17 Nov 2020

Research Briefing | Asia Pacific

APAC trade pact sends a strong free trade message

Economist

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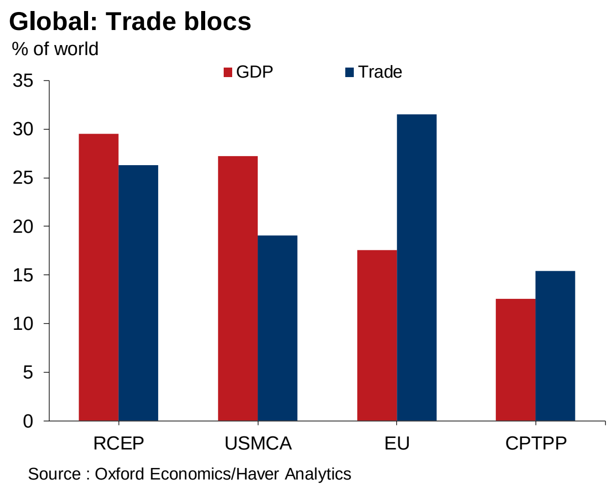
- **After eight years of discussion that saw the withdrawal of India, the ASEAN economies, China, South Korea, Japan, Australia, and New Zealand finally signed the Regional Comprehensive Economic Partnership (RCEP) on November 15.**
- **The RCEP agreement is important both for the messages it sends and the economic benefits it will bring. It signals strong support for free trade and regional co-operation at a time of rising de-globalisation concerns.**
- **The economic gains are likely to become visible over a longer period. With the bloc accounting for around 30% of the world's GDP and population, and 26% of its trade, it has the potential to deliver a notable boost to growth.**

Perhaps it is befitting that the largest trade pact globally in recent history (**Figure 1**) has been signed just as President Trump prepares to leave office. While the focus is on the economic benefits that the deal will yield, the symbolism of RCEP shouldn't be underplayed in a world that has seen a shift toward protectionism, led by the US in the last four years.

Globalisation has been on a downtrend since the global financial crisis of 2008-2009. Partly, this has been a natural economic outcome, reflecting rapid growth and industrial development in some emerging markets, the internalization of the environmental impact of transport, a shift of production closer to end-markets, and labour-saving technological progress. But it also reflects policies that have erected barriers to trade and investment, such as rising instances of trade disputes. In such an environment, RCEP sends a clear message in favour of openness and underscores our view that globalisation is unlikely to reverse in the coming decades (**Figure 2**).

Figure 1: RCEP is among the largest global trade pacts historically



RCEP size: the largest trading bloc by GDP and second largest by trade positions it favourably to reap long-term gains, with more than 90% of trade within the bloc likely to be liberalised over the next twenty years.

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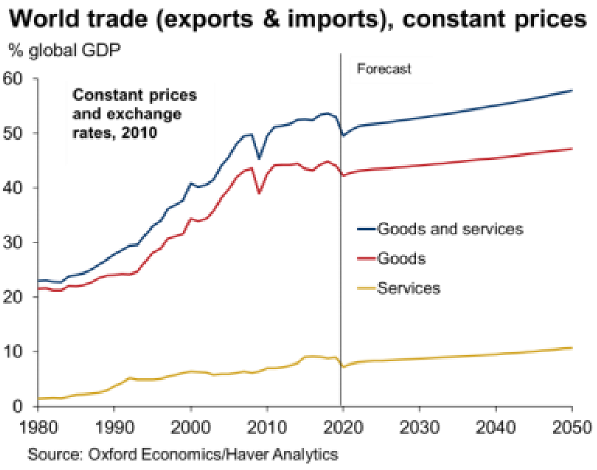
Figure 2: Globalisation to continue at a slow pace



The global trade-to GDP ratio has edged up only gradually since the GFC. We expect the economic and political factors driving this slowdown to persist in coming decades. But unlike some observers, we don't expect globalization to go into reverse.

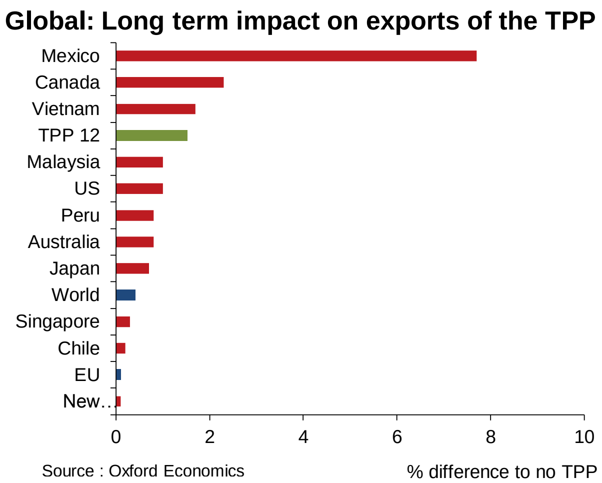
Economic gains from the RCEP will likely be visible in the long run, but receding trade uncertainties are a positive in the short-term as well

Economically, gains from the RCEP will likely take time to accrue. Other than Japan-China and Japan-South Korea, the members already have FTAs in place and we will have to wait and see how RCEP rules stack up alongside the existing arrangements in practice. As such, the agreement proposes a long timeline of 20 years to eliminate tariffs and restrictions within the bloc. Also, member countries have already lobbied to delay the implementation of certain provisions, according to their individual requirements.

Still, **with 90% of trade within the bloc likely to be liberalised over the next 20 years, it has the potential to deliver a notable boost to growth in the long-term. Common rules of origin, which mean that RCEP members will require only one certificate of origin for trading within the bloc, also make it easier to establish supply chains.** The Peterson Insitute for International Economics estimates that the partnership could boost global incomes by $186bn in 2030, barring escalation in US-China trade tensions.

Lastly, the signing of RCEP is likely to **renew interest in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership**. Seven out of 15 RCEP members are also signatories to the CPTPP, which could tempt a rethink by the US. Of course, this would involve lengthy renegotiations, including further measures to protect intellectual property rights and tough environmental and labour standards. It's also not clear how a renegotiated deal would change benefits to exports and GDP growth for the other 11 members. **Our modelling estimates that including the US in the TPP agreement would boost exports for participating countries by at least 1.5% a year in the long term, amounting to an annual 0.1% (US$150bn) gain in GDP** (**Figure 3**).

Figure 3: US would have a positive impact on TPP



TPP exports would be 1.5% higher if the US were a member of the bloc, with Malaysia and Vietnam seeing the most gains within APAC.

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As such, we wouldn't expect Asian members to be worse off than now under any new deal that includes the US, which accounts for around 10% of global goods and service exports. Adding the US to the CPTPP would likely mean a larger boost to exports, including services, than the deal currently generates.

In all, the tailwinds appear to be turning favourable for the more open Asian economies, both in the short and long-term, with trade uncertainties reducing with the departure of President Trump and a renewed emphasis on global trade pacts.

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