

## TPP an impressive achievement

Today's announcement that the Trans-Pacific Partnership agreement (TPP) has been concluded is good news for Kiwi firms and households. It's not perfect, and the dairy sector in particular will naturally be frustrated. But TPP offers valuable benefits – and limited costs – across the economy.

Achieving full tariff elimination over time, aside from beef into Japan and some dairy products, on all of New Zealand's exports to some of the largest economies in the world, is a very positive outcome. That and the likely gains to New Zealand firms from lower costs of doing business in Asia-Pacific regional production networks and from enhanced investment flows, will positively contribute to lifting Kiwis' living standards.

On the wider stage this New Zealand-initiated process has delivered the first large scale improvement in the global trading environment for years. It shows that globalisation's support for improving world standards of living can continue. This is one more step in the long road to further integration in the Asia-Pacific region and puts pressure on others not involved to make similar adjustments.

### Considering the negotiating challenges facing New Zealand...

All policy analysis starts with a policy imperative. In relation to the TPP, the challenge can be summarised as: what can we do about the following developments?

- Asia-Pacific regional integration rules will change as a result of the TPP, the Regional Comprehensive Economic Partnership (RCEP) and potentially the Free Trade Area of the Asia Pacific (FTAAP).
- The growth potential of New Zealand's agricultural exports is reduced by being highly sensitive and thus highly protected by larger economies in the TPP (US, Japan, Canada, Mexico).
- It is "unthinkable"<sup>1</sup> that New Zealand should not be part of any such changes – this would be detrimental to Kiwis' living standards. We need to be 'insiders' on world trade and the TPP assists this effort.

And this is subject to the practical constraints that:

1. New Zealand is a small economy with low trade barriers. We offer limited additional market opportunities for TPP partners.
2. We are dealing with countries in which there are often multiple, conflicting vested interests and stakeholders with warped views on how economies operate, all of whom take considerable

convincing about how any negotiation can deliver a mutually acceptable outcome.

In short, New Zealand needed to ask some of the world's largest economies to give our exporters and investors additional opportunities in their most protected and sensitive sectors, with the promise of very little in return. So TPP – as with all trade negotiations for New Zealand – was very much a 'constrained optimisation' problem.

### ...the TPP agreement is an excellent outcome for us

Our negotiators have delivered a good deal, given the hand they have been playing. Their skill and the way they have clearly respected the fundamental interests of the community, while gaining real returns, is now evident.

The end result is that, outside of some dairy products and beef into Japan, all of New Zealand's goods' exports to all TPP countries will see tariffs completely removed over time.<sup>2</sup>

New Zealand's exports of fruit, vegetables, wine, seafood, forestry products, wool and manufactured goods, which account for around 65% of our \$20 billion of goods exports to TPP countries, will all enjoy tariff-free access to TPP markets over time.

<sup>1</sup> As Helen Clark correctly stated last week.

<sup>2</sup> MFAT. (2015). 'Overview of sector outcomes'. [http://www.tpp.mfat.govt.nz/assets/docs/TPP\\_Overview\\_of\\_Sector\\_Outcomes.pdf](http://www.tpp.mfat.govt.nz/assets/docs/TPP_Overview_of_Sector_Outcomes.pdf)

On **dairy**, there are modest gains. Tariffs will be eliminated over time in the US on infant formula, milk powders and some cheese, and where tariffs are not reduced, New Zealand exporters will have greater quota access. Clearly this is a disappointment relative to an ideal outcome for New Zealand, but an ideal outcome isn't a sensible comparator. The dairy sector is better off today than it was yesterday, and certainly better off compared to a scenario where New Zealand is excluded from the TPP.

On **meat**, sheepmeat will be tariff free when the agreement is implemented, apart from in Mexico where tariffs will be phased out over eight years. Beef exports to the US will face no tariffs or quotas after five years, and beef tariffs into all other TPP countries will be eliminated. And let's not forget that beef into Japan has not been excluded altogether from liberalisation. Japan has agreed to gradually reduce tariffs from 38% to 9% over 15 years.

Officials estimate the tariff reductions on our goods exports equate to tariff savings of some \$260 million per year once fully implemented.<sup>3</sup>

### It's about more than tariffs; it's about competitiveness

But it's important to remember that the real gains from the TPP are not short-run tariff savings for goods exporters – although these are clearly welcome.

Rather, a concluded TPP will help New Zealand firms remain competitive over the medium- to long-term. And the TPP is a helpful shot in the arm of a flagging global trade liberalisation patient. As Minister Groser has stated, "long after the details of this negotiation on things like tons of butter have been regarded as a footnote in history, the bigger picture of what we've achieved today will be what remains."

The Government estimates gains to the New Zealand economy of **\$2.3 billion per year by 2030**. Of course, such modelling estimates are subject to uncertainty, but even if they are a fraction of the expected amount, it's still a big number. And previous estimates of the gains from trade liberalisation have typically understated the benefits, as the 'dynamic gains' that come from new market-opening opportunities are usually not included.

Kiwi exporters' **competitiveness will be enhanced** relative to non-TPP competitors, and they will be on a more level playing field compared to those firms with

which they compete within the TPP. Improvements in areas such as customs, non-tariff barriers and food safety processes will reduce the cost of doing business and encourage greater participation in regional production networks. There is also an untested but potentially path-breaking new chapter on 'Regulatory Coherence' covering the role of Regulatory Impact Analysis, which can be important in minimising non-tariff barriers over time.

So TPP will remove some of the grit in the wheels of Asia-Pacific supply chains. This will **lower transaction costs** for Kiwi firms, again boosting competitiveness and opening new avenues.

There will likely be small **benefits for Kiwi services exporters**, although the detail is yet to be released.

For New Zealand investors seeking to invest in TPP countries, the investor state dispute settlement provisions to the investment chapter will provide protection from discriminatory, unfair or unjust government actions. New Zealand firms' assets will not be able to be expropriated without compensation. This all **reduces the risk premium associated with overseas investment from New Zealand**, helping New Zealand better integrate into the Asia-Pacific economy.

New Zealand will also become a **more attractive destination for foreign investment** from TPP economies, and from those countries with whom we have existing free trade agreements.<sup>4</sup> The threshold above which foreign investors must meet business experience and good character tests (i.e. bear additional costs to get approval to invest here) has risen from \$100 million to \$200 million.<sup>5</sup> Policy space around foreign investment in sensitive land has been retained.

### There will be costs but earlier concerns are largely unwarranted

As the negotiations have unfolded, most concern in New Zealand has centred on a few high-profile areas of the agreement. Although we are yet to see all of the details, from material released to date it appears these concerns have been over-stated:

- **Investor state dispute settlement** – tobacco claims have been carved out, meaning that a tobacco company could not, for example, lodge a plain packaging claim against the New Zealand Government. Policy space to legitimately and in good faith regulate in the interests of health and

<sup>3</sup> Note that it is doubtful that tariff savings will all accrue to Kiwi firms. Rather they are likely to be split between exporting firms and households in our key markets who can now buy imported goods at lower cost. But the outcome is the same: our exporters are more competitive and get better returns. Tariff savings are used in this article as a point of comparison with expected costs.

<sup>4</sup> This is because of the 'Most Favoured Nation' clauses of our FTA investment chapters with those countries, which ensure they are not treated less favourably than countries in trade agreement signed subsequently (i.e. TPP).

<sup>5</sup> Australia already has a higher threshold.

the environment seems to have been retained. It is hard to see how New Zealand's sovereignty will be materially affected.<sup>6</sup>

- **Costs of medicines** – the core of Pharmac's operating model has not been dismantled. Additional processes to encourage greater transparency in its purchasing will cost \$4.5 million upon implementation, and then \$2.2 million per year thereafter. This is small in the context of an \$800 million annual Pharmac budget.  
And relative to gains elsewhere, it is trivial. The \$2.2 million cost is less than half the expected tariff savings on New Zealand's exports of offal, for example.
- **Intellectual property** – copyright terms will be gradually extended from the current 50-year period to 70 years. This is expected to cost \$55 million in foregone savings once fully implemented after 20 years. This is about the same amount as the tariff savings on our cheese exports.<sup>7</sup>
- **Biologics** – it does not appear that data exclusivity for biologics in New Zealand will be extended past the current five-year term, though the details here are not yet clear.
- **Parallel importing** – there will be no change to New Zealand's laws in this area.
- **Imposition on Internet Service Providers to manage copyright** – there will be no requirement for ISPs to terminate accounts for copyright infringements. New Zealand is left to manage its own regime – subject, of course to lobbying by the usual suspects.
- **Decreased tariff revenue** – given New Zealand's already-low level of applied tariffs, MFAT expects a reduction in tariff revenue of around \$20 million per year. But New Zealand does not look to tariffs as a serious source of government income.

## And on the world stage this shows that trade negotiations are not dead

On a pragmatic note, the WTO has been working on a major output since tentative beginnings in 1998 were turned into the Doha round in 2001. And despite the significant and useful advances made in 2013's Bali package, the underlying WTO mechanism has been

unable to do one of its central jobs – delivering a large scale improvement in the world trading environment.<sup>8</sup>

So New Zealand started looking at alternatives and with three other like-minded countries (Singapore, Chile and Brunei-Darussalam – the P4) commenced the journey that closed in Atlanta last night. The demonstration effect of this achievement cannot be overstated. An enormously complicated deal was pulled and pushed into being. It shows what can be done if the political will is strong enough.

## In sum: TPP is an important step in the right direction for regional integration

In the coming weeks and months, we will get a better idea of the details of the TPP agreement for New Zealand firms and households. No doubt there may be some devil in these details, but based on what we have seen to date, we suggest that TPP will be highly net beneficial for New Zealand.

While there may be more trials and tribulations to come as TPP is subjected to 'legal scrubbing' and goes through the US Congress, today is a good day for the New Zealand economy, and our negotiators deserve a celebratory drink and a decent sleep.

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<sup>6</sup> Also see NZIER. (2015). 'ISDS and sovereignty: The use of investor-state dispute settlement mechanisms in trade agreements and their impact on national sovereignty'. Report to ExportNZ, 17 September 2015.

[http://nzier.org.nz/static/media/filer\\_public/bc/21/bc21a5b2-3a6b-4ba2-8cf7-2f90fd5c6909/isds\\_and\\_sovereignty.pdf](http://nzier.org.nz/static/media/filer_public/bc/21/bc21a5b2-3a6b-4ba2-8cf7-2f90fd5c6909/isds_and_sovereignty.pdf)

<sup>7</sup> This doesn't mean that US corporate demands around intellectual property more broadly will go away now that TPP is signed. We can expect pressure to continue to be applied through other channels, such as direct lobbying of Ministers.

<sup>8</sup> Although it has continued to be important for resolving trade disputes.