



NEW ZEALAND
FOREIGN AFFAIRS & TRADE



Minister of
Foreign Affairs and Trade
Maurice Williamson

18 MAY 2016

Andrew Riddell

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Dear Andrew Riddell

I refer to your email of 19 April 2016 in which you request the following information under the Official Information Act 1982 (OIA):

"Thanks for sending those five documents in response to my request fyi-request-3664-53eab4fc@requests.fyi.org.nz

The three documents that are not emails are undated. What are the dates for each of the three documents supplied that isn't an email?

The email dated Monday 15 February 2016--you have deleted the identity of the sender of the email. That is fine in so far as I am not interested in the name of the person sending the email. However please provide a description of the organisation and country the person sending the email works for.

The email dated Wednesday 20 January is clearly a response to a query from a person most likely in Treasury about the "Tufts report". Why hasn't that originating email been included in this release of information I asked for. Are there other documents relating to the "Tuft's report" that haven't been provided?

There is an undated 10 page report titled "Comment on Trading Down: Unemployment, Inequality and Other Risks of the Trans-Pacific Partnership Agreement". Despite this title the claim is made that most of the report is out of scope. Please provide this report in full.

There is a six page report titled "Modelling of Trans-Pacific Partnership: Summaries and New Zealand Outcomes" where a significant portion of the report is claimed to be out of scope. Why does the report include comment on Coates et al reference to the Tufts report, yet claim that another report that "counter Capaldo et al claims" is out of scope. Please provide the full report.

In the information released, the statement is made in several places that "There is a considerable amount of empirical evidence showing the exact opposite. For example, in New Zealand as the wool sector declined people took new jobs producing dairy products, kiwifruit and wine." Please provide the empirical evidence supporting this statement."

Where information has been withheld under section 9 of the OIA, no public interest in releasing the information has been identified that would be sufficient to override the reasons for withholding it.

You have the right under section 28(3) of the OIA to seek a review of this response by the Ombudsman.

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Joana Johnston', with a stylized flourish at the end.

Joana Johnston
for Secretary of Foreign Affairs and Trade

From: s9(2)(a) (TND)
Sent: Wednesday, 20 January 2016 10:54 a.m.
To: s9(2)(a) [TSY]
Cc: s9(2)(a) (ECO)
Subject: RE: Alternative TPP model released

Hi s9(2)(a) – I don't think we've done a summary (s9(2)(a)). But from my understanding the Tufts report's use of the UN model was extremely unusual, in that it's not designed for trade. The idea that trade liberalisation would not result in transfer of labour between sectors (even over the long term), but only in increased/decreased employment in individual sectors seems to go against the entire idea of comparative advantage.

s9(2)(a)

Senior Policy Officer
Trade Negotiations Division
New Zealand Ministry of Foreign Affairs & Trade | Manatū Aorere

s9(2)(a)

www.mfat.govt.nz | www.safetravel.govt.nz | www.nzuhsc.govt.nz

From: s9(2)(a) [TSY] [mailto:s9(2)(a)@treasury.govt.nz]
Sent: Wednesday, 20 January 2016 10:13 a.m.
To: s9(2)(a) (TND); s9(2)(a) (ECO); s9(2)(a)
Subject: Alternative TPP model released

Hi all

You've probably already seen this alternative (much more pessimistic) TPP model that has been released by Tufts University in recent days.

http://www.ase.tufts.edu/gdae/policy_research/TPP_simulations.html

Thus far i've only seen commentary in Inside Trade and from some Senate figures but I do wonder whether it is likely to get some domestic coverage at some point. If you do put together some reactions / comms points on this i'd be keen to be involved.

Cheers

s9(2)(a)

s9(2)(a) | Senior Analyst | The Treasury

s9(2)(a)

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Modelling of Trans-Pacific Partnership: Summaries and New Zealand Outcomes

This document summarises recent models analysing the implications of the Trans-Pacific Partnership. The table compares key New Zealand outcomes as estimated in these models, with estimates generated for MFAT by Strutt, Minor and Rae.

	GDP	Exports	End date	Goods NTM gains	Treatment NTMs
Strutt Minor and Rae 2015	1.4%	2.2%	2030	70% (54% with gains halved as reported by MFAT)	Goods NTMs for all TPP countries to mean of the TPP region; services NTMs to the top quintile of the TPP region
World Bank 2016	3.1%	12.8%	2030	53%	75% of G&S NTMs assumed to impede trade. Of these, 75% of goods NTMs, and half of services NTMs are assumed "actionable" (able to be addressed in a trade agreement)
Petri and Plummer 2016	2.2%		2030	43%	As with WB, with 20% reductions in NTBs and investment barriers applied also to non-TPP countries
Tufts 2016*	0.8%	2.1%	-	-	-

*Capaldo and Izurieta in the Tufts report do not model reductions in NTMs (or tariffs)

Key points: General

- Computable General Equilibrium (CGE) trade models are useful for indicating the size and the magnitude of changes to GDP, trade and other macroeconomic variables from changing barriers to trade. They are not intended, and nor are they able, to forecast precise changes to these variables.
- CGE models that are generally accepted as credible and comprehensive by modelling experts estimate small but significant gains in New Zealand GDP and trade from TPP.
- MFAT commissioned modelling by Strutt et al estimate that New Zealand's GDP will expand by 1.4% by 2030 - an additional NZ\$2.7 billion in the economy. This estimated positive gain is consistent with estimates by Petri et al and the World Bank.

Key Points: World Bank 2016

- The World Bank estimates that the TPP will cause New Zealand's GDP to increase by 3.1% by 2030.
- The World Bank estimates a much larger increase in New Zealand exports than Strutt et al.
- The difference between World Bank and Strutt et al outcomes is largely due to differing treatment of NTMs with in the model. Strutt et al reduce NTMs to regional means and top quintiles, whereas the World Bank assumes three quarters of NTMs impede trade, and half to three quarters of these are able to be addressed within TPP.
- There is no "correct" method for modelling how reducing NTMs influences trade and GDP – a relatively new area of modelling. Both approaches are credible.
- We take some confidence from the fact that two different approaches to modelling NTMs both estimate small but significant positive gains to New Zealand GDP.
- [The World Bank report is based on work by Petri and Plummer]

Key points: Tufts University

- Capaldo, Izurieta and Sundaram, use the United Nations Global Policy Model, an inappropriate model for assessing the economic effects of trade or a trade agreement (UN agencies do not use this model when analysing changes in trade policy). Almost all trade models "shock" the model by changing trade barriers, and relative prices of imported and domestic goods, and then allowing the economy to adjust with movement of labour, land and capital.
- Capaldo et al instead shock their model by introducing a change in exports (with the export values taken from Petri et al estimates of the TPP – modelling criticized by Capaldo et al). They assume that labour and capital doesn't respond to the change in exports. As a sector declines for example, people previously employed in that sector stay unemployed rather than taking employment in growing sectors. New competition from trade liberalisation therefore lowers wages and causes unemployment.
- Capaldo's model suggests that employment declines around the world due to the TPP. Capaldo estimates that TPP will cause a global recession.
- There is a considerable amount of empirical evidence showing that removing barriers to trade encourages economic activity. For example, in New Zealand as the wool sector declined new jobs were created producing dairy products, kiwifruit and wine. Generally exports tend to increase when barriers to trade are lowered, and evidence shows that wages are higher in export-intensive industries.
- Capaldo used the same model and approach to estimate changes to GDP, employment and inequality from the Transatlantic Trade and Investment Partnership, with similar results. Economists from the European Center for

International Political Economy (ECIPC) studied Capaldo's methodology, the model used and data, and concluded that:

"The Capaldo study is associated with such serious flaws that its results should neither be regarded reliable nor realistic. It fundamentally contradicts all other existing studies of the effects of FTA's and the reality of what liberalised trade actually brings about."

- The ECIPC economists point out that:
 - The model is ill-suited to analysing trade reforms.
 - Model deficiencies are covered up with unrealistic assumptions.
 - Capaldo's thesis is not supported by history.
 - Capaldo's results conflict with the United Nations global rebalancing assessments based on the same model.
 - Economists are denied access to the model to try to replicate Capaldo's findings.
- Other critics of Capaldo modelling include Noble Prize-winning Paul Krugman.
- Capaldo et al have two key criticisms of Petri, Plummer and Zhai, both of which are misleading. One is the use of pre-2007 data that doesn't reflect the world post the GFC, the other is the assumption of full employment:
 1. More recently reported Petri and other modelling has post GFC data and produces similar results as their earlier analysis:
 - Petri et al use 2011 trade data, updated to 2015, as reported on in January 2016 (with similar results – see relevant section).
 - The World Bank use 2015 GDP and similar data, and 2011 trade data updated for new trade agreements, with similar results as Petri et al
 2. Earlier Petri et al modelling doesn't claim that TPP will create full employment; rather their model doesn't capture how TPP influences employment. Petri and Plummer in a 2016 Peterson Institute working paper 2016

Key points: Peterson Institute (Petri and Plummer)

- Petri and Plummer estimate that New Zealand GDP will increase 2.2% by 2030; New Zealand's real income will increase US\$6 billion, and; New Zealand exports will expand by 10.2%.
- This is an update of Petri et al 2012 modelling of the TPP, based on the actual agreement and extended to 2030. They also use new data on NTMs and include previously unconsidered effects.
- There are small improvements in outcomes relative to 2012 modelling, largely due to the estimated benefits from reducing NTBs being higher than in 2012. The

2015 study also accounts for non-preferential provisions in the TPP agreement, and recognises heterogeneity in firm productivity within sectors.

- In aggregate for the TPP group the Peterson model estimates:
 - 12% of the GDP gains derive from tariff reductions
 - 43% derive from goods NTB reductions
 - 25% from service NTB reductions
 - 20% from investment barrier reductions

Other studies

- Inkyo Cheong and Jose Tongzon (2013) find that the TPP would have no significant effects. They authors consider tariff reductions only however – a small part of Strutt et al and Petri et al estimated gains.
- Hiro Lee and Ken Itakura (2014) estimate that the TPP will cause a 20 percent cut in service NTBs and estimate income gains of slightly less than 1% for Australia, Canada, Japan, Mexico, and the United States.
- Kenichi Kawasaki (2014) estimates annual gains of 1.8 percent of GDP for TPP members assuming that 50 percent of TPP liberalization is non-preferential.

Summary of reporting and observations

World Bank: Potential Macroeconomic Implications of the Trans-Pacific Partnership

In January 2016 the World Bank's *Global Economic Prospects spillovers amid weak growth* included a section titled *Potential Macroeconomic Implications of the Trans-Pacific Partnership*. The note draws from a forthcoming background paper by Petri and Plummer with modelling analysis based on a preliminary assessment of the TPP published in November 2015 (also reported on following).

The World Bank's estimate of New Zealand GDP growth is broadly consistent with Strutt et al analysis commissioned by MFAT. It is also consistent with the often referred to earlier Petri et al analysis estimate of 0.9% (excluding FDI effects). That is, all three studies estimate a small but significant positive gain to New Zealand GDP.

Estimated gains from trade are largely due to reductions in non-tariff measures (NTMs). For TPP members collectively the World Bank reports that 15% of the estimated GDP gain is due to cuts to tariffs, 53% is due to reductions in goods trade NTMs, and 31% is due to reductions in services trade NTMs.

The World Bank's approach to modelling NTM reductions is quite different from Strutt et al. Both approaches seem appropriate.

Strutt et al reduce goods NTMs for all TPP countries to the mean of the TPP region, and reduce services NTMs to the top quintile of the TPP region. In the World Bank report, goods and services' NTMs are first estimated. Three-quarters of these NTMs are assumed to be impeding trade and subject to reduction. Of these, three-quarters of goods NTMs,

and half of services NTMs are assumed to be "actionable" (able to be addressed in a trade agreement).

Tufts University: Trading Down: Unemployment, Inequality and Other Risks of the Trans-Pacific Partnership Agreement

Capaldo, Izurieta and Sundaram

In January 2016 Capaldo, Izurieta and Sundaram released Global Development and Environment Institute working paper 16-01 criticising Petri, Plummer and Zhai's modelling, and reporting their own estimated TPP outcomes based on a very unusual approach to trade modelling. Rather than model how economies may adjust to lower barriers to trade, the authors used Petri's estimates of changes to exports from TPP as input to a model, and then estimate how economies adjust to the estimated change in exports. Their results rely on unrealistic assumptions. The model and report gives the impression that either the authors don't understand economics, or are purposely trying to mislead the reader.

Capaldo et al report on employment and equality outcomes. They suggest that TPP will decrease employment in all TPP countries including New Zealand (a decline of either 5,000 or 6,000 for New Zealand - 5,000 is reported in the text and 6,000 in a table). Their model suggests that employment in the rest of the world will also decline due to TPP. Capaldo et al report that labour share of income will decline in all TPP countries, and that inequality will increase.

Central to the Capaldo et al argument and results is that liberalising trade creates competition which leads to lower wages. Few economists would argue against the claim that freer trade encourages competition. However, claiming competition reduces wages is disingenuous. Trade liberalisation and competition tends to encourage labour and other resources into more productive and better paying sectors and companies. Inefficient companies are forced to improve productivity or shut their doors. Trade encourages specialisation which in turn encourages productivity gains. In the United States export-intensive industries pay about 16% more on average than domestically focused industries. Similar results have been found in New Zealand data.

It appears that the Capaldo et al assumption of declining wages introduces deflation into their model. This add on effectively creates recessions in TPP economies, hence the across the board reduction in TPP countries' GDP. In fact the model result suggests that employment declines around the world due to the agreement. In other words Capaldo estimates that TPP will cause a global recession.

Other weaknesses in Capaldo et al include: aggregation of countries (Brunei, Malaysia, Singapore and Vietnam are analysed as a group rather than individual countries, as are Chile and Peru) and: aggregation of sectors (four only: energy, primary commodities, manufacturing and services). These flaws in the analysis pale into insignificance relative to their assumed adjustment process however, and the use of a model not designed to analyse trade agreements.

Petri and Plummer 2016 (next section) counter Capaldo et al claims.

Capaldo, Izurieta and Sundaram's modelling is referred to in *The Economics of the TPPA* by Coates, Oram, Bertram and Hazledine, in the body of the report and under key points, dot point five (the previous dot points criticise the significantly more robust and realistic Strutt et al modelling). *The Economics of the TPPA* highlights Capaldo et al findings of: a 0.77% increase in GDP; a small decline in employment; and increased levels of income inequality. It would be interesting to ask either Oram or Bertram what they think of the modelling.

Peterson Institute for International Economics: The Economic Effects of the Trans-Pacific Partnership: New Estimates

Petri and Plummer

The Peterson Institute for International Economics Working Paper 16-2 from January 2016 is [The Economic Effects of the Trans-Pacific Partnership: New Estimates](#).

The authors estimate the economic effects of the Trans-Pacific Partnership (TPP) using a comprehensive, quantitative trade model, updating results reported in [Petri, Plummer, and Zhai \(2012\)](#) with recent data and information from the agreement. In aggregate and for all TPP countries Petri and Plummer's latest results suggest TPP has a larger positive effect on GDP than their 2012 modelling (with Zhai).

Petri and Plummer consider how TPP might impact on the labour market in the United States. The agreement is estimated to increase United States wages but is not projected to change US employment levels; it will slightly increase "job churn" (movements of jobs between firms) imposing adjustment costs on some workers. Both labour and capital benefit from TPP, but labour gets a greater share of total gains – hence TPP is estimated to reduce income inequality in the United States (contradicts the finding of Capaldo et al). Petri and Plummer find that United States employment increase due to TPP (the opposite to Capaldo et al).

Petri and Plummer refer to Strutt et al in this report (comparing GDP outcomes in the box on page 16).

Comment on *Trading Down: Unemployment, Inequality and Other Risks of the Trans-Pacific Partnership Agreement*

Tufts University

Capaldo, Izurieta and Sundaram

January 2016

- Capaldo, Izurieta and Sundaram, use the United Nations Global Policy Model (GPM) to estimate the impact of TPP. GPM was developed to consider the macroeconomic consequences of unexpected shocks such as the global financial crisis, and how such shocks spread between countries. The model doesn't capture exports, imports, foreign direct investment or shifts in industry structure. The model therefore ignores benefits of freer trade such as increased specialisation, greater consumer choice, or economies of scale. (UN agencies do not use this model when analysing changes in trade policy.)
- There are alternative economic models designed to assess trade. To assess the economic impact of a trade agreement like TPP, almost all of these trade models "shock" the model by changing trade barriers, and hence relative prices of imported and domestic goods, and then allowing the economy to adjust with movement of labour, land and capital.
- In order to model the effects of TPP, Capaldo et al instead shock their GPM model by introducing a change in exports (with the export values taken from Petri et al estimates of the TPP – modelling criticized by Capaldo et al). They assume that labour and capital does not respond to the change in exports. This has the result, for example, that if a sector declines in a country, people previously employed in that sector stay unemployed rather than taking employment in growing sectors. Similarly, a sector experiencing increase is unable to draw in new labour and capital, which limits the extent to which it can grow. Under the model, new competition from trade liberalisation is assumed to lower wages and cause unemployment.
- There is a considerable amount of empirical evidence showing the exact opposite. For example, in New Zealand as the wool sector declined people took new jobs producing dairy products, kiwifruit and wine. Generally exports tend to increase when barriers to trade are lowered, and evidence shows that wages are higher in export-intensive industries. It should also be noted that given New Zealand's already open economy, the effects of trade agreements in different sectors are often best viewed in relative terms. Faster growing sectors tend to attract more labour and capital over time, which can be accompanied by decline in some other sectors.
- Robert Lawrence from The Peterson Institute for International Economics compared Capaldo et al analysis of the TPP with Petri and Plummer analysis. He suggested considering each model's credibility by asking three questions:
 - Is the model appropriate for exploring trade policy.
 - Has the TPP been depicted in that model in a sensible way.

- Are the results of the model credible.
- As noted by Lawrence:

“[Capaldo modelling] predicts a decline in employment in every country in the TPP, which totals 770,000 [people]. The authors claim their model is “more realistic,” yet their model also predicts declines of 5.4 million jobs in the rest of the world! Indeed, GDP in non-TPP developing countries (i.e., China, India, Indonesia etc.) falls by 5.24 percent. It is not believable that a trade agreement of this magnitude could cause the rest of the world to plummet into recession. Whatever the merits of the model used by [Capaldo], it is simply not suited for credibly predicting the effects of the TPP.”
- In response to Lawrence, Capaldo has stated:

“in line with the limited scope and purpose of our paper, we do not claim to have provided reliable and definitive projections of the TPP’s likely effects”
- Capaldo used the same model and approach to estimate changes to GDP, employment and inequality from the Transatlantic Trade and Investment Partnership, with similar results. Economists from the European Center for International Political Economy (ECIPC) studied Capaldo’s methodology, the model used and data, and concluded that:

“The Capaldo study is associated with such serious flaws that its results should neither be regarded reliable nor realistic. It fundamentally contradicts all other existing studies of the effects of FTA’s and the reality of what liberalised trade actually brings about.”
- The ECIPC economists point out that:
 - The model is ill-suited to analysing trade reforms.
 - Model deficiencies are covered up with unrealistic assumptions.
 - Capaldo’s thesis is not supported by history.
 - Capaldo’s results conflict with the United Nations global rebalancing assessments based on the same model.

Comment on the *Economics of the TPPA*

Barry Coates, Rod Oram, Dr. Geoff Bertram and Professor Tim Hazledine
January 2016

The report focuses in large part on criticising the Computable General Equilibrium (CGE) modelling contracted by MFAT to Anna Strutt, Peter Minor and Alan Rae¹. General criticisms include that the estimated gains are small, the report is not a cost benefit analysis of TPP as a whole, and that Strutt et al provided only 20 pages of explanation. Specific criticisms are levelled at modelling reductions in tariffs, Non-Tariff Barriers (NTBs), and improved trade facilitation.

Comment on general points in *Economics of TPPA*

Magnitude of gains from TPP

Coates et al suggest that the estimated economic gains to New Zealand from TPP should be seen as modest: "extrapolating from current growth rates, GDP would increase by 47% by 2030 without the TPPA or 47.9% with the TPPA".

- This is based on the estimated gain to New Zealand GDP of 0.9% in 2030, which the Government has used based on the report by Strutt et al. (Note that technically, an additional 0.9% growth on a 47% increase in GDP is equivalent to a 48.3% increase, not 47.9%.) The 0.9% increase in baseline GDP in 2030 is equivalent to NZ\$2.7 billion. We would argue this represents a significant increase in New Zealand's income.
- As outlined in the National Interest Analysis, not joining TPP would almost certainly result in an overall loss of competitive advantage for in some TPP markets, which would be expected to result in a net decline in what New Zealand's GDP would otherwise have been.

Effect of TPP on employment and income in New Zealand

Coates et al suggest TPP would reduce employment and increase income inequality in New Zealand.

- Coates et al are referring to the Capaldo modelling described above (estimates an employment decline of either 5,000 or 6,000 for New Zealand - 5,000 is reported in the text and 6,000 in a table).
- There are costs as people move between different types of employment, particularly if these changes occur in the short term. But it is not correct to suggest that transition between sectors does not occur, as Capaldo et al claim. For example, as demand for shearers in New Zealand has declined, employment opportunities have grown in dairy farming, wine cultivation, horticulture, tourism, education etc. It is also important to note that given New Zealand's already open economy, few sectors are expected to experience sudden decline. Rather, changes are much more likely to result from increased productivity in certain sectors compared to others.

¹ Published on 5 November 2015, see www.tpp.mfat.govt.nz.

- Capaldo et al report that employment in TPP and non-TPP countries would decline due to the Agreement. Alternatively, Petri and Plummer estimate that TPP will increase United States wages but is not projected to change United States employment levels; it will slightly increase "job churn" (movements of jobs between firms).

Undertaking a full cost-benefit analysis of TPP

Coates et al argue that the modelling commissioned from Strutt et al by MFAT is not a full cost benefit analysis of TPP.

- The cost-benefit analysis for TPP is the National Interest Analysis. This comprehensively assesses the impact on New Zealand across the Agreement. The economic modelling undertaken by Strutt et al is a key component of this.
- This is explicitly noted on page 2 of the report by Strutt et al:

"Other factors that are not considered will also influence the impact of any TPP agreement on New Zealand and a number of potentially important issues lie outside the scope of this report. As such, this report is not intended to be a cost-benefit analysis of the TPP."

- It should be noted that the modelling undertaken by Strutt et al seeks to capture the net effects of changing trade barriers under TPP. This kind of modelling has the potential to be positive or negative, and includes for example changes in imports as well as exports, changes in the economy, dynamic effects, and trade with the global economy. The modelling found TPP would have a substantial net economic benefit for New Zealand.
- A number of potentially beneficial influences are also excluded from the modelling – such as explicitly modelling FDI (Petri et al found this to cause NZ GDP to increase by more than 4% when considered together with other gains from TPP).

Gains relative to fluctuations in commodity prices and the exchange rate

Coates et al argue that gains in agriculture production from TPP would be small relative to fluctuations in commodity prices and the exchange rate.

- This is correct - commodity prices and the exchange rate fluctuate. There is very little New Zealand can do about either. But we can help New Zealand exporters get improved access to international markets. And the estimated gains to production from improved market access through TPP are not immaterial.

Standard of documentation of the modelling

Coates et al criticise the level of documentation in Strutt set al, for example in explaining assumptions used.

- Strutt et al are transparent and fully explain their assumptions and approach to modelling. (We note that if this were not the case then Coates et al would not have been able to produce a 31 page report for *The Economics of the TPPA*). Strutt et all refer extensively to supporting material. About 30% of the 67 page report describes data and methodology

Comment on economic modelling points in *Economics of TPPA*

Strutt et al utilised the well-established, internationally recognised Computable General Equilibrium (CGE) approach to modelling to estimate the impacts of TPP. This is a common approach by which economists seek to capture the effects of changing trade barriers (such as under a Free Trade Agreement like TPP). In an earlier publication *No more than a case of beer*, Hazledine had agreed that "CGE is a well-established, internationally recognised approach to modelling trade policy changes", and that "I am happy to endorse MFAT's choice of Anna Strutt, Peter Minor and Allan Rae as a team of internationally respected and experienced trade modellers."

As stated in the report and the TPP NIA, CGE model results rely on assumptions and are subject to data limitations, and hence are better suited to indicating the size and direction of effects rather than providing precise estimates.

Strutt et al modelled the economic impact of TPP by first estimating how New Zealand's economy would be expected to develop as part of the global economy in the absence of TPP (the "baseline"), and comparing this to the case where TPP liberalised trade in goods and services in four areas. The result of the CGE model takes account of the complex adjustments that might take place in an economy following changes in policies and regulations and consequential effects on prices, trade flows and resource allocation in the economy.

The four ways in which TPP was assumed to liberalise trade were:

- Reductions in tariffs and quota barriers on goods trade.
- Reductions in non-tariff barriers (NTBs) on goods trade.
- Improved trade facilitation measures.
- Reductions in barriers on services trade.

The section titled "Modelling of Economic Benefits for New Zealand" in Coates et al includes four sub-sections ((i) to (iv)) that correspond to the four components in Strutt et al.

(i) **Tariff reductions**

Coates et al point out that the benefits from tariff reductions on New Zealand exports do not accrue in their entirety to exporters. The report refers to two different estimates: Strutt et al CGE modelling of TPP where tariff reductions generate about NZ\$624 million in additional New Zealand GDP by 2030, and the NZ\$259 million in eliminated tariffs from the MFAT *Goods Market Access factsheet*.²

- The CGE modelling used by Strutt et al does not assume that tariff changes accrue to exporters only. CGE modelling assumes that changing barriers to trade change relative prices.

² Note that this estimate of tariff savings was updated to \$274 million in the TPP NIA, reflecting the transposition of tariff schedules as part of legal verification.

- The figure of \$259 million tariff savings reported in MFAT's *Goods Market Access factsheet* is New Zealand's average trade for each product multiplied by the size of the tariff reduction, summed over all TPP markets. This is indicative only, and is standard practice for communicating tariff outcomes from a FTA. The factsheet, for example, used these tariff savings for kiwifruit and apples to provide an illustrative example of the outcome per individual grower.
- The Government has not claimed that tariff savings accrue directly to New Zealand exporters. Estimating the net economic benefit of tariff reductions and elimination is the job of economic modelling, for example as undertaken by Strutt et al.

(ii) Trade Facilitation

Coates et al suggest that there should be a greater breakdown of the specific inefficiencies and barriers that trade facilitation will address. The authors also question the assumed 25% reduction in trade delays used in Strutt et al modelling.

- Modelling the degree of detail suggested by Coates et al is simply not feasible when considering such a large-scale modelling effort. Simplifying assumptions had to be made, as with all modelling.
- The assumption of 25% is feasible, reflecting the scope of TPP. Whereas trade facilitation is good in many TPP countries, there is room for improvement. In terms of Trading across Borders The World Bank ranks TPP countries from 34th in the world (the United States) down to 121st (Brunei Darussalam). The World Bank Ease of Doing Business indicator, Trading across Borders, measures the time and costs of exporting and importing.

(iii) Non-Tariff Barriers

Coates et al argue that there is not enough detail, including on the specific types of NTBs, which countries maintain them, the difference between NTBs and legitimate non-tariff measures, and what proportion of NTBs are assumed removed. Coates also suggest that factors such as the right of foreign banks to challenge New Zealand laws are modelled by Strutt et al as an NTB benefit.

- There is no "correct" method for modelling how reducing NTBs influences trade and GDP. Modelling NTBs is at an earlier lower stage of development than modelling tariffs, as highlighted in the NIA. This was the basis for the Government assuming the contribution to GDP gains from the reduction of non-tariff barriers (NTBs) on goods trade would be less (by half) than that estimated by the Strutt et al.
- We do know that NTBs have a significant impact on trade. UNCTAD and the World Bank research tends to estimate the trade costs of NTBs to be three to four times greater than for tariffs alone. Economics is still coming to terms with NTBs, but New Zealand exporters know that these barriers are significant. New Zealand's

Food and Beverage Exporters Council is in discussions with MFAT on identifying and estimating the trade impact of NTBs on their members' exports.

- Our options were, therefore, to model the impact of NTBs on trade with imperfect data and technique, or to ignore the influence of NTBs. Of these options, asking the modellers to do the best they could with available data and techniques was considered to be more realistic.
- Coates et al are correct that it is difficult to estimate the benefits from reducing NTBs. They claim it may be overstated in the model. It is also possible that the benefits from reducing NTBs are understated.
- Strutt et al point out that they utilise the UN TRAINS database of more than 50 categories of NTB (appendix V, page XVI). To avoid issues related to aggregating NTBs to the stage where they can be analysed in the model Strutt et al use the World Bank overall trade restrictiveness index, which provides estimates for all individual TPP countries other than Malaysia, Singapore, Viet Nam and Brunei.
- Strutt et al did not assume trade benefits in their NTB modelling from enforcing copyright or intellectual property rights or provisions allowing foreign investors to challenge government regulations.
- Strutt et al took account of the fact that many non-tariff measures may be legitimate, i.e. would remain in place once TPP had been implemented. The model did this by assuming non-tariff measures were estimated to reduce to the mean of the TPP region. This is deemed to be a reasonable assumption, that countries with high levels of barriers would see some removed under TPP, but that all countries would continue to have legitimate non-tariff measures in place.
- The NIA undertakes a full analysis of the implications for New Zealand of TPP, including provisions relating to financial services and other areas.

Projections for economic gains in modelling analyses

Coates et al claim that Strutt et al NTB assumptions are not repeated in MFAT commentary on the TPP; provide their own estimates of the benefit to New Zealand from TPP; claim a lack of information on TPP costs (see above commentary on NIA and following comments on ISDS); suggest gains will be slow to materialise and; suggest the Tufts report discussed earlier provides a better estimate of TPP outcomes.

- MFAT do not state the estimated benefit from TPP with "absolute certainty" as claimed by Coates et al. MFAT recognises that modelling results are estimates.
- MFAT reporting is a summary of Strutt et al hence does not include all details. MFAT have made the complete report from Strutt et al available online, with all of the stated assumptions and limitations to modelling.
- Coates et al take a very crude approach to estimating benefits and costs to New Zealand from TPP. In essence, they assume that the only benefit to New Zealand will be from exporters paying lower tariffs, and that there will be no reduction in non-tariff measures, trade facilitation, or liberalisation of trade in services. They also effectively assume that New Zealand exports to the TPP region

will remain static under TPP. This is not New Zealand's experience under previous FTAs.

- There will be some immediate gains as tariffs are reduced on EIF and due to less tangible factors, such as interest in the agreement highlighting TPP market opportunities. Other gains will accrue over the medium to longer term.

Agriculture and Trade rules

Coates et al claim that New Zealand agriculture gains from TPP would be limited, and that the Agreement locks in remaining barriers to trade. They highlight that TPP does not remove domestic subsidies to agriculture production. Coates et al suggest that TPP will make it difficult for New Zealand producers to label their products to highlight factors such as animal welfare.

- The benefits to New Zealand agriculture trade and production in TPP are considerable. Strutt et al estimate that real output will increase in all agriculture sectors other than wool (and no change to "all other crops"). Production of fruit and vegetables, live animals, beef and sheepmeat, other meats, dairy and milk and other food is estimated to expand. Other food output is estimated to increase 1.6%. Production of other meats is forecast to go up by 3.7%.
- Even before considering benefits in a CGE framework there are some significant gains to New Zealand agriculture trade:
 - Japan, New Zealand's third-largest beef export market, will reduce its 38.5% tariff on beef to 9% over 15 years.
 - Japan tariffs on offals will be eliminated over 10–12 years with a 50% cut at entry into force.
 - Mexico will eliminate sheepmeat tariffs
 - Tariffs on cheese will be eliminated in Japan
 - Tariffs on one of New Zealand's highest-traded US cheese lines will be eliminated.
 - Tariffs for milk powders will be eliminated in the US.
 - Tariffs on infant formula will be eliminated in the US, Canada and Mexico.
- These gains are into some extremely wealthy and important markets. Markets where New Zealand has been battling for years to improve access.
- There is no reason to believe that current barriers will be "locked in" (page 4 dot point 10). TPP is to be a living agreement which can evolve to facilitate extension to new trade issues and new countries.
- There is nothing to suggest that TPP will make it "increasingly difficult for the New Zealand dairy and meat sectors to use labelling to differentiate its higher standards of animal welfare, consumer health and food safety" (page 14, Coates et al).

- The United States has been paying subsidies to its farmers for years. TPP is not making these worse, and perhaps opens an avenue to negotiating their removal. The playing field won't be level, but post TPP it will be more level than it has been.

Implications of TPP for New Zealand's value chains

Coates et al claim that TPP benefits will be asymmetric along value chains, with larger foreign companies benefiting at the expense of their smaller New Zealand counterparts, and suggest that TPP will restrict New Zealand companies to exporting raw and low value products only.

- There is absolutely no evidence to support the claim that TPP will prevent New Zealand companies from accessing value chains. The main implication from OECD global value chain (GVC) research is that countries benefit from lowering barriers to trade on both imports and exports. TPP will lower barriers to trade and hence will encourage the development of GVCS in the TPP region.
- The European Union provides evidence of the strong link between low barriers to trade and GVC participation. Trade along GVCs has grown significantly within the EU since the forming of the common market, and GVC trade in the EU is more intense than in any other region. Small countries, such as Denmark, are part of this trade.
- New Zealand firms are actually fairly well positioned in agriculture and Food & Beverage global value chains, and a number of kiwi high tech firms are already demonstrating how to succeed without worrying about scale, distance or thin markets. The challenge is to do more of it, and to seek to increase the returns to New Zealand (growing 'Domestic Value Add'). The research is clear that in policy terms are no 'silver bullets'. It highlights industry institutions, logistics, innovation and standards as areas that policy makers and business could focus on.
- The claim that GVC benefits from TPP will be asymmetric, favouring large overseas companies is unsubstantiated. Small companies are heavily engaged in GVCs, and benefit considerably from this engagement. This is another key finding from the OECD: GVCs provide a means for smaller firms to specialise and engage in international trade – the opposite of Coates et al claims.
- For example, New Zealand firm Tait Communications has a good working relationship with the much larger Airbus. The partnership allows Tait to specialise and introduces the New Zealand company to a much wider range of markets and customers than it would otherwise have access to.
- TPP will reduce the kinds of barriers that disproportionately affect smaller firms; for example making information on domestic regulations and requirements more transparent and simplifying customs procedures. While large firms can generally find their way around such issues, making it easier for smaller firms to operate in TPP markets and cross borders will make it easier for them to link into value chains.

Economic implications of restraints of government power to regulate

Coates et al argue that ISDS is designed to chill government policies, with the uncertainty of claims causing governments not to risk regulations that might upset large foreign companies.

- The possibility of a successful and significant ISDS claim being taken against the New Zealand government is extremely slim. This is addressed in the TPP NIA, Section 4.8. It is not a question for economic modelling.

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