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## **Impact of TPP-11 on Japanese Manufacturing Affiliates in ASEAN**

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### **Abstract**

This paper discusses how tariff reductions through TPP may affect Japanese manufacturing affiliates in ASEAN countries. Without the U.S., there is some uncertainty in the impact of TPP on the investment and expansion plans of Japanese affiliates in Malaysia and Vietnam's textile and footwear industries. Similarly, it is also uncertain that Japanese affiliates in ASEAN non-TPP member countries will shrink their business in these industries. In the case of other industries, the TPP-11 will not affect Japanese affiliates because market access will not be different between TPP and non-TPP member countries.

Keywords: Trans-Pacific Partnership; ASEAN; Japanese Affiliates; Tariffs

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# Impact of TPP-11 on Japanese Manufacturing Affiliates in ASEAN

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## 1. Introduction

Trans Pacific Partnership (TPP) agreement was largely agreed on 5 October 2015 and was signed in 4 February 2016 by 12 countries, namely, Japan, four ASEAN countries (Brunei, Malaysia, Singapore, and Vietnam), and seven non-Asian countries (Australia, Canada, Chile, Mexico, New Zealand, Peru, and the U.S.). These countries accounted for approximately 40% of the world's GDP. Even though the U.S. has withdrawn from the TPP, the remaining eleven member countries (TPP-11) have indicated their interests to ratify the agreement.

TPP-11 may have some potential impacts on business activities by Japanese manufacturing affiliates in ASEAN though the withdrawal of the U.S. from the TPP has created some uncertainties. Such impacts will emerge in the Japanese affiliates in not only TPP-member countries (Brunei, Singapore, Malaysia, and Vietnam) but also non-member countries. While the former effect will be positive, the latter effect may be negative. According to ASEAN Stats, in almost all recent years, Japan is a top country in terms of the value of foreign direct investment (FDI) flow into ASEAN countries. Therefore, any change in their activities will have a great impact on the economy of ASEAN countries.

In this paper, we investigate how Japanese manufacturing affiliates in ASEAN is expected to change their business activities if the TPP-11 is implemented. Specifically, we focus on the effects of tariff provision in this paper. The liberalization level of TPP is very high. All member countries are expected to eliminate their tariff rates in almost all products. Except for Japan, tariff elimination rates are expected to be 99 percent or 100 percent in all countries, in terms of both number of tariff lines and trade values. In the case of Japan, the tariff elimination rate will be 95 percent, which is nevertheless the highest among all regional trade agreements (RTAs) concluded by Japan thus far. Therefore, although one important feature of TPP is the inclusion of various rules on non-tariff

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issues, we should not understate the effects of tariff reduction in TPP. To investigate these effects, it is important to discuss the general effects of tariff reduction on business activities in TPP-member countries. In particular, we discuss the effects on their exports to other TPP-members. Then, based on this discussion, we examine the effects on Japanese manufacturing affiliates in ASEAN.

The rest of this paper is organized as follows. The next section takes overview of the distribution of Japanese manufacturing affiliates particularly in ASEAN in addition to ASEAN exports to the U.S. Section 3 discusses the general effects of tariff reduction on exports from ASEAN TPP-member countries. In Section 4, we examine the effects of tariff reduction on Japanese manufacturing affiliates in ASEAN. Last, Section 5 concludes on this paper.

## **2. ASEAN Exports to the U.S. and Japanese Affiliates in ASEAN**

In this section, we first take an overview of ASEAN exports to the U.S.. Even though the U.S. has withdrawn from the TPP, this overview will provide an indication of how much of the potential gains of the TPP are lost without the U.S.'s participation. Table 1 reports the share of exports in 2015, by industries (Section of Harmonized System) and countries. The data are obtained from the World Trade Atlas. The cells of top two industries (excluding miscellaneous industries) in terms of share are colored. Several countries have a high share of exports in machinery industry. Those include Vietnam, Malaysia, Singapore, Indonesia, Thailand, and the Philippines. Also, textiles industry also shows a high share in Vietnam, Brunei, Indonesia, Philippines, Myanmar, Cambodia, and Laos. Another noteworthy finding is that the share of plastics and rubber industry is relatively high in Thailand while Laos has a relatively high share in precision metals industry.

Next, we show the distribution of Japanese manufacturing affiliates. To do that, we employ the *Basic Survey of Overseas Business and Activities* collected by the Ministry of Economy, Trade, and Industry (METI), Japan. The survey covers: (i) a foreign affiliate in which a Japanese corporation has invested capital of 10 percent or more; (ii) a foreign affiliate in which a subsidiary, funded more than 50 percent by a Japanese corporation, has invested capital of more than 50 percent; and (iii) a foreign affiliate in which a Japanese corporation and a subsidiary funded more

than 50 percent by a Japanese corporation have invested capital of more than 50 percent. We use the survey for the Japanese fiscal year 2014.

**Table 1: Export from ASEAN to the U.S. in 2015 (%)**

	VNM	MYS	SGP	BRN	IDN	THA	PHL	MMR	KHM	LAO
Live animals	2.7	0.3	0.1	1.6	6.0	1.6	1.1	25.4	0.1	0.0
Vegetable products	4.0	0.0	0.0	0.1	3.2	2.3	2.2	5.6	0.1	12.4
Animal/vegetable fats and oils	0.1	1.9	0.1	0.0	3.4	0.0	5.2	0.2	0.0	0.0
Food products	1.6	0.7	0.4	0.0	5.3	7.9	5.3	2.0	0.7	0.6
Mineral products	0.5	0.1	0.7	0.0	4.4	0.1	0.0	0.0	0.0	0.0
Chemical products	0.6	2.0	32.4	27.4	3.0	1.0	0.9	0.0	0.0	20.1
Plastics and rubber	1.4	5.3	1.5	0.0	10.0	9.1	2.1	0.0	2.2	7.0
Leather products	3.0	0.0	0.0	0.0	0.9	0.5	3.0	20.2	1.8	0.1
Wood products	0.4	0.5	0.0	0.0	2.0	0.3	0.5	3.3	0.4	0.9
Paper products	0.3	0.2	0.3	0.0	1.8	0.1	0.3	0.0	0.0	0.0
Textiles	28.6	1.7	0.1	29.3	26.6	4.4	11.2	30.3	83.2	20.4
Footwear	12.3	0.0	0.0	0.4	8.6	0.5	0.1	10.4	7.8	0.3
Plastic or glass products	0.4	0.3	0.2	0.0	0.6	0.6	0.4	0.0	0.0	0.0
Precision metals	0.4	0.0	1.8	0.0	0.7	5.9	0.2	0.8	0.2	21.6
Base Metal	1.8	1.5	0.6	0.1	2.8	3.8	1.4	0.4	0.4	12.0
Machinery	28.5	74.2	32.7	4.0	11.4	51.9	55.6	0.0	0.2	0.0
Transport equipment	0.8	0.6	0.8	0.8	0.7	3.1	0.6	0.0	0.7	0.0
Precision machinery	0.8	5.6	14.0	0.5	2.4	3.2	4.2	0.0	0.0	3.4
Miscellaneous	11.8	4.9	14.4	35.8	6.3	3.7	5.6	1.3	2.3	1.3
Total Imports (Mil. USD)	38,020	33,971	18,267	19	19,602	28,632	10,234	144	3,025	45

*Source:* World Trade Atlas

*Note:* The cells of top two industries (excluding miscellaneous industries) in terms of share are colored.

The number and share of affiliates are reported in Table 2. The major location is Asia, which accounts for 77 percent of all affiliates in the world. In particular, China has attracted a largest number of Japanese manufacturing affiliates (38 percent of all). However, due to the recent wage hikes in China, the number of investors in ASEAN countries is growing.<sup>1</sup> As a result, ASEAN countries attract 30 percent of the Japanese affiliates. One third of Japanese affiliates in ASEAN are located in Thailand. A relatively large number of Japanese affiliates are also found in

<sup>1</sup> Also, using a logit or multinomial logit model of Japanese firms' FDI choices, Hayakawa and Matsuura (2015) showed that the tariff reduction in Asian countries has lowered the productivity cutoff for vertical type of FDI (VFDI). Namely, since Asian countries have experienced a relatively rapid decrease in tariff rates, the increase in VFDI through tariff reduction led to the recent surge of Japan's FDI in Asian countries.

Indonesia. This is followed by other ASEAN countries such as Vietnam and Malaysia, both of which are TPP-member countries.

**Table 2: Distribution of Japanese Manufacturing Affiliates in FY2014**

	Number	Share (%)
North America	1,125	11
Middle/Latin America	331	3
Asia	8,167	77
China	4,025	38
Taiwan	392	4
Korea	325	3
ASEAN10	3,145	30
Philippines	267	3
Malaysia	396	4
Thailand	1,183	11
Indonesia	607	6
Singapore	201	2
Vietnam	455	4
India	235	2
Europe	804	8
Oceania	99	0.9
Africa	47	0.4
Total	10,573	

*Source:* Basic Survey of Overseas Business Activities  
(Ministry of Economy, Trade and Industry, Japan)

In Table 3, we take a closer look at the industry composition of Japanese manufacturing affiliates in Asia. The cells of top two industries (excluding miscellaneous industries) in terms of number are colored. Roughly, transport equipment and information and communication electronics equipment industries are the main industries for Japan's FDI in Asia. In Thailand, Indonesia, and Singapore, the chemical industry also has a relatively high share, while metal products show a relatively large number of Japanese affiliates in Vietnam. On the other hand, there are, in general, a relatively small number of Japanese affiliates in food and textiles industries.

**Table 3: Japanese Manufacturing Affiliates in Asia in FY2014, by Industries**

	CHN	TWN	KOR	ASEAN10							IND
				PHL	MYS	THA	IDN	SGP	VNM		
Food	175	13	12	138	6	15	55	23	14	23	5
Textiles	295	8	5	140	3	6	55	36	2	25	3
Lumber, wood, paper, and pulp	67	3	3	62	2	14	18	11		16	
Chemicals	338	74	68	324	20	44	110	68	45	35	27
Petroleum and coal	12	1	3	14		2	3	4	4	1	1
Ceramic, stone, and clay products	109	21	15	60	2	13	17	10	5	13	4
Iron and steel	108	5	7	115	6	10	47	29	5	17	11
Non-ferrous metals	139	10	7	113	10	26	43	14	6	13	5
Metal products	239	15	19	212	18	22	78	37	17	38	5
General-purpose machinery	145	27	22	84	7	12	29	17	10	9	12
Production machinery	315	28	35	188	14	13	97	29	16	19	14
Business oriented machinery	123	14	13	80	13	13	23	11	6	14	6
Electrical machinery	311	20	19	150	16	11	70	15	10	28	15
Information and communication electronics equipment	443	67	33	332	55	93	75	37	31	37	6
Transportation equipment	599	53	40	692	57	46	317	172	7	84	105
Miscellaneous manufacturing industries	607	33	24	441	38	56	146	94	23	83	16
Total	4,025	392	325	3,145	267	396	1,183	607	201	455	235

*Source:* Basic Survey of Overseas Business Activities (Ministry of Economy, Trade and Industry, Japan)

### 3. Impacts of Tariff Reduction on ASEAN TPP-members' Export

This section discusses the general effects of tariff reduction on export from ASEAN TPP-member countries, particularly Malaysia and Vietnam.

#### 3.1. Exports to Japan under TPP

We start with the discussion on whether Malaysia and Vietnam will increase exports to Japan under the TPP. In general, exporters are more likely to utilize RTA schemes when the preference margin is larger. Such tendency has been found in many countries and preference schemes (e.g., Bureau et al. 2007; Cadot et al. 2006; Francois et al. 2006; Manchin 2006; Hakobyan 2015; Hayakawa 2014; Hayakawa et al. 2014, Hayakawa and Laksanapanyakul 2017)<sup>2</sup>. Since the most

<sup>2</sup> Bureau et al. (2007) examine utilization of the Generalized System of Preferences (GSP) granted by the European Union and the U.S. to developing countries in the agri-goods sector, while Cadot et al. (2006) focus on the trade of the European Union and the U.S. with their preferential trading partners. Francois et al. (2006) and Manchin (2006) examine the preferential trade relations of the European Union and non-least-developed African, Caribbean, and

avored nation (MFN) rates are already low or zero in a large number of products (e.g., zero in approximately 40 percent of tariff lines), there is little incentive to export to Japan under TPP.

Furthermore, from the past experience of Japan's imports, we expect that the availability of other RTAs further reduces the incentive to utilize TPP scheme in exporting to Japan. Malaysia and Vietnam already have economic partnership agreements (EPAs) with Japan. These include the ASEAN-Japan Comprehensive Economic Partnership (AJCEP), Japan-Vietnam EPA (JVEPA) and Japan-Malaysia EPA (JMEPA). The AJCEP, JVEPA, and JMEPA entered into force in 2008, 2009, and 2006, respectively.<sup>3</sup> Unless TPP provides better conditions such as lower tariff rates or less restrictive rules of origin (RoOs) or firms prefer self-certification system (discussed later), firms in two countries will continue to utilize these existing RTAs when exporting to Japan.

Indeed, even among currently-existing RTAs, we can see inertia on the choice of RTA schemes in Japan's imports from these two countries. Table 4 reports those imports under each RTA scheme in Japanese fiscal year 2015.<sup>4</sup> In this table, products are restricted to those eligible to both bilateral EPA and AJCEP and those with the same preferential rates between two schemes, i.e., zero rates. Due to the latter restriction, bilateral EPA and AJCEP are indifferent in terms of market access although we do not take the difference in RoOs into account here. Nevertheless, we can see much larger imports under AJCEP in the case of Vietnam and under JMEPA in the case of Malaysia. One critical source of this difference between two countries will be the order of EPA's entry into force. AJCEP entered into force earlier than bilateral EPA in the case of Malaysia but did not in

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Pacific (ACP) countries under the Cotonou Agreement, while Hakobyan (2010) examines the U.S. GSP utilization by 143 GSP-eligible countries. Keck and Lendle (2012) analyze utilization of both unilateral and bilateral preferences by not only the European Union and the U.S. but also Australia and Canada. Hayakawa (2014) examine Japan's import from Thailand, in which not only bilateral EPA (i.e., Japan-Thailand EPA) but also plurilateral EPA (i.e., AJCEP) are available. RTA utilization in exports from ASEAN countries to Korea is investigated in Hayakawa et al. (2014). Hayakawa and Laksanapanyakul (2017) examine the impacts of sharing RoOs with other ASEAN+1 FTAs on ASEAN-Korea FTA/ASEAN-China FTA utilization in Thai exports in 2011. These studies consistently found that FTA utilization is higher in the products with the larger tariff margin and the less restrictive RoOs.

<sup>3</sup> One of the important reasons for the coexistence of both bilateral and multilateral EPAs with some ASEAN countries is that Japanese multinationals have developed international production/distribution networks in ASEAN since the 1990s (see, for example, Baldwin, 2006). Japanese affiliates in ASEAN get actively engaged in trading intermediate goods across ASEAN countries. Therefore, cumulation within ASEAN enables Japanese affiliates easily to comply with RoOs. As a result, the reduction of tariff rates based on AJCEP is more significant for products in which the international production networks are more developed. On the other hand, bilateral EPAs are designed to reduce tariff rates for products in which two countries have special interest. Those also include deeper economic rules such as those on intellectual property or labor standards.

<sup>4</sup> Some other tables are available in Hayakawa et al. (2017).

the case of Vietnam. Based on this observation, exporters are expected to keep utilizing the familiar EPA scheme rather than start the utilization of TPP.

**Table 4: Japan’s Imports under Each EPA in FY 2015**  
(Million Japanese Yen)

	Viet Nam	Malaysia
# of Products	1,034	610
Imports under AJCEP	390,151	44,186
Imports under Bilateral EPA	91,880	153,406

*Sources:* Ministry of Finance and Tariff Analysis Online

*Notes:* In this table, products are restricted only to those in which the level of AJCEP rates is same as that of bilateral EPA rates and both AJCEP rates and bilateral EPA rates are lower than MFN rates.

### 3.2. Exports to Other ASEAN TPP-members under TPP

Due to the same reason as the case of Japan, exports to other ASEAN TPP-member countries under TPP will not increase (unless TPP provides better conditions). In intra-ASEAN trade, six plurilateral RTA schemes are already available; ASEAN FTA, ASEAN-Australia-New Zealand FTA, ASEAN-China FTA, AJCEP, ASEAN-Korea FTA, and ASEAN-India FTA. Therefore, as in the above case of Japan, firms will utilize the more familiar scheme of preferences when trading with other ASEAN TPP-member countries. One additional exception is the case where inputs from other ASEAN countries play a significant role in cumulation when the non-Asian TPP-member countries (i.e., countries with which Malaysia and Vietnam have not concluded any RTAs) are final export destinations (except for Australia and New Zealand). We later discuss the role of cumulation in the impacts of TPP on ASEAN TPP-member countries.

### 3.3. Exports to Non-Asian TPP-members under TPP

In contrast to the above cases, we expect an increase in the exports of ASEAN TPP-member countries to other non-ASEAN TPP member countries, such as Canada, Mexico, and Peru. This



increase is because TPP is the first RTA with those countries for Malaysia and Vietnam. On the other hand, the withdrawal of the U.S. from the TPP will have a significant effect on the economic gains from TPP in terms of export opportunities for Malaysia and Vietnam. The U.S. provides generalized scheme of preference (GSP) to some developing countries. However, Malaysia and Vietnam are not the beneficiaries of GSP although some other ASEAN countries are the beneficiaries. Therefore, for Malaysia and Vietnam, TPP would have become the first preference scheme for exports to the U.S. Thus, the TPP would have had the potential to dramatically increase the exports of Malaysia and Vietnam to the U.S.

To further assess the impact of U.S. withdrawal from TPP, we focus on which industries would have increased their exports to the U.S. under TPP had the U.S. remained as a TPP member. To do that, it is helpful to consider the potential competitors' market access in each industry. Specifically, it is valuable to examine in which industries GSP/special preferential treatment for the least developing countries (LDC) beneficiaries have preference access. In particular, given the fact that tariff rates in the U.S. would have been removed in all products through TPP, exports under TPP will be likely to increase for products in which the GSP/LDC rates are not available and for which the MFN rates are high. Thus, when exporting such products, TPP-member countries will have better market access although the member countries of other RTAs involving the U.S. may also have a similar level of market access to the U.S.

Table 5 reports the number and share of products that are ineligible to GSP/LDC in addition to the simple average of MFN rates for such products in each industry in the year 2014. From this table, it can be seen that food products, textiles, and footwear meet the above conditions. Namely, in these industries, the GSP/LDC rates are not available, and the MFN rates are relatively high. Therefore, it might be expected that exports in those industries to the U.S. would have dramatically increased if the U.S. had not withdrawn from the TPP. Vietnam, in particular, would have been a major beneficiary - its exports of textiles and footwear industries currently accounts for 40 percent of total exports to the U.S., as shown in Table 1. Therefore, the loss of export opportunities in these industries due to the U.S. withdrawal from the TPP will be huge. This is in contrast with other industries such as plastics and rubber and precision metals industries which have relatively low shares of exports to the U.S.

**Table 5: GSP/LDC Ineligible Products and Their Average MFN Rates**

	Non-GSP Products			Non-LDC Products			All
	Number	Share	MFN (%)	Number	Share	MFN (%)	Number
Live animals	590	0.89	4.55	340	0.51	0.85	663
Vegetable products	318	0.57	5.18	170	0.30	3.47	562
Animal/vegetable fats and oils	50	0.71	3.02	18	0.26	0	70
Food products	499	0.65	14.05	296	0.38	16.00	772
Mineral products	185	0.91	0.17	152	0.75	0	204
Chemical products	1,128	0.66	0.98	934	0.54	0.01	1,715
Plastics and rubber	164	0.44	1.02	136	0.36	0.29	375
Leather products	113	0.51	4.88	83	0.38	5.55	220
Wood products	153	0.64	0.61	143	0.60	0.37	240
Paper products	275	1	0	275	1	0	275
Textiles	1,534	0.96	8.89	1,527	0.96	8.90	1,598
Footwear	169	0.87	11.94	169	0.87	11.94	195
Plastic or glass products	176	0.59	5.05	117	0.39	1.13	298
Precision metals	50	0.48	0.12	48	0.46	0	105
Base Metal	612	0.62	0.41	564	0.57	0.03	988
Machinery	890	0.66	0.44	818	0.61	0	1,350
Transport equipment	171	0.68	1.87	131	0.52	0	252
Precision machinery	348	0.68	0.59	286	0.56	0.21	512
Others	192	0.60	1.47	174	0.54	0.98	322
<b>Total</b>	<b>7,617</b>	<b>0.71</b>	<b>3.81</b>	<b>6,381</b>	<b>0.60</b>	<b>3.20</b>	<b>10,716</b>

*Source:* Tariff Analysis Online

*Note:* Only products with ad-valorem rates are included in the computation of average MFN rates.

For other industries, such as food products, the absolute effect of the TPP – with or without the U.S. participation - will be trivial. For example, taking a closer look at exports from Vietnam to the U.S., the major food products include shrimps and prawns (HS1605211020, HS1605211030) - the volume of exports in 2015 was approximately only 250 million U.S. dollars.<sup>5</sup> Furthermore, the MFN rates for these products are already zero. Also, the major food product in Malaysia for the U.S. market is cocoa butter (HS180400) – their exports to the U.S. in 2015 are only 100 million U.S. dollars. Again, the MFN rates for this product are zero. For other food products, the volumes of exports from Vietnam and Malaysia to the U.S. are trivial. Therefore, although in food products industry there is a relatively large number of products that meet the above conditions, the absolute effects of TPP on exports to the U.S. would have been small.

<sup>5</sup> The figures in this paragraph are drawn from the World Trade Atlas.

### 3.4. Other Key Elements in Export to TPP-members

There are some other elements that affect export under TPP. First, as mentioned above, cumulation may play a key role in increasing intra-TPP-member trade.<sup>6</sup> In particular, relatively strict RoOs are set for the textile and footwear industries in the TPP. For garments, for example, the yarn-forward RoOs require that materials for yarns should be obtained from TPP-member countries (except for materials in the short supply list). Furthermore, the spinning, weaving/knitting, and cutting/sewing processes must also be conducted in TPP-member countries. Therefore, one possible production pattern is that Vietnam imports yarn or its materials from Japan/Malaysia, produce garments, and export them to other TPP-member countries. In this case, exports from Malaysia to Vietnam (i.e., other ASEAN TPP-member countries) under TPP will be expected to increase.

Indeed, Japanese affiliates in ASEAN TPP-member countries have high expectations for the role of cumulation. Table 6 reports top-three expectations for TPP negotiations. This is the result of “2015 JETRO Survey on Business Conditions of Japanese Companies in Asia and Oceania” conducted by Japan External Trade Organization (JETRO). In the survey, questionnaires were sent to 5,545 Japanese affiliates in ASEAN countries excluding Brunei. The response rate was 49.9 percent. As shown in Table 5, Japanese affiliates in three TPP-member countries (i.e., Malaysia, Vietnam, and Singapore) list RoOs including cumulation rules as one of the top-three expectation for the TPP. Therefore, we cannot ignore the role of cumulation when considering the effects of TPP.

The second is the existence of Information Technology Agreement (ITA) and its expansion. Originally, the ITA was concluded by 29 countries in December 1996 in order to completely eliminate tariffs against all WTO members on information technology (IT) products covered by the Agreement (157 products). Now, its members are grown to 82 countries. Furthermore, the expanded version of ITA was concluded by 53 members, including the U.S., in December 2015. This version is aimed to eliminate tariffs in additional 201 products.

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<sup>6</sup> For example, Hayakawa (2014) empirically investigate the effect of diagonal cumulation on FTA utilization by exploring Thai exports to Japan under two kinds of FTA schemes. While the one scheme adopts bilateral cumulation, the other scheme does diagonal cumulation. Comparing trade under these two kinds of FTAs, he quantified the effect of diagonal cumulation without relying on not only the variation in cumulation rules across country pairs but also the variation across years. As a result, his estimates show around 4% trade creation effect of diagonal cumulation.

**Table 6: Expectations for TPP Negotiations (Top 3, Numbers, Multiple Answers)**

	Malaysia	Singapore	Viet Nam
Facilitation of trade and customs authorities	124	107	313
RoOs (Including Cumulation)	58	49	131
Market Access for Goods	41	61	164
All responses	300	228	557
Valid responses	206	189	476

*Source:* 2015 JETRO Survey on Business Conditions of Japanese Companies in Asia and Oceania

As the U.S. is a major importer of IT products, it might be worth examining whether its withdrawal from the TPP will reduce the benefits gained by the remaining TPP-member countries in this area. In the case of the U.S., tariff rates in 239 tariff-line products are scheduled to be eliminated by the ITA expansion. Of these, tariff elimination was completed in 147 products by 1 July 2016 (Group I). Focusing on products with ad-valorem MFN rates, we can see that the average and maximum of MFN rates in this group are 2.9 percent and 7.2 percent, respectively (Table 7). Furthermore, the tariff rates in the remaining 92 products will be gradually reduced and be zero by 1 July 2019 (Group II). In this group, the average and maximum rates are 3.0 percent and 8.5 percent, respectively. Namely, there still remains sufficient preference margin in these IT products in the case of the U.S.

**Table 7: Statistics for Base Rates (%)**

Group	N	Average	Minimum	Maximum
I	140	2.9	0.8	7.2
II	91	3.0	1	8.5

*Source:* <http://docsonline.wto.org/imrd/directdoc.asp?DDFDdocuments/q/WT/LET/182-01.pdf>

*Note:* Only products with ad-valorem rates are included in this computation.

As shown in Section 2, the main export products from many ASEAN countries including Malaysia to the U.S. are IT products. The tariff rates for such products in the U.S. will be eliminated under the above ITA expansion earlier than under TPP. Furthermore, unlike the case of RTA schemes including TPP, exporters can enjoy tariff reduction without proving the origin of their products, i.e., without paying any additional costs. Therefore, exporters of IT products from Malaysia to the U.S. enjoy ITA schemes rather than TPP scheme. Furthermore, since TPP non-members can also enjoy such tariff elimination in IT products (if they are WTO members), exports from TPP members will not increase much. Thus, the withdrawal of the US from the TPP is not likely to adversely affect Malaysia's exports of IT products to the US.

The third is the self-certification system. In the above, we argued that the availability of existing RTAs (e.g., six plurilateral RTAs) discourages firms from utilizing the TPP scheme. However, one unique feature of TPP for ASEAN countries is the adoption of a self-certification system. In ASEAN, the third-party certification system has been adopted. Although these countries may choose the third-party certification system, firms that prefer self-certification system may switch to TPP schemes even when trading with other ASEAN TPP-member countries in addition to Japan, i.e., even when other RTA schemes (with third-party certification system) are available.

Indeed, Japanese affiliates, particularly large-sized ones, are expected to prefer the self-certification system. In the case of Japan, the Australia-Japan EPA adopts a self-certification system. Also, the use of a self-certification system by approved exporters is allowed in the Japan-Switzerland EPA, Japan-Mexico EPA, and Japan-Peru EPA. For example, according to the website of Japan's Ministry of Economy, Trade and Industry, large-sized firms in Japan have been using this system.<sup>7</sup> Therefore, large-sized affiliates in ASEAN TPP-member countries may switch to the TPP scheme in order to benefit from a self-certification system. For such affiliates, FTA utilization costs become lower than before. Thus, such affiliates will increase their exports, regardless of industries.<sup>8</sup>

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<sup>7</sup> The examples include Ishizaki Press Industrial Co., Ltd, Itochu Corporation, Kansai Wire Netting Co., Ltd, Kyocera Corporation, Shimano Inc., DKSH Japan, Toyota Motor Corporation, Nakanishi Corporation, Fuji Heavy Industries Ltd., Honda Motor Co., Ltd., and Mazda Motor Corporation.

<sup>8</sup> For example, by estimating gravity equations for trade among 155 countries during the period of 1981 to 2001, Estevadeordal and Suominen (2008) found that trade creation effects of RTAs are significantly larger in those with self-certification system than in those with other systems.

#### **4. Impacts on Japanese Manufacturing Affiliates**

This section examines the effects of tariff reduction on Japanese manufacturing affiliates in ASEAN countries. It is based on the discussions on the general effects presented in the previous section. We examine first the case of the Japanese affiliates in ASEAN TPP-member countries, particularly Malaysia and Vietnam, and then the case of ASEAN countries that are not members of the TPP.

##### **4.1. Effects of TPP on Japanese Affiliates in ASEAN TPP-Member Countries**

In the previous section, we pointed out the positive effects of TPP in some industries in the form of dramatic increase in exports. However, the withdrawal of the U.S. from the TPP have nullified some of these effects. These industries include textile and footwear industries. It is obvious that Japanese affiliates in those industries would have increased their investment and expanded their production capacity. Also, although Table 3 shows that the number of Japanese affiliates in these industries is relatively small, Japanese firms would have made new investments in Malaysia or Vietnam.

Prior to the withdrawal of the US from the TPP, some Japanese firms had already started to change their business. Japanese trading firm, Itochu concluded an agreement for a strategic business alliance with the Vietnam's state-owned textile firm Viet Nam National Textile and Garment Group, which is known as VINATEX, acquiring its shares.<sup>9</sup> Also, it was reported that a Japanese textile maker, Kuraray, had planned to expand its manufacturing capacity in Vietnam.<sup>10</sup> With the departure of the U.S. from TPP, it is not certain whether more Japanese firms will start to prepare for the increase of exports in the afore-mentioned industries.<sup>11</sup>

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<sup>9</sup> <http://www.itochu.co.jp/en/business/textile/project/08/>

<sup>10</sup> <http://www.nikkei.com/article/DGXLZO96134280V10C16A1TI1000/>

<sup>11</sup> It is also noteworthy that such a change of business in ASEAN countries by multinational enterprises (MNEs) is not limited to Japanese MNEs, i.e., MNEs owned by TPP-member countries. In particular, firms in Asian TPP-non-member countries also start to reorganize their production networks. For example, those include Korean firms (e.g., Hyosung), Hong Kongese firms (e.g., Huafu), and Chinese firms (e.g., Texhong Textile Group). These textile firms recently invest in Vietnam.

However, despite such uncertainties, Japanese affiliates in other industries in ASEAN TPP-member countries will not change their business activities much because the extent of market access is not so different between TPP-member countries and non-TPP-member countries. As mentioned before, in the case of GSP-eligible products, both TPP-member countries and GSP beneficiaries have similar advantages in exporting to the U.S. This also implies that the absence of the U.S. in the TPP is likely to have no effects on these industries. Also, the extent of market access in IT products is not different due to the ITA expansion. Thus, the effects of TPP – with or without the U.S. - on Japanese affiliates in these industries will be small.

#### **4.2. Impacts of Tariff Reduction on Non-TPP Member Countries**

As the U.S. is no longer part of the TPP, the effects of TPP via tariff reduction on ASEAN countries that are non-TPP members will be less. As presented in Table 1, the textile industry in many ASEAN countries is a major exporter to the U.S. A TPP-11 without the U.S. implies that TPP's impacts on this industry in addition to its intermediate products will be smaller.

Also, ASEAN non-TPP member countries is likely to maintain some of their competitiveness in other industries. Due to the ITA expansion, there will be little difference in market access for IT products between TPP and non-TPP member countries. Furthermore, countries such as Indonesia, the Philippines, and Thailand are GSP beneficiaries while Cambodia is an LDC beneficiary. Therefore, even if the U.S. is a TPP member, the difference in access to the U.S. market is not significant between ASEAN TPP-members and non-members, particularly in plastics and rubber. Indeed, plastics and rubber is one of the main products in Thailand when exporting to the U.S.

Based on the above expectations, FDI from Japan to ASEAN non-TPP member countries may not decrease in the industries such as textiles, footwear, and materials/intermediate products. Under TPP-11, investment diversion from ASEAN non-TPP member countries to ASEAN TPP member countries may occur but to a lesser extent than under TPP-12. This includes industries in which Japanese multinationals would prefer self-certification system. Furthermore, in the case of high value-added products in those industries, investment diversion to Japan may still happen. On

the other hand, as mentioned just above, Japanese affiliates in other industries will not much change their business activities in the cases of GSP/LDC beneficiaries and WTO members.

At present, we do not have specific examples on the change by Japanese affiliates in ASEAN non-TPP member countries. Instead, we draw our conclusions from the results of the survey on business expansion plans for Japanese overseas affiliates in 2015. This was derived from the “FY2015 Survey on the International Operations of Japanese Firms – JETRO Overseas Business Survey” conducted by JETRO.<sup>12</sup> The results are reported in Table 8. It shows that the percentage change in the number of affiliates that plan to expand their businesses. While Vietnam and Malaysia, i.e., TPP-members, record a positive change, negative changes are significant for Indonesia and Thailand. Although these changes are not necessarily attributed only to TPP membership, we may say at least that the number of Japanese affiliates which plan to expand their businesses was growing slower in TPP-non-members. Finally, the impact of the U.S.’s withdrawal is also not known.

**Table 8: Percentage Change of the Number of Japanese Overseas Affiliates  
Planning Business Expansion**

	FY2015	FY2014		FY2015	FY2014
Asia			Non-Asia		
China	▲ 2.8	▲ 0.4	United States	2.4	5.9
Hong Kong	▲ 1.9	0.7	Western Europe	2.5	2.4
Korea	0.6	▲ 1.3	Mexico	0.8	2.5
Taiwan	0.6	1.0	Central-Eastern Europe	0.9	2.8
Cambodia	0.7	▲ 0.1	Brazil	▲ 1.8	▲ 1.1
Indonesia	▲ 2.6	▲ 0.6	Australia	1.8	▲ 0.5
Malaysia	0.7	▲ 0.6	Russia & CIS	▲ 2.1	▲ 0.3
Myanmar	1.4	▲ 0.8			
Philippines	0.5	▲ 0.1			
Singapore	▲ 3.2	1.0			
Thailand	▲ 2.3	▲ 3.0			
Vietnam	3.7	▲ 0.9			
India	4.0	▲ 3.1			

*Source:* FY2015 Survey on the International Operations of Japanese Firms – JETRO Overseas Business Survey

<sup>12</sup> For this survey, questionnaires are sent 9,893 firms in Japan. We obtain valid responses from 3,005 firms (30.4%).



## 5. Conclusion

In this paper, we discussed how tariff reductions through TPP may affect Japanese manufacturing affiliates in ASEAN countries. Our conclusion can be summarized as follows. First, in textile and footwear industries, the withdrawal of the U.S. from the TPP will mean that it is uncertain that Japanese affiliates in Malaysia and Vietnam will increase their investment and expand their production capacity. In these industries, had the U.S. remained in the TPP, member countries of the TPP would have had better market access to the U.S. than GSP beneficiaries with the benefit from utilizing TPP scheme (i.e., preference margin) being large. Thus, there is also less certainty that the Japanese affiliates in these industries may shrink their business in ASEAN TPP-non-member countries. Second, under TPP-11, Japanese affiliates in some industries will not change their business activities much because the extent of market access is not so different between TPP-members and non-members.

Finally, the Japanese government's efforts to support the internationalization of Japanese firms should be noted. In April 2016, it established a "Consortium for New Export Nation" (CNEN) with JETRO serving as its secretariat. This consortium aims to support mid-ranking companies and small- and medium-sized enterprises to develop their markets and expand their businesses through exporting or investing in TPP member countries. The consortium is supported by a large number of government-related organizations (e.g., JETRO), commerce and industry associations, finance institutions, and local governments. As of the end of June, approximately 800 firms applied to this consortium. Based on each firm's request, the consortium provides various kinds of support, including the advice on factory location selection or local management, the introduction of local suppliers, assistance for the application of the investment license or in obtaining the import qualification, interpretation and judgment of advice on a business trip, and so on. The CNEN could have a positive impact on investments by Japanese affiliates in TPP member countries.

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