Free trade still kickin'

Asian nations sign RCEP deal

- **ASEAN and its five partners signed deal to form free trade area covering over 30% of world GDP**
- **According to HSBC projections, RCEP will account for more than 50% of global GDP by 2030, even if India does not subsequently join**
- **While a shallower agreement than the CPTPP, RCEP provides a platform for meaningful further integration in the coming years**

It's done. **ASEAN** and its five partners – **mainland China, Korea, Japan, Australia, and New Zealand** – have been trying to ink an agreement **since 2013**. While initially the negotiations moved slowly, since around 2017 there has been a renewed drive to arrive at an agreement, not least as a counterbalance to rising protectionist impulses elsewhere in the global economy. With an agreement in place, the next step requires national ratifications, after which RCEP ('Regional Comprehensive Economic Partnership') will come into force likely by the **middle of next year**.

The precise details have not yet been made public. However, according to the ASEAN statement today, the deal will **eliminate tariffs and quotas on 65 percent of goods** traded within the region. Meanwhile, other tariffs and restrictions will be liberalized over the next 20 years, covering ultimately **over 90 per cent of trade** within the bloc (although some duties on sensitive products, for example on beef and rice imports into Japan, will remain in place).

Moreover, RCEP establishes a **common rules-of-origin framework**, which will enable exporters in RCEP economies to use inputs sourced from other members in order to qualify for preferential access when trading within the bloc. Importantly, this should provide a **platform for further liberalization** over time.

RCEP is a modern and 'high quality' agreement, that also aims to tackle **non-tariff barriers** to trade in areas such as **services, investment, e-commerce, competition, government procurement, intellectual property, and the movement of people**.

Although the details of the final agreement still need to be released, the main beneficiaries from the RCEP deal are likely to be **Korea, Japan, Malaysia, Thailand, and mainland China** (see also Chart 1 below). India has withdrawn from the negotiations and will thus not see direct benefits. However, the deal provides for other economies to potentially join in the future, **keeping the door open for India to join** at a later date.

RCEP's 15 members generated USD 26 trillion of GDP in 2019, or a little over 30% of world output. This makes the free trade area slightly larger than USMCA and significantly larger than CPTPP (see chart 2). According to HSBC forecasts, the **share of RCEP-15 will rise to over 50% of global output in 2030**.

Already, the majority of RCEP economies send more than half of their exports to other members, and the **proportion is likely to rise** given the region's growing share of global GDP over time and the effect of deeper liberalization (see Chart 3).

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Frederic Neumann

Co-Head of Asian Economics Research
The Hongkong and Shanghai Banking Corporation Limited

Shanella Rajanayagam

Trade Economist
HSBC Bank plc

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The new deal also aims to streamline the various overlapping preferential trading arrangements that most RCEP members already have with each other by establishing common trade rules. This should help to reduce trade costs for businesses. In addition, RCEP is the **first trade agreement that links Japan and mainland China**, the region's economic heavyweights.

Although RCEP is not as far-reaching, in terms of tariff liberalisation, as some other deals such as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) or the EU-Japan Economic Partnership Agreement, it represents an important step towards broader regional integration. The unified rules of origin may help to **strengthen regional supply chains** in the wake of COVID-19, and provide market diversification opportunities for exporters and importers of intermediate inputs operating within the bloc.

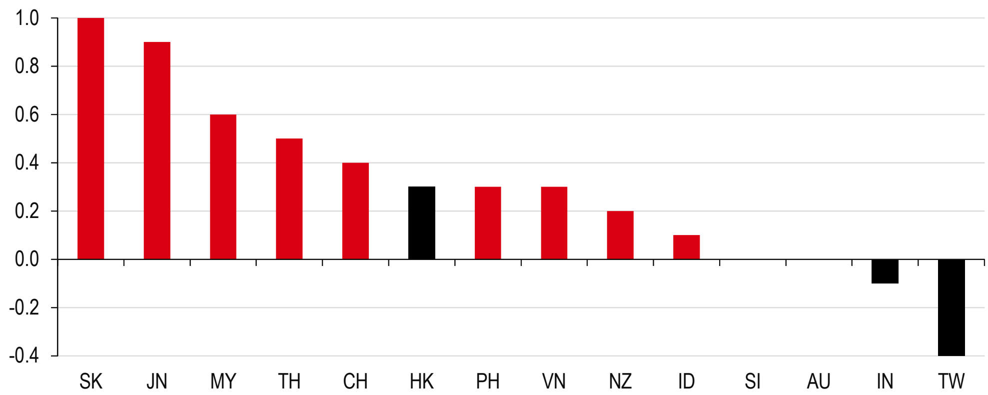
In terms of next steps, the deal is expected to **take effect sometime next year** once parties complete their domestic ratification procedures. RCEP will reportedly enter into force once it has been approved by either half the membership or by six ASEAN economies and half of the non-ASEAN parties.

From a global perspective, the RCEP agreement, even if a littler shallower than other 'mega-deals', signals that **Asia keeps pushing ahead with trade liberalization** even as other regions have become more sceptical. As such, it may reinforce a trend that's been already underway for decades: that **the global centre of economic gravity keeps pushing relentlessly to the East**.

Frederic Neumann, Co-head Asian Economics Research

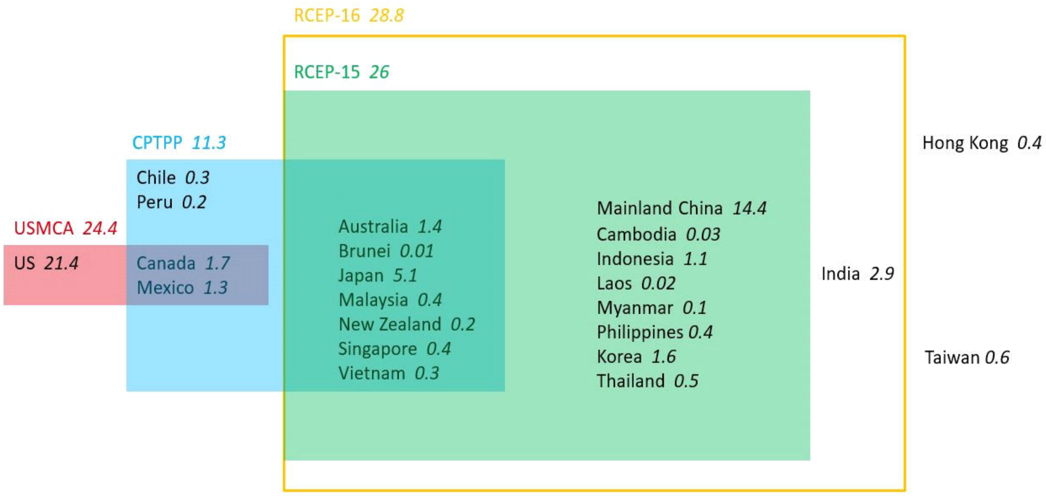
Shanella Rajanayagam, Trade Economist

Figure 1: RCEP-15 - Projected incremental real income gains by 2030* (%; red = members, black = non-members)



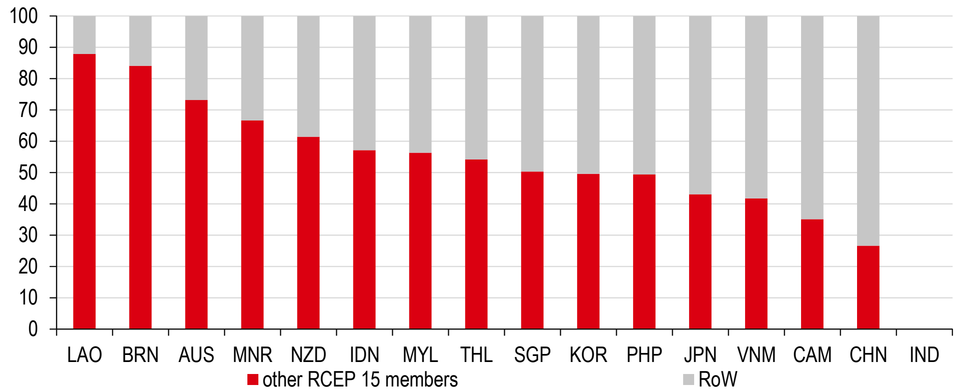
Source: Peter A. Petri and Michael G. Plummer, East Asia decouples from the United States: Trade war, COVID-19, and East Asia's new trade blocs, PIIE Working Paper, 20-9, June 2020; NB: CH refers to mainland China; *assumes ongoing trade friction between mainland China and US

Figure 2: Trade blocs and economies: GDP, 2019, trillions of USD



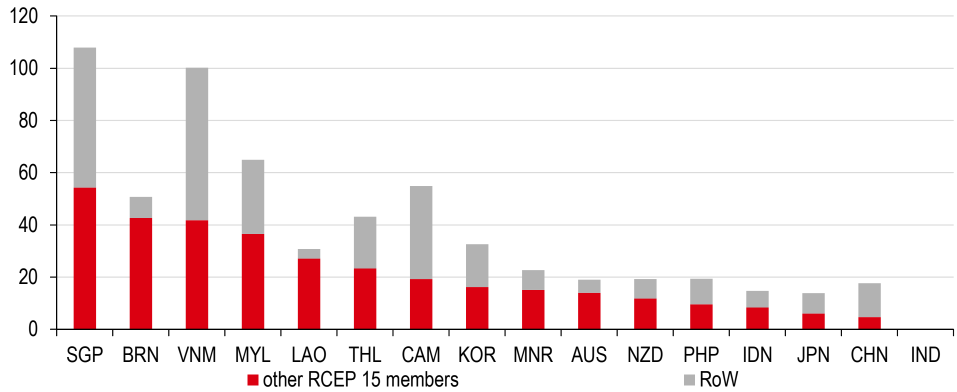
Source: IMF, HSBC

Figure 3: Exports by destination (% share, 2019)



Source: CEIC, HSBC; NB: CHN refers to mainland China, RoW refers to Rest of World, BRN refers to Brunei, LAO refers to Laos, MNR refers to Myanmar, CAM refers to Cambodia

Figure 4: Gross exports by destination (% of local GDP, 2019)



Source: CEIC, HSBC; NB: CHN refers to mainland China, RoW refers to Rest of World, BRN refers to Brunei, LAO refers to Laos, MNR refers to Myanmar, CAM refers to Cambodia

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Issuer of report
The Hongkong and Shanghai Banking Corporation Limited
Level 19, 1 Queen's Road Central
Hong Kong SAR
Telephone: +852 2843 9111
Fax: +852 2801 4138
Website: www.research.hsbc.com

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