

BASC News

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BASC Interview

Procter & Gamble's Scott Miller Comments on APEC's Corporate Cordiality and Future Prospects

Scott Miller is Director, National Government Relations for The Procter & Gamble Company (P&G). He has over twenty years' experience at Procter & Gamble in a range of manufacturing, marketing, and government relations assignments. Based in Washington, D.C., Miller is responsible for the full range of international trade, investment, and business facilitation issues for the company. He currently serves as the chairman of the U.S. Alliance for Trade Expansion (USTrade). USTrade's 250-plus members seek to promote economic growth, job expansion, and higher standards of living in the United States and abroad through rules-based trade. Miller also chairs the National Foreign Trade Council's Globalization Working Group and the U.S. Council for International Business' Investment Committee.



BASC: Has Procter & Gamble found APEC to be a useful avenue for promoting its interests in the Asia-Pacific?

Miller: P&G considers APEC to be a highly constructive forum to promote economic integration and liberalization. The twenty-one APEC member economies represent greater than 70 percent of our current sales volume, and include some of the world's fastest-growing economies. As important, APEC members have made a top-level political commitment to trade liberalization and are prepared to do so on a voluntary basis. This reinforces a virtuous cycle of economic growth. Further, APEC is unique in integrating the private sector into its decisionmaking process, which helps set a

practical, results-oriented agenda.

BASC: How could APEC foster an environment in the Asia-Pacific conducive to corporate development? Where does APEC stand now, and what obstacles remain?

Miller: In my opinion, APEC is at a crossroads. The APEC process delivered strong results in its early years. Its formation helped push forward the completion of the Uruguay round. The 1996 ITA was a direct result of agreements reached in APEC. Issues such as business facilitation were a substantial help to economic growth. Unfortunately, coincident with the 1997 financial crisis, APEC lost momentum. The EVSL (Early Voluntary Sectoral Liberalization) initiative unraveled, members fell behind on action plan commitments, etc. The Seattle WTO Ministerial dealt a further blow to APEC's credibility, as key members reneged on commitments to begin a new round, made

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Director's Notes

WELCOME TO *BASC News*. In this issue we take a break from broad questions of the institutions of trade liberalization in the Asia-Pacific, highlighting more particular matters such as piracy, corporate governance, and the “digital divide,” which together are helping to shape the political and economic climate of relations along the Pacific Rim.

In the BASC Interview, Scott Miller of Procter & Gamble—which has a significant presence in the Asia-Pacific—articulates his company’s interest in trade liberalization through APEC and the WTO. Miller emphasizes how matters not specifically related to trade, such as intellectual property rights and labor and environmental protection, may take on new salience as economic ties among countries in the Pacific Rim and beyond continue to deepen.

We have inaugurated a new feature in the newsletter, the BASC Spotlight, which will focus on political-economic dynamics within a particular APEC member country. In this issue the spotlight falls on Singapore.

Edward Eddy of the business law firm Sidley Austin Brown & Wood delves into the new corporate governance law in Singapore, which aims to promote convergence between Singaporean business practices and international business norms.

In the APEC Update, BASC staffer Justin Kolbeck takes a closer look at APEC’s recent initiatives to bridge the “digital divide” among the more and less advanced member economies. Kolbeck provides an optimistic account of APEC’s attempts to ameliorate the strains and amplify the opportunities inherent in the new economy.

In the BASC Analysis, Vinod Aggarwal and John Ravenhill warn against the siren song of open sectoralism as a mode of trade liberalization. They examine the history, the policy, and the economics of sectoralism, and conclude it to be a poor substitute for multisector and multilateral liberalization.

Finally, the BASC Book Review sizes up a new volume of globalization, trade, and product in Southeast Asia, edited by Leonard Chang and Henryk Kierzkowski.

—**Vinod K. Aggarwal**

BASC Projects

Within the past few months BASC has begun to focus on new projects while bringing the “Asia Beckons” project to a successful conclusion. The new projects will broaden the center’s research agenda. For the first time BASC will bring Latin America and Europe into its broader research agenda, while taking a closer look at the bilateralism currently in fashion among APEC members.

The “Asia Beckons” project, supported by a generous grant from the Japan Foundation Center for Global Partnership, has now come to a close. International scholars and consultants assessed the strategies used by European, Japanese, and U.S. firms in targeting Asia. A March 2001 conference at Berkeley brought together the three threads of the project, and was followed by the publication of the European volume in August 2001 (see p. 8); the Japanese and American volumes will follow in 2002.

BASC has started a new project that will analyze Latin American countries’ trade relations with one another. Changes in the language of regional affairs, which increasingly differentiates between a North America that includes Mexico and a South America dominated by Brazil, indicate the profound impact Mexico’s NAFTA membership may have on inter-American relations. A seminar in

Washington D.C. in fall 2001, supported by Berkeley’s Center for Latin American Studies, the Clausen Center at the Haas School of Business, and the Woodrow Wilson Center, convened experts from across the Americas to discuss these developments and offer perspectives on the nature and implications of the changing constellation of interests and relations in the Americas.

With the support of the Institute of European Studies at U.C. Berkeley, BASC is also considering the viability of “trans-regionalism” as an emerging level of international trade relations. In particular, it will study the effect on EU trade strategies of the growing importance of new economy firms and the halt in progress in global trade negotiations. BASC convened a preliminary conference in September 2001 to explore whether incipient EU transregionalism will make a lasting impression on the changing face of international trade.

BASC is also exploring recent developments in East Asian bilateralism. East Asian countries have begun negotiating bilateral free trade agreements within and beyond the region to secure access to export markets as a response to failures in APEC and the WTO. BASC is engaging in preliminary work on a project that would focus on whether bilateral deals are inherently more viable avenues for trade liberalization.

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Corporate Governance in Singapore: Death Knell for Crony Capitalism in Asia?

By Edward D. Eddy, III

This is the first article of a series of BASC Spotlights on different APEC member economies. The intent is to illuminate a range of political and economic trends in the Asia-Pacific by focusing on representative developments in individual member countries. In this article, Edward Eddy highlights a recent law passed in Singapore aimed at invigorating the corporate sphere. Singapore's recent actions reflect a growing trend in APEC to encourage transparency and effective business practices, goals that have been high on the agenda at all of APEC's recent meetings.

On March 21, 2001, a multidisciplinary committee released a report on corporate governance practices in Singapore, together with a proposed Code of Corporate Governance.¹ The Corporate Governance Committee was established at the behest of several Singapore government agencies, including the Ministry of Finance, the Monetary Authority of Singapore (Singapore's central bank), and the Attorney-General's Chambers. The report was initially released for public comment in November 2000, and the resulting Code of Corporate Governance has now been adopted by the Singapore Exchange for inclusion in its Listing Manual. The Code will apply to annual reports of listed companies prepared for annual general meetings of shareholders held on or after January 1, 2003 (and listed companies are encouraged to comply prior to that time, if possible).

In the report of the Corporate Governance Committee issued with the code, the code is described as taking a "balanced approach" between prescription (specifying corporate governance standards which companies must then adopt) and voluntarism (allowing companies to determine their own corporate governance practices, subject to disclosure of the practices that are adopted). Comparing the new code to U.S. practices, the report categorizes the approach of the U.S. Securities and Exchange Commission as nonprescriptive, since SEC rules require extensive disclosure about corporate governance issues but do not specify corporate governance practices. The national securities exchanges in the United States (as well as other self-regulatory bodies) do, however, specify some corporate governance practices to which issuers of listed securities are also subject.

The balanced approach of the Code is a combination of these two, with a somewhat more extensive prescription of recommended practices. Under the Code, adoption of the recommended practices is not required, but deviations from them must be disclosed to the investor community, with specific reference to the Code's guidelines and explanations for deviations from it.

Independence, transparency, and accountability of corporate directors and management are the guiding principles of the Code. Among its prescriptions are:

- Formal training of directors;
- A "strong and independent element" on the board of directors, with independent directors making up at least one-third of the board;
- A separate chairman and chief executive officer, with disclosure of any relationship between the two individuals holding those positions;
- A nominating committee to make recommendations to the board of directors on all appointments, based on a formal and transparent appointment process and with all directors submitting themselves for renomination and reelection at least once every three years;
- A formal assessment of the effectiveness of the board of directors, based on established performance criteria;
- Separate and independent access by directors to the company's senior management and, if necessary, to independent professional advisors;
- A remuneration committee comprising a majority of independent directors to make recommendations to the board of directors on compensation packages for directors and key executives, a significant component of which should be performance-related;

- Disclosure of compensation packages for directors and at least the top five key executives (as well as, on an anonymous basis, compensation paid to a family member of a director or the chief executive officer);
- A report to shareholders on a quarterly basis of the company's performance, position, and prospects;
- An audit committee of at least three directors, the majority of whom are independent and whose names are disclosed, together with past attendance records at committee meetings; and
- Avoidance of selective disclosure to a subgroup of the investor community.

The "balanced approach" of the new Corporate Governance Code of the Singapore Exchange—with its more extensive guidelines on recommended corporate governance practices—is intended to move the Singapore securities markets further in the direction of a market self-disciplined by active investor involvement and awareness. Hopefully, as the report of the Corporate Governance Committee itself indicates, the Code will evolve as investors take up the challenge offered by the committee and act on the broader range and depth of information that the code is designed to make available to them. In any event, formal steps to encourage independence, transparency, and accountability of corporate directors and management are most welcome developments in the Asian capital markets.

1. The report is available on the website of the Singapore Exchange (www.sgx.com).

Edward Eddy is Managing Partner, Singapore Office, of Sidley Austin Brown & Wood.

Scott Miller interview

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just weeks before in Auckland. Now, the question is, what is APEC to become? What are the practical limits of voluntary liberalization? And what are governments willing to deliver?

BASC: In your opinion, has APEC made meaningful progress toward its 1994 Bogor goals of trade liberalization in the Asia-Pacific? Furthermore, has your firm witnessed substantial benefits resulting from actions taken in pursuit of these goals?

Miller: The jury is out on whether the Bogor goals represent commitment or aspiration. It has been widely reported that there is a major gap between the commitments made in the Individual Action Plans (IAPs) and actual implementation in areas like customs procedures (which are typically noncontroversial). Our degree of engagement in APEC

opinion, can APEC realistically address given institutional constraints such as its consensus-based nature? Also, how do you envision the future of APEC?

Miller: I think the best future role for APEC is in the areas of “business facilitation” and “capacity building.” My opinion is that real tariff liberalization will be limited in APEC; the WTO is a better forum, anyway. Having said this, there is tremendous potential for economies to make welfare gains in the panoply of facilitation and capacity issues. These matters get to the heart of what it takes to establish, operate, and develop a business; transparency, harmonization, and stability ultimately benefit producers, consumers, and governments.

BASC: Does the Bush administration's focus on FTAA concern you with respect to

tions? If so, how?

Miller: First, it's important to recognize that concerns about labor and the environment have long had a place in trade negotiations. Worker rights provisions were first linked to trade legislation in the McKinley Tariff Act of 1890 (which prohibited imports manufactured with prison labor). Environmental provisions go back to the Migratory Bird Treaty Act of 1918. More recently, each major trade act passed in the 106th Congress included at least one provision on labor and/or environmental issues. That said, it is possible to move forward if we agree on three points. First, one size does not fit all. We need to give negotiators the flexibility to negotiate. We can get a lot done in preferential programs like GSP and AGOA, but other fora (like the WTO, which operates by consensus and has one hundred member economies opposed to the inclusion of labor provisions) will need a political reality-check. Second, trade and investment are part of the solution. Trade raises living standards, which leads to better working conditions and environmental protections. And many actions that liberalize trade (e.g., eliminating farm or fishery subsidies) are unambiguously good for the environment. Third, we must improve policy coherence in trade, finance, and foreign policy to have a shot at real improvement.

BASC: How should the concerns of developing countries be addressed?

Miller: The WTO's current work plan is quite focused on the concerns of developing nations. I think this is proper, and I credit Director-General Mike Moore for his efforts. The rich world really needs to own up to its pockets of protectionism; I think the barriers for U.S. textiles and European and Japanese agriculture, to name the most glaring, are morally and economically indefensible. That said, I believe there is potential for a grand bargain which trades developed country market access for LDC transparency/compliance with existing obligations. This will take a tremendous measure of political courage to achieve.

BASC: Do you think the president will be given fast track authority this year, and if so, what might be the conditions?

Miller: I think the president will get Trade Promotion Authority for two reasons. First, presidents almost always get what they re-

“I fully support the opportunistic approach, that is, deal with those who are ready to deal.”

will be affected by whether policy commitments will actually translate to concrete improvements. There are bright spots, like the Shanghai port project, but as said, government action will ultimately decide whether APEC is more than a series of meetings.

BASC: In your experience, has APEC taken any action to alleviate Procter & Gamble's or other similar firms' concern over intellectual property protection? Moreover, what is the company doing in response to the higher incidence of branded product counterfeiting in Asia?

Miller: APEC economies demonstrate a wide range of IP protection: Japan is great; Russia is so-so; China is awful; check the recent USTR Special 301 filing for details. Counterfeiting is a major problem for P&G particularly in China. In China, P&G led the formation of the Quality Brand Protection Group, which now has over sixty-five member companies, to work with the PRC government to combat counterfeiting. APEC's work in IP issues is in its early days. Australia and Japan have taken a leading role with an IP enforcement group, which should help improve enforcement of existing IP laws. Private sector participation has been limited so far, but we are encouraged by the work to date.

BASC: What corporate concerns, in your

broader scale liberalization efforts?

Miller: I regard the President's focus on FTAA to be sound on political and economic grounds. Importantly, I do not believe the Bush Administration will pursue an FTAA to the exclusion of the multilateral agenda; frankly, if you look at sectors like agriculture, WTO and FTAA negotiations really need to proceed in parallel. Tactically, I fully support the opportunistic approach articulated by USTR Zoellick, that is, “deal with those who are ready to deal.”

BASC: How do you see the relationship between trade liberalization in APEC and trade liberalization in the WTO? Are there points of conflict? Synergies?

Miller: Despite my practical reservations about the future of trade liberalization in APEC, it seems to me that actions in APEC are ultimately synergistic with the multilateral process. For example, the APEC Chemicals Dialogue fits hand in glove with future market access initiatives the chemicals industry is advocating through the WTO. The same is true for the FTAA; APEC includes five economies (the United States, Canada, Mexico, Chile, and Peru) which would be part of an FTAA. Ultimately, my instinct is to push for liberalization wherever it can be achieved.

BASC: Should environmental and labor concerns be incorporated into trade negotia-

APEC: On-Ramp for the Information Superhighway?

By Justin L. Kolbeck

The “new economy” is all around us, yet no one can really say just what it is. Most agree that the new economy differs from the old by way of its focus on e-commerce and information technology rather than “old economy” sectors such as manufacturing and heavy industry. Whatever the end result of the struggle over defining this new economy, there is no question that e-commerce brings both new opportunities and new challenges for economies competing in the digital era.

APEC has sought to position itself as arbiter of the new economy in the Asia-Pacific. APEC leaders have realized that the digital divide threatens to leave developing nations in the Asia-Pacific behind unless they are given the opportunity to participate in the new economy. APEC Economic Leaders at the November 2000 meeting proposed measures to bridge this digital divide. Accordingly, these leaders made an optimistic Bogor-esque pledge to bring Internet access to all members of APEC by 2010.

Leaders at the November 2000 meeting also crafted a roadmap for implementing an Action Agenda for the New Economy. The agenda seeks to capitalize on new economy opportunities for APEC member economies via novel programs such as electronic individual action plans (annual reports issued by member economies cataloguing their progress toward the Bogor aspirations), which are aimed at increasing transparency of members’ progress toward Bogor goals. The agenda also seeks to help firms operating under the APEC umbrella compete in the new economy by strengthening existing markets and institutions, encouraging investment, and technology development, and employing technology to build both human capacity and entrepreneurial ability.

APEC has also attacked the digital divide via its Telecommunications Working Group (TEL). At a meeting in May 2000, ministers issued the Cancun Declaration, which deals primarily with bridging the digital divide. TEL ministers agreed that the best approach to overcoming the digital divide is to bring Internet access to rural areas as well as to encourage life-long learning in order to help people keep up with today’s dynamic information technology.

Mitsuru Taniuchi, chair of the APEC Economic Committee, has expressed similar sentiments regarding APEC’s best approach to opportunities generated by the new economy. First, he sees a chance for small firms and even individuals to gain advantage over larger and more cumbersome firms by way of focusing on entrepreneurship and harnessing the creative power of the information economy. Furthermore, he points out that over the last decade, small firms have created the greatest number of new jobs, whereas large firms have reduced the amount of jobs due to inefficiency. Taniuchi also asserts that sustained competitiveness in the new economy requires lifelong education. Australia’s educational loan program, in which participating students do not have to repay loans until their income exceeds a certain level, is a good example of a viable scheme that encourages the development of a skilled workforce that can thrive in the technology-based new economy.

There is no doubt that APEC has a broad plan to help its members embrace the new economy. The question is, does APEC have the institutional capacity to ensure members carry out the goals proposed earlier this year in Brunei?

Successful implementation of past APEC initiatives invites a measure of optimism. First, the creation of e-action plans

has facilitated the process by which the APEC secretariat may monitor individual states’ progress toward Bogor goals. It also allows APEC members to engage in a process of peer review by monitoring the progress of other member states. In a regime in which norms of self-regulation dominate, a strong system of peer-review can be an effective means of obtaining compliance from member states that already have similar intrinsic interests.

Furthermore, APEC has made progress toward the free trade goals promoted in the 1994 Bogor Declaration. Lockwood Smith, chair of the APEC Ministerial Meeting, said of an independent review carried out by the Pacific Economic Cooperation Council (PECC), that members are making strides toward Bogor goals particularly in the areas of reducing tariff and investment barriers, conformance to standards, and intellectual property rights.

While APEC has no formal enforcement mechanism, the same self-interested logic that has propelled members to make progress toward their Bogor goals may also translate to new economy goals. One important question that remains, however, is whether universal Internet access and full participation in the new economy are realistic expectations for some of APEC’s poorest states. Should the Internet be a priority for economies so impoverished that furnishing the most basic infrastructure is still a challenge?

Although new economy pundits argue that the rising tide of the information economy lifts all boats, APEC must be wary of neglecting the most basic needs of some of its members. Balancing new economy aspirations and old economy realities must, therefore, find a place in APEC’s new economy agenda. ●

Miller interview (continued from page 4)

ally want on foreign policy matters, and it looks to me that the president really wants it. Second, I think Congress realizes that

without TPA it actually has *less* influence over trade policy. All past grants of TPA required consultation; the 1988 Act allowed the Ways and Means or Finance committee to end ongoing negotiations if they didn’t like what the USTR was doing.

As far as conditions go, I think the authority will be fairly broad, which neither prescribes nor proscribes what a final deal must contain. Call me a cockeyed optimist, but I think it can be done. ●

Sectoral Snake Oil: The Case Against Open Sectoralism

By Vinod K. Aggarwal and John Ravenhill

Threats to world trade come in many guises. Protectionism is a usual suspect, and in recent years the coalition of activist groups that decries globalization has become a fixture in trade negotiations. Now the idea of negotiating open markets on a sectoral basis is gaining ground. While this open sectoralism may seem a benign development, it is in fact a wolf in sheep's clothing that damages the prospects for global trade liberalization and on multilateral trade negotiations.

While many commentators have seen open sectoral trade agreements as a boon to trade liberalism, we argue that an important shift in U.S. trade policy toward sectoralism has been a step backward in expanding world trade. U.S. "successes" in sectoral negotiations over the last four years—which have led to the liberalization of trade in telecommunications, information technology, and financial services—have been achieved ultimately at the expense of the multilateral trading system.

Open sectoralism is politically and economically hazardous. From a political perspective, market opening along sectoral lines has *reduced* political support for multilateral, multisector negotiations that would benefit a significantly broader group of industries and consumers in the United States and elsewhere. By giving a few economically successful sectors the trade liberalization that they demand, the administration has undermined the broad coalition for free trade. From an economic perspective, such agreements may also *reduce* economic efficiency. Put simply, by liberalizing only specific, highly competitive sectors, open sectoral trade agreements may lead to a perverse incentive to invest in or discourage exit from the least efficient areas of the economy.

The Advent of Sectoralism in Trade

While it has achieved prominence in U.S. trade strategy in recent years, sectoralism has a much longer history, first emerging in the early days of the GATT in the 1950s. In their earlier incarnation, sectoral trade agreements responded to domestic protectionist pressures by closing markets. The creation of so-called voluntary export restraints (VERs) was supposed to be a temporary measure to evade the strictures of Article 19 of the GATT that prevent importing countries from taking discriminatory action against trading partners. These arrangements typically started out as bilateral, government-to-government, sector-specific measures in mature, low-value-added, and labor-intensive industries such as textiles, apparel, and footwear.

More recent sectoral efforts have shifted away from these classic protectionist arrangements toward the current trend in promoting sector-by-sector liberalization. This recent trend began with the "zero-for-zero" tariff negotiations in the Uruguay Round in which agreement was reached on dismantling tariff barriers in several sectors. Subsequently, pushed by American firms, the U.S. government negotiated sectoral agreements in telecommunications, information technology, and financial services. The first such major

effort, the Information Technology Agreement (ITA), was negotiated in 1996. A successor to the highly contentious semiconductor trade arrangement between the United States and Japan, the ITA eliminates all tariffs on semiconductors, computers, computer equipment, integrated circuits, telecommunications equipment, and related manufactured goods. Covering over 90 percent of the total trade in IT products, the ITA took effect in April 1997 and forms the foundation upon which WTO members are currently considering further liberalization of the IT sector.

The ITA has since been championed as a model for other sectors. For example, a second sectoral arrangement, the Global Agreement on Basic Telecommunications, was negotiated in 1997. In effect since 1998, it covers over 95 percent of trade in telecoms. Following closely on its heels, the December 1997 Financial Services Agreement (FSA) to liberalize trade in banking, insurance, and securities took effect in April 1999, and covers over 95 percent of trade in these services.

Thus the trend in U.S. trade policy is to focus on expanding existing agreements such as the ITA, rather than negotiating a broader-based set of objectives. While well-meaning, this view ignores the politics and economics of sectoralism.

The Politics of Sectoral Protection

In the past, sectoral agreements raised trade barriers. Many analysts claimed that efforts to restrict trade on a sectoral basis would take the world down the same path as the elaborate protectionist arrangements in textiles developed in the 1950s. While protection in textiles and apparel in the early 1960s did eventually expand to the wool and man-made fiber textile and apparel industry in the early 1970s, the dire predictions of doomsayers did not come true. Indeed, many protectionist sectoral arrangements have been dismantled. For example, the United States negotiated a VER for color televisions with Japan in 1977 that expired in three years, and with South Korea and Taiwan in 1980 that expired after two years. In footwear, VERs with Taiwan and South Korea in 1977 were allowed to lapse in 1981. And in autos, the 1981 agreement to restrict Japanese cars was essentially inoperative by the late 1980s, as U.S. administrations raised the quota continually until it was finally removed in 1994. Even quotas in the most prominent example of sectoral market closing—textiles and apparel—are slated to be phased out by 2005.

These examples do not imply that sectoral protection has no costs or should be encouraged. Rather, the point is that by providing the politically sensitive textile and apparel industry with protection in the 1960s, the United States was able to press forward with the Kennedy Round, the most significant multisectoral market-opening effort of the time. From a politically realistic perspective, moderate protection for textiles was a price that had to be paid for the greater good of comprehensive liberalization. Without it, the powerful textile and apparel coalition might have blocked

any overall liberalization efforts—just as they managed to kill off the American effort to institutionalize the GATT into the Organization for Trade Cooperation in the 1950s.

The Politics of Open Sectoral Agreements

Open sectoralism, like APEC's open regionalism,¹ looks particularly attractive on first glance. The ITA, the Global Agreement on Basic Telecommunications, and the FSA have all gone beyond the removal of tariffs to eliminate nontariff barriers. According to conventional wisdom, these are examples of forward movement in trade opening that should be encouraged and expanded.

From a political standpoint, however, open sectoralism looks less benign. Those sectoral interests that were the most ardent proponents of liberalization in the Uruguay Round—information technology, financial services, telecommunications—now have their own sector-specific arrangements. Whereas the pro-liberalization efforts of these groups in the Uruguay Round facilitated important tradeoffs among various sectors, helping to broaden participation and cover a wide range of issues, their principal interest has now shifted to expanding their own sectoral arrangements rather than supporting the wider trade liberalization agenda. Thus, ironically, market opening along open sectoral lines has *reduced* political support for multilateral, multisector negotiations that would benefit a significantly broader group of industries and consumers in the United States and elsewhere.

The pursuit of open sectoralism in APEC illustrates some of the problems with this approach to trade liberalization. Following the successful conclusion of the ITA, the United States pressed for further negotiations within APEC for accelerated liberalization on a sectoral basis to revive APEC's stalled trade agenda. APEC member economies subsequently proposed various sectors for liberalization, with each member predictably focusing on areas in which its domestic producers enjoyed a competitive advantage. At their meeting in Vancouver in 1997, APEC leaders, in an effort to construct a package deal from which all economies would benefit, selected out of hundreds of possible sectors only fifteen for early liberalization. Embarrassingly, the package fell apart. The ostensible reason was the refusal of the Japanese government to agree to liberalization in the politically sensitive forestry and fisheries, though other governments were undoubtedly happy to hide behind the Japanese veto. In an effort to save face, APEC referred the program to the WTO, where it has since effectively been buried.

APEC's experience with sectoral liberalization demonstrates the political difficulties of constructing a package that will satisfy all participating governments when negotiations are conducted in only a limited number of sectors. In such circumstances, affected domestic protectionist interests mobilize and their political influence cannot easily be offset by groups with a strong interest in the liberalization of other sectors. And if such protectionist forces triumphed in sectoral negotiations in the APEC context—where the commitments of governments are “voluntary” and “indicative”—they are likely to be even more forceful in WTO negotiations that culminate in legally binding commitments.

The Economics of Open Sectoralism

Open sectoralism is also problematic from an economic perspective. Governments have negotiated such agreements in the past in products where tariffs were already low. This follows an obvious

political rationale: producers that enjoy high levels of protection are usually uncompetitive and dependent on the tariffs for their survival. Governments rarely have the political will to confront these producers, particularly in the absence of a package that will bring assured benefits to other sectors of the economy. Accordingly, sectoral trade agreements typically have exempted products that governments regard as sensitive. In the electronics field, for example, the United States has refused to include consumer electronics within the ITA.

In their zeal to promote any type of trade liberalization, many economists have forgotten a basic macroeconomic lesson. Put simply, when tariff cuts or the removal of other trade or nontariff barriers are concentrated in areas that have few impediments in the first place, but protection is maintained elsewhere, the result is to increase distortions in the domestic economy. Resources will move to or be maintained in the protected (and inefficient) segments resulting in a loss in allocative efficiency. For instance, econometric studies indicate that APEC's sectoral liberalization proposals would have caused economic losses in several APEC economies by exacerbating the misallocation of resources. Liberalization proposals in a number of sectors concentrated on products that were inputs for downstream users, which would continue to enjoy high levels of protection. In China, for instance, a reduction in protection for the chemical industry, leading to lower priced inputs for heavily protected downstream users, would have encouraged an expansion of production in the textiles, clothing, and toys sectors.² Similarly, in the foodstuffs sector, a loss in allocative efficiency was projected for several APEC economies, including Malaysia, Japan, and New Zealand, as resources were shifted from partially liberalized products into more protected food sectors.

The Path Ahead

The conventional wisdom that any liberalization is good and that all restrictions are bad is wrong. Liberalization of some sectors and not others undermines broader, more inclusive efforts, while temporary protection of some sectors can be worthwhile if it allows broad scale liberalization elsewhere. However well-meaning the proponents of sectoral approaches to liberalization may be, we should not be lulled into a false sense of security that open sectoral agreements will clear the path to free trade in the new millennium. If we wish to promote widespread trade liberalization and efficient resource allocation, we must return to multisector, multiproduct negotiations, and to the tradeoffs that such discussions entail. This is the task facing governments in reviving the Millennium Round in Doha. This agenda, rather than an open sectoral approach, should be the top priority of negotiators. ●

Vinod Aggarwal is Professor of Political Science and Director of BASC at the University of California, Berkeley. John Ravenhill is Professor of International Relations at the University of Edinburgh. This article has been adapted from "Undermining the WTO: The Case Against 'Open Sectoralism.'" Analysis from the East-West Center, No. 50, February 2001.

¹“Open regionalism” calls for the provision of market access to outsiders on the same terms as APEC members.

² Dee, P., A. Hardin, and M. Schuele. 1998. *APEC Early Voluntary Sectoral Liberalisation*. Canberra: AusInfo.

Productive Fragmentation in Southeast Asia

Leonard Cheng and Henryk Kierzkowski, eds. 2001. *Globalization of Trade and Production in Southeast Asia*. New York: Kluwer Academic Press.

Globalization once again takes center stage in this new anthology by Leonard K. Cheng and Henryk Keirzkowski. This time, the discussion focuses on international production fragmentation, described as the dispersion of vertically-related processes in two or more countries or regions that are required to produce a final output (otherwise known as "international production sharing"). This process of fragmentation is attributed to advances in transportation and communication technologies and the liberalization of trade policies that make the vertical division of labor practical.

The book uses theoretical explorations of fragmentation to inform case studies of the economic aspects of fragmentation in East Asia and to derive policy implications. Alan Deardorff's chapter on financial crisis, trade, and fragmentation provides a valuable macroeconomic analysis of production in East Asia, but only mentions how these processes directly relate to the Asian financial crisis at the end. Deardorff demonstrates how countries engaging in fragmentation to increase efficiency are also more vulnerable to shocks in the economy. Ronald W. Jones and Henryk Kerzkowski present a compelling account of how fragmentation and technological innovation can become intertwined using the examples of computer chips designed for PCs now being widely produced for other products such as automobiles, toasters and the like. Other chapters link fragmentation of production, among many other aspects of trade, to why some firms decide on arms-length

transactions while others choose parts supply affiliates (such as in the case of two electronic component firms in Singapore), and the division of value-added between source and host economies. The case studies cover Japan, South Korea, China, Taiwan, Hong Kong, and Singapore, each focusing on different industries.

One of the more controversial pieces of the anthology is Robert E. Baldwin's paper on the implications of increasing fragmentation and globalization for the WTO. Baldwin predicts that by creating new products that increase the number of production stages, vertical fragmentation offers the opportunity to impose new tariff rates that can increase the degree of effective protection on many products. He argues that the basic WTO rules should be modified to permit the imposition of import barriers in response to either fair or unfair foreign competition, because the present rules ignore the existence of traded intermediate inputs. However, Baldwin also maintains that comprehensive labor standards and environmental standards are not appropriate subjects for inclusion in the WTO because, while these are important issues, they should be dealt with via outside agreements.

Cheng and Kierzkowski's collection of studies on fragmentation of production across borders provides a unique contribution to the literature on globalization and the structure of East Asian economies in the wake of the Asian financial crisis. ●

Review by BASC staff

Business and Politics

This international journal explores the strategic space in which governments and firms interact. It focuses on two areas: the integration of market with nonmarket corporate strategy, including organizational design, legal tactics, and lobbying; and government efforts to influence firm behavior through regulatory, legal, and financial instruments.

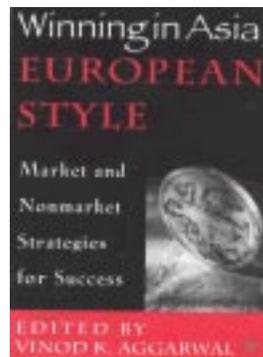
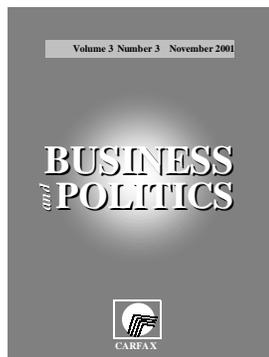
Articles in the forthcoming November 2001 issue include Glenn Fong on government and the PC revolution; Jonathan Story and Robert Crawford on efforts to cope with the Y2K bug; Aviva Geva on the Israeli bank-share crisis of the early 1980s; and Steve Tombs and Anne Alvesalo on economic crime in Finland.

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