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Research Report

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Policy Brief, No. 6

Provided in Cooperation with:

Center for Indonesian Policy Studies (CIPS), Jakarta

Suggested Citation: Gultom, Donna (2020) : RCEP: The Opportunity for Indonesia and Steps of Its Implementation, An Insider's Perspective, Policy Brief, No. 6, Center for Indonesian Policy Studies (CIPS), Jakarta

This Version is available at:

<https://hdl.handle.net/10419/249439>

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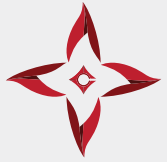
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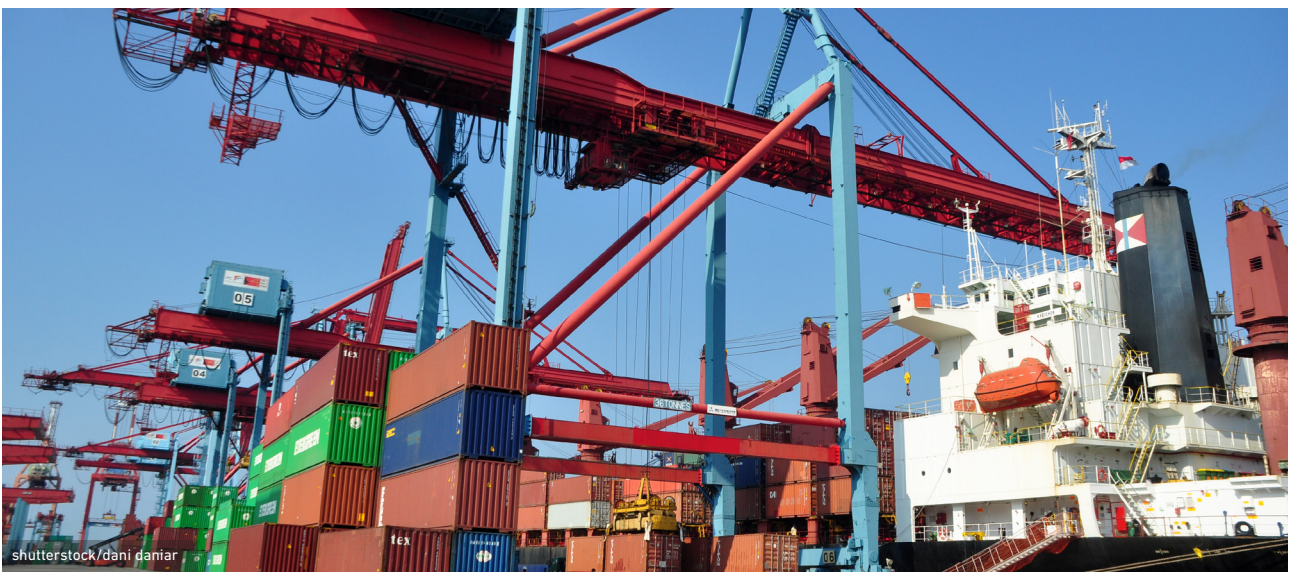
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Policy Brief No. 6

Regional Comprehensive Economic Partnership (RCEP): How Indonesia can Maximize the Opportunities An Insider's Perspective

by Donna Gultom¹



Key Messages

- The signing of RCEP sends a signal to the world that its 15 members are highly committed to work together towards a global economic recovery, and that trade and global economic relationship will continue to grow.
- The advantage of RCEP for Indonesia is the potential market access and foreign direct investment (FDI) to improve Indonesia's participation not only in the regional value chain (RVC) of RCEP but also the global value chain (GVC).
- To gain real economic benefits from RCEP, Indonesia must conduct structural and policy adjustment in order to increase the national economic competitiveness and to ensure the interest of investors, local as well as foreign ones, in manufacture industry, especially in digital industry and those oriented to Fourth Industrial Revolution.

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The Economic Power of RCEP



The Regional Comprehensive Economic Partnership (RCEP) trade agreement has been signed by Economic/Trade Ministers of its 15 member countries on 15 November 2020, witnessed by their respective Head of States. The 15 member countries of RCEP are 10 ASEAN members (Indonesia, Malaysia, Singapore, The Philippines, Thailand, Vietnam, Myanmar, Laos, Cambodia, and Brunei Darussalam), as well as five ASEAN FTA Dialogue Partner (China, South Korea, Japan, Australia, and New Zealand). While the signing was done virtually, its echo reached the entire world. In the midst of Covid-19 pandemic that brings the global economy to recession, these 15 countries are able to realize their commitment in concluding the RCEP negotiation after eight years of negotiations. By signing the RCEP, the 15 members are conveying a message to the world that they are committed to immediately work together to recover from the global economic contraction. This moment also sends a message that trade and global economic relations will continue to grow.

After the Guiding Principles and Objectives for Negotiating the Regional Comprehensive Economic Partnership was agreed in November 2012 and during negotiations that started in 2013 until November 2019, there were initially 16 participating countries of RCEP. However, India withdrew from RCEP in November 2019 when the negotiation was entering its substantial conclusion. All the other 15 countries agreed to continue the negotiation that was targeted to be completed by the end of 2020 by the 15 leaders, while in parallel working together to bring India back to the negotiation process. Without India, RCEP is still considered to have the biggest economic power for trade agreement in comparison to other agreements, such as Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CP-TPP), North American Free Trade Agreement (NAFTA), and EU-28. RCEP represents approximately 30% of the global population, 30% of the world's gross domestic product (GDP), 27% of world trade, and 29% of the world's foreign direct investment.

RCEP agreement will be officially in force after at least six ASEAN members and three ASEAN trade partners have submitted their ratifications document to ASEAN Secretariat. It is expected that RCEP agreement will be effectively enforced the soonest in 2022.

The History of RCEP

The RCEP initiative was first introduced by Indonesia in 2011 when Indonesia was the chair of ASEAN. That initiative came as a response to pressures coming from some Free Trade Agreement (FTA) Partners of ASEAN, especially from China and Japan. As it is with ASEAN, both of these partners looked forward to ASEAN establishing an FTA involving all or some of the FTA partners. China, for example, would like ASEAN to establish FTA with only three FTA Partners of ASEAN, which are China, Japan, and South Korea. However, at the same time, Japan suggested ASEAN to develop FTA involving all its FTA Partners, which are China, Japan, South Korea, India, Australia, and New Zealand.

In 2011, Indonesia successfully convinced ASEAN members to develop a mega FTA that brings all its FTA partners into a regional comprehensive economic partnership, which was later named RCEP, as an ASEAN initiative and offered the initiative to all FTA Partners in November 2011, at the end of Indonesia's leadership tenure.

After an intensive joint dialogue during 2012, all ten ASEAN Head of States and six FTA Partners announced that they will start the RCEP negotiation in 2013. All 16 countries also agreed to adopt the Guiding Principles and Objectives for Negotiating the Regional Comprehensive Economic Partnership as a guideline to carry out the RCEP negotiation.

The first negotiation started in May 2013 in Brunei Darussalam, and after almost eight years of intensive negotiations, the RCEP negotiations reached its final conclusion and was signed on 15 November 2020. The negotiation was led by Indonesia, specifically the Directorate General of Negotiation and International Trade, Ministry of Trade, from the outset of the negotiation until the signing of the agreement. Indonesia was appointed by 15 other members as the Chair of the RCEP Negotiating Committee and by 10 ASEAN Member States as ASEAN Coordinator. Throughout an intensive and long negotiation that required endurance, time, strength, and deliberation, the agreement finally came to an end, concluded and signed. As India already withdrew themselves at the end of the negotiation, the signing was done by only 15 countries.

The lengthy negotiation process was filled with various challenges due to the different ambitions from 16 members who are at different stages of economic development. Some of RCEP participating countries fall under the category of under-developed economy, such as Cambodia, Laos, and Myanmar, a majority are developing countries, and several are considered developed countries, such as Japan, South Korea, Australia, and New Zealand. The agreement was achieved after considering numerous challenges from all RCEP participating countries. Some flexibilities and exceptions had to be included to reach a consensus, but fortunately without any side-letter. Hence, RCEP Agreement is different from Trans-Pacific Partnership (TPP) Agreement, now known as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) in the absence of the United States. The agreement and the level of ambition of RCEP were decided together by consensus of all 15 participating countries, while TPP or CPTPP was already established by the US as the main initiator since the outset and the differences were resolved by issuing side-letters.

RCEP Agreement

Since it was signed on 15 November 2020, the full RCEP Agreement can be downloaded from ASEAN Secretariat's website. This agreement is the most comprehensive ASEAN FTA Agreement, with 14,367 pages consisting of 20 Chapters, 21 Annex of Agreement Text, and 4 Annex of Agreement Commitment. Those twenty chapters are:

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



Meanwhile, commitment from each RCEP members in relation to market access (Goods, Services, Investment, and Movement of Natural Persons/MNP) is stated in four Annex of the RCEP agreement, which are:

1. Schedules of Tariff Commitments;
2. Schedules of Specific Commitments on Services;
3. Schedules of Reservations and Non-Conforming Measures for Services and Investment; and
4. Schedules of Specific Commitments on Temporary Movement of Natural Persons.

This mega FTA Agreement did not come from nothing. RCEP was established with the foundation of pre-existing FTA relations between ASEAN countries and its five FTA partners. The FTA relations between each FTA partner, for example the bilateral FTA between Japan and India, or Australia and New Zealand are also used as reference during RCEP negotiations. The state of FTA relations amongst the 16 RCEP participating countries is described in Table 1. However, to achieve a consensus for the RCEP mega FTA is not easy, not only amongst partners with no FTA relations but also between the ASEAN members and the six partners as well as amongst several partners that have established FTA. To give the same commitment to all other RCEP participating countries has become a great challenge. That was the biggest challenge faced by India during the negotiation, resulting in their absence in RCEP. For Indonesia and some other ASEAN members, giving the same commitment to all partners also have its own difficulty considering the different level of sensitivity toward each of those FTA Partners. 60% of Indonesia's export, valued between USD 85 billion to USD 100 billion, is going to the other 14 RCEP members, while 65% of Indonesia's import is also coming from the same region.

Table 1.
FTA Status between RCEP Members

	ASEAN	Australia	China	India*	Japan	Korea	New Zealand
ASEAN		Yes	Yes	Yes	Yes	Yes	Yes
Australia	Yes		Yes	No	Yes	Yes	Yes
China	Yes	Yes		Yes	No	Yes	Yes
India	Yes	No	No		Yes	Yes	No
Japan	Yes	Yes	No	Yes		No	Yes-CPTPP
Korea	Yes	Yes	Yes	Yes	No		Yes
New Zealand	Yes	Yes	Yes	No	Yes-CPTPP	Yes	

Notes: *India's highest FTA commitment is only with Japan (around 80%) and with ASEAN 75%. This situation has created a great challenge in determining modality as well as level of ambition for opening the market access under RCEP.

Analysis of Potential Benefits of RCEP

A. Market Access Opening

Since the beginning of the initiative, ASEAN realized that the economic gain/benefit from the opening of market access (goods) under this RCEP would not be too significant, as most of the benefits already comes from the existing FTA agreements (5 ASEAN+1FTAs): ASEAN-China FTA, ASEAN-Japan CEP, ASEAN-Korea FTA, ASEAN-India FTA, and ASEAN-Australia-New Zealand FTA. Therefore, the additional economic gain for ASEAN could be harvested from the opening of new market access under the ASEAN+1FTAs, spill-over effect from the opening of market between each FTA partners, as well as FTA bilateral of each RCEP country with non-RCEP (as reported in the study of Ministry of Trade of Indonesia and CIPS), and also trade efficiency between RCEP members through accumulation mechanism adopted in Rules of Origin (ROO), trade facilitation scheme, and other provisions of RCEP Agreement.

B. Enhancing Foreign Direct Investment (FDI)

This agreement is expected to boost FDI growth in new industry sectors that can utilize the RCEP's potential as a global region with 2.2 billion population. If it were to rely only on existing industries and businesses, the opportunity provided by RCEP could not be fully utilized. New investment is the key to the establishment of new industries. Therefore, the RCEP member that will be able to seize this opportunity is the country with attractive investment regime and good infrastructure support. Considering the experience of the ongoing Covid-19 pandemic, investors tend to allocate their new investment into RCEP countries who are ready to support the development of industries related to the 4th Industrial Revolution and e-commerce. Rashma Banga (UNCTAD, 2020) sees that ASEAN has the opportunity in the digital sector, therefore efforts to enhance competitiveness in this sector will maximize RCEP's advantages. RCEP provides the opportunity to enhance e-commerce trade amongst RCEP countries as stipulated in Electronic Commerce Chapter, while policy space is given to the government to manage policy development of this industry, especially when it relates to the public sector. The success of a country in developing its digital economy will provide opportunities for Micro-, Small-, Medium- Enterprises (MSMEs) such as small business, farming business, and creative individuals from remote area and foster the development of factory sharing economy. It will enable countries like Indonesia to supply the RCEP market demand of 2.25 billion people.

C. Study of RCEP's Advantages

Several studies using various quantitative simulation models have supported the aforementioned benefits of RCEP. During the negotiation process in 2016, the Trade Policy Analysis and Development Agency (*Badan Pengkajian dan Pengembangan Perdagangan/BP3*) of the Indonesian Ministry of Trade conducted an analysis using Computable General Equilibrium (CGE) and found that RCEP increases welfare, but at the same time also increases Indonesia's trade deficit with the other RCEP members (Rakhman, 2016). The study further suggested that Indonesia should strengthen its ability to utilize RCEP Regional Value Chain (RVC) considering that there are 6,050 Indonesia's tariff post (tradable goods) with strong export and import connections to and from RCEP region. In 2019, the Indonesian Ministry of Finance carried out another study on the impact of RCEP to Indonesia's economy using CGE model. The result showed that RCEP will increase Indonesia's Gross Domestic Product (GDP) by only 0.05% between 2021 - 2032, much smaller comparing to the benefits gained by the other RCEP countries, like Vietnam 0.66%, South Korea 0.51%, Malaysia 0.35%, and Thailand 0.21% (Nugroho, 2020). However, the study further indicated that if Indonesia decided to leave RCEP, its economic growth (GDP) will fall -0.07%. Therefore, Indonesia has no choice but to stay in RCEP and go through structural adjustments in order to enhance efficiency and competitiveness.

Another study by Ira Aprilianti (2019), using a stochastic gravity model, showed that the FTA's spill-over effect for RCEP members and non-members can potentially increase Indonesia's export by 7.2% through expansion of Indonesia's role in Global Supply Chain. After five years of implementation, the export increase could reach 8 - 11% and investment could grow by 18 - 22%. Meanwhile, another study done by Rashmi Banga (UNCTAD, 2020), using a different model, SMART Simulations in World Integrated Trade

Solutions by World Bank and UNCTAD, concluded that the advantage of RCEP for ASEAN members is not too significant compared to the partner countries, because the market access was already open through ASEAN+1 FTAs. The analysis showed that when RCEP is implemented, the majority of ASEAN members, especially Cambodia, Malaysia, Myanmar, Thailand, Vietnam, and Laos will experience a spike on import that will cause significant trade deficits (especially for Malaysia, Cambodia, and Vietnam). Therefore, Rashmi Banga further highlighted that additional benefit of RCEP for ASEAN members will only be from the utilization of Regional Value Chain that will be connected to Global Value Chain. The challenge is then how ASEAN members will be able to create and develop efficient producers and exporters who can compete with China's efficiency. Aside from trade in goods, ASEAN also has an opportunity on the digital industry sector.

The takeaway from the four studies is that if Indonesia and other ASEAN members would like to get real and significant economic advantage out of RCEP, they must take on structural and policy adjustments to enhance the competitiveness of the national economy. The structural and policy adjustment through the implementation of Indonesia's Omnibus Law (*UU Cipta Kerja* or Job Creation Law) is one of the most important policies that will enable Indonesia to attract new investments.

Future Economic Development

As RCEP is based on ASEAN+1 FTAs (ASEAN-China FTA, ASEAN-Japan FTA, ASEAN-Korea FTA, ASEAN-India FTA, dan ASEAN-Australia-New Zealand FTA), it is almost certain that in the initial stage of its implementation, there would not be a dramatic or significant spike of utilization of RCEP's agreed scheme to tap into its 2.2 billion market population. All existing businesses and exporters will still use the current FTA scheme, except for RCEP countries that have not yet established bilateral FTA among them or for products that are newly open under the RCEP Agreement. Rashmi Banga's study (UNCTAD) (2016) most likely did not consider this factor when it showed that most ASEAN members will experience an increase in imports as soon as RCEP is implemented. The estimated increase in import that might occur right after RCEP is implemented would happen in FTA Partner countries that have not yet established FTA with each other (Japan vs China and Japan vs Korea).

On the other hand, RCEP provides opportunity to all members to develop industry that can utilize RCEP (1 country vs 14 countries). RCEP becomes even more relevant amidst the ongoing Covid-19 pandemic that still pose a serious challenge and economic pressure to all RCEP countries and the world. With this background, the industry with big potential to be further developed would most definitely be industry that is digital and oriented towards the Fourth Industrial Revolution. Similarly, it is inevitable that trade transaction and facilitation for export and import will also be conducted electronically.

Hence, to ensure RCEP is beneficial for Indonesia, aside from increasing industry competitiveness, Indonesia must also make sure that there will be investors, domestic as well as foreign, in manufacture industry sector, especially those that are digital and oriented towards Industrial Revolution 4.0. Investors who are well aware of the promising development of regional supply and value chain will enter countries with integrated infrastructure (physically as well as administratively) that are already connecting or are ready to connect with RCEP and globally. Indonesia is expected to be able to realize the prediction made by Ira Aprilianti (2019), where investment will significantly increase (18 - 22%) in five years after RCEP implementation.

Structural and Policy Adjustment

As recommended by various studies on the effect of RCEP for Indonesia's economy, Indonesia must prepare or implement policy or structural adjustment to maximize the gains from RCEP in the very near future. The government realizes that the key success to take advantage of RCEP for Indonesia's economic development is to improve national competitiveness of the existing industry and the investment climate to attract investment in digital industry and those oriented towards the Fourth Industrial Revolution.

Those steps are in line with efforts for long-term economic recovery that has to be administered in a serious, smart, comprehensive, and simultaneous manner. Covid-19 pandemic has to be Indonesia's turning point to promote the growth of industry which will support the national economic recovery program towards sustainable economic growth that can bring Indonesia to a higher economic level.

Economic development through increasing competitiveness and promoting the growth of value-added industry in the context of the Fourth Industrial Revolution must be prioritized as part of economic recovery. This priority must be considered 'urgent' if Indonesia would like to fulfil the demands coming from domestic and international market, especially from RCEP countries that is predicted to surge after Covid-19 pandemic.

Indonesia must also prepare policies that would attract investments for industry focusing on intermediate products. This policy will promote Indonesia's participation in the regional supply/value chain of RCEP, and the global supply/value chain. Intermediate products will serve as the next-step industries both located in Indonesia (to gain added value) and in other RCEP and non-RCEP countries (export). The fear that import will cause trade deficit is not the case in the future. In this regard, RCEP will contribute to the economic growth of Indonesia through the development of value-adding industries.

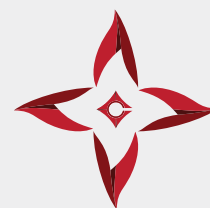
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