



POLICY BRIEFS

THE NEW DYNAMISM OF EAST ASIA & ASEAN: NEW TRADE INSTITUTIONS IN FTAS AND THE 'LIVING AGREEMENT' OF RCEP

JCI-JSC-PB-2022-01 | 10 November 2022

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For the past decade, East Asia has been facing rising protectionism and anti-globalisation in regional and global trade, which will have a large impact on growth and development in the region (Rodrik, 2021. Kimura et. al, 2022, Thangavelu, 2021). The pandemic COVID-19 shock, the United States (US)–China trade war, the Russia-Ukraine conflict in Europe, global inflationary pressures, global value chain (GVC) disruptions, and the expected global and regional recession in 2023 are expected to have significant impact on the short-run to long-run development of the region. With rising global uncertainties and GVC disruptions, it is expected that we will experience more inward-looking policies, rise in protectionism, and fragmentation of global and regional trading arrangements (Kimura, 2021). However, trade and GVCs are critical for a sustainable and inclusive post-pandemic recovery in terms of poverty reduction and for creating a stable and resilient recovery process in terms of a digital and green transformation of regional trade (World Bank and WTO, 2022).

Recent studies by Kimura (2019; 2021) have highlighted the importance of the rules-based international trading order as an essential condition for effective and efficient functioning of international production networks (IPNs) in East Asia. The production processes in the global production value chains are located overseas, requiring close coordination of the movement of intermediate goods and services, which necessitates a rules-based trading system that allows for stable and dynamic GVC activities in the region. However, the rules-based trading system has become weaker over the past decade due to the United States (US)–China trade war and the weakness of the World Trade Organisation (WTO) in supporting the current global trading system, amplified by the crisis of the WTO Appellate Body (Kimura, 2021).

In addition to the global uncertainties and pandemic shock, there are also significant pressures on trading areas and arrangements to manage key domestic and regional issues beyond the traditional trade issues related to movement of goods, movement of services, and movement of capital. The recent high-level forum organised by the ASEAN Secretariat, the Economic Research Institute for ASEAN and East Asia (ERIA), and The Ministry of Commerce of the Kingdom of Cambodia on RCEP and Regional Dynamism highlighted new economic and social agenda that trading arrangements

have to address beyond trade related issues¹. The forum highlighted the following issues: (a) environment and climate change issues, (b) digitalisation and social impacts, (c) domestic capacity building in terms of skills development and training, (d) GVC and increasing the role of SMEs, (e) strengthening the rules-based trading system, and (f) the sustainable and inclusive growth of the region. The high-level participants also highlighted the need to address the 'living' agreement of RCEP.

The above requires a new socioeconomic agenda beyond trading arrangements and the need to align global, regional, and domestic policies and structural issues. It also requires the coordination within and between countries and also between different trading arrangements to reduce overlapping effects of policies, high transaction costs in border trade, and the fragmentation of the global and regional trading framework. This highlights the urgent need for a new trading institutional framework that requires more traction of trade policies on economic and social issues at the domestic, regional, and global level.

The Regional Comprehensive Economic Partnership (RCEP), the largest free trade agreement (FTA) in the world that came into effect on 1 January 2022, is expected to provide this new institutional framework. The 'build-in' institutional feature within the RCEP agreement, is expected to provide for the progressive liberalisation of regional and global trade and also to address the contemporary issues beyond trade and investment as a 'living' trade agreement.

RCEP as a 'Living' Agreement: New Trade Institution within Multilateral Agreements

The RCEP is the largest global trading bloc in the world, with a combined population of 2.2 billion (30% of the world population), total regional gross domestic product (GDP) of around USD38,813 billion (30% of global GDP in 2019), and nearly 28% of global trade. It sets an important agenda for global trade and investment in terms of opening large domestic markets (demand), releasing huge resources for trade and investment, and creating dynamic regional and global value chain activities.

There are several key features of RCEP in terms of (a) a single rule-of-origin framework for the 15 member countries, which could have an accelerating and enhancing impact on global value chains (GVCs) in the region; (b) the key element of the China–Japan–Korea (CJK) effect, as the RCEP agreement is the first FTA for trade and investment amongst these countries; (c) elements for digital transformation and services liberalisation in crucial services trade in e-commerce, financial, professional, and telecommunications services; (d) ASEAN centrality, and (e) RCEP as a 'living' agreement.

The key institutional feature of RCEP is the institutional provision given in chapter 18 of the agreement that creates the forward-looking dimension of progressive trade liberalisation and addresses key economic and social issues beyond trade. Under chapter 18 (institutional provision), the RCEP Joint Committee (RJC) will meet within one year after the agreement enters into force, and the RCEP Secretariat will coordinate all meetings thereafter. This unique feature of RCEP, to create the 'build-in' institution within a multilateral free trade agreement, creates the new agenda for developing the next set of trade institutions within multilateral FTAs that will align domestic and regional reforms in terms of wider economic and social benefits beyond trade in a 'rules-based' trading framework. Currently, there are no other multilateral FTAs, including CPTPP, that provides the establishment of an 'build-in' institution and a secretariat, although some FTAs such as AANZFTA and AHKFTA established facilities at the ASEAN Secretariat to augment human resources in supporting the Joint Committees in overseeing the implementation of their FTAs with ASEAN (Rillo,

¹ The High-Level Forum on RCEP, 'RCEP 10th-Year Anniversary: Reminiscing the Journey of RCEP and Launching of ERIA Second Book: Dynamism of East Asia and Regional Comprehensive Economic Partnership (RCEP): The Framework for Regional Integration' on 2-3 November 2022 at Phnom Penh, Cambodia.
<https://www.eria.org/events/rcep-10-year-anniversary-reminiscing-the-journey-of-rcep-and-launching-of-eria-book-dynamism-of-east-asia-and-regional-comprehensive-economic-partnership-rcep-the-framework/>

Robeniol, and Buban, 2022). The institutional provision under RCEP also strengthens ASEAN Centrality and creates the forward-looking agenda for ASEAN to create a sustainable and inclusive growth in the region.

As a 'living' agreement, the RCEP Joint Committee will be able to create a wider regional integration agenda to address key contemporary issues such as the environment and climate change, skills development, green transformation, and developing digital and smart urban centres. The role of RCEP Secretariat as an independent and progressive institution will be critical in the implementation, monitoring, evaluation, and leveraging of the forward-looking component of the 'living' agreement of RCEP (Kimura, Thangavelu, and Narjoko, 2022; Thangavelu, Urata, and Narjoko, 2022; Armstrong and Drysdale, 2022; ADB, 2020). The RCEP Secretariat will create a complementarity in policies with the ASEAN Secretariat, mobilise more resources, and will have new institutional features to address the rising global uncertainties and emerging new challenges.

Significance of the RCEP in Sustainable and Inclusive Growth in the Post-Pandemic Era

The RCEP is a critical framework for global trade and regionalism, given the current context of uncertainty and 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 the domestic and regional activities in East Asia to open regionalism and global trade and investment.

The impact of the RCEP will be significant for ASEAN and its LDCs (Itakura, 2022; Park, Petri, and Plummer, 2021; Park, 2022). The dynamic Computable General Equilibrium (CGE) analysis by Itakura (2022) highlighted the positive impact of the RCEP on GDP for all RCEP members throughout the 2030s, particularly for the scenario with deeper trade and investment facilitation and addressing behind-the-border issues (S4: tariff reduction, services liberalisation, logistic improvements, and investment facilitation). Park (2022) highlighted that the RCEP will generate more significant gains than the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) for RCEP member countries.

Impact of the RCEP in Creating Sustainable and Inclusive Integration

The RCEP is a 'living' agreement, which allows it to address current key issues that affect regional integration in terms of trade and investment under the institutional provision (chapter 18). The following are the current important issues that the RCEP should address urgently for a sustainable and inclusive integration of the region:

- (i) The effect of the pandemic shock tends to be felt more by unskilled and older workers. It also has an uneven impact on gender and increases the vulnerability of females in the labour market and households. There could be more support to increase the technical education and skills of vulnerable groups affected by the pandemic. Economic cooperation to support skills development for the ASEAN LDCs could be undertaken with the support of other international organisations such as the World Bank and the Asian Development Bank.
- (ii) The effects of the pandemic are also felt unevenly on larger firms and SMEs. Given that larger firms have more access to financial markets and banks to leverage their risk of pandemic shock, it is likely that SMEs are 'crowded out' of the financial markets and banks. There is a need to review the financial inclusiveness of SMEs due to the pandemic shock.
- (iii) The RCEP framework also allows member countries to pursue economic cooperation to develop regional and domestic capacity against external shocks such as the pandemic. Under the RCEP economic cooperation framework, a regional platform for mass testing and vaccination rollouts against pandemic shocks such as the COVID-19 virus could be an important area of cooperation.

- (iv) The pandemic has also increased the vulnerability of the fiscal status of many East Asian countries and AMS. There is a need to review the fiscal sustainability of the RCEP member countries and to develop a platform for short-term loan support that could be provided under the RCEP framework of economic cooperation.
- (v) The RCEP will provide domestic and regional platforms for the structural transformation of GVCs in the post-pandemic recovery. The higher risks arising from the COVID-19 pandemic will induce most multinational firms to undertake digital innovation and automation, which will directly affect the GVC activities in the region. This will have implications for domestic industrial activities in manufacturing and services. ASEAN LDCs must undertake policies to induce structural transformation of their industries to higher value-added activities, which will support the GVC activities induced by the CJK effects through the RCEP. However, there is a need to accelerate the structural transformation of these industries, especially in Cambodia, to increase GVC participation in parts and components. Structural transformation in ASEAN LDCs, such as Cambodia, could be through investments in critical infrastructure, upgrading their Special Economic Zones, or improving the skills and human capital of workers.
- (vi) Digital transformation will accelerate in the post-pandemic recovery and will have a direct impact on services activities and services trade in the region. AMS should develop a policy framework to manage the structural transformation of the services sector through digital innovation and automation. The RCEP could provide the framework to manage the structural transformation of services trade and investment in the post-pandemic period (Ando, Kimura, and Yamanouchi, 2022).
- (vii) During the pandemic recovery, we expect an intensification of the unbundling effects of production and economic activities in the global production value chains, facilitating participation by developing economies which is important for the structural transformation of East Asian countries and AMS. These processes, in both goods and services value chains, will be intensified by the application of digital technologies. We also expect the acceleration of digital and services trade in the next phase of growth in East Asia (Ando, Kimura, Yamanouchi, 2022; Findlay and Roelfsema, 2022).
- (viii) Under economic cooperation, the development of skills and capacity-building of workers will have an important priority under the RCEP agreement. As the region and domestic economies experience structural transformation, it will be important to create relevant skills for the region's next stage of growth. Economic cooperation under the RCEP could play an important role.
- (ix) The RCEP framework could also address key issues related to climate change and the environment, green transformation of the region in terms of trade and infrastructure, and the development of new urban centres to drive the next phase of economic growth in East Asia.

There is an urgent need for the RCEP members to establish the independent and progressive RCEP Secretariat within a year, which will be critical to manage the global uncertainties, reinforce 'rules-based' trading activities, and also manage the economic and social issues beyond trade in the region. This will be critical for the pandemic recovery, post-pandemic structural transformation and to create sustainable and inclusive growth in the region.



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