SEA View

RCEP – bigger, but is it better? Taking Stock of Asia's new free trade agreement

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After eight years of negotiation, the Regional Comprehensive Economic Partnership on Trade (RCEP), the world's largest regional trade agreement, was signed in an online ceremony on 15 November 2020. The trade deal lowers tariffs, expands services trade, harmonizes rules of origin, and promotes regional trade.

However, few see it as being as comprehensive as other free trade agreements (FTAs) and it is frequently compared unfavorably to the more ambitious coverage of the other big Asian trade agreement, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP).

So is RCEP the way of the future for intra-Asian trade? Or much ado about nothing? We explore what exactly is in the thousands of pages of the agreement below.

Who's in?

RCEP members include the entire Association of Southeast Asian Nations (ASEAN) (Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Thailand, Vietnam, and Singapore) as well as Australia, China, Japan, South Korea, and New Zealand. The agreement's signing came about this year because India, which had become a significant roadblock to finalizing RCEP, dropped out.

The member countries cover 30 percent of the world's population (2.2 billion people), with a combined gross domestic product (GDP) of US$38 trillion, about a third of global GDP. RCEP is expected to stimulate regional Asian trade that could offset some of the U.S.-China trade war losses. The Brookings Institution has estimated RCEP will add US$209 billion a year to world incomes and US$500 billion to world trade by 2030[1]. The goal is for the agreement to enter into force by 1 January 2022, although some members are pushing for this to happen sooner.

Tariff reductions

RCEP will eliminate more than 90 percent of regional tariffs within 20 years of coming into force. Tariff reductions are more limited in coverage than those under CPTPP and other "gold standard" FTAs. RCEP appears to cover about 90 percent of tariff lines, whereas CPTPP covers around 99

[1] RCEP: A new trade agreement that will shape global economics and politics – Peter A. Petri and Michael Plummer, Brookings Institution, 16 November 2020

percent. RCEP excludes from tariff reductions import-sensitive agricultural products and has long transition periods for other politically sensitive tariffs.

Tariffs are likely to vary as well across the members, as some members (Australia, Brunei, Cambodia, Laos, Malaysia, Myanmar, New Zealand, Singapore, Thailand, and Vietnam) will calculate their tariff reductions by the calendar year, while other members will phase out their tariffs on 12-month periods starting 1 April. This discrepancy means the tariffs on goods from one member into a market may differ from those for another RCEP member until all tariff reductions are fully phased in.

However, RCEP will still make significant tariff reductions to important industries in the region. The percentage of tariff-free goods exported from Japan to China, for example, will jump from 8 percent to 86 percent, with almost 90 percent of auto parts exported to China entering duty-free. Japan will keep tariffs on farm products, such as rice and wheat, but will abolish tariffs on 56 percent of agricultural products imported from China and 61 percent on items imported from ASEAN countries as a whole.

Semiconductors and other technology products will also see tariff reductions. While many semiconductor and technology products are already duty-free under the World Trade Organization (WTO) Information Technology Agreements (ITAs), RCEP covers countries that are not listed as ITA signatories by the WTO: Brunei, Cambodia, Laos, and Myanmar.

Moreover, the agreement represents the first time China, Japan, and South Korea have entered a free trade agreement. These countries represent the largest, second-largest, and fourth-largest economies in the region, respectively. In a joint statement, the bloc members said the deal "will play an important role in building the nation's resilience through an inclusive and sustainable post-pandemic economic recovery process."

Services trade and e-commerce

RCEP is expected to boost intra-regional trade in services, including commitments that will allow businesses to deliver cross-border services such as education, engineering, and back-office processing.

The services obligations are a mixture of "positive list" (Cambodia, China, Laos, Myanmar, New Zealand, Philippines, Thailand, and Vietnam) and "negative list" (Australia, Brunei, Indonesia, Japan, Korea, Malaysia, and Singapore). This divided approach means it is unclear how much trade in services will be increased under the agreement.

RCEP contains provisions limiting governments' ability to require the localization of data as a condition for doing business in the member country. It does not include provisions preventing all mandated data localization requirements and limits on data transfers.

These provisions expand existing rules under the ASEAN-Australia-New Zealand Free Trade Agreement and update the e-commerce regulations for certain RCEP parties. It also contains more specific rules for e-commerce, such as rules limiting spam email.

Rules of origin

One of the most important benefits of RCEP is the new standardized rules of origin. Once fully implemented, products manufactured to RCEP criteria can be transported to all member countries using a single certificate of origin.

The harmonized rules of origin mean that companies will no longer need to confirm and accommodate information requirements and local content standards specific to each country.

RCEP has a 40 percent regional value content requirement, meaning that you need 40 percent of the product to be produced in the RCEP region to qualify. It also allows a change in tariff heading at the four-digit level to meet the RCEP origination criteria.

By contrast, the United States-Mexico-Canada Agreement generally has a 60 percent regional value content. The harmonized rules of origin and lower regional value content could mean more and flexible trade. Rules of origin costs can range between 1.4 percent and 5.9 percent of export transaction amounts, which means that exports could be boosted by as much as US$90 billion on average annually.

Intellectual property

RCEP contains separate provisions for the protection of a wide array of intellectual property (IP) rights, including copyright protections for authors, performers, musicians, patents, provisions protecting broadcasters, protections for broadcasts, electronics rights management, trademarks, and traditional knowledge and folklore.

RCEP also has provisions promoting transparency and due process for the identification, protection, and use of geographical indicators for all members.

As part of RCEP, member countries commit to ratifying seven international IP treaties, raising and harmonizing IP protection and enforcement standards. RCEP requires national treatment to all parties to RCEP, subject to exceptions in the Agreement on Trade-Related Aspects of Intellectual Property Rights.

Trade facilitation

RCEP promises a new set of rules and procedures for accessing preferential tariffs in any member country, improved mechanisms for addressing non-tariff barriers, including customs procedures, quarantine, and technical standards, and a common set of rules on intellectual property, trade, and e-commerce.

There are also provisions promoting the digitization of trade documentation, electronic signatures, and other electronic authentication to facilitate cross-border trade. Members will benefit from simplified customs procedures and enhanced trade facilitation provisions, allowing for the rapid transit of urgent deliveries and perishable goods.

Effects on U.S. trade in the region

The United States has been mainly on the sidelines of trans-pacific free trade agreement negotiations following President Trump's withdrawal from the Trans-Pacific Partnership upon taking office in 2017. One consequence of RCEP is that it brings many of the key Asian economies together in a regional framework that includes China but not the United States.

The agreement comes when President-elect Joe Biden seeks to return to a more traditional U.S. policy of working with its allies. RCEP will pressure the United States to re-engage in the Asia-Pacific or risk getting crowded out by China's expanding regional presence.

Companies will be able to manufacture and sell goods across the region with just a single certificate of origin, making it harder for U.S. companies to compete with products and companies in the region. It will become more difficult to export U.S. products to RCEP markets if the products are dutiable (i.e., not covered by a U.S. FTA or otherwise duty-free), since RCEP competitors will have a tariff advantage. This could be a particular concern for U.S. farmers since agricultural products are often subject to high duties and RCEP offers tariff reductions for certain agricultural products for member countries. It could also pressure U.S. companies to locate production facilities in RCEP to secure preferential access to key export markets under the agreement or lower the cost of assembling goods that require bringing together inputs from multiple RCEP signatories. RCEP may also reduce U.S. market share in Japanese and South Korean markets.

RCEP may encourage the Biden administration to pick up where President Obama left off with the unfinished "pivot to Asia" and for the United States to apply to join CPTPP. To date, President-elect Joe Biden has been noncommittal on joining CPTPP, and it is unlikely to be a key priority in his first year in office. It would also require Congress to extend the Congressional "Trade Promotion Authority"/fast-track procedures, which expire on 1 July 2021.

RCEP's limitations

There are some notable deficiencies in RCEP that may limit its tangible economic benefits. Many agricultural products and politically sensitive goods are excluded from tariff reductions. The tariff reductions apply to approximately 90 percent of goods, far less than "gold standard" free trade agreements such as CPTPP in which 99 percent of goods will be duty-free when the deal is fully implemented. Many tariffs will be phased out slowly over a period as long as 25 years.

RCEP also does not deal with problems arising from industrial subsidies and state-owned enterprises. Nor is it as ambitious as the CPTPP in addressing labor and environmental concerns.

RCEP also does not contain investor-state dispute settlement (ISDS) provisions. Instead, once the agreement is in force, member states will reevaluate the ISDS issue within two years. However, most believe it unlikely that there will be the political will to incorporate ISDS into RCEP in the future.

Lastly, the agreement does not include India, which broke off discussions because domestic industries could be adversely affected by cheaper manufactured goods from China and milk and dairy products from New Zealand and Australia. India may restart negotiations with RCEP members in the future. Still, given recent tensions with China and India's political sensitivities about lowering industrial and agricultural tariffs, it seems unlikely in the near-to-mid-term.

Conclusion

Despite its limited coverage, RCEP will likely become a driver of regional trade, given its historic geographic scope, tariff reductions, harmonized rules of origin, and trade facilitation services. Moreover, the fact that there are now two major trade agreements in Asia carries political and symbolic weight of regional trade cooperation that cannot be ignored.

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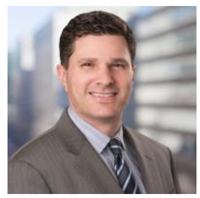

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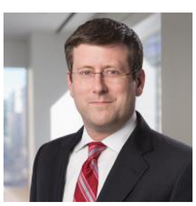

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SEA View

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