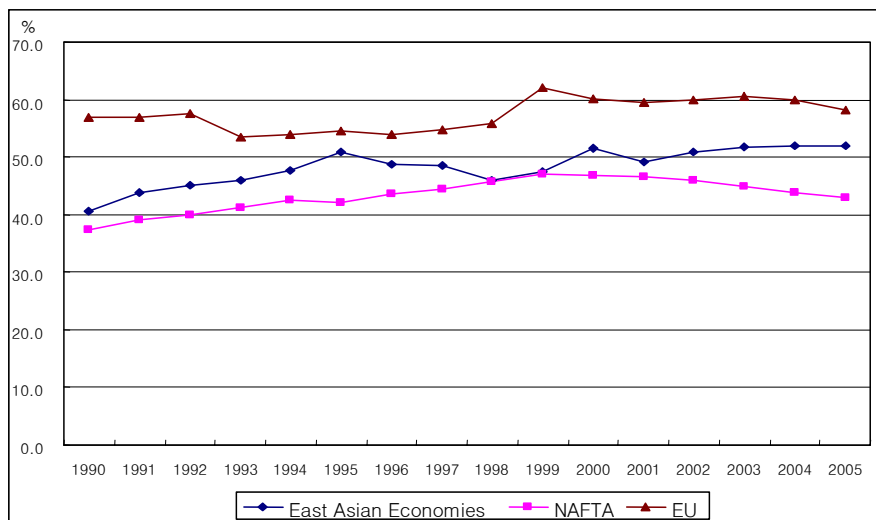
As with any FTA, the basic economic rationales for an EAFTA are larger market access and higher efficiency. In 2005, the East Asian economies as a whole represented 20.7 percent of the world's total GDP.⁷²⁾ Moreover, growing interdependence among East Asian economies in terms of trade and investment is reinforcing the economic rationale for an EAFTA.

As shown in Figure V-1, the share of intraregional trade among the East Asian economies including ASEAN+3 countries, Hong Kong and Taiwan grew from 40.6 percent in 1990 to 52.2 percent in 2005.⁷³⁾ While the level of intraregional trade among East Asian economies in 2005 was lower than that of the EU (58.2 percent), it was still higher than NAFTA's (43.0 percent). Meanwhile, the share of intraregional FDI inflows among ASEAN+3 countries

72) Calculated by the authors based on data from *Global Insight*.

73) The share of intraregional trade among ASEAN+3 countries increased from 28.9 percent in 1990 to 39.9 percent in 2005.

Figure V-1. Share of Intraregional Trade in East Asian Economies, NAFTA, and the EU



Note: East Asian Economies: ASEAN+3, Hong Kong and Taiwan.

Source: Calculated by authors based on data from IMF (2006).

rose from 26.6 percent to 47.5 percent during 1990-2003 (see Annex Table V-1).

So far, functional economic integration in terms of trade and investment has proceeded in East Asia with little help from regional governments. A region-wide FTA would certainly contribute to further enhancement of trade and investment among East Asian economies.

Vision of an East Asian Community

Should East Asians want to form a regional community, an EAFTA would be unavoidable. The East Asia Vision Group (EAVG), which was established following a decision reached at the Hanoi ASEAN+3 Summit Meeting, submitted a report to the leaders of ASEAN+3 in 2001. In this report, the EAVG described its vision of an “East Asian Community” and recommended the formation of an East Asia Free Trade Area well ahead of the Bogor goals set by APEC. Later, in 2002, the East Asia Study Group (EASG) confirmed that the recommendations of the EAVG would be useful in realizing an East Asian

vision and proposed the formation of an EAFTA as one of nine midterm and long-term measures.

Given the diversity of East Asian countries and the low level of regional awareness, an East Asian Community would be substantially different from the European Community, but, as we see from the European experience, community building starts with the institutionalization of economic integration.

1.2. Obstacles to the EAFTA

Despite these definite advantages, Herculean efforts will be needed to realize an EAFTA because there exist a plethora of obstacles to its formation.

Diversity among East Asian Countries

East Asia encompasses diverse countries and regions. Geographically, East Asia includes North Korea, Hong Kong, Taiwan, Mongolia, and parts of Russia, in addition to the ASEAN+3 countries. Even among ASEAN+3 countries, the diversity is apparent. East Asian countries differ not only in language and religion, but also the political system used. Even the size of populations and economies vary enormously from country to country.

Most significantly, the disparity in the level of economic development

Table V-1. Economic Development Gap

| | Per capita GDP (US\$) |
|-------------|-----------------------|
| Brunei | 16,135.2 |
| Cambodia | 404.0 |
| China | 1,701.8 |
| Indonesia | 1,274.8 |
| Japan | 35,729.9 |
| Laos | 485.0 |
| Malaysia | 5,060.5 |
| Myanmar | 210.8 |
| Philippines | 1,166.0 |
| Singapore | 26,839.9 |
| South Korea | 16,200.6 |
| Thailand | 2,749.9 |
| Vietnam | 623.7 |

Note: Myanmar: 2000; Brunei: 2003; Cambodia, Thailand: 2004; others: 2005.

Source: Globalinsight.

among the East Asian countries would constitute, in our view, one of the most challenging obstacles for the EAFTA.

Rivalry between China and Japan

The rivalry between China and Japan has played a positive role in the proliferation of bilateral FTAs in East Asia. For instance, China's early proposal to ASEAN to form an FTA prompted a swift response from Japan, which offered a similar proposal to the ASEAN countries. Nevertheless, the rivalry between the two East Asian economic powers is expected to be a hindrance to the EAFTA in the long run. In particular, the unlikelihood of forming a China-Japan FTA in the near future and the Japanese government's proposal to include Australia, New Zealand, and India, in addition to ASEAN+3, in the EAFTA debate as well as the East Asia Summit is likely to delay the formation of the EAFTA.

Sensitive Sectors

The existence of comparatively weak sectors—the agricultural sector in Korea and Japan, on the one hand, and various manufacturing and service sectors in less developed countries, on the other—is likely to bring strong opposition to the EAFTA from concerned interest groups in all of the East Asian countries.

Proliferation of Bilateral FTAs among East Asian Countries

The proliferation of bilateral FTAs among East Asian countries may weaken interest in the EAFTA, should East Asian countries succeed in harmonizing the rules of origin in their bilateral-FTAs in the near future.

Low Level of Regional Awareness

The more fundamental difficulty of realizing an EAFTA is the lack of community spirit in East Asia. This is especially evident in the three Northeast Asian countries, which represent 90 percent of the East Asian economy. In Northeast Asia, there still exists little awareness of being a single region, let alone being part of an East Asian community.

1.3. Scenarios for an EAFTA⁷⁴⁾

First, with recent developments in bilateral FTAs in East Asia, the most talked about scenario for an EAFTA seems to be its formation through a series

74) Similar views can be found in Joint Expert Group for Feasibility Study on EAFTA (2006) of which the author was a drafter.

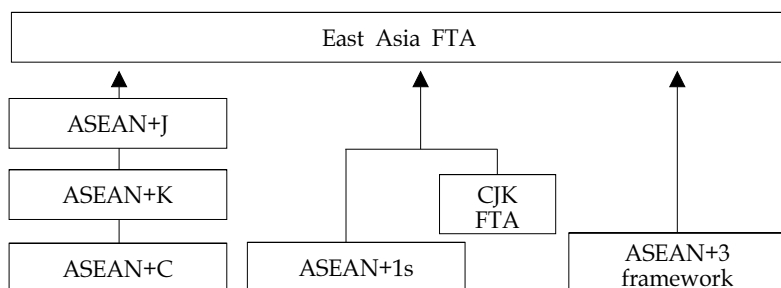
of ASEAN+1 FTAs. Since China, Japan, and Korea are each pursuing an FTA with ASEAN, these ASEAN+1 FTAs, when realized, could serve as a basic framework for the EAFTA.

In 2004, China and ASEAN signed the Trade in Goods Agreement which was implemented on July 1, 2005. Negotiations on service and investment are currently under way and are expected to be completed soon. In April 2006, Korea concluded the Trade in Goods Agreement with ASEAN (excluding Thailand) and negotiations for other agreements are expected to finish by 2007. In addition, an ASEAN-Japan FTA is also under negotiation, which is expected to conclude by 2007.

The main strength of this option is that one can start from the ASEAN+1 FTAs, which are likely to have quite similar typologies. We have already noticed the similitude of tariff concession structures of the ASEAN-China Trade in Goods Agreement and the Korea-ASEAN Agreement. However, its limitations are clear. First, an FTA or a series of FTAs between China, Japan, and Korea will have to be worked out. Additionally, as we have witnessed, due to the diversity of economic development in ASEAN countries, it will be difficult to expect a high quality EAFTA from this particular path.

Second, should the three Northeast Asian countries form a China-Japan-Korea FTA (CJK FTA) or bilateral FTAs, the formation of the EAFTA could be greatly facilitated. Unfortunately, however, given the current political climate between the three countries, a CJK FTA is not likely to be pursued in the near future.⁷⁵⁾

Figure V-2. Paths toward an EAFTA



75) So far, only a trilateral joint research project has been conducted on a China-Japan-Korea FTA since 2003 between the Development Research Center (DRC) of China, the National Institute for Research Advancement (NIRA) of Japan, and the Korea Institute for International Economic Policy (KIEP).

As for bilateral FTAs between Northeast Asian countries, negotiations on a Korea-Japan FTA, which started in December 2003, are currently at a stalemate, while a joint study on a China-Korea FTA was recently conducted between policy institutes in the two countries⁷⁶⁾ and a tripartite joint study involving people from the business sector, government, and academia is expected to begin in 2007. Therefore, chances are that a bilateral Korea-Japan FTA and Korea-China FTA will be realized instead of (or before) a CJK FTA.

Lastly, an EAFTA could be achieved using the existing ASEAN+3 framework. Following the first ASEAN+3 Summit Meeting in December 1997, the ASEAN+3 framework was consolidated as a forum for regional economic cooperation in East Asia. It was within the ASEAN+3 framework that both the EAVG and the EASG recommended the formation of an EAFTA. The Joint Expert Group on the Feasibility of an EAFTA was also created based on the decisions reached at the ASEAN+3 Economic Ministers Meeting.

However, this process may be complex and costly, both in terms of time and effort, and consensus building among the 13 countries may be difficult to achieve. Although the ASEAN+1 FTAs and a CJK FTA (or a Korea-Japan FTA and a Korea-China FTA) may facilitate the formation of an EAFTA, the final stages of realizing the EAFTA is likely to be dealt within the framework of ASEAN+3. In addition, should the ASEAN+3 framework be used from the early stages of negotiations, an ideal EAFTA could be devised to reflect the *sui generis* characteristics of the East Asian countries. However, the emergence of the East Asia Summit, which includes Australia, New Zealand, and India, in addition to the ASEAN+3 countries, and the Japanese government's preference for an ASEAN+6 (ASEAN+3, Australia, New Zealand, and India) may make the situation more complicated by raising the issue of EAFTA membership.

1.4. Membership of the EAFTA

With regard to EAFTA membership, the first key question is whether it will be limited to East Asian countries⁷⁷⁾ or go beyond geographic boundaries. The other key issue is the question of who will comprise its starting membership. Since Japan for some reason prefers to start with ASEAN+6 instead of ASEAN+3, the membership issue may complicate the debate on an EAFTA and may constitute a major stumbling block especially in the early stages of the debate.

76) DRC and KIEP.

77) As mentioned earlier, East Asia includes Northeast Asia and Southeast Asia.

Given the outward orientation of the East Asian economies, EAFTA membership should be inclusive and not just limited to East Asian countries. However, as for starting memberships, it would be more realistic for the EAFTA to include only ASEAN+3 countries, partly because of the existing ASEAN+3 framework and partly because it is difficult to form an EAFTA even among 13 countries.

The EAFTA could instead extend membership to other countries, including Australia, New Zealand, and India, in progressive years. It could also open up to other East Asian economies and countries, such as Hong Kong, Taiwan, North Korea and Mongolia, should appropriate political and economic environments be created.

1.5. Timing of the EAFTA⁷⁸⁾

All of the above scenarios are likely to produce concurrent synergy effects for East Asian economic integration. However, the timing of an EAFTA will vary depending on the progress of ongoing FTA negotiations, the type of EAFTA envisioned, and especially the political will of East Asian leaders.

The following factors should be considered when designing an EAFTA schedule:

- The EAVG recommended the formation of an EAFTA well ahead of the Bogor goals set by APEC. According to the Bogor Declaration, APEC's industrial economies should achieve the goal of a free trade and investment area no later than 2010, and developing economies, no later than 2020.
- The Leaders of the ASEAN countries agreed to an ASEAN Economic Community (AEC) that would be a "single market and production base by 2020." Recently, the Leaders of ASEAN countries agreed to pursue this "single market and production base" by 2015. Since the AEC is likely to be an FTA-plus with elements of a common market, it could serve as a subset of the EAFTA.
- The target years for an ASEAN-Korea FTA, an ASEAN-China FTA, and an ASEAN-Japan FTA are set for 2010, 2010, and 2012, respectively.
- The ASEAN+1 FTAs are likely to be concluded by 2007 or 2008.

Therefore, we suggest that East Asian countries start EAFTA negotiations

78) Almost identical views can be found in Joint Expert Group for Feasibility Study on EAFTA (2006) of which author was a drafter.

within the ASEAN+3 framework as early as 2009 with a view to concluding it no later than 2012. Meanwhile, various preparatory steps can be made among researchers, business people and government officials in East Asia.

2. Options for the EAFTA

2.1. Main Characteristics of Existing East Asian FTAs

In Chapters II-IV, we examined around six FTAs between East Asian countries. We first looked at the AFTA, which began at the signing of the Agreement on Common Effective Preferential Tariff (CEPT) Scheme in 1992 and was reported under the enabling clause. We then examined the AFAS (the ASEAN Framework Agreement on Services), which was signed in 1995 and is still in progress. We also mentioned that for the ASEAN-China FTA and the Korea-ASEAN FTA, only the Trade in Goods Agreements were signed, while the Agreements on Services and Investment are still under negotiation. Finally, we covered the two FTAs involving free-trading Singapore, i.e. the Japan-Singapore EPA and the Korea-Singapore FTA and the Japan-Malaysia EPA. Given the limited number of FTAs covered here, it seems a little bit premature to talk about a typology for existing East Asian FTAs. However, our examination of FTAs still revealed interesting characteristics.

First, the diversity among the East Asian countries constitutes the most prominent feature of the East Asian FTAs examined. Each has a very different tariff concession structure and, even within the agreements themselves, parties often have substantially different tariff concession schedules. For instance, in the ACFTA and the KAFTA, the tariff concession schedules for China and Korea are quite different from Cambodia's. Thus, we conclude that existing FTAs between the East Asian countries cannot be regarded as high in quality, especially in terms of the market access for goods.

There are basically two different types of tariff concession structures: one that pertaining to ASEAN and the other covering the remaining countries (each with variants). The AFTA, the ACFTA, and the KAFTA have basically similar tariff concession structures—consisting of a Normal Track and a Sensitive Track, the latter dividing into two further categories. In contrast, the KSFTA, the JSEPA, and the JMEPA have a more simplified structure consisting of several categories. Korea's tariff concession structure has four categories in the KSFTA, while Japan's has six categories in the JSEPA. In the JMEPA, Japan and Malaysia's tariff concession structures have ten and fifteen categories, respectively.

The rules of origin also vary in existing East Asian FTAs; in many instances, an individual country may have separate rules of origin for the different FTAs it has concluded. For instance, let us consider the FTAs in which Japan is involved. For most electrical machinery and equipment (HS 85), the JSEPA sets stricter rules of origin than the JMEPA. The JMEPA rules of origin require that the products satisfy changes in tariff subheadings or that the regional value content is not less than 40 percent. On the other hand, in the JSEPA, originating status is only conferred if there is change in chapter heading or the regional value content is not less than 60 percent. Given the extent of differing rules of origin in one country, it could be possible that a producer, who manufactures and exports, for example, televisions to ASEAN countries, would enjoy preferential tariff treatment from Malaysia, but not from Singapore, if the regional value content of its televisions was 50 percent. So, it would be up to the producer to either obtain preferential tariff treatment by changing the supply schedule for manufacturing televisions for the Singaporean market, or simply give up on receiving it in Singapore. As we can see in this hypothetical example, changing the supply schedule or maintaining a dual supply schedule is costly for manufacturers, making it likely that they will simply give up their rights to obtain preferential tariff treatment.

If we evaluate each of the existing FTAs in terms of rules of origin, the AFTA and ACFTA clearly have simpler rules of origin compared to the other four FTAs. In the AFTA and ACFTA, the main method for determining the country of origin is the percentage criterion, but this method does carry some exceptions, such as in textile and garment products. The advantage of the percentage criterion is that it requires the regional value content to be not less than 40 percent for most products, which is quite low. On the other hand, the Korea-ASEAN FTA, KSFTA, JMFTA, and JSFTA have rather complicated rules of origin. The main methods used here are changes in tariff classification and the percentage criteria; however, there are no guidelines as to what products apply to which methods. These FTAs virtually set rules of origin on a product by product basis and oftentimes a single country has different rules of origin for the same product. A lack of consistency and increased complexity are the main weaknesses of these FTAs.

In this study, we have examined four cases with regard to service and investment: the AFTA, the JSEPA, the JMEPA, and the KSFTA. A negative list method was adopted in the KSFTA, while a positive list method was adopted in the JSEPA and the JMEPA. Moreover, Japan's liberalization in services was relatively limited, whereas Korea and Singapore agreed to similar levels of service

and investment liberalization. In particular, Japan has put greater emphasis on intellectual property rights in its EPAs. Regarding the degree of market opening among the four FTAs, Singapore has the highest service sector opening ratio (95.6 percent vis-à-vis Korea), while Malaysia has the lowest at 27.7 percent vis-à-vis Japan, mainly in part due to the weak competitiveness of its service industry. As for facilitation in trade and investment and development cooperation, these issues were not dealt with substantially in the existing East Asian FTAs.

2.2. Relationships between East Asia FTAs and the EAFTA

The current trend of increasing bilateral FTAs in East Asia is likely to create a favorable environment for an EAFTA. Since most East Asian countries would like to join the growing preferential trade web, the proliferation of bilateral FTAs among East Asian countries is expected to aggravate the spaghetti bowl phenomenon. In order to avoid these complications, it is expected that a growing number of countries will regard an EAFTA as an attractive alternative.

Furthermore, in the process of forming an EAFTA, the FTAs between East Asian countries could serve as useful reference points. Among them, ASEAN+1 FTAs will be of particular importance, because these agreements are between ASEAN countries, which are key binding elements of an EAFTA, and the three Northeast Asian members of the ASEAN+3 framework.

Thus, the ASEAN+1 FTAs and other FTAs among East Asian countries could facilitate the formation of an EAFTA. However, it is also evident that an EAFTA cannot be constructed using only these FTAs. In particular, if an EAFTA is formed mainly on the basis of the least common denominator of the existing FTAs, it is likely to result in a low quality FTA. Therefore, it is important that the EAFTA go beyond existing East Asian FTAs.

Another key issue that we have to consider is the relationship between the EAFTA and other FTAs among East Asian countries when the EAFTA is finally realized. Should an EAFTA be created, what would its relationship be to the other FTAs among member countries? Will it replace all or some of the existing FTAs? Or will it be just another FTA on top of existing and forthcoming FTAs? These choices will be of critical importance, because they have direct implications for the type of EAFTA, *inter alia*.

If East Asian countries choose to form an EAFTA that will co-exist with many other East Asian FTAs, it would only add to the multi-layered, complex FTA web in East Asia. Politically speaking, this type of EAFTA would be relatively easy to negotiate among the East Asian countries, but since such an EAFTA would not prevent the worsening of the spaghetti bowl phenomenon in

East Asia, one may question the rationality of creating a largely symbolic region-wide FTA.

Another option is pursuing a high quality EAFTA that would replace most of the other FTAs among the East Asian countries. However, given the diversity of East Asian economies, this will be rather difficult to achieve. Nevertheless, it is precisely this sort of EAFTA that would maximize economic benefits and prevent further proliferation of bilateral FTAs in the region.

Thus, we are faced with a dilemma. In order to prevent the spaghetti bowl phenomenon, an EAFTA must be high enough in quality so that it can replace a substantial number of existing bilateral FTAs. However, given the diversity of the East Asian countries and the current political climate in the region, it is very likely that the EAFTA will end up being symbolic, unless member countries show more willingness.

2.3. Proposed Option for the EAFTA

If forming a high quality EAFTA is our ultimate goal, the most “ideal” path to achieving it would be, in our view, to start with those East Asian countries who are best prepared to accommodate a high quality FTA, then gradually expand to other East Asian countries who could be accepted on agreed conditions. In this case, some East Asian countries would not be able to join the EAFTA in its initial stages. And, considering that ASEAN countries are not inclined to forgo the oneness of ASEAN, this path will likely be left on the drawing board. Taking into account the political realities in East Asia, our policy option proposes that all ASEAN+3 countries be members of an EAFTA from the beginning.

Our analysis of the six existing FTAs between East Asian countries confirms that the economic disparity among East Asian countries is the most serious obstacle to the formation of the EAFTA. For instance, in the ASEAN-China Trade in Goods Agreement, the items under Cambodia’s Sensitive or Highly Sensitive List represent more than two thirds of Cambodia’s imports from China in 2004, even though they amount to less than 10 percent in terms of the number of tariff lines. So, it would be very difficult to conclude a high quality FTA under such uneven market access for goods. In addition, given the backwardness of the service sector in many East Asian countries, our study supports the assertion that the scope of service liberalization is likely to be limited.

On the other hand, our study shows that even an EAFTA with moderate quality could substantially facilitate trade among East Asian countries by solving

the spaghetti bowl phenomenon. Moreover, with well-devised rules of origin, the development of production networks among East Asian economies could also be promoted.

In Chapter III, we suggest the adoption of a diagonal cumulation provision. Given that complexity and diversity of rules of origin in the region cause regional integration difficulties and market inefficiency, diagonal cumulation could help to resolve much of the problems discussed earlier. It would improve the integration of the production market in the region and its impact would be equivalent to a single, unified rules of origin under the EAFTA. Countries would be able to diversify their sources of intermediate materials and deepen specialization processes. Developed countries, in particular, could lower the cost of production by using less expensive labor; on the other hand, less developed countries would be able to enhance comparative advantages, i.e. cheaper labor, in the region.

However, greater access to cheap labor may threaten developed countries because such diversification and specialization would cause their domestic unemployment rates to rise as more and more outsourcing would occur for labor intensive products or materials. Also, countries have a tendency to use rules of origin as tools to protect domestic industries by intentionally setting strict rules to receive preferential tariff concessions. If the EAFTA included high quality or comprehensive sectors, some countries would be hesitant to agree on simpler and looser rules of origin. However, if the EAFTA allowed countries to set aside their highly sensitive sectors, or allowed limited coverage, the possibility of simplifying regional rules of origin would increase because the impact of rules of origin on the domestic labor market would be mitigated to a certain extent. In this regard, limited coverage would increase the chances of adopting looser rules of origin, which would in turn be helpful in minimizing the negative impacts of existing rules of origin in the region.

In addition, given East Asia's diversity of economic development, an EAFTA should cover a larger number of trade and investment facilitation measures, as well as a concrete mechanism for regional development cooperation. Insufficiency in terms of market access could be supplemented by including diverse trade and investment facilitation measures and a development cooperation package that includes concrete human resource development projects could help less developed countries liberalize their economies and reduce development gaps.

Regarding tariff concession structures and schedules, in order to accommodate less developed countries, we believe that a tariff concession structure similar to that of the Korea-ASEAN FTA, which adopts both a Normal Track and a Sensitive Track, could be used in the EAFTA. Instead of setting tariff elimination

or reduction schedules for each item, an ASEAN-type tariff concession structure could be used to define tariff elimination or reduction schedules for a group of items with a fixed share of tariff lines. Then, specific items belonging to the group can be chosen at a later time by individual countries. This system could provide more flexibility to less developed countries that find it difficult to identify sensitive items in the midst of rapid industrial structural change. Needless to say, more time needs to be given to less developed countries, but, at the same time, clearly defined timetables for liberalization must be provided.

Replacing existing FTAs in East Asia is a daunting task, but an EAFTA with i) a relatively flexible tariff concession structure, ii) simple and liberal rules of origin, iii) strengthened trade and investment measures, and 4) a concrete development cooperation mechanism would be much more than symbolic and tangibly contribute to creating freer trade and investment in East Asia.

3. Future Tasks for the EAFTA

Many East Asian countries have adopted active FTA policies and have pursued an increasing number of bilateral FTAs, including those with East Asian countries. In addition, various efforts have been made to enhance the level of research on East Asian economic cooperation and to discuss the future of East Asian economic integration in international fora such as the Network of East Asian Think-Tanks (NEAT), the East Asia Forum (EAF), the East Asian Development Network (EADN), the East Asian Bureau of Economic Research (EABER), the Asian International Forum in Fukuoka, and the East Asian Institutes Forum.

Moreover, the Joint Expert Group for Feasibility Study on EAFTA, which was initiated by China, was the first serious attempt to address a region-wide FTA, but came short of submitting its report to the ASEAN+3 Summit. In addition, the Japanese government has made two important proposals: 1) the establishment of an Economic Research Institute for ASEAN and East Asia (ERIA) and 2) the launching of another feasibility study on an EAFTA among experts from ASEAN+6 countries, including Australia, New Zealand, and India. While an ERIA addresses broader East Asian economic cooperation issues, the latter proposal seems to be focused on an EAFTA among ASEAN+6 countries.

As various ASEAN+1 FTAs are likely to conclude by 2007 or 2008, the debate on an EAFTA is expected to start in earnest around 2008 or 2009 at the ASEAN+3 meetings. However, research on an EAFTA cannot afford to wait

one or two years. In our view, to maintain the momentum created by the Joint Expert Group, the Korean government, which proposed both the East Asia Vision Group and the East Asia Study Group, should take the initiative and continue feasibility studies on the EAFTA.

A joint study could be conducted by experts from ASEAN+3 countries to deepen the study started by the Joint Expert Group. Now that we have examined the rationales, macroeconomic benefits, modalities and proposed a roadmap, this new study could analyze the economic effects of an EAFTA in more detail. At the same time, various ways to assist these countries could be examined as a means to overcome the development gaps in the less developed countries, including human resource development projects and other development cooperation projects with concrete funding mechanisms. Furthermore, in addition to trade and investment liberalization, possibilities of including substantial trade and investment facilitation measures could also be sought after and, given the importance of the rules of origin, greater attention could be made to examining the rules of origin that are to be adopted in the EAFTA.

In order to benefit from the existing FTAs between East Asian countries and to speed up research, the joint study could start off by analyzing the existing FTAs. A much more thorough analysis on the increasing number of FTAs between East Asian countries, than presented in this study, could serve as a stepping stone for the formation of the EAFTA.

Another important task for the EAFTA concerns Northeast Asian countries. Since an EAFTA cannot be formed unless there is a *de facto* China-Japan-Korea FTA, the three Northeast Asian countries should not neglect the importance of a CJK FTA in their pursuit of an EAFTA. In this regard, the Korean government is called upon to play the role of facilitator in the formation of a CJK FTA, by persuading both China and Japan on the importance of a CJK FTA in achieving the EAFTA. To this end, the Korean government could conclude a Korea-Japan FTA and a Korea-China FTA to hasten the formation of a CJK FTA and ultimately an EAFTA.

With regard to technical issues, the standardization of HS codes is urgently needed among East Asian countries. As noted in chapter II, many East Asian countries adopt different HS code digits, which make it very difficult to compare the degree of trade liberalization in goods among the existing East Asian FTAs. As a result, standardization of HS code digits would help alleviate technical burdens of research. In addition, the standardization of HS code digits could facilitate the creation and use of unified, digital international trading documents.

Successful conclusion of an EAFTA rests on the political determination of regional leaders. Therefore, it is important to build a consensus on the need for an EAFTA and the method of achieving it among core members first, and to expand it to other opinion leaders such as intellectuals, journalists, government officials, and political leaders.

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Appendix

Annex Table II-1: Implementation Timeframes of the Early Harvest Program, ACFTA
(percent)

(i) China and ASEAN-6:

| Product Category | Not later than Jan. 1, 2004 | Not later than Jan. 1, 2005 | Not later than Jan. 1, 2006 |
|------------------|-----------------------------|-----------------------------|-----------------------------|
| 1 | 10 | 5 | 0 |
| 2 | 5 | 0 | 0 |
| 3 | 0 | 0 | 0 |

(ii) CLMV countries:

Product Category 1

| Country | Not later than Jan. 1, 2004 | Not later than Jan. 1, 2005 | Not later than Jan. 1, 2006 | Not later than Jan. 1, 2007 | Not later than Jan. 1, 2008 | Not later than Jan. 1, 2009 | Not later than Jan. 1, 2010 |
|---------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| Vietnam | 20 | 15 | 10 | 5 | 0 | 0 | 0 |
| Lao PDR and Myanmar | - | - | 20 | 14 | 8 | 0 | 0 |
| Cambodia | - | - | 20 | 15 | 10 | 5 | 0 |

Product Category 2

| Country | Not later than Jan. 1, 2004 | Not later than Jan. 1, 2005 | Not later than Jan. 1, 2006 | Not later than Jan. 1, 2007 | Not later than Jan. 1, 2008 | Not later than Jan. 1, 2009 | Not later than Jan. 1, 2010 |
|---------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| Vietnam | 10 | 10 | 5 | 5 | 0 | 0 | 0 |
| Lao PDR and Myanmar | - | - | 10 | 10 | 5 | 0 | 0 |
| Cambodia | - | - | 10 | 10 | 5 | 5 | 0 |

Product Category 3

| Country | Not later than Jan. 1, 2004 | Not later than Jan. 1, 2005 | Not later than Jan. 1, 2006 | Not later than Jan. 1, 2007 | Not later than Jan. 1, 2008 | Not later than Jan. 1, 2009 | Not later than Jan. 1, 2010 |
|---------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
| Vietnam | 5 | 5 | 0 - 5 | 0 - 5 | 0 | 0 | 0 |
| Lao PDR and Myanmar | - | - | 5 | 5 | 0 - 5 | 0 | 0 |
| Cambodia | - | - | 5 | 5 | 0 - 5 | 0 - 5 | 0 |

Annex Table IV-1. AFAS Schedule for Specific Commitments

1) Brunei

| | 1st Package | 2nd Package | 3rd Package | 4th Package |
|-------------------------------|----------------|--|--|--|
| Air Transportation | 8868 | | Computer reservation system service Selling and marketing of air transport | 734 |
| Business Service | | 8671 | 8672, 86742, 841, 842, 843, 845, 849 | 86742, 862, 83104 |
| Construction | | 512, 513, 514, 516, 517, 515 | 511-518 | 511-518 |
| Financial Service | | 8131 | | 8121, 8129, 81299, 8140, 8131, 9312, Services auxiliary to insurance |
| Maritime Transport | 7212, 7211 | | | |
| Telecommunicati on Service | | Telex services Telegraph services | Public switched voice telephone services (Local/ International) (2) Public Cellular mobile telephone service 7523, 7522, 7523 | Public switched voice telephone services (Local) 7523(Voice Mail), 844, 7523(Data Transmission), 7521+7529, 7523(Electronic mail), 7523 (On-line info. and database retrieval), 7523(Elec. data interch.), 7523(Facsimile) |
| Tourism | 64110 | | 64110 | 642, 643 |

2) Cambodia

| | 1st Package | 2nd Package | 3rd Package | 4th Package |
|---------------------------|----------------|---|--|--|
| Air Transportation | | Computer reservation system Selling and Marketing of air transport | 8868 | |
| Business Service | | Trading company | 862, 8671, 86742 | 8671-8674, 87905, 86401, 83107 |
| Construction | | | 511-518 | 511-518 |
| Financial Service | | Acceptance of deposits | | |
| Maritime Transport | | | 7211, 72121, 72122 | 7211, 7212, 742 |
| Telecommunication Service | | | 7523, 843, 75291 Internet Service provision | 7523(Voice mail, On-line Info and data, Electronic data)(3), 843, 75291, Internet services provision, excl. voice telephony and facsimile. 841, 842, 843, 844, 845+849 |
| Tourism | | 641-643 | 64110, 64210, 64310 | 64110, 642, 643 |

3) Indonesia

| | 1st Package | 2nd Package | 3rd Package | 4th Package |
|-----------------------------------|---|----------------|--|-----------------------------------|
| Air Transportation | | | Selling and marketing of air transport Aircraft repair and maintenance services | |
| Business Service | | | 86721, 86725, 84100, 86601, 842, 853, 8676, 884, 885, 633+8861+8866, 86220, 84400, | |
| Construction | | | 511-518 | |
| Financial Service | | | | |
| Maritime Transport | 7211, 7212, 741 | | Rental of Vessel without crew | |
| Tele- communication Service | | | 7521(local), 7523(local), 75292(local), 7521(long distance), 7523(long distance), 75292(long distance), 7521(Int'l), 7523(Int'l), 75292 (Int'l), 7523(Public data network), Telex services, Telegraph services 75213, 75291, Internet Access services | |
| Tourism | Int'l Hotel Operator Tourism Consultancy Ser. | | 64110, 64210, 64310, 74710, 91136, 91135 | 64210, 64310 7471, 74710 |

4) Laos

| | 1st Package | 2nd Package | 3rd Package | 4th Package |
|-----------------------------------|----------------|---|---|----------------|
| Air Transportation | | Computer reservation system Selling and marketing of air transport services | | |
| Business Service | | 8671, 8672 | 84100, 842, 84400, 86742, 86732, 86733, 862 | 86742 |
| Construction | | 512, 513 | 511-518 | |
| Financial Service | | 81321, 81339 | | |
| Maritime Transport | | 7212, 742 | | |
| Tele- communication Service | | 75211, 75232 | 7523, 7521, 7529, 7522, 75291, 75440 | |
| Tourism | 641-643 | 64110, 64310 | 64110, 64310, 64210 | 64110, 64310 |

5) Malaysia

| | 1st Package | 2nd Package | 3rd Package | 4th Package |
|---------------------------|---|---|--|---|
| Air Transportation | Selling and Marketing of air transport services Computer reservation system services | | Aircraft repair and maintenance services | |
| Business Service | | 6111, 6113, 6121, 6130, 6221, 6222, 6223, 6224, 6225, 6226, 6227, 6228, 631, 632, 8672 | 8671, 8672, 862, 86742, 86752, 86753, 841, 842, 8440 | 862, 863, 8671, 8672, 86742, 87905, 86401, 83107, 85202 |
| Construction | | 511-517 | 511-517 | 511-517 |
| Financial Service | | Banking and other financial services, excluding insurance Operational headquarters Insurance services | 7523 (data, mobile data) (2) | |
| Maritime Transport | Maritime freight forwarding services | | | Rental of cargo vessel with/without crew for international shipping (2) |
| Telecommunication Service | | 7523(3) | | 7523(Data and message transmission, Mobile data)(2) 7522, 7521, 75213, 75291, 841, 842, 8440 |
| Tourism | Convention centre Theme Parks | | 64110, 64210, 64310 | 64110, 7471 |

6) Myanmar

| | 1st Package | 2nd Package | 3rd Package | 4th Package |
|---------------------------|---------------|---|--|--------------------------------|
| Air Transportation | | Aircraft Repair and maintenance service | Air Transport Services selling and marketing Aircraft repair and maintenance services | |
| Business Service | | 86401, 86503 | 862, 8671, 8672, 86742 | |
| Construction | | 51400 | 511-517 | |
| Financial Service | | 811 | | |
| Maritime Transport | | 7454 | Int'l passenger transport (excl. cabotage) Int'l freight transport (excl. cabotage) | |
| Telecommunication Service | | 754, 75450 | 7523 | 7521, 75213, 7522, 7523, 75291 |
| Tourism | 641-643, 7471 | 96194 | 64110, 64210, 64310 | 64210 |

7) Philippine

| | 1st Package | 2nd Package | 3rd Package | 4th Package |
|---------------------------|--------------|---|--|---------------------|
| Air Transportation | | Computer reservation system | Selling and marketing of air transport Computer and reservation system services | |
| Business Service | 86211, 86212 | 8671, 86741, 86742, 87907, 8672, 86211, 86212 | 86221, 86212, 8671, 86742, 86741, 8672, 87907, 841, 842, 843 | |
| Construction | | 511-517 | 511-518 | |
| Financial Service | | Commercial Banking | | |
| Maritime Transport | | International Transport | | 83103, 8868 |
| Telecommunication Service | | 75291 | Voice telephone services Telegraph Telex, etc. | |
| Tourism | 64110 | 64110 | 64110, 64210, 64310 | 64110, 64210, 64310 |

8) Singapore

| | 1st Package | 2nd Package | 3rd Package | 4th Package |
|----------------------------|--|--|---|--|
| Air Transportation | Selling and Marketing of Air Transport | | Aircraft repair and maintenance services | |
| Business Service | | 8672, 86724, 86729, 86723, 86729, 86725 | Auditing Accounting, bookkeeping 84100, 842, 84400 | 863, 86742, 87905, 86401, 85202, 8671, 93121, 98122, 93123 |
| Construction | | 83107 | Construction services | |
| Financial Service | | | | |
| Maritime Transport | | Maritime auxiliary service | 7211, 7212 | Shipping agency services Shipping brokerage services |
| Tele-communication Service | | Store and retrieve VAN service | VAN service | Basic telecom. services Mobile services Resale basis Computer service (data processing) |
| Tourism | 7471 | | 64110, 64210, 64310 | 96194, 7471 |

9) Thailand

| | 1st Package | 2nd Package | 3rd Package | 4th Package |
|---------------------------|---|--|--|---|
| Air Transportation | | Selling and marketing of air transport services Computer Reservation system service | Selling and marketing of air transport services Computer Reservation system service Aircraft repair and maintenance services | |
| Business Service | | 85101, 85102, 85103, 85104, 85109, 85202, 85203, 85204, 86502, 86504 | 86221-86213, 86219, 86220, 86711-86714, 86719, 86741-867422, 86721-86727, 86729, 84100, 84400 | 862(86211-86213+86219+86220), 863, 8671(86711-86714+86719), 86742, 8672(86721-86727+86729), 85202, 83107, 86401, 87905 |
| Construction | | 511,514, 515, 517 | 511-518 | 511-518 |
| Financial Service | | Securities Companies Asset management companies | | |
| Maritime Transport | 7212 Customs clearance services | 7212 Customs clearance services | 7211, 7212 | 7211, 7212, Maritime cargo handling services Maritime agency services 742 |
| Telecommunication Service | | 75410 Domestic VSAT | 75420, 75440, 7523 | 7523, Fixed-line voice telephone service, 75213, 75219, 84100, 84400, 842(84210+84220+84230+84240+84250), 843(84310+84320+84330+84390) |
| Tourism | 64120, 64192, 64195, 96194 Marina facilities | Convention Center over 2000 | 64110, 64210, 64310 | 64110, 64210, 64310, 64195 |

10) Vietnam

| | 1st Package | 2nd Package | 3rd Package | 4th Package |
|------------------------------|----------------|---|--|--|
| Air Transportation | | 8868 Selling and marketing of air transport services | Selling and marketing of air transport services (746) Aircraft repair and maintenance services (8868) Computer Reservation system service (746) Rental/Leasing aircraft without operator services (746) | |
| Business Service | | 862, 863 | 8671, 86742, 8672, 862 | 8671, 86742, 8672, 862 |
| Construction | | | 511-518 | 511-518 |
| Financial Service | | 8121, 8129, 81212, 81299, 81401, 81115-81119 | | |
| Maritime Transport | | | 7211, 7223 | 7211, 7212, 8868 Ship broking services |
| Telecommunication Service | 7523 | | 7523, 7522, 7523, 7522, 75291, 7521 | 7521, 7523, 7521+7529, 7522+7523, Radio based services Value added services in 7523(Voice mail, On-line info., EDI, Facsimile)+Code and protocol conversion+843(on-line info and data processing) |
| Tourism | 641-643 | | 64110, 64210, 64310 | 7471 |

Annex Table IV-2. Korea-Singapore Service Reservation for existing Measure: Korea

| Sector | Industrial |
|---|--|
| Business Services | 821, 822, 82130, 862, 863, 86309, 867, 8671, 8672, 8673, 8674, 8675, 86752~4, 86762, 86763, 86769, 92900, 93199, 8720, 87909, 88442, 88700, 91132, Certified labor affairs consultant, Investigation and Security Services |
| Communication Services | 7512, 9611, 9612, Basic Telecommunications Services |
| Construction and Related Engineering Services | 511~515, 518, 83107, 8510, 8862 |
| Distribution Services | 62111, 6221, 63211 |
| Education Services | 923, 924 |
| Environmental Services | 86761, 94010~90, 94090 |
| Financial Services | |
| Health Related and Social Services | 932 |
| Tourism and Travel Related Services | |
| Recreational, Cultural and Sporting Services | |
| Transport Services | 6111, 6112, 8867, 8868, 721, 7211, 7212, 7213, 7214, 745, 74520, 74530, 74540, 83101, 83105 |
| Other Services Not Included | |

Annex Table IV-3. Korea-Singapore Service Reservation for existing Measure: Singapore

| Sector | Industrial |
|---|---|
| Business Services | 87204, 86211, 82202, 87301, 87302, 87305, Patent Agent, Professional Engineering services, Architectural Services, Testing, analytical and certification services on animals, plants, and products derived from animals and plants, Land Surveying Services |
| Communication Services | Telecommunications Services |
| Construction and Related Engineering Services | |
| Distribution Services | Distribution and Sale of Hazardous Substances, Retailing Services, Wholesale Trade Services |
| Education Services | |
| Environmental Services | |
| Financial Services | |
| Health Related and Social Services | 952, 93191, 9312, Pharmacy Services, Import, export and trading services |
| Tourism and Travel Related Services | |
| Recreational, Cultural and Sporting Services | |
| Transport Services | 741, 74520, Maritime Transport Services |
| Other Services Not Included | Power supply, Power transmission and distribution, Production, retail, transportation and distribution of manufactured gas and natural gas |

Annex Table IV-4. Korea-Singapore Service Reservation for Future Measure: Korea

| Sector | Industrial |
|---|---|
| Business Services | 88 (except 883, 8847, 8854, 8855, 8856, 8857, 8852), 88442, 882, 861, 82400 Credit Reporting Services |
| Communication Services | Broadcasting Service, 7511, |
| Construction and Related Engineering Services | 82, 8674, 51, |
| Distribution Services | 621(excluding 62111), 622, Trade Services |
| Education Services | 921, 922, 923, 924, 929 |
| Environmental Services | 18000, 71390, 94010, 94020, 94030, 94060, 94090, |
| Financial Services | |
| Health Related and Social Services | 952, 913, 93 |
| Tourism and Travel Related Services | |
| Recreational, Cultural and Sporting Services | 96520, 96492 |
| Transport Services | 711, 712, 74, 8868, 83102, 722, 733, 742 |
| Other Services Not Included | (Electric energy) 17100, 5164, 5165, 52243, 87909 (Gas industry) 12020, 52241, 61300, 62271, 63297, 71122, 71232, 71310, 72222, 74220, 88700 (Nuclear Industry) 13000, 33710, 33720, 42310, 88450, 94090 Arms and explosives, Minority Affairs, National Electronic System(including but not limited to Geographical Information System) |

**Annex Table IV-5. Korea-Singapore Service Reservation for Future
Measure: Singapore**

| Sector | Industrial |
|---|--|
| Business Services | 82, 87305, Betting and Gambling Services, Credit Reporting Services, Professional Services |
| Communication Services | Broadcasting Service, 7511 |
| Construction and Related Engineering Services | |
| Distribution Services | Distribution(publishing and printing of newspapers), Trade Service |
| Education Services | |
| Environmental Services | |
| Financial Services | |
| Health Related and Social Services | 952 |
| Tourism and Travel Related Services | |
| Recreational, Cultural and Sporting Services | |
| Transport Services | |
| Other Services Not Included | |

Annex Table IV-6. Korea-Singapore Investment Reservation for Existing Measure: Korea

| Sector | Industrial |
|--|--|
| Business Services | 871, 8510, 0113, 0115, 01212, 51312, 82130, 86761, 86762, 86763, 86769 |
| Telecommunications | Basic Telecommunications Services |
| Construction Services | 511~518 |
| Distribution Services | 62111, 6221 |
| Educational Services | 923, 924 |
| Manufacture of Chemical Products | 24212 |
| Recreational, Cultural and Sporting Services | 962 |
| Manufacturing and Distribution Services | |
| Transport Service | 731, 732, 734, 7211, 7212, 7213, 7214, 721 |

Annex Table IV-7. Korea-Singapore Investment Reservation for Future Measure: Korea

| Sector | Industrial |
|--|---|
| Business Services | 88 (except 883, 8847, 8854, 8855, 8856, 8857, 8852), 88442, 882, 861, Credit Reporting Services |
| Construction Services | 82, 8674, 51 |
| Trade Services | - |
| Business and Production Services | 82400 |
| Arms and explosives | - |
| Community, Personal and Social Services | 952 |
| Communication Services | Broadcasting Service, 7511 |
| Distribution Services | 621(excluding 62111), 622 |
| Education Services | 921, 922, 923, 924, 929 |
| Electric energy | 17100, 5164, 5165, 52243, 87909, 88700 |
| Environmental Services | 18000, 71390, 94010, 94020, 94030, 94060, 94090, |
| Recreational, Cultural and Sporting Services | 96520, 96492 |
| Gas industry | 12020, 52241, 61300, 62271, 63297, 71122, 71232, 71310, 72222, 74220, 88700 |
| Minority Affairs | - |
| Nuclear industry | 13000, 33710, 33720, 42310, 88450, 94090 |
| Social Services | 913, 93 |
| Transport Services | 711, 712, 74, 8868, 83102, 722, 733, 742 |
| National Electronic System, including but not limited to Geographical Information System | - |

Annex Table IV-8. Korea-Singapore Investment Reservation for Existing Measure: Singapore

| Sector | Industrial |
|---|---|
| Business Services | Professional Services, Patent Agent Services, Professional Engineering services, Architectural Services, 86211, 82202, 87301, 87302, 87305 |
| Manufacturing | |
| Power supply | |
| Power transmission and distribution | |
| Trade services | |
| Community, Personal and Social Services | 952 |
| Educational Services | 92390 |
| Production, retail, transportation and distribution of manufactured gas and natural gas | |
| Transport Service | 731, 732, 741, 74520, Maritime Transport Services |

Annex Table IV-9. Korea-Singapore Investment Reservation for Future Measure: Singapore

| Sector | Industrial |
|--|--|
| Business Services | Credit Reporting Services, Betting and Gambling Service, Professional Services, 87305 |
| Administration and operation of national electronic systems | - |
| Trade Services | Distribution Services, Commission Agents' Services, Wholesale Trade Services, Retailing Services, Franchising, 18000 |
| Arms and explosives | - |
| Arms and explosives | - |
| Community, Personal and Social Services | 952 |
| Broadcasting Services | - |
| Distribution Services | - |
| Education Services | 921, 92210, 92220 |
| Defense | - |
| Health and Social Services | Services provided by health-related professionals, 933 |
| Sewage and refuse disposal, sanitation and other environmental Protection services | 9401 |
| Post and Telecommunications Services | Postal Services, Postal Services—Express Letters, Courier Services |
| Telecommunications Services | Telecommunications Services |
| Transport services | Air Transport Services, Land Transport Service, Maritime Transport Services, 742, 748, 749 |

Annex Table IV-10. Japan-Singapore Services: Japan's Schedule of Specific Commitment

| Sector | Industrial |
|---|--|
| Business Services | 5115, 663, 821, 822, 83101, 83102, 83103, 83104, 83105, 83106, 83107, 83108, 83109, 832, 841, 842, 843, 844, 845, 849, 851, 852, 853, 861, 86119, 8612, 8613, 8619, 862, 863, 864, 865, 86601, 86609, 86711, 86712, 86713, 86714, 86719, 8672, 86721, 86722, 86723, 86724, 86725, 86727, 86729, 8673, 8674, 86741, 86742, 86751, 86752, 86753, 86754, 8676, 86761, 86763, 871, 87201, 87202, 87203, 87209, 873(except 87301), 87301, 87401, 87402, 87403, 87409, 875, 876, 87905, 87907, 87909, 883, 884, 88442, 885, 8861, 8862, 8863, 8864, 8865, 8866, 887, 9312, 93191 |
| communications services | 7521, 7522, 7523, 7524, 7529, 843, 9611, 9612, 9613 |
| Construction and Related Engineering Services | 511, 512, 513, 514, 515, 516, 517, 518 |
| Distribution Services | 61111, 61112, 61130, 61210, 621, 622, 631, 632, 8929 |
| Educational Services | 9211, 92110, 9219, 9221, 9222, 9223, 9231, 9239, 924, 929, 93321 |
| Environmental Services | 9401, 9402, 9403, 9404, 9405, 9406, 9409 |
| Financial Services | All Insurance-Related Services, Banking and other Financial Services |
| Health Related and Social Services | 93192, 93199, 933, 9331 |
| Recreational, Cultural and Sporting Services | 9619, 962, 96311, 96312, 9632, 9633, 964, 9641, 96491 |
| Tourism and Travel Related Services | 6411, 6412, 64194, 6421, 6422, 6423, 6431, 6432, 7471, 7472 |
| Transport Services | 6112, 7111, 7112, 7113, 71211, 71212, 71213, 71214, 71221, 7123, 7124, 7131, 7139, 7211, 7212, 7214, 7223, 7224, 733, 741, 742, 744, 7454, 7459, 748, 749, 8867, 8868, Air Transport Services, Services Auxiliary to All Modes of Transport, Other Services not Included Elsewhere, Rail Transport Services |

Annex Table IV-11. Japan-Singapore Services: Singapore's Schedule of Specific Commitment

| Sector | Industrial |
|---|---|
| Business Services | 5115, 633, 821, 822, 83101, 83102, 83103, 83104, 83105, 83106, 83107, 83108, 83109, 832, 841, 842, 843, 844, 845, 849, 851, 852, 853, 861, 862, 86211, 863, 86309, 864, 865, 866, 8671, 8672, 86724, 8673, 86741, 86742, 86751, 86752, 86753, 86754, 8676, 86763, 871, 872, 87302, 87303, 87305, 874, 875, 876, 87903, 87904, 87905, 87906, 87907, 87909, 881, 882, 883, 884(except 88442), 885, 8861, 8862, 8863, 8864, 8865, 8866, 93121, 93122, 93123, 93191, 932, Other Professional Services |
| Communications services | 7512, 9611, 9612, telecommunications services, Audiovisual Services, telecommunications services |
| Construction and Related Engineering Services | 511, 512, 513, 514, 515, 516, 517, 518 |
| Distribution Services | 61111, 61112, 61130, 61210, 621(except 62117), 62117, 622, 62251, 62252, 6310, 632, 63211, 8929 |
| Educational Services | 92230, 92240, 92310, 92390, 92400, 92900 |
| Environmental Services | Environmental Services except sewage services and new environmental services, 94010 |
| Financial Services | All Insurance-Related Services, Banking and other Financial Services |
| Health Related and Social Services | Other Health Related and Social Services, 93110, 93192, 93193, 93311, 93312, 9332 |
| Recreational, Cultural and Sporting Services | Other Recreational, Cultural and Sporting Services News Agency Services, 9619, 9631, 96311, 9632, 9633, 964, |
| Tourism and Travel Related Services | 641, 642, 643, 7471, 7472 Other Tourism and Travel Related Services |
| Transport Services | aircraft repair and maintenance services, selling and marketing of air transport services 61120, 7111, 7112, 7113, 71222, 71223, 7123, 71231, 71232, 71233, 71234, 71240, 7131, 7139, 7211, 7212, 7214, 7221, 7222, 7223, 7224, 733, 734, 742, 743, 744, 74430, 748, 749, 88, 8868, 9701, 9702, 97030, |

Annex Table IV-12. Japan-Malaysia Investment Reservation: Japan

JSIC code

| Sector | Industrial |
|--|---|
| Agriculture, Forestry and Fisheries, and related services | 0119, 0243, 0413, 0415, 01, 02, 03, 04, 6224, 6225, 791 |
| Finance | 612, 621 |
| Heat Supply | 3511 |
| Information and Communications | 3721, 3741, 3721, 3722, 3729, 3731, 4011, 381, 382, 383 |
| Manufacturing | 1763, 1257, 1259, 1794, 202, 21, 3234 |
| Matters Related to the Nationality of a Ship | - |
| Mining | 05 |
| Oil Industry | 053, 181, 182, 1841, 1899, 4711, 4721, 5231, 6031, 6032, 9099 |
| Security Guard Services | 9061 |
| Transport | 4611, 4621, 4441, 4821, 4441, 4821, 42, 4851, , 4311, 452, 453, 4542 |
| Water Supply and Waterworks | 3611 |
| Aerospace Industry | 271, 274, 275, 279, 28, 29, 304, 3059, 3099, 8711, 872 |
| Arms and Explosives Industry | 1792, 271, 274, 275, 279, 28, 29, 303, 3059, 3099, 3281, 8711, 872 |
| Energy | 0519, 2491, 271, 274, 275, 279, 28, 29, 303, 3059, 3099, 331, 3411, 3412, 3413, 8711, 872 |
| Fisheries | 031, 032, 041, 042, 8493 |
| Land Transaction | - |
| Public Law Enforcement and Correctional Services and Social Services | - |

Annex Table IV-13. Japan-Malaysia Investment Reservation: Malaysia

| ISIC code | |
|---|---|
| Sector | Industrial |
| Manufacturing | 1513, 1514, 1542, 1551, 1552, 1553, 1600, 2010, 2021, 2022, 2320, 2694, 2710, 2230, 1711, 1712, 1810, 3410, 2429, 2927, Collection, Storage, Treatment and Disposal of Hazardous and Toxic Wastes |
| Agriculture, Forestry, Fisheries and Mining | 0200, 0500 |
| Oil and Gas Upstream Industries | 1100 |
| Mining and Quarrying | 10, 12, 13, 14 |
| Statutory Bodies | - |
| National and State Unit Trusts | - |

Annex Table V-1. Share of Intraregional FDI Inflows

| (Unit: percent) | | | | | | | | | | | | | | |
|-----------------|------|------|------|------|------|------|------|------|------|------|------|------|------|------|
| | 1990 | 1991 | 1992 | 1993 | 1994 | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 |
| ASEAN +3 | 26.6 | 31.6 | 47.4 | 57.7 | 58.7 | 62.9 | 47.5 | 55.7 | 57.6 | 37.6 | 41.7 | 43.8 | 53.7 | 47.5 |
| EU | 52.6 | 60.8 | 66.8 | 59.3 | 53.1 | 49.7 | 52.9 | 58.7 | 56.4 | 77.2 | 90.9 | 67.3 | 48.8 | 47.4 |
| NAFTA | 12.1 | 14.9 | 37.4 | 21.1 | 32.0 | 20.9 | 20.2 | 19.2 | 18.6 | 18.6 | 14.3 | 25.6 | 33.1 | 45.1 |

Sources: Calculated by authors based on data from ASEAN: *Statistics of Foreign Direct Investment in ASEAN: Comprehensive Data Set - 2003 Edition*, ASEAN Secretariat; EU, NAFTA, Korea, Japan: *International Direct Investment Statistics Yearbook 2002, 2003, 2004 Edition*, OECD; China: *Annual Statistical Yearbook 1998 - 2004 Edition*, Bureau of Statistics, China.

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