



NEW ASIA-PACIFIC TRADE DEAL

Implications for East Asia and globalisation



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Abstract

The conclusion of a new overarching Regional Comprehensive Economic Partnership (RCEP) Free Trade Agreement (FTA) between 15 Asia-Pacific countries has been celebrated across the globe. Its signatories are the 10 members of the Association of Southeast Asian Nations (ASEAN) countries and Japan, Korea, China, Australia and New Zealand; India withdrew from the agreement at the last moment.

The signing of the RCEP is certainly good news for world trade and investment. It brings together a group of countries representing 30% of the global population and generating 29% of its GDP. It aims to facilitate and solidify global value chains; accept opening-up in terms of tariffs (while aiming to discipline non-tariff barriers); build a legal framework for services, trade, and investment; and address e-commerce issues such as the commitment not to impose data localisation. Much like the EU-Canada Comprehensive Economic and Trade Agreement (CETA), the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) (an FTA between 11 APEC countries, without the US), and the EU/Japan Economic Partnership Agreement (EPA), the RCEP demonstrates once again that the US under the Trump administration was effectively alone in its attempts to disrupt further globalisation. Nevertheless, the RCEP is not a deep FTA and stipulates slow liberalisation over long periods of time, among its other peculiarities. It may also impact East Asian regionalism in the long term.

This paper explains the Association of Southeast Asian Nations (ASEAN)-led origin of the RCEP in the context of APEC,¹ summarises the substance of the agreement, and gives an inevitably crude first estimate of its impact on trade and overall income, as well as its structural implications. It concludes with reflections on the possible long-term implications of the RCEP for East Asian regionalism, for world trade and investment, and for the European Union.

¹ Asia-Pacific Economic Cooperation, 21 countries from East Asia and Australasia, as well as from North and South America.

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List of Abbreviations

AEC ASEAN Economic Community
AFTA ASEAN Free Trade Area
APEC Asia-Pacific Economic Cooperation, 21 countries from East Asia and Australasia,
as well as from North and South America
ASEAN Association of Southeast Asian Nations
CAI Comprehensive Agreement on Investment
CETA Comprehensive Economic and Trade Agreement
CPTPP Comprehensive and Progressive Agreement for Trans-Pacific Partnership
EPA Economic Partnership Agreement
FTA Free Trade Agreement
GATS General Agreement on Trade in Services
GVCs global value chains
MRA mutual recognition agreement
NAFTA North American Free Trade Agreement
RCEP Regional Comprehensive Economic Partnership
ROO rules of origin
SOEs State-owned Enterprises
SPS Sanitary and Phytosanitary Measures
TBT Technical Barriers to Trade
TPP Trans-Pacific Partnership
TRIPs Agreement on Trade-Related Aspects of Intellectual Property Rights
WTO World Trade Organisation

1. The RCEP as the latest child of APEC

The RCEP is the second big follow-up to APEC's original goal to pursue "concerted unilateral liberalisation" and "open regionalism" as methods of liberalisation of trade and investment without binding treaties.² While APEC's stimulus ultimately proved to be short-lived, it did successfully remove some of the fears held by its Asian signatories around hard commitments in trade and investment, aided by the inauguration of the World Trade Organisation (WTO) in 1995, to which China gained membership in 2001. In 1992, ASEAN initiated the ASEAN Free Trade Area (AFTA) in a move that proved much less controversial and more beneficial than first expected. Emboldened by AFTA's success, in 2003 it initiated an ASEAN Economic Community (AEC), with the longer-term option of creating a single market.³ Moreover, despite not having a common trade policy (as it is itself an FTA), ASEAN consulted with its 'dialogue partners' to explore interest in concluding FTAs. What became the ASEAN Plus Six culminated in FTAs between the ASEAN-10 and each one of six partners: Japan, Korea, China, India, Australia, and New Zealand. Establishing FTAs with the Six was especially significant in terms of tariffs and customs facilitation critical to value chains. How important this was for ASEAN might be better appreciated if one realises that – even with AFTA – trade and investment for ASEAN countries was predominantly with OECD⁴ markets, and later on with China and India, with intra-ASEAN transactions only gradually taking on greater importance.

At the same time, APEC had weakened to the point of no longer providing a forum for truly joint trade liberalisation. North America had its North American Free Trade Agreement (NAFTA) and FTAs with APEC members Peru and Chile. The US was however concerned by the rapid rise of China, with the Obama administration pursuing more aggressively a 'pivot to Asia' In 2012, the US joined an initiative of deeper trade liberalisation which, by 2016, developed into the Trans-Pacific Partnership (TPP) agreement between 12 APEC countries, with the deliberate exclusion of China. APEC now comprised two trade initiatives, one ASEAN-led with no less than six partners, and the emergent, relatively 'deep' TPP agreement without China or the ASEAN-10. The evolving ASEAN Plus Six FTAs were replete with complex rules of origin (ROO) between parties.⁵ Moreover, as ASEAN is not a customs union with a common trade policy, all ASEAN countries concluded their own versions of bilateral FTAs with each of the six partners. The result was considered so problematic that an APEC business conference in Seoul a decade ago, prior to the APEC summit, collectively called for a common East Asian arrangement around rules of origin, in order to support value chains.

Both the RCEP and TPP negotiations (following the involvement of the US) began in earnest in 2012. The TPP treaty was concluded in 2016 but in 2017 President Trump withdrew the US and the 11 remaining countries slightly modified the treaty, renaming it CPTPP. Table 1 lists the countries in RCEP and the CPTPP. The RCEP, concluded on 15 November 2020, is the result of

² For a detailed and careful review, see De Dios (1998).

³ For an extensive analysis of the AEC, see Pelkmans (2016).

⁴ Organisation for Economic Cooperation and Development (33 developed countries)

⁵ Between parties and not to ASEAN directly, for which the six FTAs would usually simplify matters.

a strong desire to consolidate and simplify the ASEAN Plus Six process, while incorporating a number of further additions. One test of the value of the new RCEP is therefore what impact it has on reducing the existing complexity of origin rules and the facilitation of value chains.

2. What is the RCEP?

RCEP is a massive treaty in the sense that the 15 countries (indeed, even the ASEAN-10, to some degree) often have their own liberalisation or market access schedules as well as a host of schedules about services and investment. (Remember that ASEAN countries have their own trade policies, despite ASEAN's common strategy vis-à-vis the RCEP partners). The following cannot be more than indicative, at best, of the substance of RCEP.

Table 1. Membership of CPTTP and RCEP; ASEAN members = AS

CPTTP	ASEAN members	RCEP	ASEAN members
Australia		Australia	
Brunei Darussalam	(AS)	Brunei Darussalam	(AS)
		Cambodia	(AS)
Canada			
Chile			
		China	
		Indonesia	(AS)
Japan		Japan	
		Laos	(AS)
Malaysia	(AS)	Malaysia	(AS)
Mexico			
		Myanmar	(AS)
New Zealand		New Zealand	
Peru			
		Philippines	(AS)
Singapore	(AS)	Singapore	(AS)
		South Korea	
		Thailand	(AS)
Vietnam	(AS)	Vietnam	(AS)

Source: author.

The RCEP has 20 chapters⁶ comprising goods, unified rules of origin, customs procedures and trade facilitation, SPS and Technical Barriers to Trade (TBT),⁷ trade remedies, services (with 3 sectoral annexes),⁸ the General Agreement on Trade in Services (GATS) mode-4 services (the temporary movement of natural persons, mostly in reference to business representatives but

⁶ All texts can be downloaded via www.rcepsec.org/legal-text/ and annexes via ZIP files.

⁷ The precise heading of this chapter is Standards, Technical regulations and Conformity Assessment Procedures.

⁸ On financial services, telecoms services and professionals ones respectively.

also spouses with a short stay of a few years), investment, intellectual property, electronic commerce, competition,⁹ small and medium sized enterprises (SMEs), Economic and Technical Cooperation, government procurement, dispute settlement¹⁰ as well as institutional, general and final provision chapters.

The most basic drive behind the RCEP is to adapt and simplify the application of rules of origin. This has been achieved, including the right for business originating in the RCEP area to claim cumulation of origin (often called diagonal cumulation in the EU). A hypothetical case illustrates the point. Suppose an Australian producer of intermediate goods exports these goods to RCEP countries X and Y. When in country Y, the final good incorporating the Australian input is exported to X, the RCEP tariff preferences will also apply to the Australian input. This may appear complex but reflects how regional and global value chains [GVCs] operate. When GVCs are the leading business model – as is the case in East Asia – this cumulation matters a lot. In addition, cumulation might, in the margin, attract more foreign direct investment (FDI) hoping to exploit its benefits.

At the moment, it is unclear how much RCEP exporters will benefit in the short term given that some liberalisation schedules are extremely slow (up to 20 years). There is already considerable concern that a number of the parliaments in ASEAN countries and possibly Australia will prove unreceptive to trade and investment arguments, because anti-Chinese sentiment or the fear of competing with an influx of Chinese goods might prevail.¹¹ The final result of trade liberalisation will thus be diverse and country-specific. The Australian government claims that no less than 89% of current Australian exports to the region will benefit from immediate duty-free access. Japan claims that 86% of goods exported to China will see tariffs eliminated (with no exact timing indicated, but significantly higher than the current 8%), 81% for exports to Korea and 88% to ASEAN. On the face of it, these shares seem high, but a general rule of thumb for FTAs is that shares should be above 90% before hitting the sensitive subsectors where the true gains in market access come into play. In other words, selective estimates can be (too) suggestive or even misleading. In farm products, liberalisation is considerable but it is not surprising that Japan has insisted on the exclusion of five products: rice, wheat, dairy, sugar, beef, and pork. On non-tariff barriers, only cooperation and transparency is in.

On services, the RCEP is mainly concerned with the lock-in of existing regulatory provisions in RCEP countries. Surprisingly, negative listing has been adopted to this end, a method typically

⁹ With 4 annexes for countries without much, if any, tradition in this respect: Myanmar, Lao, Brunei and Cambodia. The AEC does however comprise a joint cooperative framework for domestic competition policies.

¹⁰ Although dispute settlement is a standard tool in the WTO, and applies to TBT and SPS questions as well, in the RCEP, dispute settlement does not apply to these two chapters. This might be due to old sensitivities in ASEAN about dispute settlement in its own AFTA. See Pelkmans (2016), pp. 84-5.

¹¹ An example from the recent past is telling. When the Indonesian-China FTA (under the ASEAN umbrella FTA with China) was concluded a decade ago, it generated a groundswell of opposition, especially amongst SMEs in Indonesia. The upshot was that the Indonesian Trade Minister at the time, Dr. Mari Pangestu, had to resign (and subsequently became Tourism Minister).

regarded as pro-liberalisation. The chapter does go further in sectoral issues such as e-commerce where (sensitive) data localisation obligations are prohibited (except in the case of national security, leaving open the question of how China will interpret the rules). Commitments on professional services (country by country), education services, healthcare services and a series of “other business services” will improve access (with a ratchet effect) and new commitments have been undertaken, again by country (e.g. China on transport). While investment protection is in the treaty, some RCEP members already have bilateral investment treaties (BITs) with each other, so the overall picture of progress is disparate. Interestingly, the non-inclusion of the Investor-State Dispute Settlement (ISDS) will be reviewed in two years; an opportunity for the EU to promote the multilateral court approach it advocates. In financial services (with the usual carve-out for financial stability), transparency improvements are non-trivial. In telecoms the conventional approach (e.g. the WTO telecoms paper of 1998, co-sponsored by the EU) has been adopted, including “reasonable roaming rates.” On mode-4, the temporary movement of business persons, the RCEP comes close to CETA, which is remarkable in itself but also in light of the AEC, which has only highly prudent openings via MRAs.¹²

As concerns intellectual property, it is held that the RCEP will complement the WTO TRIPs Agreement¹³ e.g. on the basis of due process mechanisms to support the granting of geographical indications. But little more. Finally, the chapter on government procurement is only about transparency and “cooperation” and does not (at least not yet) move towards the regime in the WTO plurilateral Government Procurement Agreement (GPA). When joining the WTO, China signed the Accession Protocol in which it promised to join the GPA. But it never did so, despite having submitted seven separate offers, which were judged insufficient by GPA partners.¹⁴ However, it is the first time that China has signed an FTA with a chapter on public purchasing.

Overall, the RCEP cannot be considered a progressive treaty from an EU point of view. Adopting an EU-lens however may not be the most appropriate way to consider the RCEP. A number of its signatories have been pulled into a significantly more transparent and open trade and investment environment. Moreover, this treaty incorporates expectations of further deepening and widening in scope.

That the RCEP is built on existing FTAs with the ASEAN, but of course also on AFTA and the AEC, must be kept in mind. Even though technically the RCEP comprises welcome administrative and customs improvements as well as considerable trade facilitation for GVCs, concurrent policy in terms of additional market access remains limited for ASEAN (as the hub) and via the ‘spokes’ with ASEAN-partners. It is still worthwhile, however, as ASEAN is keen to attract and maintain FDI as part of value chains and the facilitation of trade via the spokes is precisely one of its

¹² See Pelkmans (2016), pp. 136-7. MRA = mutual recognition agreement, referring to negotiated recognition under certain conditions limited to specific professions here.

¹³ TRIPs stands for Agreement on Trade-Related Aspects of Intellectual Property Rights.

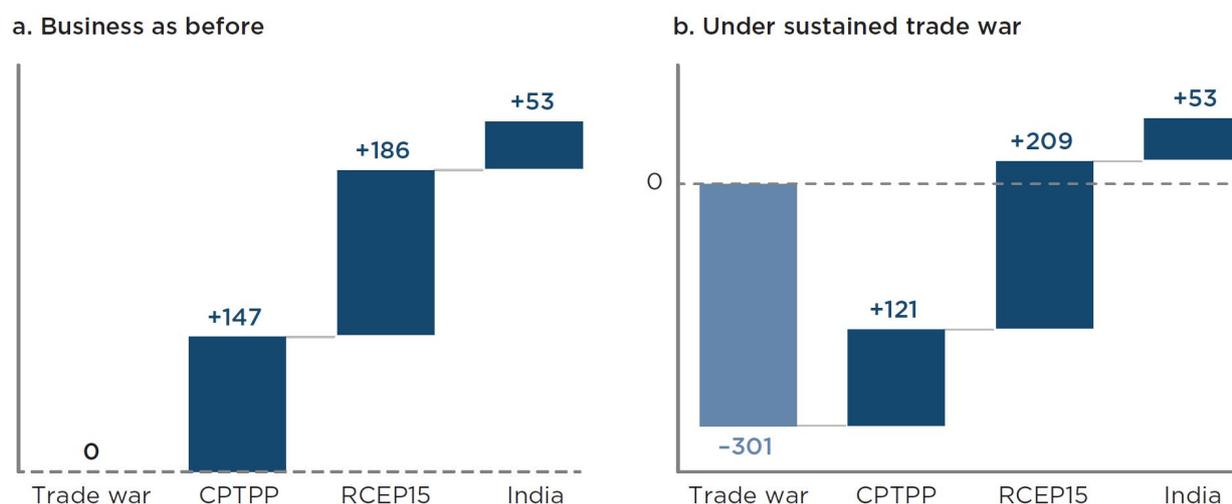
¹⁴ For an extensive analysis, including the first six offers, see chapter 12, Pelkmans, Hu, Francois et al., (2018).

objectives. However, larger trade and economic effects should be expected *between* the spokes, that is, trade and FDI directly between the partners of the ASEAN.

3. Trade and economic impact of RCEP, a first estimate

There have been several attempts to estimate the trade and economic effects of RCEP.¹⁵ A recent attempt by two seasoned empirical trade economists, Petri & Plummer (2020) familiar with Asia-Pacific and ASEAN trade initiatives, work with a sophisticated CGE model.¹⁶ Due to the simultaneity of the China/US trade war and the conclusion of the RCEP (in 2020) and of CPTPP (in 2018), so important for trans-Pacific trade, the authors simulate income and trade effects of the trade war and compare them with the simulated effects of the two trade initiatives. The income effects of both are juxtaposed in Figure 1.

Figure 1. Global income effects of Asia-Pacific trade policies in 2030 (income gains/losses in billions of US dollars)



CPTPP = Comprehensive and Progressive Agreement for Trans-Pacific Partnership
RCEP = Regional Comprehensive Economic Partnership

Note: “Business as before” assumes a return to a pre-trade war path; “Sustained trade war” assumes path defined by post-phase one tariffs. Bars show incremental effects of adding each policy to all previous policies. The policy denoted “India” involves adding India to the RCEP15 agreement to form RCEP16.

Source: Petri & Plummer (2020), p. 4.

¹⁵ See for example Itakura & Lee (2019) and Mahadevan & Nugroho (2019).

¹⁶ For a basic overview, see Appendix A of Petri & Plummer (2020). Technical details are found in www.asiapacifictrade.org and in Petri, Plummer & Zhai (2012). For trade economists, the authors work with heterogeneous firms (a la Melitz) and a nested production process in the model which – importantly – allows for intermediate inputs, reflecting the GVCs. Note that, at the time of their writing, the literal text of RCEP was not available but all the basics from the core chapters had been leaked or provided in press releases. The stylised trade liberalisation changes in RCEP are specified in their Table 2. These changes are rather basic and employ general averages, implying that the estimates are therefore rather crude.

Normally, such estimates would amount to what is shown in the left panel of Figure 1. RCEP-15 would generate some \$186bn in additional income. In the right-hand panel (under sustained trade war), the starting point is a loss of \$301bn but the two trade initiatives compensate with their benefits: CPTPP makes \$121bn and RCEP-15 considerably more at \$209bn. The incremental value of the CPTPP is \$26bn less under the trade war as compared to the incremental value of the RCEP-15 with an increase of \$23bn, because China benefits from trade switching.¹⁷ Nevertheless, in a business-before-Trump ('as usual') scenario, the overall income gains of RCEP-15 amounting to \$186bn is not high given the enormous relative size of the group in terms of GDP and of population. The three reasons for these limited simulated gains are that i) ASEAN intra trade is barely affected, ii) trade over the ASEAN-partner spokes is facilitated and stimulated via cumulation, but tariff concessions are few (mostly already made before in FTAs), and iii) NTBs have not been addressed in earnest (Petri & Plummer assume a stylised 10% lower trading costs).

Turning to trade flows, world trade due to RCEP¹⁸ would augment by \$504bn. The large bulk of this increase is enjoyed by China (\$236bn) and Japan & Korea (together \$193bn), leaving only \$56bn for the other 12 RCEP countries and a relatively pitiful \$4bn for the US and a meagre \$14bn for the rest of the world. However, those 14bn are generated largely by interaction by outsiders with RCEP countries – when focusing only on trade between non-RCEP countries, there is a *fall* of some \$39 bn-\$48bn. This is likely to reflect trade diversion. The biggest winner in this simulation is China. Given that China has better market access to the four non-ASEAN countries of RCEP, this is hardly surprising. That is also why China was in favour of the RCEP from the outset. The positive income effect of RCEP for China is \$100bn and the sectoral export effects are all positive for five categories,¹⁹ ranging between 4.4%-8.8%. For Europe, a very small benefit for the CPTPP (\$8bn) compares with an even smaller but negative impact of RCEP on EU exports of \$4bn. The EU should therefore consider whether the sole focus on separate FTAs with countries in the region would suffice. Some form of linkage with both initiatives makes both trade and economic sense.

Finally, it ought to be mentioned that FDI effects are hard to model and even harder to include in these types of models. The positive expectations about FDI induced by the RCEP are therefore based on typical business reasoning.

¹⁷ India seems to shoot itself in the foot. It forgoes some \$53 bn income increase, but will lose \$6 bn by staying out of RCEP, a difference of \$60 bn. On the other hand, going by the stylised differences used in the model (in their Table 2), with India in, overall tariff liberalisation in RCEP as well as agricultural liberalisation in particular would have been *lower*. This is exactly why India slowed down the negotiations for years, and still exited. Although the overall effects of RCEP on Europe are tiny, Europe might expect a net income benefit of \$13 bn due to RCEP15, but a loss of \$1 bn under RCEP16!

¹⁸ Under 'business before Trump scenario', and with CPTPP also being implemented (as is indeed happening).

¹⁹ They are: raw materials, light manufactures, advanced manufactures, domestic services and traded services.

4. What does the RCEP imply for global and EU trade strategies?

It is too early for a full assessment of this question, but it is possible to highlight some features and offer broad policy recommendations.

First, the US and various European news media have announced the RCEP as comprising a grouping of China and 14 other countries, with suggestions or assertions that China has led this process. This interpretation is mistaken, based perhaps on a foreign policy perspective common, in particular in the US concerning China's more dominant role. The process leading to the RCEP was ASEAN-led from the beginning and these countries were heavily involved in ensuring positive momentum. It is not at all clear what would have resulted if the process had been fundamentally China-led over the more than eight years involved, although China did provide strong initial support, if only because of expected benefits. It is also likely that the upshot of India not joining the RCEP and the US being absent in both FTAs has effectively led to a clearer East Asian economic regionalism (if one considers Australasia as part of East Asia, which is the preferred perception among the countries involved). Since China now has market access to 14 other countries in the region – with the greatest access gains in 4 non-ASEAN developed countries, one can expect a boost to regional value chains and, with it, a more prominent trade and investment role for China.

Second, RCEP sends a strong signal that East Asia does not seek more trade protection, let alone intend to threaten trade wars, but aims for steady progress and greater openness for trade and investment in the region. Ministerial statements published on November 15th proudly announce the liberalisation accomplishment and underline the commitment to responsible globalisation by the participating countries – this message has now become more credible for Europe and will hopefully be heard in the US. However, India's withdrawal has been widely interpreted as a sign of weakness (yet again) when it comes to more trade liberalisation. It is true that the RCEP negotiations were considerably lengthened in an attempt to accommodate India's concerns, not least over Chinese competition negatively affecting its industry, and India's insistence on continued protection of its poorly developed agricultural sector. It is debatable whether with a more modest treaty, including long periods of tariff liberalisation and targeted exceptions, India might still have joined but, by not joining, it appears to have also foregone significant opportunities, as discussed.

Third, the legacy of APEC is now fragmented in complex ways, with the Comprehensive and Progressive Agreement for TPP involving 11 countries, but without the US or China and only 4 ASEAN countries, and the RCEP involving 15 countries, also without the US, but with a considerable (and uneven) overlap with the CPTPP (with China included in the RCEP as well as South Korea, which is not in CPTPP).²⁰

²⁰ The principal reason for not joining CPTPP by South Korea at the time was that it already had agreed FTAs with the US and the EU.

The obvious query is whether the two FTAs can be brought together, in particular because the absence of China from the CPTPP weakens the credibility of that treaty. Informal talks on China joining the CPTPP have not yielded positive results. The CPTPP is noteworthy for its ambitious chapter concerning the role of State-Owned Enterprises and its more extensive commitments in some other respects. On the whole, it is regarded as a 'deeper' FTA. Since seven countries are a member of both FTAs, of which one is Vietnam (with an SOE issue too), there does not appear to be any serious obstacle to China also joining the CPTPP. It is worth noting that Japan, China and South Korea have been negotiating over 16 rounds and for more than six years to form a three-way FTA without success. Via the RCEP, their aims now appear to have been achieved to a considerable extent.

The EU could reach out to East Asia via the RCEP and explore how coalition possibilities to promote responsible globalisation could be forged, in informal or even formal ways. The RCEP might also help to reinvigorate the EU FTA talks with several ASEAN countries, which are presently deadlocked. More generally, however, it is striking that debates about the two FTAs in the region and their connection with the US/China trade war are conducted without any reference to the EU. One wonders whether this has been realised in the EU. It would serve the interests of the EU to retain, if not deepen and widen, its FTA-based approach with a series of East Asian countries, while working with China on trade and investment still more determinedly, given the possible longer-run implications of the RCEP in terms of East Asian economic regionalism.

While the EU has misgivings concerning China, that is equally the case for most East Asian countries, yet these countries have managed to establish and maintain a balanced and rewarding trade relationship through FTAs. Furthermore, ASEAN is steadily deepening its AEC, with a similar economic objective; namely to make ASEAN attractive for GVCs, preferably in the higher value-added sectors. Therefore, even if there are varying European views on the extensiveness or otherwise of the RCEP, that treaty clearly has implications worth considering. The economic gains are likely to be genuine, though not huge, and its long-term effects in East Asia may lead to particular developments in the structure of trade and FDI (and hence GVCs), with more leadership for China. For the EU, these scenarios underscore once more the importance of successfully concluding the CAI (Comprehensive Agreement on Investment), to facilitate engagement with East Asian production networks.

Finally, the EU should consider establishing more direct links with both the CPTPP and the RCEP, despite the EU not being an APEC member. While the EU is a member of ASEM, ASEM has refrained from holding meetings of trade ministers since 2005. Perhaps the ministerial consultations that ASEAN regularly organises with its partners, including the EU, might provide an informal but practical means to explore such links, especially with ASEAN likely to be more open to discussion, given its achievement in developing the RCEP.

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