The Regional Comprehensive Economic Partnership (RCEP): Separating Fact from Fiction

By:

Bryan Mercurio

February 9, 2021

The signing of the Regional Comprehensive Economic Partnership (RCEP) at a virtual ceremony on 15 November 2020 has been proclaimed an economic game-changer and a political coup for China which heralds a paradigm shift in trade relations. Both statements are exaggerations. This is not to say that the RCEP is of little to no value or that it should not be helpful to Beijing's greater aims; quite the opposite. The RCEP is a geopolitically strategic agreement which lays the foundation for stronger economic cooperation and growth in the region and will allow China to attain an even stronger foothold in the region. Consisting of the ten member countries of the Association of Southeast Asian Nations (ASEAN) together with five of its free trade agreement (FTAs) partners – China, Japan, South Korea, Australia and New Zealand[1]– the RCEP will be the world's largest trade bloc covering approximately 30% of global economic

output, trade and population. Its negotiation represents a significant accomplishment – completed at a time of rising protectionist sentiment and economic nationalism across the globe – and one that should not be easily dismissed.

The Economics

The RCEP signatories are already well linked, integrated and supported by several FTAs. China is the hub, serving as the largest or second-largest trading partner for all other RCEP signatories. Japan also has significant trade and investment ties to all other signatories. Computer simulations recently published by Plummer and Petri estimate that the RCEP could add $186 billion annually to world incomes and nearly $400 billion to world trade by 2030, but it must be noted that 90 percent of the income gains and 88 percent of the trade will accrue to China, South Korea, and Japan.[2] This is simply the result of these three large trading nations not having an existing FTA between and among each other.

Although the RCEP contains less liberalisation and more exceptions and carve-outs than the mega-regional Comprehensive and Progressive Trans-Pacific Partnership (CPTPP) and other "gold standard" agreements, there is economic value in the attempt to consolidate the separate existing agreements into one larger agreement. This is particularly the case for niche products and between certain partner countries in the agreement. Exporters and importers will be wise to comb the details of the agreement to find where opportunities exist. The benefits accruing from the RCEP are likely to be incremental, however, as tariffs on most trade flows between the countries are fairly low and most RCEP tariff reductions are staggered over a ten-year period. That, combined with the fact that no country has yet ratified the agreement, should temper any discussion about the RCEP as an immediate game changer.

Perhaps the largest economic gains will come from the attempt to harmonise the rules of origin (RoO), which allow a product produced in one country to qualify as an RCEP product even if it contains inputs and materials from other RCEP-partner countries. This, along with improvements to transparency, customs facilitation and reduction of red tape, will boost the region's supply

chain efficiency. These benefits should not be overstated, however, as the agreement's limited tariff reductions means the gains experienced in the United States, Canada and Mexico following the harmonisation of RoO in the North American Free Trade Agreement (NAFTA) will not be immediately emulated. This is to say, while the NAFTA resulted in little to no tariffs on hundreds of key products and led to integrated supply chains in countless sectors, it simply cannot be repeated in the RCEP owing to the high level of tariff and non-tariff barriers remaining in place.

The limited nature of trade liberalization is understandable, as the signatories were not only mindful of the varying economic developmental levels between negotiating countries but also to political sensitivities. With several least developed countries lacking infrastructure and know-how, the RCEP was therefore never going to be a cutting-edge agreement. And as is always the case with ASEAN, pragmatism trumped ambition the negotiations took the form of the lowest common denominator. Thus the RCEP is also not so ambitious in regards to chapters such as agriculture, intellectual property and e-commerce, while it is essentially silent on issues of contemporary importance such as the environment, labour, industrial subsidies and state-owned enterprises.

In short, the RCEP offers limited incentives to further integrate supply chains across Southeast Asia but should better integrate Northeast Asia, thus providing tangible indirect benefits for the Southeast. There are opportunities for further gains should the parties wish to upgrade the agreement at some point in the future, in particular through further liberalisation of investment, trade in services, electronic commerce, competition, agriculture and through enhanced consolidation of existing agreements.

China's Agreement?

More significant than trade liberalisation is the RCEP's geopolitical statement. Initial commentary from the West has mostly misread the signal, with narratives that the RCEP is a huge economic and political win for China, that the RCEP was a China-led initiative to counter the TPP, and that the agreement provides further evidence of a rising China and a global geopolitical shift – all of which misrepresent the reality of the agreement and overstate reality.

The often-repeated line of “ASEAN centrality” in the RCEP is not merely a slogan – it was ASEAN who initiated discussions and shepherded partner countries with vastly different economic profiles throughout the eight years of negotiations. It was this effort that concluded with an agreement containing China, Japan, and South Korea, all while the tripartite negotiations between those three powers foundered and ground to a halt due to political differences. It is also worth highlighting that while an active party in the negotiations, China’s focus remained on the traditional issues of tariff liberalisation and market access for goods. Countries such as Australia and Japan played a critical role in advancing chapters such as services, investment and e-commerce, and in shaping the text of every chapter of the agreement. It is also worth highlighting that China’s effort to prioritise the RCEP negotiations and quickly conclude the agreement in the wake of the US withdrawal from the TPP was met with significant resistance and ended in failure. Finally, it is a mistake to cast the RCEP as China’s counter to the US led (and abandoned) TPP, since in reality there was not a choice of “us vs them” and seven countries are signatories to both agreements.

China clearly benefits from the RCEP, in that its can increase its (already large) presence and geopolitical influence in the region. There is also symbolic value, as the RCEP is also China’s largest multilateral negotiation since its accession to the World Trade Organization. That being said, China did not use the RCEP negotiations to assert its power or attempt to reconfigure the trade architecture – in fact, in many ways China remained comfortable in its role of ‘rule taker’. As such, the RCEP was not an attempt by China to establish itself as the region’s ‘rule-maker’. Chinese exports will find a clearer path into RCEP supply chains and markets and outward investment into RCEP countries will be eased, thus allowing China to exert more influence on the region as others come more closely within its economic orbit. With China accounting for nearly half of RCEP’s GDP, closer integration will go some way in countering any economic ‘decoupling’ coming from the West.

United States (again) on the sideline

Washington has been universally deemed to be the loser as RCEP was conceptualised, negotiated and completed without a US presence. Given the importance to the US as hegemon to continue influencing if not driving the trade agenda, the US certainly appears to have lost some regional influence. This follows President Trump's withdrawal from the TPP, and with it the dismantling of the centrepiece of President Obama's much-trumpeted 'Pivot to Asia'. American influence was further diminished as the other eleven negotiating parties to the TPP did not allow the agreement to collapse but rather temporarily removed several provisions key to US interests and proceeded to sign the re-shaped agreement (in the form of the CPTPP).

American exporters may also face losses, or slower growth in the region than they would have done if not for the RCEP, as barriers to trade between the RCEP countries are (slowly) removed over time. However, this point should not be overplayed as US multinational companies are heavily invested in the region and will also benefit from the more integrated value chains which the removal of barriers should bring about. Indirect benefits to American workers and consumers could follow with the arrival of cheaper inputs and goods.

The negotiation and completion of the RCEP demonstrates that the region does not need US leadership (or participation) to come together and make advances in the trade architecture and agenda. While this is not the death knell for the US, it should serve as a wake-up call to Washington that it needs to be doing more to retain its sphere of geopolitical and economic influence. With President-elect Biden likely be occupied with domestic issues for the foreseeable future – and appearing set to continue with Trumpian-like nationalism – swift action on regional trade appears unlikely. This is unfortunate, as the fast-growing and dynamic region is rapidly changing and although historically most signatory countries are loyal allies with Washington this may not be the case in the future with sufficient care and attention being paid to their needs.

Signed, sealed and…

While the RCEP is signed and sealed, it is not quite delivered. The pact will come into force when at least six ASEAN members and three other signatories

ratify the agreement. This is expected before 1 January 2022, as for some signatories, ratification is but a mere formality (e.g. – China, Vietnam, Singapore, Brunei, Laos, Cambodia and Myanmar).

For others, however, ratification may be delayed. Malaysia and Thailand are examples of the latter, as both are experiencing political turmoil and appear hesitant to embrace the changes necessary for liberalisation – Malaysia has signed but not ratified the CPTPP and enthusiasm for Thailand joining that agreement has waned. Australia is another country where ratification may be delayed, not only due to the procedural hurdles of the Australian system but also now due to its trade and diplomatic dispute with China. China-related issues may also become problematic in Japan, Korea and New Zealand. The celebration of regional unity may abruptly end if ratification is delayed in more than a handful of periphery countries.

---

[1] Concerned about the effect of increased imports from China on domestic manufacturing and general reticence to freer trade, India withdrew from the negotiations after participating in the first 28 (of 31) rounds.

[2] The study estimated that India's participation in the agreement would boost gains by 25 percent, with most of those gains flowing to India and very little to other RCEP countries. This indicates that the RCEP would have been most beneficial to Indian industry as they would increase efficiency and become better integrated in global supply chains.

View online: The Regional Comprehensive Economic Partnership (RCEP): Separating Fact from Fiction

Provided by Afronomicslaw