Policy Analysis Focus 21-2
Economic Impact of RCEP Tariff Reductions[1]

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I. Introduction

The fifteen Asia-Pacific countries (Japan, China, Korea, Australia, New Zealand and the member states of the Association of Southeast Asian Nations (ASEAN)) signed the Regional Comprehensive Economic Partnership (RCEP) Agreement in November 2020. It is expected to enter into force in ten of the signing countries at the beginning of January 2022.[2] India has withdrawn from RCEP, but the RCEP Ministers have confirmed that "the RCEP Agreement is open for accession by India."[3]

This article will examine the economic impact of tariff reductions resulting from the RCEP Agreement using a Computable General Equilibrium (CGE) model of global trade. The estimated economic impact will be compared and considered across several policy scenarios, including implementation of RCEP with India and without India.

II. Framework of modeling studies

The economic impact of tariff reductions was estimated using a CGE model of the Global Trade Analysis Project (GTAP)[4] incorporating the dynamic effects of capital accumulation with endogenous international capital flows and pro-competitive productivity improvements. Construction of the model used in this article is based on the version 10 GTAP database[5] and GDP levels updated to 2022, to align with *World Economic Outlook Database,* International Monetary Fund (IMF).

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[1] The views expressed in this article are the author's own and do not represent those of GRIPS Alliance or other organizations to which the author belongs.
[2] Japan, China, Australia, New Zealand, Brunei, Cambodia, Laos, Singapore, Thailand and Viet Nam.
[3] See Ministers' Declaration on India's Participation in the Regional Comprehensive Economic Partnership (RCEP), 11 November 2020.
[4] The current version of the standard GTAP model is version 7. The classic version, GTAP model version 6.2, is used in this article for the sake of consistency with earlier studies.
[5] The most recent benchmark year of the GTAP 10 database is 2014.

The tariff data are derived from the International Trade Centre (ITC) *Market Access Map*.[6] The specific assumptions regarding the tariff levels in the individual policy scenarios in this article are as follows:

Baseline: Tariff reductions under major regional trade agreements entered into force before the RCEP Agreement including the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP),[7] even those extending beyond 2022, will be fully implemented.

RCEP15: Tariffs (in addition to the baseline tariff reductions) among the fifteen members of RCEP without India will be reduced according to the RCEP Agreement.

Remaining: All remaining tariffs in the above RCEP15 scenario will be removed among the fifteen RCEP countries.

India joining: in addition to tariff removals among the fifteen RCEP countries, India and the fifteen RCEP countries will remove all tariffs between them.

It should be noted that RCEP has not yet agreed to one hundred per cent tariff removals among the member countries. Calculations by the Japanese government[8] suggest that under the RCEP Agreement, Japan's tariff revenues paid on imports from the RCEP countries would be reduced by around 57 per cent, and Japan's payments of tariffs imposed by the RCEP countries would be reduced by around 61 per cent.

III. Estimated economic impact

Table 1 shows, in an incremental manner, the results of estimated changes in real GDP in the RCEP countries for the three policy scenarios studied in this article.

It is estimated that, as a result of tariff reductions under RCEP without India, increases in real GDP would be larger in Japan, China and Korea than in the other twelve RCEP countries. The fifteen RCEP countries had agreed and implemented a number of bilateral and multinational trade agreements before the implementation of the RCEP

[6] ITC has studied the tariff reduction schedule under regional trade agreements concluded and in force in the world as a whole and has provided tariff data projected a few decades into the future, depending on the timing of the implementation of those agreements. The tariff data used in this article have been updated to reflect the 2020 RCEP Agreement and figures provided by ITC in 2021.

[7] It is assumed here that CPTPP would eventually be implemented by all eleven member countries. As of November 2021, CPTPP had entered into force in eight member countries (Japan, Australia, New Zealand, Singapore, Viet Nam, Canada, Mexico, and Peru), with Brunei, Malaysia and Chile not yet implemented.

[8] https://www.mof.go.jp/customs_tariff/trade/international/epa/jrcep_kanzei.pdf

Table 1 Changes in real GDP, by scenario

(%)

	RCEP15	Remaining	India joining
Japan	1.20	0.56	-0.09
China	0.17	0.15	0.09
Korea	0.30	0.58	0.36
Australia	0.12	0.08	0.11
New Zealand	0.03	0.19	-0.05
ASEAN	-0.15	0.44	0.28
Brunei	0.09	0.33	0.07
Cambodia	0.20	0.84	-0.02
Indonesia	-0.06	0.16	0.40
Laos	0.08	0.30	0.12
Malaysia	-0.16	0.35	0.26
Myanmar*	0.04	0.25	-0.04
Philippines	-0.10	0.15	0.11
Singapore	-0.16	0.03	-0.06
Thailand	-0.35	1.38	0.31
Viet Nam	-0.29	0.79	0.48
All 15 countries above	0.31	0.27	0.10
India	-0.05	-0.07	1.54

Note: * Proxied by the composite region of Myanmar and Timor-Leste.
Source: Author's simulations.

Agreement. Only two bilateral country pairs have not yet implemented any trade agreements: Japan and China; and Japan and Korea. Those three countries would enjoy greater benefits from trade creation effects stemming from tariff reductions under RCEP. On the other hand, it is estimated that real GDP would not necessarily increase in several ASEAN countries. This could be attributed to the balance of trade creation and diversion effects resulting from tariff reductions. The magnitudes of tariff reductions, and therefore the benefits of their trade creation effects under RCEP in the twelve countries discussed above, would be limited and could be more or less offset by adverse trade diversion effects resulting from trade creation effects among the other RCEP countries.

The magnitudes of real GDP increases resulting from the remaining tariff removals among the fifteen RCEP countries (0.27 per cent on average) are estimated to be not substantially smaller than gains from tariff reductions under RCEP (0.31 per cent on average), and much larger than those from the removal of tariffs between India and each of the fifteen RCEP countries (0.10 per cent on average). Meanwhile, it is estimated that real GDP in the ASEAN countries would increase more due to removal of the remaining tariffs than as a result of RCEP tariff reductions. Further tariff reduction efforts would be expected from the perspective of enjoying larger economic benefits.

It is estimated that India's real GDP would decrease as a result of tariff reductions under RCEP without India, but would in turn increase when India joins RCEP and removes all tariffs on trade with the fifteen RCEP countries. Conversely, it is estimated that real GDP would decrease in some RCEP countries. This too could be explained by the trade creation and diversion effects discussed above. India has already implemented trade agreements with Japan, Korea and the ASEAN countries, but not yet with China, Australia or New Zealand. That said, it should be noted that higher or lower tariffs would remain under existing trade agreements between India and the RCEP countries. The net effect of trade creation and diversion would be determined by the relative levels of those remaining tariffs. The actual economic impact of India's participation in RCEP will depend entirely on the magnitudes of tariff reductions between India and the fifteen RCEP countries.

It is important to note that the economic impact of tariff reductions will be of much greater concern at the sector level than the macro level. Current estimates indicate that Japan's production would increase more in textiles and apparel and electronic products as a result of RCEP tariff reductions, but due to remaining tariff removals among the fifteen RCEP countries would decrease in rice and sugar while increasing in motor vehicles and parts. The greater the tariff reductions, the larger would be the effect on sector production.

IV. Concluding remarks

The RCEP Agreement has been signed and is expected to enter into force in the near future. Among the fifteen RCEP countries (without India), Japan, China and Korea would enjoy larger macroeconomic benefits of tariff reductions. On the other hand, there would still be sizable macroeconomic benefits of the remaining tariff reductions among RCEP countries. Meanwhile, by joining RCEP, India would also enjoy macroeconomic benefits. It will be worth watching further efforts toward the realization of free trade in relation to "Free and Open Indo-Pacific."