



# CHAPTER 1

## The Regional Comprehensive Economic Partnership: Challenges and Opportunities for ASEAN and East Asia

**Fukunari Kimura**

*Keio University and ERIA*

**Shujiro Urata**

*Waseda University and ERIA*

**Shandre Mugan Thangavelu**

*Jeffrey Cheah Institute for Southeast Asia, Sunway University  
Institute for International Trade, University of Adelaide*

**Dionisius Narjoko**

*ERIA*

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The chapter provides an overview of the challenges and opportunities of the Regional Comprehensive Economic Partnership (RCEP), the largest global regional trading bloc, which came into force in January 2022. It highlights the importance of RCEP for pandemic and post-pandemic recovery of East Asia. It also summarises the chapters of the book, *The Dynamism of East Asia and Regional Comprehensive Economic Partnership (RCEP): The Framework for Regional Integration*.

## Introduction

The Regional Comprehensive Economic Partnership (RCEP) is the world's largest regional trading bloc, consisting of a combined population of 2.2 billion people (30% of the world), total regional gross domestic product (GDP) of around \$38,813 billion (30% of global GDP in 2019), and nearly 28% of global trade. This regional multilateral free trade agreement (FTA) sets an important agenda for trade and regional integration and the creation of dynamic regional and global production value chains (GVCs). It mobilises and releases huge resources for trade and investment in global trade in terms of opening the large domestic markets (i.e., demand) of East Asia. RCEP is expected to benefit not only East Asia but will also have a global impact, as indicated by recent studies (Park, 2022; Itakura, 2022; Petri and Plummer, 2020). Open regionalism and global trade in terms of a rules-based trading framework will be enhanced by RCEP, which is expected to have a significant impact on the post-pandemic recovery of the region as well.

The RCEP, signed on 15 November 2020, is the largest FTA in the world. It comprises the 10 Association of Southeast Asian Nations (ASEAN) Member States (i.e. Brunei Darussalam, Cambodia, Indonesia, Lao People's Democratic Republic [Lao PDR], Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Viet Nam) and 5 countries in the region with which ASEAN has FTAs – Australia, China, Japan, the Republic of Korea, and New Zealand.<sup>1</sup> The RCEP came into effect on 1 January 2022 through the ratification of six ASEAN Member States (i.e. Brunei Darussalam, Cambodia, Lao PDR, Thailand, Singapore, and Viet Nam) and Australia, China, Japan, and New Zealand.

The RCEP is critical for the post-pandemic recovery of ASEAN and East Asia and to manage the global uncertainty from the Russia–Ukraine war. It has elements crucial for regional transformation, such as (i) the first free trade area of China–Japan–Korea; (ii) a single rules-of-origin (RoO) framework for the 15 member countries, which may have

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<sup>1</sup> ASEAN leaders adopted the ASEAN Framework for RCEP during the 19th ASEAN Summit in November 2011 in Bali, Indonesia. The Joint Declaration of Ministers on the Launch of Negotiations for the Regional Comprehensive Economic Partnership was made on 20 November 2012 during the 21st ASEAN Summit in Phnom Penh, Cambodia (ASEAN, 2012).

an accelerating and enhancing impact on GVCs in the region; (iii) elements for digital transformation and services liberalisation in e-commerce, financial, professional, and telecommunications services; and (iv) the notion of ASEAN centrality, which is critical for sustainable and inclusive growth.

The RCEP is a 'living' agreement that allows member countries to address current and contemporary issues with regard to regional integration and sustainable growth. Technical cooperation and capacity building elements allow least-developed countries in ASEAN to implement key reforms and liberalisation policies to induce structural transformation in their respective economies to fully benefit from regional FTAs. Their 'special and differential treatment' in RCEP allows flexibility to undertake necessary reform policies to fulfil FTA commitments (ADB, 2020; Fatmawati, 2020).

This chapter provides an overview of the challenges and opportunities posed by RCEP and summarises the chapters of the book, *The Dynamism of East Asia and Regional Comprehensive Economic Partnership (RCEP): The Framework for Regional Integration*.

## Challenges and Opportunities of Regionalism and the Importance of RCEP

Regional and global integration have recently been affected due to rising protectionism and anti-globalisation in regional and global trade, which will have a significant impact on growth and development in the region (Rodrik, 2021). For example, United States (US)–China trade war tensions will impact regional trade and investment in terms of inward-looking policies and the decoupling effects of GVCs to more developed countries away from China and East Asia (Bown and Irwin, 2019; Evenett and Fritz, 2019).

Globalisation and trade had an uneven impact in the pre-COVID-19 period. First, the gains from trade were unequally distributed and biased against the unskilled (Thangavelu, et al., 2022; UNCTAD, 2013). UNCTAD (2013) showed that although trade increased the wages of unskilled workers, 70% of the income generated from trade went to the top two income groups. Firms encompassed less skilled and more labour-intensive jobs, such as those in the garment and textiles and agricultural sectors, tended to experience fewer gains from trade in terms of wage increases for the unskilled and less educated (UNCTAD, 2013).

Second, a wage gap between skilled and unskilled workers during that period is observed, and the polarisation of semi-skilled jobs increased with trade and globalisation. ASEAN Member States have experienced a large decline in the share of semi-skilled jobs – mostly white-collar jobs – compared to unskilled and skilled jobs (Thangavelu and Wang,

2021). Third, over the past 2 decades, East Asia has also been experiencing the rise of protectionist policies from increasing anti-globalisation trends in regional and global trade (Thangavelu, 2021). This rise is reflected in the increasing trends of country-level new trade interventions since 2009 (Thangavelu, 2021). Harmful interventions accounted for nearly 72% of total state-level interventions from 2009 to 2021.<sup>2</sup>

Fourth, the COVID-19 pandemic shock also increased and intensified the vulnerability of openness and induced more inward-looking policies. The uneven impact of the shock on unskilled workers and increasing digitalisation of the economy widened the welfare gap between the skilled and unskilled (World Bank, 2021). The imbalanced impact of COVID-19 is also apparent within and between countries; negative impacts were more severe in developing and least-developed countries that do not have sufficient fiscal resources to cushion the economy and populations from shocks. The key dimension of the COVID-19 pandemic shock, however, is the diversion from open economic policies to those more inward-looking (Kimura et al., 2020).

It is expected that the pandemic shock will have long-term impacts on regional growth, as greater persistence of the shock is observed. Long-term impacts should induce structural transformation in the region by (i) adopting more digital technology; (ii) intensifying technology adoption and streamlining the supply process in GVCs, making them more resilient to economic shocks; (iii) transforming human capital and skills via restructuring to more technology-intensive and skills-based GVCs; (iv) increasing the fragmentation of the production process across countries participating in a GVC; (v) adopting and investing in communications technology to increase the agglomeration of manufacturing and services activities in the region; and (vi) increasing investment in digital and communication infrastructure in the region. These structural transformations will impact GVCs in the region and production structures of ASEAN and its least-developed Member States.

Further, the pandemic shock has increased the cost of trade at borders and intensified behind-the-border issues in the ASEAN region and East Asia. Rising trade costs at borders and behind-the-border issues directly affect trade in goods and services in East Asia and GVC activities (Baldwin and Evenett, 2020; World Bank, 2022). Recent studies by UNCTAD (2021a, 2021b) highlighted the rise in border and behind-the-border issues, such as increasing logistics and maritime freight costs due to bottlenecks in logistics supply chains, which directly affect goods and services trade in GVC production activities. UNCTAD (2021a) emphasised that the impact of rising border and behind-the-border

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<sup>2</sup> Global Trade Alert defines harmful measures (in terms of colour codes) as follows: (i) red; the intervention almost certainly discriminates against foreign commercial interests; (ii) amber; the intervention likely involves discrimination against foreign commercial interests; and (c) green; the intervention liberalises on a non-discriminatory (i.e. most favoured nation) basis or improves the transparency of a relevant policy. Global Trade Alert. Independent Monitoring of Policies That Affect World Commerce, <https://www.globaltradealert.org> (accessed 15 July 2021).

costs are significant in East Asia. The 9.9% increase in the intra-regional contract freight costs for Asia reflects these issues, which will impact the region's trade and economic recovery. Rising logistics and transport costs from freight charges will also effect the prices of imported goods and intermediate goods, which are expected to impact GVC activities in the region (UNCTAD, 2021a, 2021b).

UNCTAD (2021a) also showed that the increased cost of intermediate goods are centred in computer, electronics, and optical products (11.4%); furniture and other manufacturing (10.2%); textiles, apparel, and leather products (10.2%); rubber and plastics (9.4%); pharmaceutical products (7.5%); electrical equipment (7.5%); other transport equipment (7.2%); motor vehicles, trailers, and semi-trailers (6.9%); and machinery and equipment (6.4%). Simulated results of rising freight costs show that production costs will increase by 1.4%, intermediate goods by 3.1%, and imports by 11.9%. The rising costs of production and imports of intermediate inputs will affect the supply-side activities of GVCs in the region.

## Importance of RCEP for Managing Regional Integration

RCEP is critical for global trade and regionalism, given the current context of global uncertainty from the Russia–Ukraine war, inward-looking policies induced by the COVID-19 pandemic, and the US–China trade war. It provides the key impetus for global trade and investment and shifts domestic and regional activities in East Asia to open regionalism and global trade and investment. RCEP is also important for East Asia and ASEAN regional recovery in the post-pandemic era and to move the region to the next stage of inclusive and sustainable growth in regionalism and regional and global production value chain activities.

The impact will be significant for ASEAN and its least-developed Member States as indicated by various recent studies (Itakura, 2022; Park, Petri, and Plummer, 2021; Park, 2022). A dynamic computable general equilibrium (CGE) analysis by Itakura (2022) highlighted RCEP's positive impact on GDP for all members throughout the 2030s, particularly for the scenario with deeper trade and investment facilitation in which behind-the-border issues are addressed. Cambodia, the Lao PDR, Myanmar, and Viet Nam are particularly likely to have significant positive gains, given their young populations and GVC effects from China–Japan–Korea effects. Park (2022) posited that RCEP will generate more significant gains than the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) for members.

The economic impact of RCEP as a regional trading bloc will contribute significantly to East Asia mitigating the negative effects of the US–China trade war and COVID-19 pandemic shock (Plummer and Petri, 2020; Park, Petri, and Plummer, 2021). The trade agreement under RCEP creates a positive impact on output in the region through market access, greater flexibility in GVCs, and better technology adoption in the region.

## Structure of the Book

Recent research conducted by the Economic Research Institute for ASEAN and East Asia (ERIA) on RCEP examines its commitments, modalities, and mechanisms. It discusses potential implications of the integration process in the region and compares RCEP commitments to those of other agreements, including the CPTPP. It analyses how key features of RCEP can strengthen domestic and regional integration. The impact of businesses, behind-the-border issues, and domestic capacities of RCEP members are also discussed, in addition to potential benefits of RCEP. Finally, it addresses emerging issues, especially with respect to the COVID-19 pandemic recovery.

The first book, *The Regional Comprehensive Economic Partnership (RCEP): Implications, Challenges, and Future Growth of ASEAN and East Asia*, focusses on the key social, economic, and political dimensions of RCEP from the initial conceptualisation of the ASEAN Plus Six framework to detailed trade negotiations. It also undertakes recursive CGE analysis to identify the impact of RCEP, reviews services commitments, conducts a comparative analysis of RCEP with the ASEAN Plus One framework and CPTPP, examines the emergence of regional architecture from RCEP, outlines the role of RCEP in international production networks and China–Japan–Korea effects,<sup>3</sup> and looks at the role of RCEP in pandemic and post-pandemic recovery.

This second book, *The Dynamism of East Asia and Regional Comprehensive Economic Partnership (RCEP): The Framework for Regional Integration*, addresses selected questions regarding trade in goods, trade in services, investment, and economic cooperation. These are more technical in nature, but it is important for the private and public sectors to understand how the agreement is positioned vis-à-vis other agreements, including the CPTPP. Each chapter highlights key policy issues to increase the impact of a regional FTA – such as RCEP – on domestic and regional integration.

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<sup>3</sup> The RCEP provides the first free trade and investment arrangement for China, Japan, and Korea, which is expected to have significant impact on the regional and global production value chain activities in the region.

A study on the preferential nature of RCEP's tariff liberalisation commitment is presented in Chapter 2, '**How Preferential are RCEP Tariffs?**', by Kazunobu Hayakawa. RCEP does not necessarily adopt a common concession rule in tariffs, and the speed and depth of tariff reduction/elimination also differ by country. The chapter shows that RCEP tariffs are the best choice in trading some products with some countries in some years. Furthermore, there are some cases in which the use of RCEP tariffs becomes beneficial even if RCEP tariffs are not lower. The chapter demonstrates that RCEP tariffs are beneficial in specific types of GVCs.

The analysis of the restrictiveness of RoO in RCEP and other multilateral FTAs in East Asia with a view to facilitate GVCs is undertaken by Archanun Kohpaibon and Juthathip Jongwanich in Chapter 3, '**Restrictiveness of RCEP Rules of Origin: Implications for Global Value Chains in East Asia**'. The analysis begins by dissecting product-specific rules in these FTAs and quantifying them. Product-specific rules in RCEP are the most flexible compared to those in other multilateral FTAs – and more facilitative to GVC operations. This is driven by RCEP-specific features, such as high intra-member trade and member coverage. The main policy inference is that a full cumulation clause is needed in RCEP to allow a regional value content alternative to be in full effect. Meanwhile, harmonisation in RoO provision across these multilateral FTAs remains a challenge for ongoing negotiations.

Trade facilitation under RCEP is discussed by Wenxiao Wang and Shandre Thangavelu in Chapter 4, '**Trade Facilitation in RCEP Countries**'. Using available data sets on the trade facilitation index, the chapter compares current trends in trade facilitation across RCEP countries in four dimensions: the World Trade Organization's Trade Facilitation Agreement, digital trade streamlining, ease of doing business, and trade logistics performance. It finds that RCEP countries have improved significantly in trade facilitation measures, but these vary across countries. For example, China should further enhance its performance in cross-border paperless trade, whilst ASEAN Member States should improve documentary their compliance of trade, infrastructure of trade, and trade logistics performance.

Chapter 5, '**RCEP and Modern Services**', presents the first of three chapters on services commitments in RCEP, by Christopher Findlay, Xianjia Ye, and Hein Roelfsema. This chapter provides an overview of trade flows in modern services within RCEP and identifies the main challenges for policymaking that have emerged in negotiations. Providing a quantitative basis for the analysis, the chapter presents a general equilibrium Poisson pseudo-maximum likelihood analysis of the gravity model to cover several scenarios including structural adjustments that can guide future cooperation in liberalisation and development of modern services. The analysis then demonstrates opportunities for further liberalisation within the framework of RCEP.

A discussion of the RCEP commitment to liberalise e-commerce is presented in Chapter 6 by Jane Kelsey, '**Opportunities and Challenges for ASEAN and East Asia from the Regional Comprehensive Economic Partnership on E-Commerce**'. RCEP is a microcosm of the current tensions in negotiations on digital trade involving parties that have divergent positions on the digital economy, data, and regulations – including within ASEAN itself. The chapter adopts a prudent approach that recognises that the state parties need flexibility and policy space at the national and regional levels to develop policy and regulations in the rapidly changing digital ecosystem and to advance their collective interests through dialogue and cooperation. This chapter contrasts that approach with the disciplinary nature of binding legal obligations that are enforceable by other states and their investors, as in the CPTPP and other recent treaties. An analysis of key differences focusses on matters of particular importance to ASEAN, such as local content and government procurement, data rules and flexibility, financial data, source codes, and transparency. RCEP's cautious approach enables ASEAN Member States to deepen their national and regional understanding of the opportunities and challenges that these agreements present whilst developing and implementing their own digital development strategies.

Commitments for traditional services sectors in RCEP are analysed in Chapter 7 by Zhang Yan and Shandre Thangavelu, '**Traditional Services Trade in the Regional Comprehensive Economic Partnership**'. Traditional services trade, including tourism and transport services, is the basic component of the services trade in RCEP. RCEP implementation will provide a platform for further liberalisation in this sector and thus promote the growth of the whole services trade and development of the travel and transport industry. The chapter outlines the trade pattern of traditional services amongst RCEP member countries to consider the extent of trade of the services. It then analyses the commitments on these services for each member country. On this, a Hoekman index is constructed to measure the liberalisation levels for each.

Investment liberalisation in RCEP is considered in Chapters 8 and 9. Chapter 8, '**The Investment Chapter in the Regional Comprehensive Economic Partnership: Enhanced Rules without Enforcement Mechanism**', by Henry Gao examines the legal rules in the investment chapter of RCEP. It begins with an overview of the main provisions in the chapter, followed by an assessment of the rules by comparing established FTAs, especially the CPTPP. The discussion notes that in the RCEP investment chapter – whilst largely following established approaches to investment – also has important twists in the common rules to favour the host country. This chapter also discusses the conspicuous absence of an investor–state dispute settlement mechanism, its pros and cons, and wider implications on regional integration, and then concludes with some thoughts on future developments.



Chapter 9, '**Investment Liberalisation in East and Southeast Asia**', by Toshiyuki Matsuura examines investment liberalisation in South-East and East Asia in an effort to analyse the potential benefits from implementing the investment liberalisation commitment of RCEP. It presents the trends and patterns of the inflows and outflows of foreign direct investment (FDI) and reviews FDI liberalisation in South-East and East Asia. The analysis shows that inward FDI has been significantly increasing in Singapore as well as in Cambodia, the Lao PDR, Myanmar, and Viet Nam. Outward FDI has also been increasing in China and major ASEAN Member States. Moreover, intra-regional FDI is growing in South-East and East Asia. Although there has been significant liberalisation of FDI in the region, restrictions remain – especially in the primary and tertiary sectors. Nevertheless, the quantitative analysis indicates that there is room for increasing FDI by means of investment liberalisation in non-manufacturing in ASEAN Member States.

Joseph Wira Koesnaidi and Yu Yessi Lesmana analyse trade remedies in RCEP in Chapter 10, '**Trade Remedies**'. Based on the comprehensive analysis method, the chapter explains each trade remedy instrument and compares it to the World Trade Organization Agreement and other relevant regional trade agreements to review any distinct features in the RCEP trade remedies chapter. These features are important to assess, together with this chapter's consistency with the World Trade Organization Agreement, to avoid the abuse of trade remedy instruments and to provide more legal certainty.

Chapter 11, '**Economic and Technical Cooperation in the Regional Comprehensive Economic Partnership: Focus Areas and Support for Small and Medium-Sized Enterprises**', by Cassey Lee discusses the RCEP chapter on economic technical cooperation. To ensure that the benefits of RCEP are distributed equitably, economic and technical cooperation are needed between developing members and more developed members. This chapter identifies areas of economic and technical assistance needed by developing RCEP members as well as economic and technical assistance that can be implemented under RCEP to support the growth and development of small and medium-sized enterprises in the region. A comparison between the CPTPP and RCEP regarding small and medium-sized enterprises provides some ideas on how economic and technical cooperation can evolve and support further growth of such enterprises in the region.

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