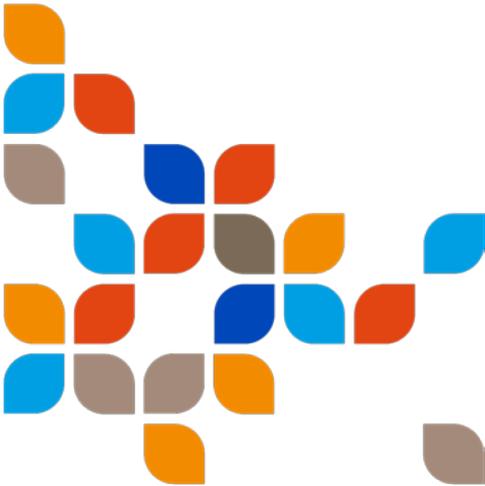

FOREIGN POLICY WHITE PAPER SUBMISSION



Australian trade diplomacy: Shaping the future of the Asian economic architecture through regional trade multilateralism

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Key Points

- With headwinds facing the Trans-Pacific Partnership, Australia needs to recalibrate its trade strategy.
- The turn towards bilateral FTAs during the 2000s posed several challenges – collectively known as the ‘noodle bowl problem’ – for Australia’s economic ties with Asian economies.
- The Australian economy will benefit most from a regionally-focused multilateral trade strategies. Trade multilateralism enables greater engagement and integration with the Asian economic region than bilateral agreements.
- The emergence of mega-regional FTAs such as the Trans-Pacific Partnership (TPP) and Regional Comprehensive Economic Partnership (RCEP) promised to ‘multilateralise’ the regional trade architecture. As a small open economy, Australia stood to gain significantly from this process.
- Of the two mega-regional agreements, the TPP’s emphasis on regulatory rule-making provided the best fit with Australian trade interests. However, the US withdrawal from the TPP has seriously compromised its prospects. RCEP is now the best vehicle for trade multilateralism in the region.
- The ongoing RCEP process offer Australia a critical opportunity to shape the newly-emerging trade architecture of Asia-Pacific. Market access, services and accession provisions should be a key focus for Australian trade diplomacy as RCEP moves towards completion in 2017

Introduction

Australia’s trade diplomacy is at a cross-roads. After a decade of pursuing bilateral free trade agreements (FTAs) with its major trade partners, in the 2010s Australia became involved in two ‘mega-regional’ FTAs in Asia: the US-led Trans-Pacific Partnership (TPP) and ASEAN-centre Regional Comprehensive Economic Partnership (RCEP). These trade agreements promised to transform both the Asia-Pacific trade system and Australia’s place within it. They aimed to ‘multilateralise the noodle bowl’ of over 100 bilateral FTAs that exist in the region, and placed Australia at the centre of a newly-emerging architecture for Asian economic integration.

With the election of Donald Trump to the US Presidency, regional trade diplomacy is now in flux. Having campaigned against the TPP during the Presidential election, the Trump Administration formally withdrew the US in January 2017. Given its current legal design, the TPP cannot enter into force without US ratification.

Australia had been one of the leading proponents of the TPP, and since negotiations began in 2010 the TPP had been a central pillar of Australian trade diplomacy. With the TPP now facing serious political headwinds, Australia needs to recalibrate its trade strategy to adjust to the new regional environment.

As a small open economy with deep trade and investment ties to Asia, Australia’s trade interests are best served by multilateral approaches to regional trade liberalisation. These avoid many of the challenges associated with bilateral FTAs – which trade economists collectively label the ‘noodle bowl problem’ – and provide an integrated institutional platform for Australia to deepen its linkages with the dynamic economies of Asia.



As the potential collapse of the TPP deprives Australia one vehicle for achieving a multilateral trade agreement in Asia, ongoing negotiations for the RCEP agreement have become increasingly important. Australia stands to gain considerably if RCEP is completed, as it provides an opportunity to more fully integrate with the economies of the Asia-Pacific region. Australia is well-positioned to contribute to the RCEP negotiations, and should actively work to shape its provisions in ways that maximise the benefits for the Australian economy.

The fragmented trade architecture of the Asia-Pacific

In the early years of the 21st century, the trade architecture of the Asia-Pacific was dramatically transformed. Regional governments were previously committed multilateralists – pursuing trade liberalisation either through the WTO at the global level, or APEC and ASEAN at the regional level.

But during the 2000s, many Asian governments turned their attention toward bilateral FTAs. Simpler to negotiate than multilateral agreements, bilateral FTAs were considered a ‘quick and easy’ way to open new export markets. As the WTO’s Doha Round began to stall in the mid-2000s, they also presented a ‘second best’ trade strategy: to advance liberalisation on a bilateral basis while multilateral efforts were delayed¹.

The Asia-Pacific quickly became the epicentre of a global move towards trade bilateralism. By the end of 2016, fifty-two bilateral FTAs had been signed by Asia-Pacific governments, and a further fifty-four were negotiated with extra-regional partners². The Asia-Pacific is currently home to half of all bilateral FTAs in-force globally. This process dramatically restructured trade architecture of the region, from one based on regional multilateralism to one criss-crossed by numerous bilateral deals.

Australia has been an active participant in the turn towards trade bilateralism (Table 1). Nine bilateral FTAs have been signed, which now cover all but two of Australia’s top ten trading partners. In 2009, Australia and New Zealand jointly secured a trilateral FTA with the ASEAN bloc. Negotiations are underway with India and Indonesia, the two main Asian economies without a current FTA. Australia is also an active participant in two the mega-regional FTA processes in Asia: the multilateral Trans-Pacific Partnership (TPP) completed in 2015; and negotiations for the Regional Comprehensive Economic Partnership (RCEP) ongoing since 2013.

¹ Christopher Dent (2010), ‘Free trade agreements in the Asia-Pacific a decade on: evaluating the past, looking to the future’. *International Relations of the Asia-Pacific*, 10(2): 201-45; Barry Desker (2004), ‘In Defence of FTAs: From Purity to Pragmatism in East Asia’, *The Pacific Review*, 17(1): 3–26.

² Author’s calculations, from World Trade Organization, *Regional Trade Agreements Database*, available at <http://rtais.wto.org/UI/PublicMaintainRTAHome.aspx>



Table 1 Australia's free trade agreements, February 2017

Agreement	Type	Current Status
Australia-New Zealand (CER)	Bilateral	In-force (1980)
Australia-Singapore	Bilateral	In-force (2003)
Australia-Thailand	Bilateral	In-force (2004)
Australia-US	Bilateral	In-force (2005)
Australia-Chile	Bilateral	In-force (2008)
Australia-NZ-ASEAN	Trilateral	In-force (2009)
Australia-Malaysia	Bilateral	In-force (2013)
Australia-Korea	Bilateral	In-force (2014)
Australia-Japan	Bilateral	In-force (2015)
Australia-China	Bilateral	In-force (2015)
Trans-Pacific Partnership	Regional multilateral	Signed, awaiting ratification (2015)
PACER Plus	Regional multilateral	Under negotiation (2009)
Australia-Indonesia	Bilateral	Under negotiation (2010)
Australia-India	Bilateral	Under negotiation (2011)
Trade in Services Agreement	Global multilateral	Under negotiation (2012)
Regional Comprehensive Economic Partnership	Regional multilateral	Under negotiation (2013)
Environmental Goods Agreement (WTO)	Global multilateral	Under negotiation (2014)
European Union	Bilateral	Under study (2015)

Source: DFAT, *Australia's Free Trade Agreements*, available at <http://dfat.gov.au/trade/agreements/Pages/trade-agreements.aspx>

Trade bilateralism and the noodle bowl problem

The proliferation of bilateral FTAs in the Asia-Pacific has led to a phenomenon trade economists call the “noodle bowl problem”³. Rather than having a single, integrated set of trade rules that apply equally to all parties, the region is now criss-crossed by over a hundred bilateral deals. These bilateral FTAs are often wildly inconsistent. Each contains its own rules for tariff reduction, non-tariff trade policy reforms, and standards for administrative procedures. Some include rigorous implementation of rules for ‘WTO-Plus’ issues – such as investment, services, and intellectual property – while others include these issues in either a piecemeal fashion or not at all⁴.

Trade economists argue that the noodle bowl problem is bad for the global and regional trade systems. Rather than delivering genuinely ‘free’ trade, bilateral FTAs only *preferentially* remove trade barriers between select countries. Some of the difficulties posed by the noodle bowl problem includes:

- **Undermining the GATT/WTO's most-favoured-nation (MFN) principle.** By preferentially lowering trade barriers only between certain countries, bilateral FTAs breach the MFN principle that a country should give equally good trade treatment to all WTO members. While bilateral FTAs are legally allowed under GATT Article XXIV if they liberalise “substantially all trade”, many have extensive carve-outs and sectoral exclusions⁵.
- **Trade diversion rather than trade creation.** Trade flows are distorted by bilateral FTAs, where economies gain (and lose) market share due to the preferential effect of the FTAs rather than

³ Richard E Baldwin (2007), ‘Managing the Noodle Bowl: The Fragility of East Asian Regionalism’, *ADB Working Paper Series on Regional Economic Integration* (No. 7), Manila: Asian Development Bank.

⁴ Jeffrey D. Wilson (2015), ‘Mega-Regional Trade Deals in the Asia-Pacific: Choosing Between the TPP and RCEP?’, *Journal of Contemporary Asia*, 45(2): 345–353.

⁵ Mark Manger (2012), ‘Preferential agreements and multilateralism’, in *Ashgate Research Companion to International Trade Policy*, K. Heydon and S. Woolcock (eds.), Farnham: Ashgate.



underlying patterns of competitiveness. They often simply ‘redistribute’ trade between countries, rather than creating new trade flows⁶. An example is Australia’s diary trade with China, where Australian exporters faced discrimination due preferences given to NZ competitors in the China-NZ FTA of 2008.

- **Imposing transaction costs on businesses.** Bilateral FTAs pose transaction costs for businesses, which must maintain compliance with different rules for all key markets rather than meet a single set of WTO provisions. The cost of securing multiple Rule-of-Origin (ROO) certificates is a key example⁷. These costs are especially prohibitive for small- and medium-enterprises (SMEs), who lack the scale to secure commercial and legal advice.
- **Failure to supporting regional and global value chains.** Many contemporary industries are organised as complex ‘value chains’, where the various stages of production are in different countries. The electronics, automobile, machinery and agro-food sectors are all examples where production is spread across many economies in Asia. As bilateral FTAs only liberalise trade between two nodes, they do little to facilitate the complex trade and investment flows needed for network growth. DFAT has recently identified the importance of *multilateral* liberalisation for Australia’s participation in regional value chains⁸.
- **Power asymmetries and disadvantaging of small economies.** Ensuring robust outcomes from bilateral FTAs depends on the bargaining power of the involved parties. Small economies typically fare worse, as the small size of their home market limits their ‘negotiating coin’ during FTA talks. When negotiating with larger economies (such as the US, China or Japan), power asymmetries often mean small economies cannot obtain as good a result as they would have through multilateral approaches where they could pool negotiating resources⁹.

These problems especially afflict countries like Australia. As a small and open economy, Australia has less capacity than larger economic powers to secure robust FTAs that ensure major market access gains in key sectors such as agriculture and services¹⁰. The transaction costs associated with bilateral FTAs are also highly prohibitive for Australian SMEs, who have struggled to make full use of the agreements¹¹.

Multilateralising the Asian noodle bowl? The TPP and RCEP agreements

Given the potential benefits of trade multilateralism for Australia, a positive development has been the recent emergence of two ‘mega-regional’ trade agreements in Asia-Pacific: The Trans-Pacific Partnership (TPP) and Regional Comprehensive Economic Partnership (RCEP) agreements.

The TPP was launched in 2010, and by the completion of negotiations in October 2015 had grown to twelve member states drawn from the APEC group. RCEP negotiations commenced in 2013 between the ASEAN

⁶ Mian Dai *et al.* (2014), ‘On the trade-diversion effects of free trade agreements’, *Economics Letters*, 122(2): 321-325.

⁷ Patricia Augier *et al.* (2005), ‘The impact of rules of origin on trade flows’, *Economic Policy*, 20(43): 568-624.

⁸ DFAT (2016), *TPP Background papers: Global Value Chains and the TPP*, available at

<http://dfat.gov.au/trade/agreements/tpp/outcomes-documents/Pages/background-papers-global-value-chains-and-the-tpp.aspx>

⁹ Ann Capling and John Ravenhill (2015), ‘Australia’s flawed approach to trade negotiations: And where do we sign?’, *Australian Journal of International Affairs*, 69(5): 496-512.

¹⁰ Jeffrey D. Wilson (2015), ‘China-Australia trade agreement a compromised victory’, *The Conversation*, 18 June.

¹¹ HSBC (2014). ‘Australian companies under-utilising Free Trade Agreements, HSBC research’, available at <http://www.about.hsbc.com.au/news-and-media/australian-companies-under-utilising-free-trade-agreements>



and its 'Plus Six' FTA partners, and at the time of writing an ongoing. While having different memberships, both are roughly equal in size in terms of their GDP, total trade and intra-regional trade (Table 2).

Table 2: Key features of the TPP and RCEP agreements

	Trans-Pacific Partnership	Regional Comprehensive Economic Partnership
Negotiations commence	March 2010	May 2013
Negotiating process	Negotiations complete October 2015; awaiting ratification	Initial goal for late-2015 completion; now expected late-2017
Scope and coverage	<i>WTO-Plus</i> approach: Market access commitments alongside 24 additional trade-related measures	<i>WTO-consistent</i> approach: Focus on trade liberalisation and investment facilitation
Member states	Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, United States, Vietnam	ASEAN bloc, Australia, China, India, Japan, Korea, New Zealand
Membership model	Open to all APEC parties; includes accession mechanism	Only open to current ASEAN FTA partners during negotiation phase
Total GDP of members	USD 27.4 trillion (36.6% of global economy)	USD 22.7 trillion (30.4% of global economy)
Total two-way trade of members	USD 8.7 trillion (26.2% of world trade)	USD 9.5 trillion (28.8% of world trade)
Intra-regional trade of members	USD 3.7 trillion (43.2% members' total trade)	USD 4.3 trillion (44.6% members' total trade)

Source: Jeffrey D. Wilson (2017), 'The Regional Comprehensive Economic Partnership: An Indo-Pacific approach to the regional trade architecture?', *Indo-Pacific Insights Series* (Vol. 2), Perth: Perth USAsia Centre.

The significance of the TPP and RCEP lies in their promise of inducing systemic change in the regional trade architecture: a return from a fractured bilateral to an integrated multilateral system. Indeed, they are the first multilateral trade initiatives to be launched in Asia since the ASEAN FTA of 1992. However, the TPP and RCEP also offer very different models for how Asian trade multilateralism should be achieved.

One difference is their type of trade reform. The TPP is described as a "21st century" trade agreement, which combined tariff reduction with regulatory rule-making in a range of 'WTO Plus' areas. Investment, services, intellectual property, Investor-State Dispute Settlement, e-commerce, finance, and labour and environmental standards were amongst those included. In comparison, RCEP has more modest reform ambitions. It aims only to be 'WTO consistent', and is focused on the more traditional concern of market access for goods and services trade. RCEP lacks most of the regulatory provisions in the TPP, instead featuring mechanisms for technical and economic cooperation designed to close development gaps in the region.

A second is their membership. The TPP uses the long-standing *Asia-Pacific* model, and is open to all APEC member economies. Twelve ultimately took up membership, though an open accession clause allows new parties to join following ratification. RCEP instead uses an *Indo-Pacific* model based on the ASEAN+6 group, and at time of writing membership is closed to only these countries. As a result, neither have perfect coverage of all the major economies in the region. Australia, Japan, Singapore are parties to both. However, the US, Canada and Mexico are only in the TPP; while China, India and several ASEAN economies only feature in RCEP.



Australia was a founding member and active participant in of both mega-regional agreements. However, the TPP arguably provided the better fit with Australia's trade policy interests than RCEP:

- The TPP delivered a **very high level of tariff elimination** – 98 percent of tariffs within the bloc. Based on current trade flows alone, \$9 billion of previously dutiable Australian exports would enjoy duty-free access under the agreement¹².
- Its inclusion of **WTO-Plus regulatory provisions** – particularly for investment, intellectual property and several services sectors – is of considerable value in opening new export opportunities for Australia's services-based economy¹³.
- Its **market access provisions in agriculture** would also offer many new opportunities for Australia, particularly in the (hitherto heavily protected) Japanese beef, dairy and horticulture sectors¹⁴.
- As a multilateral agreement, it would also provide a platform for Australian firms to increase **participation in regional value chains** in sectors as diverse as food processing, mining services and intermediate manufactures¹⁵.

Unfortunately, the TPP has struggled to achieve ratification due to political headwinds in the US. It became a key issue during the US Presidential election of 2016, which was characterised by unprecedented levels of populist attack upon free trade. Both parties' candidates campaigned on an anti-TPP platform, including Democratic nominee Hillary Clinton who had previously been the Secretary of State that launched the negotiations¹⁶. Republican nominee Donald Trump promised to withdraw the US from the TPP ratification entirely, and following the election victory did so with his first executive order upon taking office¹⁷.

The US withdrawal terminally compromises the TPP as presently articulated. According to Article 30.5, at least six members – accounting for 85 percent of the GDP of the bloc – must ratify before the agreement enters into force¹⁸. As the US accounts for 65 percent of the TPP's economic size¹⁹, its withdrawal means it is numerically impossible to meet this requirement. Any attempt to reconstitute the TPP without the US will at minimum require a renegotiation of entry into force provisions.

As a result, many Asian governments have begun reappraising their regional trade strategies. With the TPP no longer viable in its present form, ambitions to multilateralise the regional trade system have begun to shift to ongoing RCEP negotiations. These moves took center stage during the Lima APEC Summit of November 2016, where discussion was dominated by the issue of trade policy and RCEP's potential role therein. The Chinese government – which has been the primary driver behind RCEP – used the Summit to

¹² DFAT (2016), *TPP Outcomes: Goods Market Access*, available at <http://dfat.gov.au/trade/agreements/tpp/outcomes-documents/Pages/outcomes-goods-market-access.aspx>

¹³ DFAT (2016), *TPP Outcomes At A Glance*, available at <http://dfat.gov.au/trade/agreements/tpp/outcomes-documents/Pages/outcomes-at-a-glance.aspx>

¹⁴ DFAT (2016), *TPP Outcomes: Goods Market Access*, available at <http://dfat.gov.au/trade/agreements/tpp/outcomes-documents/Pages/outcomes-goods-market-access.aspx>

¹⁵ DFAT (2016), *TPP Background papers: Global Value Chains and the TPP*, available at <http://dfat.gov.au/trade/agreements/tpp/outcomes-documents/Pages/background-papers-global-value-chains-and-the-tpp.aspx>

¹⁶ *Bloomberg* (2016), 'Hillary Clinton: I Oppose TPP Now, I'll Oppose It as President', 12 August.

¹⁷ *CNN Politics*, "Trump signs order withdrawing from TPP", 24 January 2017.

¹⁸ Per Article 30.5 of the *Trans-Pacific Partnership Agreement* (2015), available at <https://ustr.gov/trade-agreements/free-trade-agreements/trans-pacific-partnership/tpp-full-text>

¹⁹ Authors' calculations, from *UNCTADStat Database*, available at <http://unctadstat.unctad.org/>



pledge its commitment to economic openness, and push for a speedy completion of RCEP negotiations²⁰. In a frank assessment, Japanese Prime Minister Abe Shinzo recently remarked “*It’s safe to say that we will shift focus to RCEP if TPP is disbanded*”²¹.

New options for Australian trade diplomacy: Regional-focused multilateralism

Australia now finds itself in need of a new trade strategy. The collapse of the TPP denies Australia its number one trade policy priority – an open, multilateral and ambitious reinvigoration of the regional trade architecture. New approaches and institutions for strengthening integration with Asia are necessary to maximise trade and investment opportunities for the Australian economy. The defining principle which should inform this strategy is an active commitment to regional multilateralism in Australia’s trade diplomacy.

Some analysts have suggested that pursuing a new set of bilateral FTA negotiations is Australia’s best response to the collapse of the TPP²². However, this is unlikely to deliver major gains for exporters, nor do much to improve economic integration with the Asian region. This is because bilateral FTAs are already in place with most key trade partners:

- Of Australia’s top ten two-way trade partners, only two economies – India and Germany – are not currently FTA partners (Table 3).
- FTA negotiations with India (8th) and Indonesia (13th) are already underway, and an agreement with the EU is currently under study.
- The ‘FTA coverage ratio’ for Australian exports is already high, at 74.6 percent²³.

Negotiating more bilateral FTAs will therefore produce steadily diminishing returns. For example, a bilateral FTA with the UK – which has been suggested as a possibility once the Brexit process is complete²⁴ – would only fractionally increase the FTA coverage ratio from 74.6 to 76.1 percent²⁵. Indeed, even the herculean task of securing FTAs with all Top-20 trade partners would only raise the ratio to 87.6 percent. Given their complexity, these agreements also have long lead-times: JAEPA took eight years from the start of negotiations to entry-into-force, while ChAFTA took ten years. Such long negotiation periods would delay the benefits of any new bilateral FTAs to the mid-2020s at best.

Nor will further bilateral agreements do much to address the noodle bowl problems facing Australian exporters. They will continue to impose new transaction costs on business, which are especially prohibitive for SMEs. They do little to enable Australian firms to participate in the regional value chains that are driving growth in Asia. As research by the Productivity Commission has recently concluded, “*Multilateral trade reform offers potentially larger improvements in national and global welfare than a series of bilateral agreements*”²⁶.

²⁰ ABC News (2016), ‘APEC Summit: Xi Jinping pledges economic openness as leaders seek free trade options’, 20 November; Reuters (2016), APEC leaders vow to fight protectionism, look to China on trade, 21 November.

²¹ Jakarta Post (2016), ‘RCEP negotiators conclude 2nd chapter’, 10 December

²² Giovanni de Lieto (2017), ‘Brexit, Trump and the TPP mean Australia should pursue more bilateral trade agreements’, *The Conversation*, 17 January.

²³ Authors’ calculations, from UNCTADStat Database, available at <http://unctadstat.unctad.org/>

²⁴ ABC News (2016), ‘Australia and UK take first step to post-Brexit free trade deal, but final agreement could take years’, 7 September.

²⁵ Authors’ calculations, from UNCTADStat Database, available at <http://unctadstat.unctad.org/>

²⁶ Productivity Commission (2016), *Trade and Assistance Review 2014-15*, Canberra: Productivity Commission, p. 48.



Table 3: Australia's Top-20 trade partners and FTA coverage, 2015

	Economy	Share two-way trade	Share exports	Current FTAs	Prospective FTAs
1	China	27.7%	32.5%	ChAFTA (2015)	RCEP
2	Japan	11.5%	15.9%	JAEPFA (2015)	RCEP; TPP
3	United States	8.4%	5.3%	AUSFTA (2005)	TPP
4	Korea	6.2%	7.1%	KAFTA (2014)	RCEP
5	Thailand	3.5%	1.7%	TAFTA (2004); AANZFTA (2009)	RCEP
6	Singapore	3.1%	2.7%	SAFTA (2003); AANZFTA (2009)	RCEP; TPP
7	New Zealand	3.1%	3.3%	CER (1980); AANZFTA (2009)	RCEP; TPP
8	India	3.0%	4.2%		RCEP; AI-CECA
9	Malaysia	2.8%	1.8%	MAFTA (2013); AANZFTA (2009)	RCEP
10	Germany	2.7%	0.6%		
11	China, Taiwan	2.1%	2.5%		
12	United Kingdom	2.1%	1.5%		
13	Indonesia	2.0%	2.0%	AANZFTA (2009)	RCEP; IA-CEPA
14	Vietnam	1.5%	1.4%	AANZFTA (2009)	RCEP
15	Italy	1.3%	0.3%		
16	United Arab Emirates	1.1%	1.3%		
17	France	1.1%	0.5%		
18	Papua New Guinea	0.9%	0.7%		PACER Plus
19	China, Hong Kong SAR	0.9%	1.3%		
20	Netherlands	0.9%	0.9%		
	<i>Memo: ASEAN</i>	<i>13.6%</i>	<i>10.4%</i>	<i>AANZFTA (2009)</i>	<i>RCEP</i>
	Total Top-20	85.8%	87.6%		

Source: Author's calculations, from UNCTADStat Database and Table 1.

The collapse of the TPP has complicated Australian efforts to trade multilateralism in the Asia-Pacific. Some commentators have suggested that the TPP could be salvaged in the absence of the US²⁷. This could be achieved either by revising Article 30.5 to allow entry-into-force as an 11-party agreement; and/or through the inclusion of new countries (potentially China, Korea or Indonesia) via the Article 30.4 accession mechanism. Following official notification of the US withdrawal, the Australian government has indicated that it intends to explore such options²⁸.

While legally feasible, these proposals are not politically realistic. Many of the governments in developing Asia – particularly Malaysia and Vietnam – were attracted to the TPP due to the ‘pull’ of access to large US consumer markets. In the absence of the US, these governments will seek a renegotiation of the TPP, particularly seeking amendments to its regulatory provisions for investment, labour standards and the environment. It remains to be seen whether such compromises could be settled without significantly diluting the agreement. Indeed, the Japanese government has recently indicated the TPP is “meaningless” without the US, and will not seek to revive the deal with a different membership or ratification requirements²⁹.

For these reasons, active participation in ongoing RCEP negotiations provide the best fit for Australia's trade policy interests. In 2015, RCEP members accounted for 65.0 percent of Australia's two-way trade, and

²⁷ *The Australian* (2017), ‘Leaders warn of trade war after Donald Trump pulls out of TPP’, 25 January.

²⁸ *ABC News* (2017), “Trans-Pacific Partnership: Government ‘flat out’ to revise TPP deal without Donald Trump's support”, 23 January 2017.

²⁹ *MarketWatch* (2017), “Japan says TPP ‘meaningless’ without US, but still hopes to save pact”, 24 January.



73.4 percent of exports³⁰. While RCEP has lower reform ambition than the TPP, it nonetheless offers major benefits for Australia:

- It promises **genuinely multilateral trade architecture** for the region, which avoids the various noodle bowl problems and enables participation in regional value chains.
- It offers an opportunity to **build on Australia's existing FTAs** in the region, capturing additional market access gains in areas such as agriculture and services.
- It will also be Australia's **first trade agreement with India**, an important emerging market in the region.
- RCEP negotiations are **already well-advanced**, reducing the lead time before the agreement is concluded, ratified and enters into force.

At the time of writing, RCEP negotiations are ongoing. Following the US election in late 2016, many Asian governments have signaled a renewed commitment to advancing RCEP talks, including China³¹, Japan³², Korea³³, Indonesia³⁴, Malaysia³⁵, Thailand³⁶, the Philippines³⁷ and India³⁸. During the Sixteenth round of RCEP negotiations in December 2016, parties committed to the aspirational goal of completing the agreement by the end of 2017. Much remains to be settled, including the scope of the agreement itself, the design of regulatory provisions for investment and services, as well as the all-important market access commitments³⁹. However, renewed commitment from many governments augurs well for increased productivity during – and results from – future negotiating rounds.

Shaping the future of Asian economic regionalism through RCEP

As RCEP negotiations enters a critical stage in 2017, Australia is presented with a unique opportunity to shape the future of the regional trade architecture. It is imperative that trade negotiators play an active role in ongoing talks, to ensure the final RCEP agreement provides the best fit with Australian trade interests. Three areas are of particular importance:

1. Australia should work towards securing the **strongest market access deal possible**. While the presence of 'sensitive' sectors may mean achieving the level of tariff elimination in the TPP (98 percent) is not possible, a figure in the high-90s would still offer major gains for exporters. Minimising the number of agricultural 'carve-outs' will be essential to ensuring a positive result for the Australian farm sector.
2. **Service sector liberalisation** will be critical in supporting Australia's emerging trade interests in Asia. This will be achieved both through the service market access commitments, as well as the

³⁰ Author's calculations, from Table 3.

³¹ Reuters (2016), 'APEC leaders vow to fight protectionism, look to China on trade', 21 November.

³² Jakarta Post (2016), 'RCEP negotiators conclude 2nd chapter', 10 December

³³ Korea Herald (2017), 'Trump's TPP abandonment fans trade fears in Korea', 24 January.

³⁴ Tempo (2017), 'Gov't Turns to RCEP as US Scraps TPP', 27 January.

³⁵ Straits Times (2017), 'China-backed RCEP trade pact gains as Trump threatens to ditch TPP', 19 January.

³⁶ Bangkok Post (2017), 'TPP pull-out likely to kick-start RCEP', 26 January.

³⁷ GBTimes (2017), 'China hopes to work with Philippines to finalise RCEP trade talks', 23 January.

³⁸ Economic Times (2017), 'On partnership anniversary, India-ASEAN vow to strengthen cooperation', 28 January.

³⁹ Jeffrey D. Wilson (2017), 'The Regional Comprehensive Economic Partnership: An Indo-Pacific approach to the regional trade architecture?', *Indo-Pacific Insights Series* (Vol. 2), Perth: Perth USAsia Centre.



regulatory provisions governing certain sub-sectors (such as e-commerce, education, and financial and other professional services). Australia's service-based economy will stand to gain considerably if a robust and region-wide set of regulatory provisions are embedded in the RCEP text.

3. Ensuring an **open accession mechanism** will help 'future-proof' RCEP. While the negotiation phase is only open to the ASEAN+6 governments, parties have agreed to include an accession clause which will enable more countries to join in the future⁴⁰. The design of this mechanism, and the requirements which would be imposed on accession parties, has yet to be decided. Australia should press for the most open mechanism possible, to ensure RCEP will be able to grow in future years.

As a small, open economy with deep trade and investment links to Asia, Australia's economic prospects are greatly influenced by the shape of the regional trade architecture. The proliferation of bilateral FTAs during the 2000s has delivered mixed results for Australia: offering some market access gains while posing several noodle bowl problems. A regionally-focused multilateral trade strategy – as embodied in the mega-regional TPP and RCEP proposals – will offer the greatest benefits for Australia in the future. With the future of the TPP now uncertain, active involvement in ongoing RCEP negotiations will allow Australia to shape the future of the regional trade system in ways that best reflect and advance its unique economic interests.

About the author

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⁴⁰ RCEP Parties (2013), *Guiding Principles and Objectives for Negotiating the Regional Comprehensive Economic Partnership*, Article 6, available at <https://dfat.gov.au/trade/agreements/rcep/Documents/guiding-principles-rcep.pdf>

