THE REAL MEANING OF THE RCEP: CHINA AND THE OTHERS?

Mateusz Chatys

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SUMMARY

The conclusion of negotiations on the Regional Comprehensive Economic Partnership (RCEP) on November 15, 2020 was greeted with great relief by the business world and the governments of the countries involved in this initiative. The RCEP, once ratified by all countries, will be the largest free trade zone in the world, which, due to the dramatic economic effects resulting from the COVID-19 pandemic, will be of great importance for the pace of return to economic growth from before the pandemic. It is true that RCEP is not as comprehensive as the CPTPP signed in 2018. It does not regulate such areas as the environment, labor law or state-owned enterprises, but it solves the problem of the so-called *spaghetti bowl effect*, which ASEAN has so far dealt with, which has a separate FTA with other RCEP countries (China, Japan, South Korea, Australia and New Zealand). Given the nature of this trade pact, it can be assumed that the biggest beneficiaries will be China, Japan and South Korea. This has been argued by discussing the cooperation-competition in the area of the automotive industry. Clearly, the Southeast Asian countries that initiated the creation of the RCEP in the ASEAN format will also enjoy tangible benefits, for example the relocating of supply chains or the strengthening of existing ones, as well as better trading conditions. Nevertheless, these three countries that cooperate with ASEAN in the Plus Three format have the greatest economic and technological potential, thanks to which they will be able to enhance the region's future economic integration. The underdog in such developments in the region will be Taiwan, which is not part of any multilateral free trade agreement (FTA) due to the risk of political and economic repercussions from Beijing due to the 'one China policy'.

INTRODUCTION

Since the financial crisis of 2008, it has been clear that the center of gravity for economic development will increasingly shift towards Asia. The first significant sign of this trend was the completion of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) in 2018, which is a multilateral free trade agreement signed by 11 countries. Despite the fact that the United States withdrew from negotiations immediately after Donald Trump was sworn in as president in 2017, the CPTPP still plays an important role in shaping the global economic situation.

To elaborate further, China saw in the RCEP an opportunity to balance American economic influence in Asia. As a result, Beijing took an exceptionally active role in negotiating the agreement, which was noticed by the other 15 countries. Therefore, India's presence in the format was a key element oriented towards balancing Beijing's influence in the RCEP. New Delhi at the end of last year - on the final straight of negotiation - withdrew from the formula for fear of further liberalization of trade in goods and increasing the trade deficit with RCEP countries, especially with China. It is worth noting that Beijing, seeing the vacuum left by the United States, tried to fill it as quickly as possible. This is evidenced by President Xi Jinping's declaration at the last 27th APEC Economic Leaders' Meeting, in which he stated that China "favorably considers" joining the CPTPP. Prime Minister Li Keqiang, for whom the finalization of the RCEP is a symbol of the victory of unity and cooperation over conflict and confrontation, spoke in a similar vein of deepening the economic integration of the region, especially in the context of the serious effects of the COVID-19 pandemic on the global economy. He also pointed out that all countries of the format agree that RCEP will remain open to India, which ASEAN countries are particularly interested in.

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WHICH COUNTRY WILL BENEFIT THE MOST?

The RCEP, as a multilateral FTA, brought the attention of the vast majority of observers to the economic effects of the agreement. Nevertheless, these kinds of initiatives are equally, if not more, politically relevant. Undoubtedly, the conclusion of the RCEP negotiations is a great success for ASEAN which, despite a rigid negotiating framework based on consensus within the "ASEAN Way", managed to finalize it. In this way, the countries of Southeast Asia sent a signal that they still play a vital role in the region and haven’t been dominated by the recent increasing rivalry between Beijing and Washington. Moreover, RCEP should be seen as part of a strengthening of “ASEAN centrality” and a platform for greater integration of ASEAN with other countries of the region, which in the time of the COVID-19 pandemic, and the increasingly strong tendencies towards diversification of supply chains, is of great importance for the further development of the Southeast Asian countries.

As a side effect the ratification of the RCEP may also contribute to accelerating negotiations on an FTA between China, Japan and South Korea. The agreement was proposed as early as 2002, while the negotiations did not begin until ten years later. After 16 rounds of negotiations so far, there is still no significant progress. Up to now, challenges in the form of complicated historical relations as well as current political issues, such as the territorial dispute in the East China Sea and tensions in relations between South and North Korea, have effectively prevented any significant progress in negotiations on the FTA. However, the benefits of the RCEP could shift this dynamic towards accelerating possible progress in the next rounds of negotiations.

Ultimately, the finalization of the RCEP is a great political success for China. Firstly, Beijing's strong involvement in the work on the RCEP created the misleading impression that China was the author of the initiative. Scholars across the world repeat the narrative that places China as the frontrunner. Secondly, after the CPTPP, multilateral format focused on trade liberalization in Asia in which the United States is absent. Thus, it is a perfect justification of Beijing's narrative that Washington is an advocate of protectionist practices, while China upholds the current international order based on free trade and multilateral cooperation on a win-win basis. Therefore, under the RCEP, China will be able to give new impetus to the Belt and Road initiative and to side initiatives such as the Digital Silk Road - especially given that Beijing places great emphasis on the development of modern technologies, as well as their implementation in developing countries, using the still strong fear of the coronavirus pandemic and ways to counter it with the use of Artificial Intelligence (AI), the Internet of Things (IoT) and advanced monitoring systems.

According to the forecasts, RCEP is capable to add 209 bln USD annually to world incomes, and 500 bln USD to world trade by 2030. Even though Southeast Asian countries are behind the foundations of the RCEP, all indications are that they will benefit less than the countries of Northeast Asia as they have not had any FTAs so far. ASEAN members can expect profits of 19 bln USD annually by 2030, while according to the predictions of Peter Petri of the Peterson Institute for International Economics, and Michael Plummer of Johns Hopkins University, RCEP's greatest beneficiaries over the next decade will be Japan and South Korea. Their real incomes are expected to be 1% higher than without RCEP, while in the case of China the indicator is only 0,3%. It is worth noting, however, that for any of the forecasts to become real, the

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RCEP must first be ratified by 15 countries, and this is unlikely to happen earlier than next year. It is much easier, however, to predict who is going to lose the most on RCEP.

It is very likely that after RCEP takes effect, Taiwan will experience two consequences: one is an increase in unemployment (which is now around 4.4%), and the other is a stagnation or decline in average wages. The most recent big spike in unemployment took place in Taiwan after the 2008 financial crisis, and it reached over 6%. In the case of the average monthly wage in Taiwan, there has been a systematic increase since 2009 and a decade later the average salary is around USD 1,900. However, the shrinking external market of the manufacturing industry will not be able to create new well-paid positions. Moreover, workers who will be forced to abandon traditional industries may be transferred to the service sector after a short period of unemployment. Therefore, the already low wages in the service industry will be reduced even more, resulting in a more lasting effect of the low salary. The potential losses resulting from the implementation of the RCEP could be offset by Taiwan's accession to the CPTPP, but this seems unlikely without the US in this format.

RCEP AND AUTOMOTIVE INDUSTRY: CHINA’S COMPARATIVE ADVANTAGES?

In relation to RCEP, it is worth taking a closer look at the automotive sector, as all indications are that, under the new regulations of the world's largest free trade agreement, this area is set for dynamic development. This is all the more important for China as it overtook Japan and the United States in 2009, thus taking the lead in automobile production. In the RCEP agreement, the reduction of tariffs on parts and components will expand to varying degrees the competitive advantage of Chinese car companies going overseas. At present, compared with the whole vehicle export model, independent brand car companies generally adopt overseas knock-down kit assembling plants (export semi-finished products or parts and assemble finished products locally). The reduction of tariffs on parts and components will further optimize the cost structure of complete vehicles in overseas markets. Upon closer analysis of the situation on the financial markets, with particular emphasis on Chinese companies from the automotive sector, ambiguous stock market reactions can be noticed. Some of them recorded a significant increase, as in the case of Changan Automobile (+ 10.02%), Dongfeng Motor Group Company Limited (+5.50) and a slight one in the case of Zhejiang Geely Holding Group Co., Ltd (+1.11 %), while the others recorded slight declines, such as FAW Jiefang Group Co Ltd (-0.89%) and SAIC Motor Corporation Limited (-1.11%). It is worth noting, however, that the companies recording growth have joint ventures with other automotive companies, including Japanese companies such as Honda and Mazda. These, in turn, recorded a clear increase in share prices a day after the announcement of the RCEP closing. Share prices increased: respectively, Nissan increased by more than 5%, Mazda by 6.82%, Mitsubishi jumped 2.54%, and Honda gained almost 5%. South

Korean industry players also recorded a rise in the stock market, but a much more moderate one, as Hyundai Motor Company share prices had gained 1.11% and Kia Motors Corporation 0.34%.

In addition, RCEP will benefit China's two-wheeler exports. China, Indonesia, Vietnam and Thailand are the world's largest motorcycle sales countries. In the RCEP agreement, Indonesia has substantial tax incentives for Chinese motorcycles and mopeds of all kind of cylinder capacity from 10-30% base rate to 0%. It is worth emphasizing that in the case of electrically powered motorcycles, the reduction of tariffs from 30% to 0% will take place in the 15th year of the RCEP. On the other hand, Vietnam maintains a high base rate for almost all types of motorbikes (75%) including electric motors (60%). Exceptions are motorbikes with a cylinder capacity exceeding 250 cc but not exceeding 500 cc and those with a cylinder capacity exceeding 800 cc, because the base rate from 75% is reduced to 0% after 20 years of RCEP being in force. In the case of China, the base rate for almost all types of motorbikes is 45%, but it will be gradually reduced in relation to the ASEAN countries. Customs tariffs for motorcycles with piston engines with will drop to 0% only after the RCEP has been in force for 20 years, and for electric bikes there will be a significant drop from 45% to 5% after the first year, but the rate will remain in place for the next years. On the basis of this one sector alone, it is difficult to clearly indicate who will benefit the most, and to what extent from this free trade agreement.

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Last year, China launched a pilot project to export used cars as a response to rising demand from abroad. The main destination was Africa and the countries of Southeast Asia. It is worth noting that Southeast Asia used to have the highest import tariffs on secondhand cars in the world, but after the implementation of RCEP and hence the lowering of tariff barriers, this region is expected to become the largest export market of used cars for China. The potential of this market is demonstrated by the fact that while the average increase in purchases of cars in Asia was 3.7% in 2017, in Southeast Asia it was 8.1% in 2017.

However, Beijing realizes that in this sector it will have to cope with strong competition from Japan and South Korea. Both countries are famous for being a source of high-quality auto parts, and lowering customs barriers will allow for even greater penetration of the Chinese market. The percentage of tariff-free products traded between China and Japan will increase from 8% to 86%, increasing Japan's exports of auto parts. Considering that they account for 27% of bilateral trade between countries, it will be an important factor of not only economic but also political importance.

China efficiently selected specific sectors for which the reduction or lifting of the tariff was spread over a longer period. One of them is the industry of eco-friendly vehicles. China is already a world leader in the development and export of solar and wind power solutions, so the electric and autonomous vehicle sector is also at the heart of the People's Republic of China. It should therefore come as no surprise that tariffs on electrodes and materials for electric car batteries will be lifted after the RCEP has been in force for 16 years.

CONCLUSIONS

Trade with countries involved in the RCEP accounts for 1/3 of China's total trade. In addition, the RCEP countries account for 10% of foreign investment in China. While it is difficult to predict when and whether the pact will be ratified, it seems that the effects of the new multilateral trade agreement will be most evident in the case of South Korea, Japan and China. It is worth remembering that the last two countries do not have an FTA so far, and thus the greatest dynamics should be expected in these bilateral relations. Japan is China's second largest trading partner after the United States. Although the US trade war with China can be expected to ease with the presidency of Joe Biden, given the strong anti-Chinese sentiment and the cross-party agreement to further limit Chinese influence in the region and the world, it is hard to expect a complete cessation of rivalry.

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Beijing's enhanced cooperation with Japan and South Korea within the RCEP may be crucial to maintaining economic growth at a level that will maintain the legitimacy of the Chinese Communist Party's power inside the country. The reaction to the finalization of the RCEP was clearly evident in the car industry's quotations on the stock exchange, and thus a steady development of cooperation in this area can be expected. The development of cooperation between Chinese companies and their counterparts from Japan and South Korea will certainly improve the quality of Chinese car brands, thanks to which they will increase their share in the domestic market, which is mainly dominated by foreign manufacturers. Demand for cars in Asia is growing, thus it is a promising industry worth investing in, especially given that the government in Beijing places great emphasis on expanding the country's middle class, whose demand for good quality cars is very high.

A significant step forward in the direction of this approach would be the elaboration of a trilateral trade agreement with Japan and South Korea, i.e. countries involved in both the CPTPP and the RCEP. However, the question remains as to whether the political differences between the three will allow for the conclusion of the FTA negotiations, which have been going on since 2002.


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