



# Geoeconomic Opportunities and Geopolitical Risks of the RCEP

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## I. Key Features of RCEP

### A. Overview

The Regional Comprehensive Economic Partnership (RCEP) signed by 10 ASEAN members with Korea, Japan, China, Australia, New Zealand on November 15, 2020 is a unique RTA that combines five "ASEAN + 1" FTAs. It is a mega-FTA covering a region that accounts for 30% of the world's GDP, 28.7% of trade in goods, and 30% of world population. The objective of RCEP is "to establish a framework for a modern, comprehensive, high-quality, and mutually beneficial economic partnership." The RCEP negotiations started in May 2013. After 8 years of back-and-forth negotiations, India withdrew and the remaining 15 countries signed the Agreement.

Table 1. Structure of the Agreement

Chapter		Chapter	
1	Initial Provisions and General Definitions	11	Intellectual Property
2	Trade in Goods	12	Electronic Commerce
3	Rules of Origin	13	Competition
4	Customs Procedures and Trade Facilitation	14	Small and Medium Enterprises
5	Sanitary and Phytosanitary Measures	15	Economic and Technical Cooperation
6	Standards, Technical Regulations and Conformity Assessment Procedures	16	Government Procurement
7	Trade Remedies	17	General Provisions and Exceptions
8	Trade in Services	18	Institutional Provisions
9	Temporary Movement of Natural Persons	19	Dispute Settlement
10	Investment	20	Final Provisions

Source: Ministry of Industry, Trade and Resources (<https://www.fta.go.kr/rcep/>)

The RCEP Agreement is composed of 20 chapters and consists of massive 14,367 pages including the Annexes and Schedules of Commitments. Compared to "ASEAN + 1," RCEP has a lower level of commitment for goods but broader in scope. It has a lower level of liberalization and limited scope of coverage compared to other mega-FTAs such as USMCA (United States-Mexico-Canada Agreement), TPP (Trans-Pacific Partnership), as well as CPTPP (Comprehensive and Progressive Agreement for Trans-Pacific Partnership).

## B. Commitment on Goods

Article 1.1 of the RCEP Agreement states that it is consistent with Article XXIV of GATT 1994 and Article V of GATS. RCEP's "tariffs elimination in 20 years" makes it more ambitious than Korea-China FTA (90%): an average of 91.5% of the tariff lines will be eliminated. But 83% of these tariff lines is already covered in existing FTAs. For all member countries except for Singapore, concession levels are lower than the "ASEAN + 1" FTAs.

The 3 most substantial achievements of RCEP in its commitment for goods are the introduction of a unified Rule of Origin (ROO), cumulation, a simplified Product Specific ROO (PSR), and Self-certification of Origin. However, full cumulation will only be possible if the negotiations for amendment is launched and completed within 5 years after the Agreement enters into force in all member countries. The PSR of manufacturing goods can be either the Change in Tariff Classification (CTC) criterion - mostly consisting of change in any of the 4 digits of the HS code (CTH, Change in Tariff Heading) - or the Value-Added (VA) criterion. In the latter case, RVC (Regional Value Contents) requirement is standardized at 40%.

## C. Services and Investments

Trade in services has been made more transparent by applying Market Access (MA), National Treatment (NT), and prohibiting Performance Requirements (PR). The MA level goes beyond GATS, and in financial services, provisions on new financial services and cross-border movement of financial information was added. China has, for the first time, eliminated restrictions on foreign ownership for life insurance and securities services.

Considering the different level of development of domestic service markets, the services obligations are a mixture of Negative List (NL) and Positive List (PL) approaches. The countries that have adopted the ratchet mechanism for NL and "reservation for existing NCMs" are Australia, Brunei, Indonesia, Japan, Korea, Malaysia and Singapore. The remaining 8 countries will need to switch to NL within 6 years (15 years for C, L and M) after RCEP goes into effect. However, it cannot be said that NL has a broader scope of liberation than PL. For example, the Annex for Indonesia's Schedule of Reservation Appendix amounts to 111 pages.

The chapter on investment contains investment protection, liberalization, investment promotion and facilitation. It also includes NT with ratchet, Most Favored Nation Treatment (excluding CLM), Fair and Equitable Treatment, Prohibition of PR(excluding some CLM), and prohibition of nationality requirements for Senior Management and Boards of Directors(SMBD). Unlike for services, all members have opted NL with ratchet, MFN, PR and SMBD in investment. In the case of China, 22 were added to the 100 liberalization sectors committed in the WTO and went beyond WTO commitments in 37 areas. China applied the ratchet mechanism for the first time in an FTA and added NT and PR to pre-establishment investment.

Investor-State Dispute Settlement (ISDS) was not included due to the strong opposition of New Zealand. Instead, expropriation provisions are laid out in detail in the text and annexes. The matter is to be discussed again if members agree to do so within 2 years of RCEP's entry into force, and is to be concluded within 3 years from the start of discussions.

#### D. Other Trade Rules

The chapter on e-commerce prohibits levying tariffs on electronic transmission, but of the 3 major provisions in TPP's digital trade, only the prohibition on data localization requirements for computer-related equipment, and the prohibition on impeding cross-border data flows were introduced. This was the first time China introduced such provisions.

The Government Procurement chapter only covers for central governments. It includes investment protection measures (NT, MFN, N / L), but it was decided that market access will be discussed at a later time with the consent of the member countries. The chapter on Dispute Settlement also does not apply to Sanitary and Phytosanitary (SPS) measures or e-commerce. The chapter on Trade Remedies includes a prohibition of zeroing when calculating the dumping margin. The chapter on Intellectual Property Rights (IPR) generally has a higher level of protection than TRIPs (Agreement on Trade-Related Aspects of Intellectual Property Rights) and seeks a balance between copyright protection and improvement of social welfare. It also assures the exceptions of the dispute settlement provisions for screening regime to approve or admit a foreign investment proposal for security purposes. The establishment of an RCEP Secretariat to support the RCEP Joint Committee and its subsidiary bodies is a unique feature that differentiates it from other FTAs. Some members are already indicating interest in hosting the Secretariat. If ratified by 6 ASEAN members and 3 non-ASEAN members, the RCEP will enter into force 60 days later, and all members must complete ratification within 5 years. Countries wishing to join RCEP can start negotiations 18 months after its enforcement, with the exception of India which can start negotiations for accession or participate in other economic cooperative projects in the capacity of an observer without waiting for the 18 months to pass.

## II. RCEP's Geoeconomic Opportunities

#### A. Key Features of RCEP-RVC

The first opportunity element lies in the fact that RCEP-RVC is led by China, the economic giant. Over the past 2 decades, the growth of RCEP's intra-regional exports surpassed global exports growth, mainly driven by China. However, China's extra-regional dependence is slightly higher than intra-regional one. Meanwhile, the RCEP 15's growth of exports to India exceeds that of intra-regional or global exports, which means that the withdrawal of India implies a loss of a significant market in the region.

Table 2. Trade Growth of RCEP Member Countries (CAGR, 2000-2019, %)

Importers Exporter		RCEP15							RCEP16		US	EU 28	World
			Japan	China	Korea	ASEAN	Australia	NZ		India			
RCEP15		8.0	4.8	11.9	7.2	8.0	7.6	6.5	8.2	13.9	5.1	6.6	7.4
	Of Japan	4.2	-	8.2	2.2	2.3	2.8	3.3	4.3	8.1	-0.1	0.1	2.1
	China	12.3	6.7	-	12.8	17.3	14.8	14.8	12.8	22.6	11.6	13.2	12.9
	Korea	8.0	1.7	11.1	-	8.5	6.0	8.7	8.2	13.7	3.6	4.0	6.2
	ASEAN	7.2	3.5	14.1	7.3	6.6	6.6	9.4	7.4	10.8	4.4	4.8	6.5
	Australia	9.8	6.3	19.4	7.0	6.2	-	3.5	9.9	12.4	2.7	5.1	8.0
	NZ	8.1	1.5	19.5	3.8	7.1	4.4	-	7.4	10.2	3.7	2.7	6.2
RCEP16		8.1	4.8	12.0	7.3	8.1	7.7	6.6	8.3	13.9	5.3	6.8	7.6
	India	13.1	5.4	17.9	13.0	14.2	11.0	9.9	13.1	-	9.9	9.3	11.3

Source: Hiromi Oki (2020a)

China's prominent role is also apparent in intra-regional bilateral trade. The top bilateral trades among RCEP15 in terms of volume share is "China → Japan (6.5%)" followed by "Korea → China (6.2%)", "Japan → China (6.1%)", and "China → South Korea (5.1%)." This makes up a typical "hub and spoke" structure centered by China.

Table 3. GVC Participation of China, Japan, Korea, and the US (2015)

Total GVC participation (A + B, %)		China		Japan		Korea		US	
		34.9		37.6		51.7		31.7	
Forward Participation <sup>1)</sup> (A)		17.5		24.4		19.1		22.2	
Top 3 Exporters	1	Korea	11.0	China	19.9	China	37.1	Mexico	11.9
	2	US	9.2	Korea	10.1	Vietnam	6.6	Canada	10.1
	3	Mexico	7.7	Singapore	7.5	Mexico	5.0	China	9.5
Backward Participation <sup>2)</sup> (B)		17.3		13.2		32.6		9.5	
Top 3 Importers	1	Korea	11.4	China	19.0	China	21.3	China	18.5
	2	US	11.2	US	11.7	US	10.5	Canada	15.6
	3	Japan	9.3	Australia	6.4	Japan	9.0	Mexico	7.3

Source: WTO "Trade in Value Added and Global Value Chains: statistical profiles" Country data

Note: 1) "Forward GVC participation" is the ratio of domestic value-added content in total gross exports of intermediate goods. Therefore, the "top 3 exporters" mean ranking of the share of intermediate goods exports.

2) "Backward GVC participation" is the ratio of foreign value-added content of total gross exports of intermediate goods. Therefore, "top 3 importers" mean ranking of the share of intermediate goods imports.

The second factor is RCEP-RVC's linkage with global value chain (GVC). China has emerged as a supply hub of the RVC since 2000. China was merely one of spokes connected to Japan, the RVC hub in 2000. But by 2017, China had become the hub with

Korea, Taiwan, and Japan becoming spokes. On the other hand, Japan, China and Korea are closely linked with the US in the GVC. The <Table 3> depicts GVC participations by country, based on the latest 2015 data. It shows that the US (including Mexico targeting the exports to the US) is second and third intermediate goods exporting country for China and Korea, respectively in terms of forward participation. China is also US's third largest parts and components exporting market. Even in terms of backward participation, Japan, China and Korea's dependence on the US and the latter's dependence on China are evident.

The linkage between RCEP and GVC is manifested in the low level of integrity in terms of internal exports. The share of RCEP members' intra-regional exports out of total GDP (8.4%) is lower than that of the EU (21.6%). This suggests the need for RCEP's "open regionalism."

Table 4. Intra-regional Dependence by Exports to GDP Ratio in Mega FTAs (2019) (%)

Importing Exporting	RCEP	CPTPP	USMCA	EU28	World
RCEP	8.4	4.4	3.7	2.8	20.8
CPTPP	9.7	3.8	9.4	2.5	26.1
USMCA	1.7	3.2	5.2	1.6	10.4
EU28	2.9	1.6	3.2	21.6	34.1
World	5.3	3.1	3.8	7.1	21.4

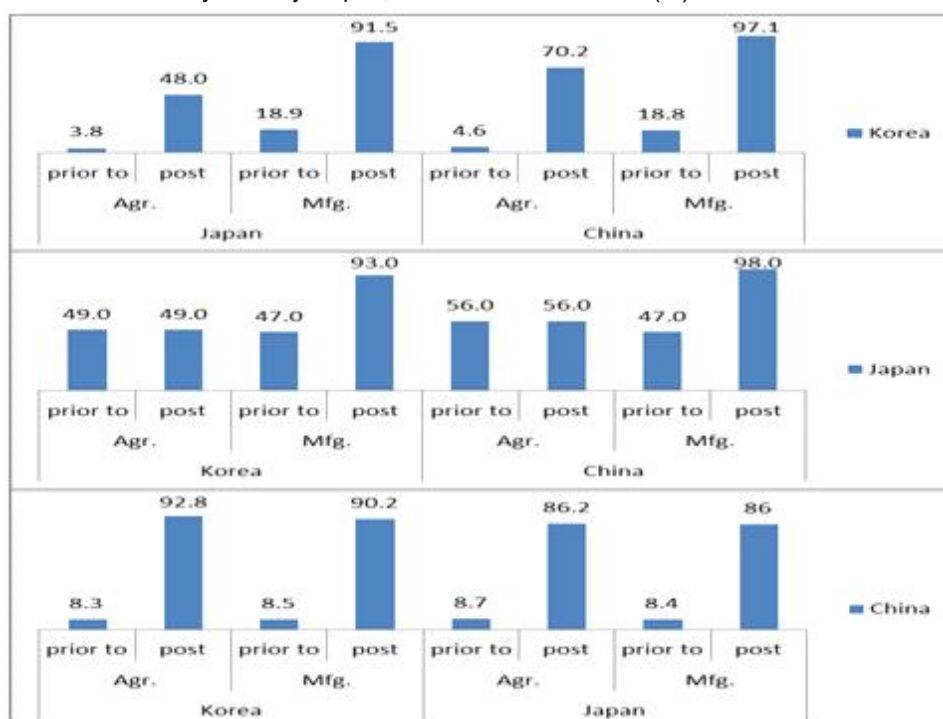
Source: Hiromi Oki (2020b)

Note: RCEP's GDP are for 2018, the others are for 2019

## B. Anticipated Economic Impact of RCEP

Patri and Plummer (2020a) estimate that the conclusion of RCEP will increase the real GDP of RCEP in 2030 by 0.4%, but the largest beneficiaries will be Japan, China and Korea which have relatively large economies. Japan will be concluding an FTA for the first time with China and Korea, which are relatively high tariff countries. This means that Japan's gain from increased trilateral exports will exceed that from RCEP exports. On the other hand, according to Patri and Plummer(2020a), RCEP's effect of increasing global GDP will surpass that of CPTPP. Furthermore, RCEP can provide a cushion against any adverse effects of the US-China trade dispute. If it becomes RCEP16 with the participation of India, the GDP of RCEP15 is estimated to decrease with only Singapore and Australia increasing their GDP by a slight margin. The authors call attention to the competitive relationship between India and RCEP in light industries and high-tech manufacturing. However, Kensuke Yanagida (2020) estimates that if RCEP16 is signed GDP will increase in all countries except New Zealand. Ken Itakura and Hiro Lee (2019) and Kawasaki (2017) anticipated results similar to that of Kensuke Yanagida(2020).

Fig 1. Tariff Concession Levels by Country: Japan, China and South Korea (%)



Source: Created based on the research of the Mizuho Research Institute (November 30, 2020) and Ministry of Trade, Industries and Energy (2015)

Note: Assuming tariffs between Korea and China to be eliminated within 20 years

The effect of RCEP's opening of trade in goods stems from almost, if not all, the liberalization between China, Japan and Korea. The order of trilateral concession levels for primary goods are China> Korea> Japan, and Japan> South Korea> China for industrial goods are. These orders reflect the comparative advantages of each country. However, for a more accurate comparison, a comparison needs to be done with the RCEP Schedule of Commitments.

If we compare the level of China's concession on goods to Korea (based on Korea-China FTA) and Japan (based on RCEP), there was an increase of 84.5%p from 8.3% to 92.8% for primary products, and an increase of 81.7%p from 8.5% to 90.2% for industrial goods in terms of China's market opening vis-à-vis Korea. China expanded its primary goods market for Japan from 8.7% to 86.2% - a significant increase of 77.5%p, and the industrial goods market was expanded by 77.6%, from 8.4% to 86.0%. RCEP is also a Japan-Korea FTA. The mutual concession levels between the two countries are 83% for both countries based on the tariff lines (Japan's calculation: South Korea 83%, Japan 81%), and based on import value, 76% for Korea and 78% for Japan. South Korea's concession level for Japan increased from 3.8% to 48% (44.2% p +) for primary products, and from 18.9% to 91.5% (Korea's calculation: 91.7%) (72.6% p +) for industrial products. Japan's concessions to Korea increased from 49% → 49% for primary products and 47% → 93% for industrial products (Korea's calculation: 94.1%) (46% p +) in terms of tariff lines.



### III. The Geo-economics and Geopolitics of RCEP for Each Country

#### A. Korea

RCEP is Korea's first mega-FTA. With the conclusion of RCEP, Korea now has FTAs with the world's five largest economies. South Korea attaches great significance to RCEP, because it means being integrated into a vast regional market with great potential at a time when the global economy shrunk due to the COVID-9 crisis. (Ministry of Industry and Trade, 2020)

RCEP also is a Korea-Japan FTA. The reason why Japan-Korea FTA negotiations were suspended in 2004 was due to the highly competitive relationship between the industries of the two countries and the strong opposition by domestic automotive and machinery industries – a situation that remains almost unchanged. On the other hand, the CJK FTA will help lower the price of intermediate and capital goods that Korea imports from Japan to put into products exported to other countries.

RCEP is also a China-Japan FTA. Therefore, in the long term, it means that the comparative advantage Korea enjoyed over Japan regarding the Chinese market will eventually diminish. The detailed effects of this will only be known with an item-by-item comparison of commitment schedules and levels, but since one of the reasons behind Korea's reluctance to sign a CJK FTA has become a moot point, it is necessary to revise Korea's strategy toward China and adjust the pathway toward a CJK FTA.

RCEP may increase Korea's dependence on China, which has been pointed out as a weakness of the Korean economy. The US-China strategic competition is showing signs of becoming a protracted war, so Korea will have to assure its relations with China within the framework of RCEP. The strained Korea-Japan relations is another challenge. There are great expectations for the current government's New Southern Policy. But it will not be easy to formulate a relationship with ASEAN that differentiates Korea from China or Japan, as both countries have already put a great deal of energy in two forming close ties with ASEAN.

#### B. China

China is the largest beneficiary of RCEP. It put a great amount of effort into RCEP as a way to counter Japan which took over the lead after US's departure from TPP and succeeded in having CPTPP enter into force. China, whose outlook for exports to the US and EU markets dimmed due to intensifying strategic competition with the US, has now established the basis to improve access to the Japanese market and can diversify its export market. Above all, it was the first mega-FTA for China. Encouraged by this, President Xi Jinping announced his intention to participate in the CPTPP at the APEC summit meeting on November 20. China appears to be bracing itself to use RCEP as a springboard and aggressively embark upon the CJK FTA.

It was a strategic win for China as well. For some time, Wuhan city was being blamed as

the origin of COVID-19, and China was criticized for how it responded to the outbreak, but China could deflect international attention to RCEP. Furthermore, with the US's presence weakening in the region, China has gained an important foothold to expand its sphere of influence. At the RCEP signing ceremony, Prime Minister Li Keqiang implicitly criticized the US by referring to RCEP as "a victory of multilateralism and free trade" and "a ray of light and hope amid the clouds." In contrast to US's America First policy or UK's Brexit, RCEP has helped China become a guardian of free trade and an advocate for less developed countries in the region. Scholars from the Chinese government and affiliated organizations emphasize that RCEP is characterized by inclusiveness, unlike CPTPP (Weixin, 2020). China also expects that RCEP will help improve relations with Japan and ASEAN by reducing geopolitical tension. (Cyrill Melissa, 2018) China ratified the agreement on March 22, 2021 following depositing the instrument of ratification with the ASEAN Secretary-general on April 15, 2021. By means of it, China completed all process of it next to Singapore who first completed it on April 9, 2021.

### C. Japan

Economically, Japan is by far the largest beneficiary. Japan needed something to cushion itself against an ever-intensifying US-China dispute. It also needed RCEP to increase access to the Korean and the Chinese markets that have relatively high tariffs. With the signing of RCEP, Japan was now participating in all three major mega-FTAs in the world and has emerged as a hub in the global mega-FTA network. It also signed a Trade Agreement (TAG) and Digital Trade Agreement with the US. As a result, 75% of Japan's trade is with FTA partners, and it has gained a strong position for setting trade rules at WTO.

Nevertheless, Japan probably had some difficulties in deciding to join RCEP. Japan hesitated to sign the RCEP which would be a diplomatic win for China. But the delay in negotiations due to unreasonable demands by India provided an excuse and obscured Japan's reluctance. However, Japan changed its attitude after India's withdrawal, and when China pressed for the conclusion in the final stages, it felt a need to prevent China from gaining an even stronger position in RCEP. On the other hand, it seems that Japan had the hidden motive to push the US into joining CPTPP by joining RCEP. In fact, Japan once expressed its intention to join RCEP, and the US changed from its previous negative attitude and supported Japan's participation in TPP (Takahide Kiuchi, 2020). In Japan, there is also a view that RCEP should be linked with Japan's FOIP (Free and Open Indo-Pacific) and Quad (Quadrilateral Security Dialogue) initiatives (Kensuke Yanagida, 2020).

While it is apparent that Japan has gained confidence as it emerged as a hub of global mega-FTA network, the current LDP administration had ambivalent feelings and seemed to hesitate the conclusion of RCEP which will expand the influence of China. However, Japan also finished ratifying it on April 28, 2021.

### D. ASEAN

ASEAN has high expectations for RCEP. Signed against the backdrop of the US-China trade



dispute and the COVID-19 crisis, RCEP combines 5 "ASEAN + 1" FTAs, introduces a unified Rules of Origin, and expects to mitigate the spaghetti bowl effect. ASEAN anticipates that it will not only consolidate member countries (Patunru, Arianto A., and Aprilianti, Ira, 2020) but also serve to strengthen ties with Korea, China and Japan (Cripps Tony, 2020). This is because if the three countries decide to leave China because of the US-China dispute, they are likely to take their investment to ASEAN. (Cripps Tony, 2020) However, RCEP's concession level is lower than the ASEAN + 1 FTA, and ASEAN's dependence on intra-regional trade is already high, so there are doubts as to whether RCEP will substantially create trade and investment diversion effects.

During RCEP negotiations, ASEAN notes that "ASEAN centrality" as a middle-power bloc was strengthened. Indonesia is proud of being the ASEAN leader who played a key role. It was Indonesia that first proposed RCEP, and the country consistently played a leading role throughout the negotiations. Administratively, the ASEAN Secretariat took initiatives. In this regard, ASEAN strongly disagrees with the general notion that RCEP is a China-led RTA (Patunru, Arianto A., and Aprilianti, Ira, Dec. 3, 2020). Petri and Plummer (2020b) also maintain that RCEP, generally known as a China-led FTA, is a victory of ASEAN's "middle-power diplomacy" and would not have been launched without ASEAN centrality.

Considering the different developmental stages of members, the "RCEP Negotiation Principles" was adopted from the very beginning with emphasis on the importance of phased liberalization and consensus. The fact that ASEAN, a regional coalition of small and medium-sized countries, had to take the lead reflects how difficult regional integration is. However, in the long run, the predominant view is that RCEP is more likely to contribute to not ASEAN but China's growing influence within the region (Economist, 2020). Singapore was the first country of RCEP who ratified and deposited the instrument of it with the ASEAN secretary-general. On February 11, 2021, Thailand's parliament approved the agreement.

#### E. Australia / New Zealand

Australia and New Zealand are heavily dependent on the RCEP region for both imports and exports. In the case of Australia, the RCEP is an important trading partner, accounting for 58% of bilateral trade in goods and services and 67% of exports. Nine out of the RCEP members are among Australia's top 15 trading partners. Despite the friction with China, Australia welcomes RCEP under the slogan "smart engagement with Asia." In view of the diminishing role of WTO and intensifying trade dispute between US and China, Australia welcomes the rules-based trade agreement in East Asia, which means that instead of isolation it will engage with the growth engine of the world. The same is true for New Zealand. The RCEP region is important for New Zealand, accounting for 61% of its goods exports, 45% of service exports and 61% of foreign direct investment. Furthermore, 7 of the top 10 trading partners of New Zealand participate in RCEP.

Australia and New Zealand already signed bilateral FTAs with almost all the RCEP member countries. Thus, they are less interested in concessions in the market for goods which is at a lower level than the FTAs. Rather, they are more interested in additional opening of the service sector and new rules for protection of intellectual property rights in which they

have a competitive edge. Since both countries have also joined the high-level CPTPP, they seem to be assigning different roles to RCEP and CPTPP and make them functionally complement each other.

In April 2020, Australia's Prime Minister Scott Morrison's called for an independent investigation into the cause of COVID-19 and China's response. A tit-for-tat ensued and escalated into a trade dispute and diplomatic war. Australia also hopes that the RCEP will contribute to its key foreign policy goal, the Indo-Pacific Strategy. New Zealand considers it a diplomatic feat that ISDS was successfully left out as a result of its strong opposition. Discussions are to resume within 2 years of RCEP's entry into force by all members, but again, a consensus is required. So, insofar as New Zealand is opposed, it will be difficult to introduce ISDS.

#### F. India

India's extra-regional dependence for exports relative to GDP is more than 4 times that of intra-regional dependency. The same is true for imports. Meanwhile, the share of exports to India out of total exports was 7.1% (2019) for Indonesia. It was also relatively low for Korea (2.8%) and Japan (1.6%). India was concerned about the expansion of the trade deficit with China due to RCEP. The inferiority of its dairy products compared to those of Australia and New Zealand was another factor that made India withdraw from the negotiations.

During the negotiation process, India wanted the base year for tariff cuts to be 2019, rather than 2014 as proposed by other countries. India raised tariffs that year on several items as part of its "Made in India" campaign and wanted to increase its manufacturing share to 25% of GDP by 2022. India was dissatisfied because other countries were reluctant to open the service market (particularly the temporary movement of service workers) where it had a competitive advantage. Even in the chapter on e-commerce, India wanted to introduce "data localization" requirements but failed to push it through. (CSIS, 2019)

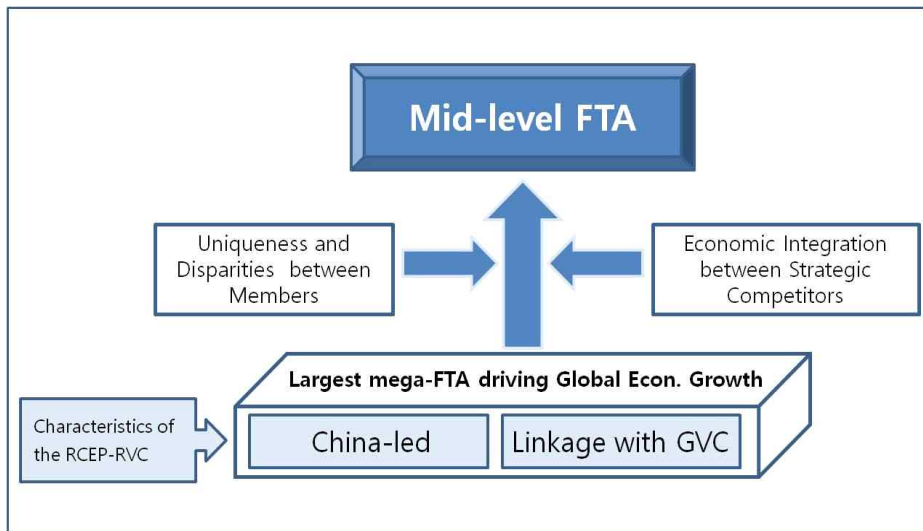
Domestic politics was another factor behind India's withdrawal. When the FTAs with ASEAN, Japan and Korea led to an increase of India's trade deficit, India's ruling party, its support base, the agriculture sector and SMEs opposed RCEP. Conflict with China also held India back. India was not happy that China invited Sri Lanka and Pakistan into the One Belt One Road initiative, and China was becoming increasingly dissatisfied with India joining Quad. Conflict between the two countries became serious. India seems to oppose the conclusion of RCEP which would expand China's influence in the absence of an India-US FTA. Considering such circumstances, it is unlikely that India will attempt to join RCEP soon.

## IV. RCEP Development Challenges and Prospects

### A. Future Development and Challenges for RCEP

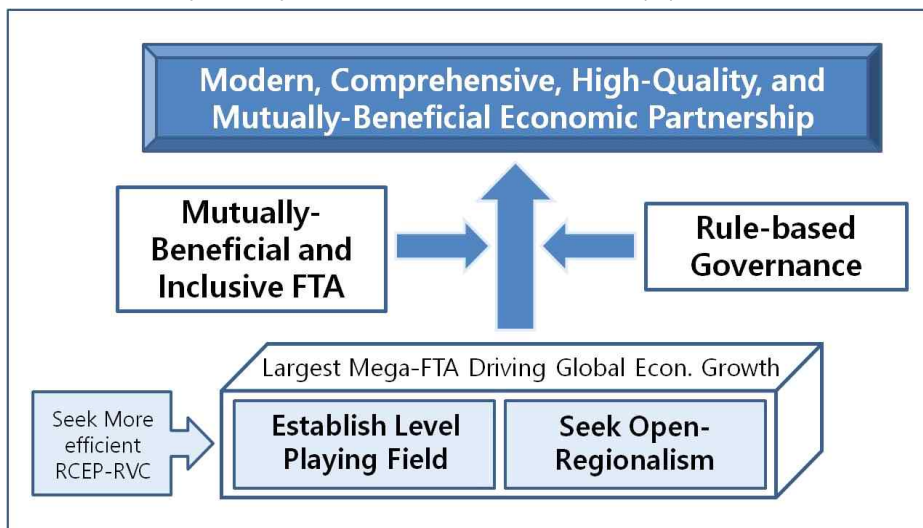
As previously mentioned, RCEP provides both geo-economic opportunities as well as geopolitical risks. Geo-economic opportunities exist because RCEP is an FTA based on the RVC of a region that is the manufacturing hub and growth engine of the world economy. The geopolitical risks stem from the disparity and developmental gaps between member countries and the "economic integration of strategic competitors." The realistic point of compromise is an "ASEAN-led inclusive FTA" in a "China-led bloc." As of now, RCEP stands as a mid-level FTA. (<Fig. 2>)

Fig 2. Current Status of RCEP



Source: Created by the author

Fig 3. Tariff Concession Levels by Country: Japan, China and South Korea (%)



Source: Created by the author

What then are the common challenges for all member countries in achieving RCEP's objective "to establish a framework for a modern, comprehensive, high-quality, and

mutually beneficial economic partnership?" Based on the above-mentioned structural characteristics of RCEP, the challenges boil down to maximizing geo-economic opportunities and minimizing geopolitical risks. Considering the nature of RCEP-RVC, the former requires establishing "a level playing field" which requires mitigating China's too strong presence in RVC and "pursuing open regionalism" based on the linkage between RCEP-RVC and GVC. The latter requires "pursuing a mutually beneficial and inclusive FTA" to reduce disparities between member countries and to "build a rules-based governance" to enable a more stable integration between strategic competitors. (<Fig. 3>).

### 1) Maximizing Geopolitical Opportunities

#### **Ensure A Level Playing Field**

The region as a market, and in particular, the Chinese market need to function properly by adhering to rules such as the rules for "Trade Remedies (Chapter 7), "Trade in Services (Chapter 8)" and "Investment (10)," "Intellectual Property (Chapter 11)," "Competition" (13 sheets)," "Institutional Provisions (Chapter 18)," and "Dispute Settlement (Chapter 19)." This is the best way for RCEP to become self-sufficient. This can have a synergistic effect when linked with China's "dual circulation" strategy aimed at growing both domestic and foreign demands. A level playing field will also enhance China's ability to join CPTPP.

Concluding the CJK FTA, which has been adrift for a long time, can serve to deepen RCEP. The negotiations for CJK FTA started in 2012, however, RCEP was concluded first. China was initially eager to conclude the trilateral FTA, and Japan also saw it as a means to upgrade RCEP and further open the Chinese market. The three countries must, therefore, make sure that the rules of the CJK FTA related to IPR, investment, labor, environment, SOEs, and subsidies are set at a high level. The concluded EU-China CAI (Comprehensive Agreement on Investment), although it has been suspended recently, which is deeper than RCEP, and negotiations for upgrading the Korea-China FTA service agreement took place at the same time and mutually enhanced each other.

#### **Seeking Open Regionalism**

"Open regionalism" is necessary in consideration of the RCEP-RVC's dependence on China and linkage with GVC. RCEP's PSR's RVC is as low as 40%, reflecting the linkage with GVC. This level is required to be maintained to minimize trade diversion effects. NAFTA's rigorous ROOs for final goods led to a decrease of foreign import of intermediate goods by about 30% (Conconi, Paola, et al., 2016). Felbermayr et al. (2019) argues that in today's world where GVC is well developed, stringent ROOs for the purpose of preventing trade distortion only impedes global trade.

Flexible FTA rules can also be a useful medium for cooperating with outside RCEP countries. There was a recent case where the Vietnam-EU FTA has decided to approve apparel products processed in Vietnam using Korean fabrics as Vietnam-originated goods when exported to the EU (Ministry of Trade, Industry and Energy, 2021). There should be more such cases among CPTPP members. Furthermore, a blueprint for long term regional integration should be drawn up and shared among member countries.

## 2) Minimizing Geopolitical Risk Factors

### **Promoting Reciprocal and Inclusive FTAs**

It is imperative to attract more investment into the developing countries of the region by engaging in comprehensive development cooperation aimed at better transparency and predictability of relevant rules, capacity building, administrative reform, digital transition, infrastructure upgrade, and elimination of corruption. It is also necessary to build the infrastructure in developing countries to support FTA certificate of origin. Currently, among the FTAs signed by Korea, the utilization rate of Korea-ASEAN FTA for exports is only 50.0%, and the rate is only 43.4% for Korea-Vietnam FTA.

Mitigating inequality and poverty will also help increase the purchasing power of an integrated regional market. This can be linked with SDGs (Sustainable Development Goals), as well as China's One Belt One Road strategy, Korea's New Southern Policy, and Japan's Indo-Pacific strategy. Development cooperation projects can be launched by identifying common areas of these similar initiatives. Reducing RVC's dependence on China should be sought from expansive balancing perspectives by "enhancing the competitive edge, productivity, and influence of the other countries." Also, the principle of pursuing an "inclusive FTA" should not only be a state-level goal. Polarization is expected to exacerbate in a state as well in the post-COVID era. If the gains from trade liberalization are not evenly distributed among the people, it will only nurture trade protectionism and xenophobic nationalism.

When the time arrives and conditions are ripe, North Korea could be included in the RCEP as an observer. This will help North Korea's capacity building and bring the country into the international division of labor structure of RVC. In the long run, There is a need to study the feasibility of designating Kaesong Industrial Complex as an "Offshore Processing Zone(OPZ)" so that it can grow into a trusted member of the international community.

### **Establishment of A Rules-based Governance System**

Regardless of the disparity among member states, it is essential to establish transparent and predictable rules, ensure international legal binding force, and establishing a security-neutral governance system in order to facilitate a more stable economic integration of strategic competitors. Middle-power countries in the region, including ASEAN, have high expectations regarding the "Secretariat" provision which is unique to RCEP. RCEP should clarify its functions and roles in the future as a central pillar of a rules-based governance, and ensure authority and independence based on rules. There still incidences where diplomatic and security issues between major countries in the region develop into trade disputes. There needs to be a mechanism to prevent such occurrences within RCEP. Only then can RCEP present a model for a sustainable "economic integration between strategic competitors."

Building a governance structure that leverages RCEP's strengths as a "mini WTO" will be a model that can help revive WTO's multilateralism. It is worthy of note that RCEP serves

to validate and revitalize regionalism, - not multilateralism. Since RCEP is more likely to promote regionalism rather than multilateralism, efforts must be made to make RCEP a testbed for restoring the order of rules-based multilateralism.

## B. Future Outlook

In the future, RCEP's geo-economic opportunity factors and geopolitical risk factors will fiercely compete against and offset each other. As of now, it is difficult to foresee what the sum of vectors will be.

The greatest accomplishment of RCEP is the single, unified ROO. Meanwhile, its medium-level liberalization and loose RVC (40%) will limit the effect on short-term trade promotion and trade diversion. Nevertheless, in the long term, these factors will enhance the efficiency of products "made in RCEP." There are concerns in the US that the application of the cumulative ROO could make the criteria for "products originated in China" ambiguous and could neutralize the effects of high tariffs against Chinese goods. (Petri and Plummer, 2020b). There is also a possibility that a more efficient RVC could reinforce China's leading stance and further expand China's influence. The decoupling strategy of the US to separate China from the GVC high-tech industries could further exacerbate the situation by weakening the link between RVC and GVC.

The best dynamic scenario would be when RCEP stimulates competition, raises productivity, and advance the institutions of member countries. It is of great concern, however, that excessive competition could adversely affect labor, environment, human rights, etc., and result in a "race to the bottom." But RCEP lacks the rules to prevent this from happening. Therefore rules are needed to control such unintended outcomes.

The geopolitical risks of the "economic integration of strategic competitors" portends a rocky road for long-term development. Clearly, there is an absence of a wise and dedicated leadership such as that of West Germany during the long process of European integration starting with ECSC (European Coal and Steel Community). This is clearly a risk factor. At present, much attention is focused on RCEP's low level of commitments and China's potentially stronger influence. But depending on the members' efforts, the conclusion of RCEP could mean that China's presence will be reduced to being only 1 out of 15 equal members.

Risk factors can also be opportunity factors. The development gap between member countries enables complementary trade and investment, and the developing countries' strong desire for growth can be a driving force for growth. RCEP which is characterized by divergence and disparity deserves to be called a "mini WTO." There are two possibilities: the weakness of governance in WTO could be replicated in a smaller scale, or WTO could step in and create rules that will be most widely accepted.

At present, China, Japan, Singapore and Thailand have completed the ratification of RCEP, and China with Singapore among them even completed further procedures. Korea will probably ratify it without major obstacles. It is, yet, questionable whether Australia which is at odds with China will be quick in ratifying it. Malaysia and Brunei yet to even ratify



CPTPP. When RCEP comes into effect, the timetable for a mega-FTA will also speed up. China's response to Taiwan's interest in joining RCEP will be a litmus test. It will allow us to gauge the sustainability of the economic integration model among strategic competitors. The US is expected to address the matter in the medium term, say, after the 2023 midterm elections, as it is currently preoccupied with urgent domestic issues. However, the US is likely to pursue a TPP+ that is upgraded to the level of USMCA rather than simply join the CPTPP which entered into force minus the 22 provisions that the US was interested in.

Economic integration itself is not an end but a means. In today's world when the spirit of international cooperation and solidarity has disappeared, and every country is fending for itself, RCEP can set an example by establishing an Asia-Pacific regional order anchored on peace and prosperity. Rather than discounting RCEP as a shallow agreement, we need to take the attitude and effort to minimize geopolitical risk factors and maximize geo-economic opportunities. Ultimately, RCEP will be a test bed of the region's collective intelligence and diplomatic capacity.

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