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Submission to the Joint Standing Committee on Treaties (JSCOT) *Inquiry into the Regional Comprehensive Economic Partnership Agreement*

April 2021

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Executive Summary

- In November 2020, fifteen Indo-Pacific governments signed the Regional Comprehensive Economic Partnership (RCEP) agreement.
- Upon entry-into-force, RCEP will be the largest regional trade agreement in the global trade system, and the first agreement in the Indo-Pacific to achieve near-universal coverage of regional economies.
- RCEP principally functions as a 'harmonisation' agreement – providing a single and cohesive set of regional trade rules, which unify existing liberalisation conducted in prior bilateral agreements.
- It also contributes to 'WTO Plus' rule-making, by incorporating trade-related regulatory provisions in areas important for 21st century economies, such as services, e-commerce and investment.
- RCEP's principal economic benefit for Australia will come from its value chain effects, rather than its direct market access gains.
- Coming amid a global turn towards protectionism, RCEP politically signals the commitment of Indo-Pacific governments to trade cooperation, and will buttress the rules-based trading system in the region.

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1. The function of RCEP in the regional trade architecture

The Regional Comprehensive Economic Partnership (RCEP) is the latest addition to the global and regional trade architectures. It is a regional trade agreement, comprising fifteen economies in the Indo-Pacific. It is built on top of the existing network of "ASEAN Plus One" FTAs[1], which connect the ten-member ASEAN bloc to five other regional economies: Australia, China, Japan, Korea and New Zealand. Upon entry-into-force, RCEP will be only the second regional trade agreement in the Indo-Pacific, alongside the eleven-member Comprehensive and Progressive Agreement for the TPP (CPTPP) that was completed in 2018.

RCEP has an extremely long genesis. Beginning in 2013, governments completed thirty-one rounds of negotiations and eighteen ministerial meetings[2]. India – an original party – departed in late 2019 due to differences over the scope of tariff reductions. The COVID crisis forced negotiations to shift to a virtual modality in April 2020. Yet RCEP has survived all these setbacks. The 'text' (i.e. the regulatory components) was settled in late 2019, with market access negotiations completed through 2020. Members signed the agreement in November 2020, with governments now undertaking domestic ratification processes. RCEP will enter-into-force sixty days after six ASEAN and three non-ASEAN members have completed ratification[3].

RCEP enters a crowded landscape of trade agreements in the Indo-Pacific. Over the last two decades, regional governments have negotiated an extensive array of beyond-the-WTO trade instruments (Table 1). These include the ten-member ASEAN FTA, its six "Plus One" extensions, the eleven-member CPTPP, and a further XX bilateral free trade agreements between the governments within the bloc. As a result, RCEP has a unique function in the regional trade architecture: as an additional instrument that will operate 'over the top' of an existing network of interlocking bilateral and minilateral trade agreements.

RCEP's contribution to Indo-Pacific economic integration, and Australia's engagement therein, must be understood in terms of its role within this regional trade architecture. It functions primarily as a harmonisation platform, offering a single and cohesive set of trade and trade-related rules for participating economies. It is particularly configured to supporting the growth of regional value chains, by providing compatibility between existing bilateral trade mechanisms. It also contributes to buttressing rules-based trade in the Indo-Pacific, at a time when the regional trade system is under increasing stress.

Table 1 Free trade agreements in the Indo-Pacific

Trade instrument	Year of completion	Members
ASEAN FTA (AFTA)	1992	10x ASEAN members: Brunei, Cambodia, Indonesia, Laos, Myanmar, Malaysia, Philippines, Singapore, Thailand, Vietnam
ASEAN "Plus One" FTAs	2002 onwards	6x: Between ASEAN bloc and Australia, China, India, Japan, Korea, New Zealand
Bilateral free trade agreements	2001 onwards	
Comprehensive and Progressive Agreement for the TPP (CPTPP)	2018	11x: Australia, Brunei, Canada, Chile Japan, Malaysia, Mexico New Zealand, Peru, Singapore, Vietnam
Regional Comprehensive Economic Partnership (RCEP)	Signed 2020, awaiting ratification	15x: ASEAN-10, Australia, China, Japan, Korea, New Zealand

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2. RCEP objectives: Harmonisation, liberalisation and rule-making

In comparison to Australia's existing FTAs, RCEP advances a distinct set of trade policy objectives. In principle, a free trade agreement may have one of three potential functions:

- *Liberalisation:* Reducing conventional barriers to trade – typically tariffs, quotas and customs procedures – between members.
- *Harmonisation:* Providing a consistent set of trade rules and procedures amongst a group of countries, particularly where multiple (and inconsistent) bilateral FTA exist
- *Rule-making:* Establishing rules in trade-related areas of economic regulation that are not currently covered by WTO disciplines.

Of the three functions, RCEP's principle objective is harmonisation. It takes the existing network of five "ASEAN Plus One" FTAs in the region, and creates a single integrated trade bloc. This creates a set of harmonised rules and practices for trade amongst the fifteen participating economies, establishing a transparent and level playing field for all parties. It also helps address the so-called "spaghetti bowl" problem, where differences between the provisions of bilateral FTAs act as a trade barrier by increasing compliance costs for businesses.

RCEP's size and regional scope means it offers significant harmonisation gains for its members. It is the most significant trade agreement ever signed, accounting for 29.1 percent of world GDP (Table 2). It is the largest regional bloc by GDP and population, and only marginally behind the EU in terms of share of world trade. It is also the only agreement to include nearly all of the Indo-Pacific, as the region's other two multilateral blocs – the CPTPP and ASEAN FTA – have comparatively poor regional coverage. RCEP means that the Indo-Pacific now has a single, harmonised and consistent set of trade rules for all economies in the region. It also establishes the region as one of the world's most important trade blocs, on par with the EU.

Table 2 Major regional trade blocs in the global trade system

	Year established	Member states	Population (millions)	Share world GDP	Share world trade
Comprehensive and Progressive Agreement for the TPP (CPTPP)	2018	11	504	12.9%	15.3%
Regional Comprehensive Economic Partnership (RCEP)	Awaiting ratification	15	**2290**	**29.1%**	28.7%
Association of Southeast Asian Nations FTA (AFTA)	1992	10	654	3.5%	7.4%
Commonwealth of Independent States FTA (CIS)	2011	8	244	2.4%	3.1%
EC/EU Customs Union	1958/1994	28	513	21.9%	**33.1%**
Common Market of the South (Mercosur)	1991	5	293	3.1%	1.8%
North American Free Trade Agreement (NAFTA/USMCA)	1994/2020	3	493	27.6%	13.2%

Source: Author's calculations from *UNCTADStat database*.

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RCEP also serves important rule-making functions for the regional trade architecture. Commonly referred to as "WTO Plus" provisions, these cover regulatory domains that are *related to and affect* trade patterns, but have not yet been addressed by a WTO instrument. These rule-making provisions are especially important for newer forms of international trade – such as e-commerce and services – which have yet to be substantively incorporated into international trade law. RCEP contains WTO-Plus regulatory provisions in seven areas: investment, e-commerce, intellectual property, telecommunications, services, financial services, and movement of natural persons (i.e. migration) (see Table 3). It also contains specific commitments to assist developing country members to implement these provisions where required. These rules will apply consistently across all members of the RCEP bloc, contributing to the harmonisation of regional trade rules.

It should be noted that RCEP's rule-making content is not as advanced as those in other trade agreements. In the Indo-Pacific, the regulatory high-water mark is set by the CPTPP agreement, which includes several provisions absent in RCEP (environment, anti-corruption, state-owned enterprises and labour); and stronger standards in others (intellectual property, e-commerce and financial services (Table 3). However, the CPTPP – with a membership skewed toward developed economies – is not an appropriate comparator for RCEP given its predominantly developing country membership. The relevant yardstick are existing WTO rules, which establish the *status quo ante* upon which RCEP's provisions build. As Table 2 shows, all of RCEP's regulatory provisions advance on existing WTO minimums, thereby extending the rules-based framework governing trade relations in the Indo-Pacific. Particularly important are its e-commerce and services provisions, which are critical for supporting newer types of trade emerging with digitisation and technological change.

By contrast, RCEP's liberalisation components are comparatively modest. Once the agreement is fully phased-in, its market access exchanges will eliminate tariffs on 92 percent of trade in goods between the members, and provide access to 65 percent of service sectors[4]. Australia will enjoy slightly higher benefits, with 94 percent of goods exports to the bloc duty-free once fully implemented[5]. These tariff elimination results are not as high as in other free trade agreements. For example, both the CPTPP[6] and the China-Australia free trade agreement (ChAFTA)[7] will eliminate tariffs on 98 percent of goods trade. Moreover, many of the tariff reductions codified in RCEP had previously been agreed in prior FTAs between its members, meaning its *new* market access gains are significantly lower than headline tariff elimination figures. For Australia, the most notable gains will be in several service sectors in China, Malaysia, the Philippines and Thailand[8].

However, RCEP's modest liberalisation outcomes need to be understood in the context of the agreement's objectives. As tariff elimination has been central in the region's existing FTAs (particularly the five 'ASEAN Plus One' agreements), most politically realistic trade liberalisation has already been delivered in other agreements. Thus, RCEP's function in the regional trade architecture is not to break new liberalisation ground (the role of bilateral FTAs), but instead to provide a framework where these FTAs can be harmonised into a single and cohesive Indo-Pacific agreement.

Table 3 Regulatory provisions in the WTO, RCEP and CP/TPP

	WTO instruments	RCEP extensions	CP/TPP extensions
Investment	*TRIMS agreement* (only goods trade-related investment measures)	All investment measures: MFN and NT protections; negative-list exceptions	All investment measures: MFN and NT protections; negative-list exceptions
Anti-corruption	None	None	Requirement to criminalise and sanction corruption, and to adopt appropriate accounting, auditing and financial disclosure standards
Environment	None. (*Environmental Goods Agreement* current under negotiation)	None	Requirements for effective enforcement of national environmental law; promotion of collaborative activities in range of areas (fisheries, CITES, biodiversity, renewable energy)
E-commerce	None. (*E-commerce negotiations* currently under negotiation)	Encourage paperless trading; online consumer protection; anti-spam measures; limitations on data localisation; data transfer rules	Privacy protections; equal treatment of digital content; protections for source code
Intellectual property	*TRIPS Agreement* (protection of trademarks, geographical indicators, patents)	Protection of genetic resources, traditional knowledge and folklore; improved transparency; mechanisms for IP enforcement cooperation	Harmonisation of patent rules; life-plus-70-years standards for copyright; requirement for enforcement regimes*
State-owned enterprises	*GATT Art XVII* (only trading activities of SOEs)	None	Requirement for SOEs to act in accordance with 'commercial considerations'; transparency rules for SOEs and government monopolies
Telecoms	None	Requirement for public networks to provide services to foreign firms on a non-discriminatory basis; transparency regulations; mobile number portability	Requirement for major suppliers to provide services to foreign firms on a non-discriminatory basis; transparency regulations
Investor-State Dispute Settlement	None	None	Yes, with public interest exceptions
Financial services	None	"Endeavour" to allow foreign firms NT	MFN, NT and cross-border-supply provisions
Services	*GATS Agreement* (MFN, NT and market access provisions, positive-list liberalisation)	MFN, NT and market access provisions; negative list exceptions	MFN, NT and market access provisions; negative list exceptions
Labour	None	None	Requirement to enforce labour standards; initiatives to discourage trade in goods made using forced or child labour
Movement of natural persons	None	Enhanced business and labour mobility provisions; commitments for spouses and dependents	Enhanced business and labour mobility provisions; commitments for spouses and dependents
Economic and technical cooperation	None	Work program to assist developing country members to implement regulatory provisions	None

Source: Author's summary from CPTPP, RCEP and WTO instrument official texts. *Note:* MFN refers to "most-favoured-nation" and NT "national treatment" protections. * Several TPP intellectual property provisions are suspended in the CPTPP. See note [9]

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3. Economic effects: Unlocking regional value chains

Value chains are an essential component of the contemporary global economy. They are cross-border industrial networks for producing goods, where countries specialise in different stages of production associated with a finished product. The Apple iPhone is a well-known example of a product dependent on global value chains. It is made from hundreds of components, which are sourced from specialised suppliers in forty-three countries across six continents, before final assembly in China for sale to world markets.[10]

Global value chains are a common feature of many modern industries, particularly the clothing, automobile, machinery, electronics and agro-food sectors. By unlocking economies of scale and scope, global value chains allow much greater efficiencies and competitiveness than fully "national" industrial models.

Unfortunately, value chains have largely been ignored by recent trade diplomacy. Since the early 2000s, there has been a 'turn to bilateralism' in the trade system[11]. Rather than pursuing multilateral agreements (at the global or regional levels), governments have preferred smaller bilateral FTAs. The primary appeal is their ease: with only two parties, deals can be negotiated far more quickly than in multilateral fora. For these reasons, bilateral FTAs are often viewed as a useful 'second best' trade strategy, to be used when multilateralism fails[12]. According to WTO data, there are currently 286 bilateral FTAs in force globally[13].

However, bilateral FTAs do not adequately support the development of value chains. As they only lower trade barriers between two economies, they are of little assistance to complex value chains that incorporate many countries. Moreover, there are major differences in the rules, standards and procedures in each bilateral FTA. This creates inconsistencies and distortions – famously known as the 'spaghetti bowl problem'[14] – that actually raise the friction in global value chains as companies are forced to comply with potentially dozens of rules. As Deborah Elms of the Asian Trade Centre has argued: "*Bilateral agreements between two countries are not particularly helpful for value chains that span dozens of places*."[15]

RCEP, by contrast, is one of the few FTAs that is specifically configured to support the development of regional value chains:

First is its size and comprehensive membership. RCEP is one of very few regional trade agreements that includes almost all economies within its region. With the exception of India, Taiwan and Hong Kong, all major Indo-Pacific governments are members. This is a major advantage over the region's other large trade agreement – the CPTPP – which does not include China, Korea, or most ASEAN economies. This regional coverage means that RCEP will better unlock value chain opportunities than any other FTA in the region.

Second, RCEP will provide a standard set of rules and procedures for regional trade. In complex value chains, there are differing governmental regulations for each involved country. This imposes significant transaction costs on businesses, which need to manage compliance with many different sets of national trade regimes. By providing a single set of trade rules, RCEP will greatly lower these costs, encouraging the development of deeper value chains.

An illustrative example are "rules-of-origin" (ROO) procedures. ROOs are the rules for deciding where a product comes from – effectively a "Made in Where?" system – and certificates need to be issued for every

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single trade shipment. But at present, there are differences in the ROO system for each bilateral FTA, requiring companies to apply for specific certificates for each possible export market. And as a product passes through the various stages of a regional value chain, repeat certificate issuance greatly adds to transaction costs[16].

RCEP will help lower these regulatory obstacles. Businesses will be able to apply for a single "Made in RCEP" origin certificate, with standardised rules for how much local content is needed to qualify. This will allow products to move across borders more efficiently and lower compliance costs for business. It will also allow value to be 'cumulated' through multiple steps, ensuring that a product continues to receive preferential treatment as it passes along the value chain. This will be a significant benefit for Australian exporters participating in regional value chains, who at present have to apply for nine different ROO certificates to export to RCEP markets[17].

Third, RCEP will liberalise many 'behind the border' regulations that affect value chains. It includes chapters covering fourteen trade-related policy areas, all of which advance on existing minimum standards guaranteed by WTO rules (Table 3). Several of these will directly augment regional value chain development:

- Investment, where members have agreed to liberalise investment on a 'negative list' basis (i.e. all sectors are open unless explicitly specified). For many RCEP members, this is the first time they have agreed to a negative list approach to investment liberalisation. That this is being done by the entire RCEP bloc will make the region significantly more attractive for investments in value chains.
- Services, where members have committed to most-favoured-nation, national treatment and liberalising market access provisions. Like investment, services liberalisation has occurred on a negative list basis. As services - such as legal, logistics, and design functions – are essential to connecting cross-border value chains, these provisions will also aid value chain development.
- E-commerce, particularly provisions that encourage 'paperless trading' and specify rules for data localisation and transfer requirements. These standards will help digitise many aspects of value chain management, reducing compliance costs.

As a result, RCEP's principal economic benefit for Australia will come from its value chain effects, rather than its direct market access gains. Goods produced in the RCEP bloc with Australian inputs will now enjoy increased access to final markets, increasing demand for Australian exports. An illustrative example is the value chain for instant noodles, where Australian wheat is produced into noodles in Indonesia before export to regional markets. By ensuring all steps in this regional value chain are covered by a single set of trade rules, RCEP will increase export opportunities for Australian wheat despite not including specific tariff reductions. Many other examples exist, particularly in the agro-food and advanced manufacturing sectors.

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4. Strategic effects: Advancing rules-based trade in the Indo-Pacific

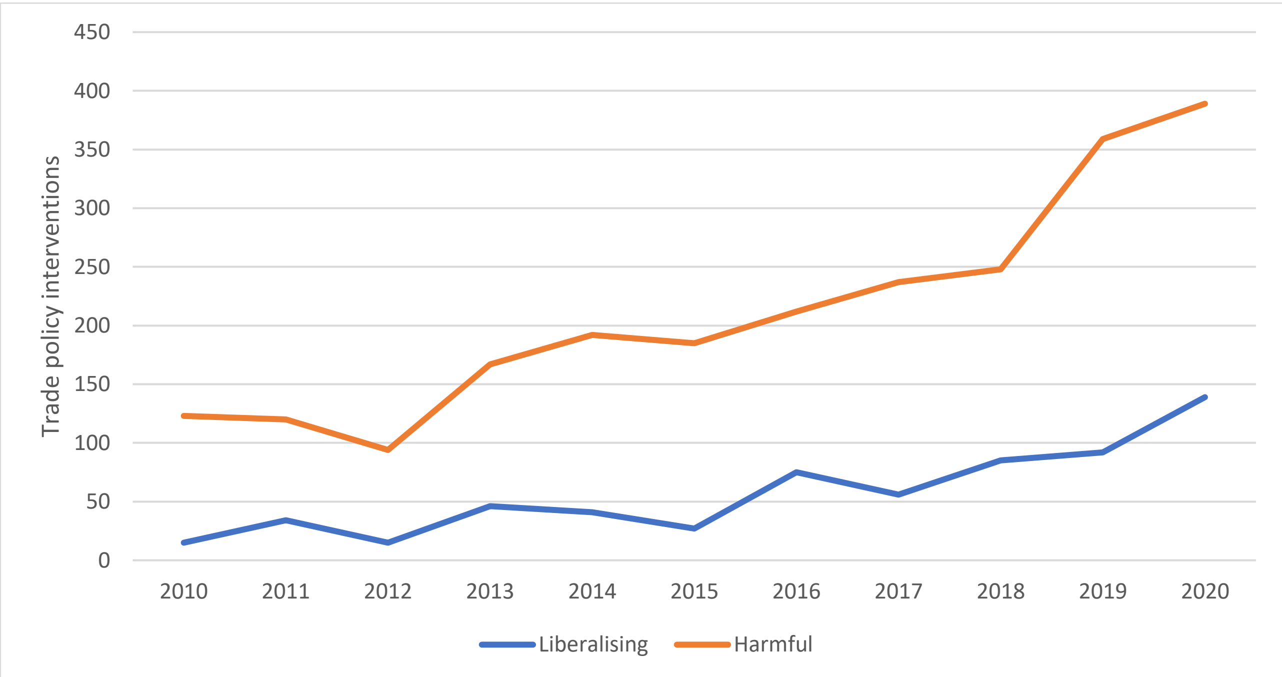
RCEP will also bring a number of strategic benefits for Australia and the broader Indo-Pacific region. In recent years, there have been several challenges to the global and regional trade architectures, which have undermined confidence in rules-based approaches to managing economic relationships in the Indo-Pacific. In this context, RCEP is critically important in buttressing a rules-based trading order in the region.

Indeed, that RCEP might be completed at all is itself an historic diplomatic achievement. Since its launch a decade ago, negotiations have persisted despite a wide array of political headwinds, including:

- A global turn towards protectionism, which has seen governments move to restrain rather than liberalise trade policy settings[18]. In the decade to 2020, governments implemented 2203 new barriers to trade, while liberalising trade only 610 times (Figure 1).
- Increasing diplomatic assertiveness from the PRC, which has led to a deterioration in its political relations with many Indo-Pacific governments, including Australia, India, Japan and Vietnam[19].
- Competition with Trans-Pacific Partnership negotiations, which preoccupied several members until the completion of the CPTPP in 2018[20].
- India's decision to withdraw from RCEP in 2019, which forced a strategic reset of objectives and further negotiations surrounding market access offers[21].
- The COVID-19 crisis, which has intensified protectionist impulses[22].

That the largest-ever regional trade agreement will be delivered against this challenging political backdrop is a testament to the commitment of Indo-Pacific governments to rules-based economic integration.

Figure 1 Trade interventions by governments by type, 2010-2020



Source: Global Trade Alert Database[23]

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Equally important, RCEP will also redraw the strategic map of the Indo-Pacific. The existence of a single, region-wide set of trade rules will change the economic outlook of its members. By lowering barriers to intra-regional trade and investment, members will progressively accord higher priority on deepening economic ties between themselves, particularly through the further development of regional value chains. by corollary, developing economic ties with extra-regional partners outside RCEP will fall in relative importance. In a context of partial US-China economic decoupling[24], and a reconfiguration of value chains in the wake of COVID-19 related interruptions[25], RCEP will change the calculus of many governments towards pursuing within-region responses.

RCEP will also buttress multilateralism in the regional economic architecture. For the past two decades, bilateralism has been the dominant mode of economic diplomacy, evident in the proliferation of bilateral FTAs while progress in global (the WTO) and regional trade institutions has stalled. Along with the CPTPP, RCEP promises a return to multilateral approach to trade cooperation in the Indo-Pacific. Multilateralism works in favour of small- and medium-sized economies, who lack the size and scale to secure strong outcomes with larger players when negotiating bilaterally.

RCEP will also balance China's economic weight in the Indo-Pacific. While it is often claimed that RCEP is a "China-led" agreement, the reality is it is an ASEAN-led initiative[26]. It is built on the foundation of the existing ASEAN Plus One FTAs, and secures ASEAN's iposition at the heart of regional economic institutions. The presence of developed (Australia, Japan and Korea) and large developing (Indonesia and Vietnam) countries also ensures a diverse mix of significant economies are represented within the bloc. It also binds China to a multilateral model for trade liberalisation, which breaks with its preference for bilateral economic diplomacy (seen in the Belt and Road Initiative).

Unfortunately, RCEP will add to India's exclusion from the Indo-Pacific economic architecture. In late 2019 India withdrew from negotiations, due to an inability to match the market access commitments of other members[27]. This reflects India's more protectionist trade policy settings, and claimed fears of a 'Chinese import surge' if it joined the agreement as proposed[28]. However, it augurs poorly for India's economic integration with Indo-Pacific partners, which was already very low due to its less-open policy settings[29]. However, RCEP includes an accession mechanism[30] that keeps the door open to India if economic and political factors change in the future, and RCEP members have expressly committed to a pathway for India to re-engage with the agreement[31].

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