

Trans-Pacific Partnership (TPP)

Background

Trans-Pacific Partnership (TPP) originally started among Brunei, Chile, New Zealand, and Singapore back in 2005. This original trade agreement, known as Trans-Pacific Strategic Economic Partnership Agreement (TPSEP or P4 and later becoming known as just TPP as more countries joined) was concluded and entered into effect on May 28, 2006 for New Zealand and Singapore, July 12, 2006 for Brunei, and November 8, 2006 for Chile. This agreement was comprehensive and broad, and the effect of its ratification was expansive, affecting trades in goods, environmental and labor laws, and intellectual property laws.

Originally drafted to improve trade relations among Asia-Pacific nations, the TPP agreement has attracted many nations to join the negotiations. Current members of the TPP include Brunei, Chile, New Zealand, Singapore, United States, Australia, Peru, Vietnam, Malaysia, Mexico, Canada, and Japan. Those who have shown interest in joining the TPP negotiations include Taiwan and South Korea. Taiwan has expressed its commitment to join the TPP negotiations in 2014 with South Korea expressing the same; however, it is evident that South Korea is prioritizing its commercial deal with China over the TPP.

Although the U.S. economy has much to gain from the TPP agreement, U.S.'s participation in TPP hides an agenda: to control and contain China's influence in South East Asia. Regardless of the U.S.'s true motives in joining the TPP negotiations, this expansive free trade agreement would significantly affect each participating nation's economy. For us, the TPP's effect on U.S. garment industry is of highest interest. This report will focus on Vietnam, the most significant non-FTA textile and garment trading partner of the U.S., and will explore how the U.S. garment industry will be affected by the TPP agreement.

TPP's Effect on U.S. Garment Industry

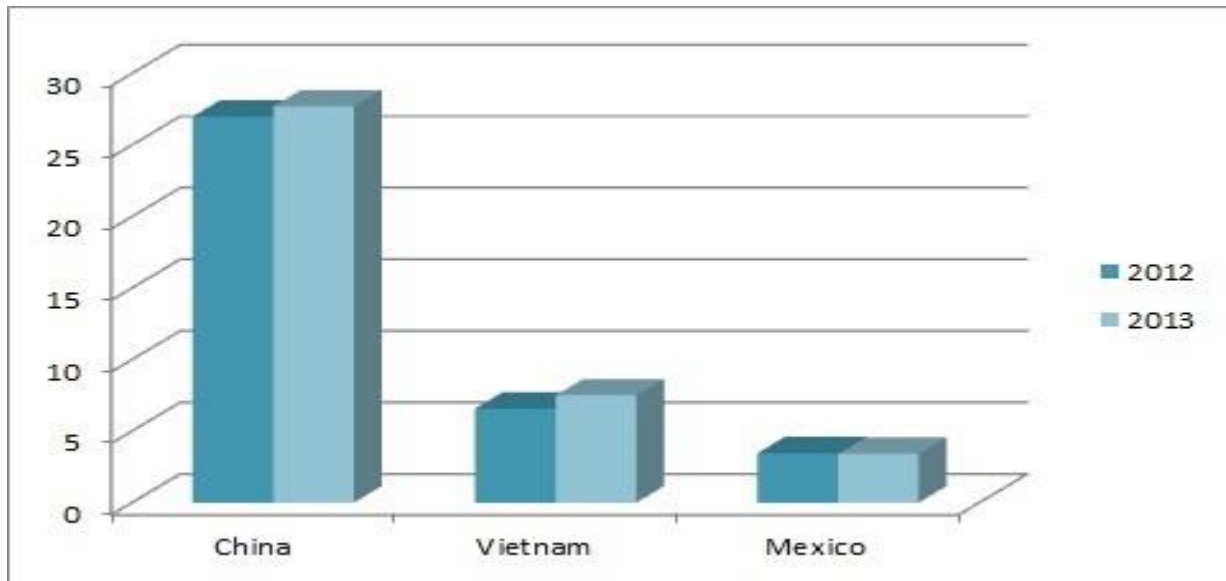
First, the significance of Vietnam's participation in TPP will be explained. Canada, Australia, Mexico, Peru, Chile, and Singapore already have a free trade agreement with the U.S. Therefore, the TPP will merely expand on the status-quo – meaning, the TPP will not significantly alter each nation's economy. Brunei and New Zealand are high-income nations and do not engage in meaningful garment trade with the U.S. That leaves Vietnam – the only true poverty nation in the TPP group, and more importantly, the only non-FTA nation with significant textile and garment trade with the U.S.

Vietnam is the second largest exporter of garment to the U.S. only behind China (Figure 1). In fact, Vietnam provided more than 15% of total U.S. imports of women's blouses, shirts,

and suits. Specializing in labor-intensive knitting and weaving, Vietnam currently does not have the capacity to produce enough yarn and fabric which its apparel industry requires. Hence, Vietnam heavily relies on foreign imports mainly from China and other Asian nations. With 80% of total material used in Vietnam being imports, the potential benefit for U.S. garment industry under the potential TPP agreement is definitely present.

Figure 1. U.S. Apparel Imports

In Billions of U.S. Dollars, by Selected Countries

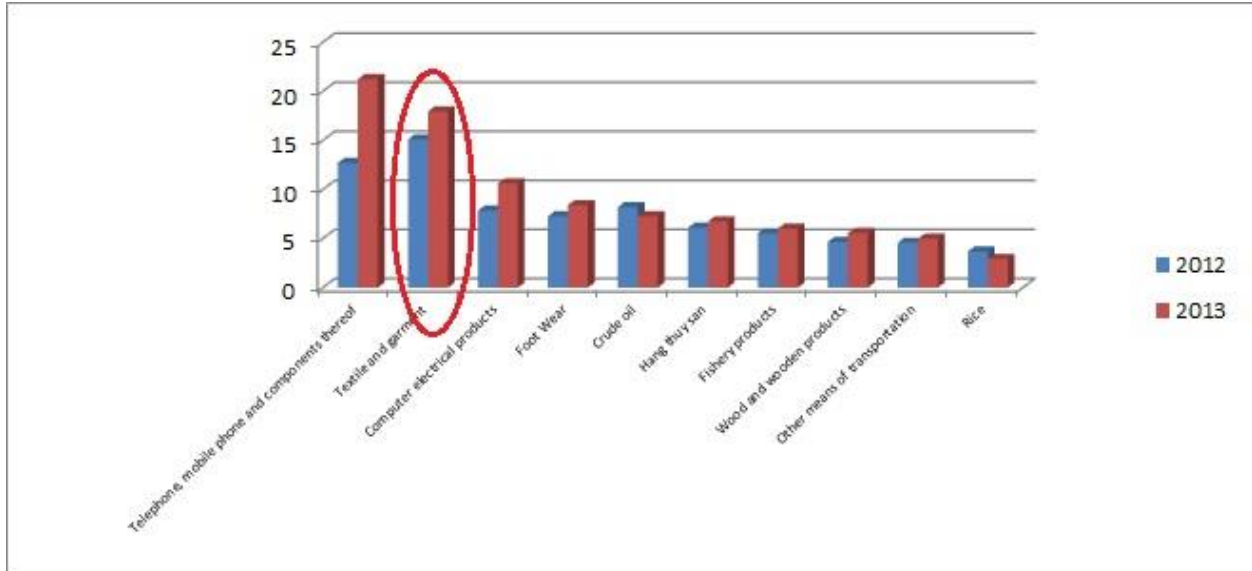


Source: U.S. Office of Textiles and Apparel (OTEXA)

Moreover, garment is Vietnam's second largest exported commodity – up from 15.09 billion dollars in 2012 to 17.95 billion dollars in 2013. Vietnamese garment exports to the U.S. grew 14.2% in 2013 – 8.6 billion dollars (Figure 2). Le Quoc An, consultant for the Vietnam Textile and Apparel Association (Vitas), predicted that the proposed TPP agreement can double Vietnam's garment exports to the U.S. Although it is overly optimistic, such prediction may not be far off from the potential reality. Vietnam has seen much foreign investments in its garment industry recently due to low labor cost and the anticipation of the TPP agreement.

Figure 2. Top 10 major exported commodities of Vietnam

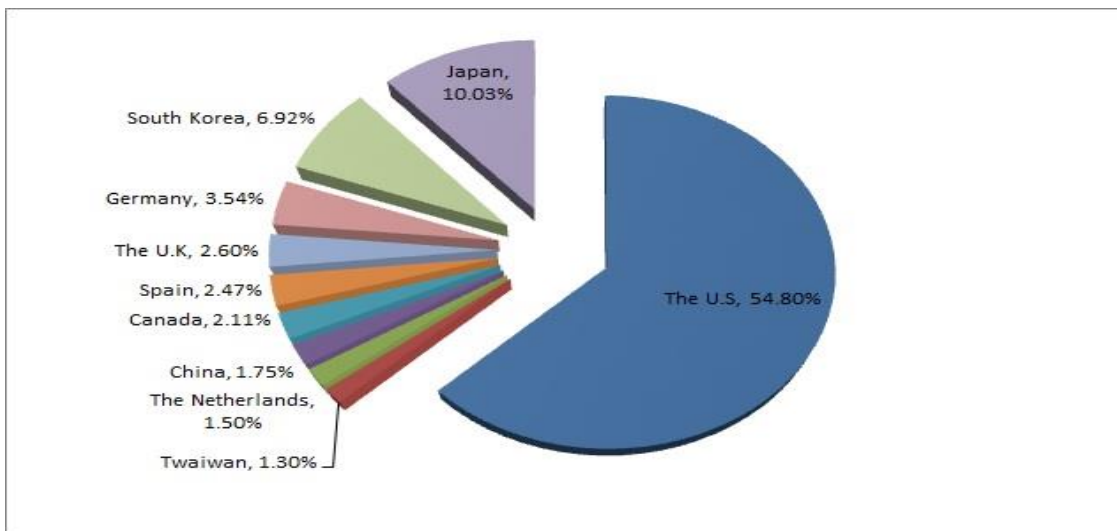
In Billions of U.S. Dollars



Source: Vietnam Customs

Currently, Vietnam is not a big importer of U.S. textiles. As mentioned above, Vietnam imports regionally either from China or other Asian nations. However, TPP agreement can provide much incentive for Vietnam to purchase more U.S. textile over Chinese textile in order to qualify for duty-free access to the U.S. market. Since the U.S. market makes up close to 50% of Vietnam’s garment exports (Figure 3), it is likely that Vietnam will increasingly import U.S. textiles under the TPP.

Figure 3. Vietnam’s textile and garment export structure by market in first 6 months of 2013



Source: General Department of Vietnam Customs

Similar case has been seen in Mexico after NAFTA (North American Free Trade Agreement) was adopted. Ever since NAFTA took effect back in 1994, Mexico experienced increase in foreign investments in its garment industry. At the same time, Mexican manufacturers began importing U.S. textile in order to access the U.S. market duty-free. Today, Mexico is the largest foreign market for the U.S. textile industry, and the majority of U.S. textile exports are made to NAFTA or CAFTA-DR (Dominican Republic-Central American Free Trade Agreement) nations. Similar scenario can unfold for Vietnam once the TPP agreement is reached.

As shown in Table 1, U.S. tariff on Vietnamese imports varies by product. Depending on the language of the agreement, TPP can potentially eliminate these tariffs for Vietnamese imports.

Table 1. Vietnam: Tariffs (percent ad valorem) for Textiles, Apparel, Footwear and Travel Goods

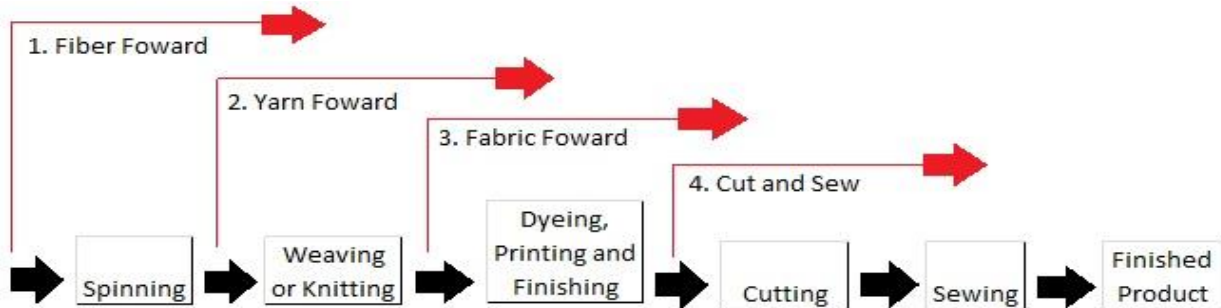
	Tariff Rate Range (%)
Yarn	
silk	5 to 10
wool	0 to 5
cotton	5
other vegetable fiber	3 to 5
man-made fiber	0 to 5
Woven Fabric	
silk	12
wool	12
cotton	12
other vegetable fiber	12
man-made fiber	12
Knit Fabric	12
Apparel	5 to 20
Footwear	5 to 36
Travel Goods (Bags and Luggage)	30

Source: U.S. Office of Textiles and Apparel (OTEXA)

Rules of Origin

Perhaps the most contentious and unresolved issue of the TPP agreement, rules of origin (ROO) will undoubtedly decide the extent in which the TPP affects the U.S. garment industry. ROO specifies how much of the content of textile or apparel must come from the TPP region in order for the product to qualify for duty-free access. Figure 4 below describes the rules of origin in detail.

Figure 4. Rules of Origin Details



1. Fiber Forward – Raw material, such as cotton, must be formed in the TPP region.
2. Yarn Forward – Raw material may be produced in any region, but each step starting with the yarn used to make textiles or apparel must be done within the TPP region.
3. Fabric Forward – Raw material and yarns may be formed in any region, but fabric must be knitted or woven in TPP region.
4. Cut and Sew – Only the cutting and sewing of the final product must be done in the TPP region.

Vietnam has publicly expressed its desire to incorporate the ‘Cut and Sew’ ROO in the TPP agreement. This will allow Vietnam to gain duty-free access to the U.S. market while using materials from China or other non-TPP nations. Obviously, this rule will be detrimental to the U.S. textile industry while benefitting the large U.S. retailers and garment importers. On the other hand, the U.S., most often, has applied the ‘Yarn Forward’ rule to textile and apparel in other FTAs. This will severely discourage Vietnam from using Chinese imports while encouraging the use of U.S. imports at the same time. This position is supported by the U.S. textile industry and other apparel manufacturers. It is unclear which rule will be applied to the TPP agreement due to the fact that the negotiations and the details of the TPP have largely been withheld from the public.

Conclusion

Because Vietnam, a major apparel producer currently sourcing from China, is included in the TPP, the Trans-Pacific Partnership agreement has the potential to dramatically affect the U.S. garment industry. As seen through Mexico and NAFTA, Vietnam has the potential to become a major player in the world's apparel trade. As China and Mexico experience ever-increasing labor costs, Vietnam grows more attractive to investors. In Mexico's garment industry, the cost of labor is \$2.06 per hour (\$330/month) while it is only \$0.51 per hour (\$82/month) in Vietnam. Low labor cost along with the potential duty-free access to the U.S. market will create many opportunities on both sides of the agreement. The extent of TPP's effect on the U.S. garment industry remains to be seen, especially with the absence of credible evidence regarding which rules of origin will be implemented.

One can only speculate on when the TPP agreement will be finalized, for the details of the negotiations have been kept in private. However, many sources point towards mid-2014 as the likely time period for TPP to be finished. In addition, Obama administration showed its commitment to finishing the TPP by introducing the Trade Promotion Authority (TPA) in Congress. TPA is a legislation which will grant Obama administration more power in trade negotiations. Normally, international trade agreements such as the TPP would first need to be agreed upon by all participating nations. Then, this agreement will be subjected to 'democratic input' – Congress will be able to review it, amend if (if needed), then vote for or against it. With the TPA, Obama administration can negotiate the TPP, come to an agreement with other nations, and introduce this agreement to Congress for a 'yes' or 'no' vote. Congress will not be able to amend the agreement at all, and Congress must vote on the agreement within 90 days of its introduction. This will provide Obama administration with increase in negotiating power, and at the same time, the TPA will certainly speed up the process of enacting the TPP. It is likely that TPA will be granted despite all the political bickering. In fact, all major international trade agreements thus far were accompanied by the TPA.

The next round of negotiation is scheduled for later this month. The 12 member countries are considering starting the ministerial meeting in Singapore on February 22 and holding a meeting of top negotiators on February 17 in Singapore. It seems likely that the TPP will be finished by April – when president Obama is scheduled to visit Asia to reinforce U.S. ties across the Asia-Pacific region.