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The Impact of RCEP on Trade and FDI for East and Southeast Asian Economies

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ABSTRACT

The Regional Comprehensive Economic Partnership (RCEP), the world's largest free-trade agreement, brings together a diverse group of 15 economies, to mutually benefit from an expansion in regional trade and investment, through reduced trade barriers and tariffs and enhanced regulatory coherence. This partnership will undeniably reshape regional economic dynamics. To better understand the ability of the RCEP to reshape the economic dynamics in the region, it is essential to evaluate its impact on trade and foreign direct investment (FDI). This paper therefore aims at critically evaluating RCEP's effects on trade and FDI in the East and South East Asian regions. Assessing the impact of RCEP on trade and FDI is crucial for policymakers, businesses, and investors, as it provides fundamental insights into how the agreement might drive economic growth, improve competitiveness, and promote regional and economic integration. Additionally, it will ensure that stakeholders are better equipped to navigate and capitalize on the opportunities associated with the agreement, while mitigating any potential downsides and overcoming inevitable challenges.

1. Introduction

The RCEP Agreement, signed on November 15, 2020 after extensive negotiations dating back to 2012, is currently in force for a diverse group of 15 countries. These include the 10 ASEAN member states (Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Vietnam) and five key partners — the People's Republic China (PRC), Japan, the Republic of Korea, and Australia and New Zealand. According to World Economics (2024), the RCEP participants collectively represent a significant portion of global trade and investment flows. Indeed, together, they have a total population of 2.3 billion, representing about 30 % of the world population. Moreover, the 15 member countries accounted for 31.6 % of the global GDP in 2023. The extensive coverage of this partnership, which creates the world's largest trading bloc, coupled with the inclusion of key economic players, ensures that a more connected, integrated, and collaborative economic environment is fostered within the region.

The modern, comprehensive, and mutually beneficial RCEP agreement has numerous overarching objectives. Indeed, the RCEP agreement has 20 chapters that aim at improving market access through the elimination of tariffs and quotas, encouragement of open and competitive markets, facilitation of trade, commitment to consistent rules of origin, and lifting restrictive barriers to trade in services, optimization of the investment environment, promotion of e-commerce, imposition of international sanitary and phytosanitary standards, enhancement of transparency in the technical regulations as well as government procurement processes, standardization of assessment procedures and enforcement of intellectual property rights with a balanced and inclusive approach (RCEP Secretariat ASEAN, 2020). The RCEP goals have crucial implications for East and Southeast Asia, which is a growingly interconnected region. These goals, which focus on boosting regional trade and investment, are likely to have a notable impact on inter-regional trade and foreign direct investment across East and Southeast Asia. As argued by Kang et al. (2020), this agreement will generate a renewed momentum for intra-regional trade and strengthen value chains among the 15 members. Moreover, they maintain that the open and inclusive trade and investment regimes will also be strengthened. Indeed, by reducing tariffs, streamlining customs procedures, standardizing trade rules, and fostering greater economic integration, the RCEP is expected to improve market access and stimulate rising

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trade flows within the region. On the other hand, the RCEP agreement also emphasizes on providing an optimal investment climate by harmonizing regulations and protecting investment rights. Such an environment will reduce the operational complexities and costs tied to cross-border investments, thereby creating a more appealing investment environment for international investors. Indeed, according to the FDI Centre (2020), the signing of the agreement, which caters to less restrictive FDI regulations, will create new FDI opportunities.

While existing research for international investors has examined the RCEP's broad economic impacts, key gaps remain, including a lack of its uneven effects across diverse member states, exploration of non-tariff barriers (NTBs), and long-term, as well as sector-specific assessments, particularly in terms of trade and foreign direct investment. This review differentiates itself by integrating some of these overlooked dimensions: it reviews the implications of RCEP for trade and FDI, while highlighting disparities between developed and developing members and focussing on tariff and non tariff concessions.

Given the pivotal influence of the RCEP on trade and FDI and its subsequent impact on economic growth, this article first describes how this initiative emerged and then critically analyzes the resulting impacts and implications of the agreement for the East and Southeast Asian countries. The rest of the paper is structured as follows: Section 2 reviews relevant literature, Section 3 evaluates the effects of the RCEP on trade within East and Southeast Asian countries, Section 4 explores the agreement's implications for FDI in these regions, and Section 5 provides a conclusion to the analysis.

2. Literature review

The effect of Regional Trade Agreements (RTAs) on intra-regional trade and the implications on the global economy has become an important area of investigation and analysis. The literature on the effects of RTAs on intra-regional trade presents a diverse array of findings. Some studies provide evidence supporting positive outcomes, demonstrating enhanced trade within regions. Conversely, other research indicates that RTAs may have either insignificant or negative impacts on intra-regional trade. For instance, Fernandez and Portes (1998) identified that RTAs can generate non-traditional advantages, including expanded market access and improved infrastructure. Freund and Ornelas (2010) similarly noted that RTAs have become the most prevalent approach to reciprocal trade liberalization, yielding a beneficial effect on trade.

Conversely, research by Kulkarni and Barnekow, 2017 found that RTAs do not exert a substantial positive effect on welfare, suggesting that greater caution should be exercised in the creation of future RTAs. To completely comprehend the effects of RTAs on intra-regional commerce, more research is required in light of the inconsistent results of the literature.

The implementation of the RCEP as an RTA is anticipated to have significant impacts on both the economy and free trade in the region, given its modern, comprehensive, high-level, and mutually beneficial nature (Lu, 2021). To comprehensively evaluate the impact of the RCEP on trade and FDI within East and Southeast Asian economies, it is important to explore the common models used to evaluate the impact of FTA. These models help illustrate how the RCEP, as a significant multilateral trade agreement, influences trade flows and investment patterns across the region. The following section discusses several common models used to analyze these impacts, including the Econometric model, the Computable General Equilibrium model, and the Knowledge-Capital model. Each model provides distinct perspectives on the economic consequences of the RCEP, contributing to a comprehensive understanding of its effects on trade and FDI in East and Southeast Asian economies.

2.1. *Brief theoretical review*

Theoretical perspectives on trade and foreign direct investment (FDI) offer useful insights into the likely effects of the Regional Comprehensive Economic Partnership (RCEP) on East and Southeast Asian economies.

Early contributions such as Dunning's (1980) Location-Based Theory set within the eclectic OLI framework, explains that FDI gravitates towards regions with advantages such as large markets, resource endowments, competitive labour, and strategic geography. RCEP's consolidation of a vast market and its harmonization of trade rules enhance these location advantages, making the region more attractive to multinational investors. At the same time, the Institutional FDI Fitness Theory underlines that the developmental impact of investment depends on domestic institutions, governance, and absorptive capacity (Bhasin & Garg, 2020). Given the institutional diversity among RCEP members, ranging from advanced economies like Japan and Singapore to developing ones such as Cambodia and Laos, outcomes are likely to vary.

Besides, Mundell's (1961) Currency Area Theory, while often applied to capital flows, also has important implications for trade. Exchange rate volatility increases uncertainty and transaction costs for exporters and importers, discouraging cross-border transactions. By contrast, greater exchange rate stability or mechanisms that reduce currency mismatches can promote trade by lowering risks and improving price predictability. In the context of RCEP, initiatives such as local currency settlement arrangements, bilateral swap agreements, and the wider use of regional currencies have the potential to reduce transaction costs and strengthen trade integration among member states. Moreover, classical and modern growth theories also provide a useful lens for examining the role of trade in development and, more specifically, for understanding the potential impact of the RCEP on East and Southeast Asian economies. The Harrod–Domar model suggests that greater savings and investment drive growth, which in an open economy can be facilitated by trade inflows that expand capital availability and improve productivity (Domar, 1946; Harrod, 1939). Within RCEP, expanded trade and investment opportunities can increase the flow of capital into member states, enabling them to build infrastructure and industrial capacity. The Solow and Ramsey models highlight how trade allows access to advanced technologies and knowledge, enabling less developed economies to converge with more advanced partners through technology transfer embedded in traded goods and services (Ramsey, 1928; Solow, 1956). RCEP's framework, by encouraging greater integration and harmonization of trade rules, can accelerate such diffusion and convergence across diverse member economies. The Endogenous growth theory further emphasizes that trade can act as a channel for human capital accumulation, learning, and innovation, as exposure to international markets encourages skill development, product diversification, and knowledge spillovers (Romer, 1986; Lucas Jr, 1988). With RCEP fostering deeper regional cooperation, members can strengthen knowledge transfer, build competitive industries, and stimulate innovation.

Taken together, these perspectives suggest that RCEP has the potential to boost trade and FDI led growth by fostering capital accumulation, technological progress, and long-term productivity gains across East and Southeast Asia.

2.2. *Common models used to analyze trade flows and investment patterns*

The Econometric Model, the Gravity Model, the Computable General Equilibrium (CGE) Model and the Knowledge - Capital model are included as trade theories and FDI theories in this paper. Firstly, the Econometric model assesses the effect of FTAs by analyzing factors such as fiscal policy, GDP, labour resources, and monetary policy through economic theory, economic mathematical model as well as statistical data. The above-mentioned factors are modeled and the findings of the econometric model are translated into data, so the model evaluates the impact of FTA quantitatively with scientific precision based on established theory. The results can then be compared with real-world data to conclude. However, because the econometric model's results are based on a built database, it is essential to carefully manage the variables, ensure that assumptions reflect real-world conditions, and use reliable and accurate data. Moreover, the model's ability to forecast future events might be unreliable.

Another common model among the many developed econometric models is the gravity model. The model was originally used by Jan Tinbergen, 1962 in his research in 1962, and scholars continue to use it extensively to assess how trade agreements affect international trade flows. Considering the variables mentioned, the model is regarded among the most stable experimental economic models since it can estimate data effectively and distinguish between reality and estimate. Nevertheless, similar to the econometric model, this model also requires the usage of a sufficiently extensive, and trustworthy database; also, during the research process, significant variables or variables that are connected can go unnoticed. Medvedev (2012) employed the gravity model with panel data to examine the effect of trade agreements on FDI. Their analysis revealed that FTAs positively influence FDI flows among the participating countries. Cuong et al. (2015) also utilized the gravity model in conjunction with panel data and the Hausman-Taylor estimation method to assess the effects of trade liberalization on the attraction of FDI to Vietnam.

Another method used is the CGE model. This is a quantitative approach that analyzes the direct and indirect effects of FTA industry-wide and sector-wise using endogenous variables, including output in exports, imports, taxes, etc., and exogenous variables, including trade policies and elasticity of endogenous variables. The assessment's completeness, conformity to reality, and potential use as an empirical foundation for long-term policy research are the model's advantages. However, a limitation of the model is its reliance on an extensive, complex, as well as detailed database that encompasses all related study areas at the macro level. This makes it challenging to obtain comprehensive and standardized data, identify non-tariff factors, and formulate relevant assumptions.

Generally, CGE simulation results indicate support for the founding of RCEP. According to research by Kawasaki (2015), the RCEP's elimination of tariffs and reduction of non-tariff barriers will boost members' income as indicated by equivalent variation as a percentage of GDP. Several studies have used a CGE model to quantify the effects of mega-regional trade agreements and/or plurilateral FTAs in the Asia-Pacific region (Cheong & Tongzon, 2013; Lee & Itakura, 2014; World Bank, 2016). The CGE model developed by Li et al. (2017) distinguishes between foreign-invested firms and domestic firms and identifies the barriers to FDI encountered by foreign-invested firms. The removal of FDI barriers can directly enhance intra-regional FDI flow. The CGE model predicts that the home country of FDI could see an increase in investment income while the host country would gain from increased diversity and improved industrial efficiency.

In addition to FDI barriers, trade barriers are addressed more profoundly. Trade barriers are further categorized into border barriers and behind-the-border barriers. Border barriers encompass tariffs and non-tariff barriers that increase trade variable costs. Behind-the-border barriers typically lead to higher fixed trading costs for exporters. Numerous empirical research has estimated the economic effect of trade liberalization on member countries under the RCEP framework. Global Trade Analysis Project (GTAP) (2017) employed the CGE model to assess the probable impact of the RCEP Agreement on FDI in China, concluding that RCEP is likely to boost FDI inflows into China by influencing both trade dynamics and direct FDI impacts. Increasing trade, attracting FDI to member nations' domestic markets, and pressuring inefficient enterprises to withdraw from the market will raise the industry's overall productivity. Furthermore, Petri and Plummer (2020) estimated the economic gains from RCEP for the global economy using a CGE model. Their findings suggest that RCEP will increase global national incomes by 2030, with China, Japan, and South Korea benefiting the most. Other RCEP winners will include Vietnam, Malaysia, Thailand, and Indonesia.

On the other hand, Markusen and Venables, 1998 introduced the Knowledge - Capital model in 1998. The model examines the effects of FTAs both vertically and horizontally at the industry and overall levels, using independent variables pertaining to a country's capital resources. The model concentrates on analyzing interrelated factors to assess their economic impact, thus providing a foundation for developing and formulating economic policies and strategies. Consequently, in practical applications, the modeling, measurement, and quantitative analysis of the variables in the model are challenging due to their interdependencies, and difficulty for clear analysis of factors. Bae and Keum, (2013) also employed the Knowledge-Capital model to assess the influence of bilateral FTAs on FDI abroad. The study revealed that nations engaged in multiple FTAs with large economies exhibit a greater capacity to attract FDI. It found that, since Korea's involvement in FTAs, both FDI inflows and outflows have risen, with outflows experiencing a notable rise compared to inflows. Additionally, the study indicated that FTAs with high-income countries significantly affected Korea's FDI capital flows.

2.3. RCEP on FDI

Empirical studies exploring the effect of the RCEP on trade and FDI offer important insights into the economic dynamics within the region. The RCEP has had a significant transformative influence, according to studies on regional trade patterns and economic integration. To illustrate how RCEP affects manufacturing trade patterns using network-based policy evaluations, Zhu and Huang (2023) constructed RCEP manufacturing trade networks and examined key manufacturing industries. Similarly, Ling and Lv (2022) investigated the effects of RCEP on China's manufacturing sector using GTAP10 simulations, identifying prospects for the development of high standards.

Liu and Chen (2014) and Wei and Yin (2022) focused on the reduction of trade barriers within the context of RCEP. Liu and Chen (2014) proposed the implementation of support mechanisms for least-developed countries and emphasized the importance of monitoring factors that influence regional integration. Meanwhile, Wei and Yin (2022) underscored the positive effects of zero tariffs on economic growth and welfare, noting that these benefits increase as technical barriers are gradually diminished.

A few research devlved into the sector-specific impacts of the RCEP. Indeed, Song and Kim (2022) explored the consequences of RCEP's tariff reductions on South Korea's agricultural trade, whereas Dong et al. (2023) analyzed its effects on China's electronics industry. According to their findings, RCEP greatly raises social welfare and economic standards in the electronics industry while promoting value chain activity's increasing dynamism.

Other studies investigated investment trends. For instance, Wang et al. (2022) studied South Korea's direct investment in RCEP member countries, offering strategies to enhance trade and investment, while also identifying significant trends in investment. Supporting this, Nguyen & Cao (2016) demonstrated that FTAs significantly boost FDI inflows into Vietnam. Similarly, Duong et al. (2020) emphasized that FTAs are important drivers in attracting domestic FDI.

Furthermore, studies on trade facilitation and the digital economy offer new perspectives. Cheng (2023) examined the exports of digital services from China and South Korea and offered suggestions for improving the development of the digital economy under the RCEP. Li et al., (2022) conducted a quantitative analysis of trade facilitation levels within RCEP countries, identifying methods to enhance China's cross-border e-commerce export potential. Overall, the empirical research underscores RCEP's significant positive impact on regional trade and FDI, offering comprehensive insights into its effects on various economic dimensions within East and Southeast Asia.

3. Impact of RCEP on trade in east and Southeast Asian economies

The RCEP agreement provides an updated coverage of provisions and commitments that are designed to mutually benefit all the members, while simultaneously ensuring that the rapidly evolving trade realities are accounted for (RCEP Secretariat ASEAN, 2020). This section will critically explore the impact that these provisions will have on trade in the East and Southeast Asian region.

3.1. The extensive coverage of the RCEP

The comprehensive free-trade agreement, RCEP, involves 15 countries in East and Southeast Asia, which represent almost a third of the global population and therefore account for a significant share of global trade. Indeed, this wide coverage has ensured that the RCEP members have collectively become major global trade players, with the ability to reshape global trade dynamics and patterns. Although most RCEP members had already participated in other regional trade agreements, other existing free trade agreements fail to alter global trade patterns to the same extent as they are limited to specific regions, and as such do not have the same geographical reach as the RCEP.

Moreover, while prior agreements within the region have spurred an already high trade openness for the diverse member states of the RCEP, their trade liberalization practices still differed significantly before the RCEP. Indeed, as stated by Nicita et al. (2021), while Australia, Brunei Darussalam, New Zealand, and Singapore had an intra-trade tariff of 0 since 2020, other countries like the Republic of Korea, Cambodia, China, Japan, Thailand, and Vietnam had average effectively applied tariffs ranging between 1.2 and 4.8. Consequently, with higher tariffs before the RCEP agreement, countries such as the Republic of Korea, Cambodia, China, and Japan will record a more substantial benefit from the RCEP. As discussed by Nicita et al. (2021), the RCEP creates an opportunity for tariff reduction among RECP members other than ASEAN members, Australia, and New Zealand, who already have zero tariffs on over 90 % of their products. Spurring trade openness for these countries will undoubtedly result in substantial economic growth in the region.

Indeed, while the RCEP offers regulatory alignment through harmonised rules across diverse economies, it also helps to mitigate power imbalances, particularly for smaller economies. As discussed by Kawharu (2015), RCEP's "negative list" approach and flexible implementation timelines are key mechanisms that allow the gradual adaptation of regulations by smaller members in their journey of gaining market access. Moreover, Kawharu (2015) points out that RCEP's softer provisions on issues like e-commerce and dispute settlement provide crucial policy space for developing economies to balance liberalization with domestic priorities. Moreover, RCEP's innovative approach of cumulative rules of origin and sectoral exemptions help reduce power imbalances, enabling developing economies to integrate into regional value chains. As such, the RCEP can function as a tool for convergence of rules, while accommodating for the diverse developmental levels of member states through different stages of tailored obligations rather than uniform demands. In fact, Chaisse et al. (2022) demonstrate how the RCEP has carefully combined liberalization clauses from agreements like CPTPP, along with safeguards from ASEAN treaties to create a tailored framework that accommodates diverse development levels. Such a combination provides an optimal balance between the regional integration and sovereign policy space.

3.2. The flexibility of the RCEP

Interestingly, the RCEP agreement is more flexible compared to the relatively more aggressive tariff reduction schedules imposed by other free trade agreements. This allows for gradual and flexible concessions. Tariff reduction can be spread over 20 years, making it particularly beneficial as it equips firms with sufficient time to gradually adapt to the new competitive environment and finance adjustment costs internally (Bacchetta & Jansen, 2003). Besides, according to Bacchetta and Jansen (2003), this gradual shift in trade policies is especially helpful for developing countries, which normally have "higher adjustment costs" and "poorly functioning credit markets". However, Bacchetta and Jansen (2003) warn that while the gradual adaptation period mitigates any potential political opposition to the reform, the gradual pace alone might not be a solution for all countries, especially low-income ones, which might still not be able to accumulate savings within that time. While 20 years might seem a long enough time for low-income countries, Bacchetta and Jansen (2003) also believe that if reforms are adopted too slowly, the intended reform might be undermined. Nevertheless, as far as the RCEP members are concerned, given that most of them already have a high level of trade openness, the 20 years are not expected to adversely affect the aim of the reform. Since trade liberalization is highly concentrated in certain states within the RCEP, a gradual adjustment process will be an optimal approach (Bacchetta & Jansen, 2003). As such, the trade liberalization benefits will be amplified in the region.

Additionally, there will be exemptions as RCEP members have preferred to avoid any commitments in strategic sectors, such as automobile and agriculture. As postulated by Deardorff and Sharma (2018), sectors exempted in free trade agreements are either vulnerable to competition or these sectors cause concern about lost tariff revenue. This approach by the RCEP ensures that jobs are protected and the economy is not destabilized, while still promoting overall trade liberalization. Indeed, the agricultural sector in the RCEP remains highly protected. According to Annex I "Schedule of Tariff commitments" of the RCEP agreement, the agricultural sector still has an average tariff of 70 % on uncommitted lines, as compared to 14 % and 15 % for the natural resources and manufacturing sectors. By recognizing the unique challenges and importance of agriculture in its member countries, the RCEP ensures that trade is enhanced in the region without compromising on the economic and market stability and competitiveness in the region.

Furthermore, the RCEP allows for varying levels of commitment among members (Nicita et al., 2021). ASEAN countries, New Zealand, and Australia have eliminated duties on 91 %, 99 %, and 99 % of their product lines, respectively, while the Republic of Korea, China, and Japan have achieved duty-free treatment on 70 %, 72 %, and 80 % of their goods. Likewise, the share of uncommitted lines stands at 5 % for ASEAN members, and 0 % for both New Zealand and Australia, compared to 9 % for the Republic of Korea and China, and 12 % for Japan. The average applied duty on these uncommitted products is approximately 21 % for ASEAN countries, 4 % for Australia and New Zealand, 17 % for China, 32 % for Japan, and 111 % for the Republic of Korea. As the countries within the RCEP are diverse and have reached different stages of economic development, their capacity to engage in the agreement will be different. Accounting for the heterogeneity within the group through such a flexible approach promotes broader participation while ensuring that a wider range of economies can be included in the partnership.

3.3. The evolving rules of the RCEP

The RCEP adopts evolving rules compared to other preferential trade agreements, increasing its suitability for the diverse ASEAN economies. As discussed by Mishra and Valencia (2023), the RCEP has evolving rules that are more flexible, especially in terms of digital trade and data flows as opposed to other preferential trade agreements like the CPTPP. Indeed, while the CPTPP bans data localization, the RCEP leaves room for countries to protect privacy and security, thereby allowing developing countries like Vietnam and Indonesia to retain regulatory space. Moreover, Mishra and Valencia (2023) also point out that the RCEP allows self-judging exceptions for data flows, increasing its appeal to sovereignty-focused states or data-sensitive economies like China.

Additionally, the gradual, consensus based model, promotes a more smooth and cautious adaptation for less-developed members of the ASEAN countries. For instance, the ASEAN E-Commerce Agreement relies on non-binding cooperation, allowing the least developed member countries to adapt slowly.

While foreign investors will feel less legal certainty with these evolving rules compared to CPTPP's rules (as it represents Investor-State Dispute Settlement challenges against potentially unfair digital policies) and slower integration, this balance between openness and sovereignty protection is deemed more appropriate for the diverse countries in East and South East Asia.

3.4. The trade effects of the RCEP's tariff concessions

The World Development Indicators data show that the trade in goods as a percentage of GDP in East Asia and Pacific countries grew from 52.8 % in 2000 to 60.6 % in 2023. The RCEP countries trade a wide array of goods traded globally, including high-tech electronics and automobiles, minerals and fuel, petroleum products, dairy and meat products, textiles, pharmaceuticals, agricultural products, and natural resources. The unique products contributed by each country to the global supply chains have a significant impact on the trade pattern, both within and outside of the region. Additionally, these distinct products in each member state create strong interdependencies among them. Moreover, Flach et al. (2021) argue that complex global value chains are more common than simple ones among RCEP countries, indicating stronger trade connections in the region.

The trade liberalization strategies adopted by the RCEP agreement include the reduction or elimination of customs duties and tariffs, and the possibility of initiating consultations to address adverse non-tariff measures (RCEP Secretariat ASEAN, 2020). These measures are designed to enhance intra-regional trade. Indeed, since the agreement plans to reduce up to 90 % of the tariffs ultimately (Flach et al., 2021) within the bloc, the costs of goods traded will be substantially reduced, thereby making the products more competitive, and promoting a rise in exports within the East and southeast region. Subsequently, market access across a relatively broad area will be enhanced. However, as stated by Nicita et al. (2021), those benefits are expected to have a relatively lower impact on smaller economies of the bloc. They further explain that this will be mainly because tariffs between other RCEP members are already low. Moreover, with an imposed average base tariff of above 5 %, some of the lower-income economies within the group (like Indonesia, Philippines, Cambodia, and Vietnam), will have a limited increase in their export volumes and competitiveness. This might consequently shield these countries from reaping the immediate benefits of the RCEP.

The overall impact of trade concessions among RCEP members is expected to be at US$ 41.8 billion, a rise driven mostly by trade diversion away from non-member countries (US$ 25.2 billion) rather than trade creation, which accounts for US $ 16.6 billion (Nicita et al., 2021). Japan, China, the Republic of Korea, Australia, and New Zealand propel the positive change in trade diversion and trade creation forward for the region. However, some countries in the block (Thailand, Philippines, Cambodia, Indonesia, and Vietnam) also record negative trade diversion effects due to the differences in the magnitude of concessions. This is a consequence of trade being diverted to other RCEP members (Nicita et al., 2021). Moreover, some countries also have an overall negative impact. However, as pointed out by Nicita et al. (2021), trade diversion would have occurred even without these concessions. They further argue that the other benefits of the agreement, as well as the trade creation generated, will help these countries alleviate those detrimental effects.

On the other hand, the RCEP goes beyond the trade in goods and also enhances market access for service providers, while simultaneously equipping them with legal protection. Undeniably, the RCEP has strengthened and improved upon the benefits that other existing free trade agreements were providing to service providers. Interestingly, the trade in services (as a percentage of GDP) in East Asia and Pacific countries recorded a smaller upward shift than the trade in goods, rising from 8.3 % in 2000 to 10.2 % in 2023. The RCEP is expected to open up 65 % of all the services sector (Deloitte, 2024). Previously restricted markets will also be opened, thereby expanding the regional services provided by the advanced services sector providers like Singapore and Hong Kong SAR. Moreover, new market access commitments are included in the RCEP in a variety of sectors (professional services, education services, and healthcare services among others) (ADB, 2021). Nevertheless, Crivelli et al. (2022) warn that there are noteworthy disparities in the rates of liberalization among countries and the modes of supply. The average rate of services liberalization commitments in the different modes of supply is as follows: Mode 1 (cross border supply): 46.1 %; Mode 2 (consumption abroad): 70.1 %; Mode 3 (commercial presence): 40.9 %; Mode 4 (movement of natural persons): 34.2 %. The highest commitment to services rate liberalization across Modes 1, 2, 3, and 4 are in Australia, Brunei, Vietnam, and Japan respectively. On the other hand, the Philippines records the lowest commitment to services rate liberalization across Modes 1, 2, and 3 while Vietnam has the lowest rate for Mode 4. Crivelli et al. (2022) argue that this inherent disparity could potentially harm the economy by affecting both the trade flows and the productivity. Furthermore, these disparities might further exacerbate the struggle of countries having the least developed services sector (Cambodia, Laos, Myanmar, and Brunei).

3.5. The trade effects of the RCEP's non-tariff commitments

As mentioned earlier, the tariff concessions within the RCEP are set to enhance market access for businesses across the region. Other commitments designed to further boost market access are also included in the agreement. Indeed, the RCEP also improves and builds on the World Trade Organisation (WTO) agreement on the technical trade barriers, thus allowing mutual understanding among members about their diverse standards and technical regulations (RCEP Secretariat ASEAN, 2020). Normally, trade barriers tend to not only reduce participation in trade and global value chains but also minimize their associated benefits (OECD, 2015). With the RCEP, increased transparency and improved information exchange are achieved, which will in turn limit the adverse effects of regulations on trade. As such, the provisions of the RCEP result in enhanced market access in the region, thereby improving trade flows.

Furthermore, the agreement also promotes consistent and transparent sanitary and phytosanitary measures adapted for the region. This measure has significant implications for agricultural and food trade in the region, especially since a substantial portion of trade in these countries is related to these sectors. Indeed, Crivelli and Gröschl (2016) argue that these measures normally increase the fixed costs of trading, which result from the adaptation process to meet the stringent standards, and as such can act as a barrier to entry. However, these measures indicate the level of safety of the product to consumers, which leads to positive trade flows once the barrier has been overcome. Crivelli and Gröschl (2016) believe that the benefits derived from the positive trade flows outweigh the costs of overcoming the barrier. Therefore, while these measures included in the RCEP will boost trade flows for the developed and developing countries in the region, the least developed RCEP states might struggle to make initial progress (Teh, Prusa, & Budetta, 2007). This could result in a more prolonged and challenging path before any positive effects on their trade flows are detected.

The RCEP also aims to promote "predictability, consistency, and transparency in the application of customs laws and regulations, and promote efficient administration of customs procedures and expeditious clearance of goods" (RCEP Secretariat ASEAN, 2020). The harmonization and simplification of customs procedures for cross-border trade will ensure more efficient trade flows. Additionally, the lower costs and minimal delays will also help improve the competitiveness in the region. Indeed, Gani (2016) argues that an inefficient customs clearance process can hinder trade, while the inverse will promote a higher trade volume.

Moreover, the RECP outlines trade remedies that cover safeguard measures and anti-dumping and countervailing duties, which are designed to be transparent and non-discriminatory (RCEP Secretariat ASEAN, 2020). These protect domestic businesses in the region against injury caused by dumped, subsidized, or unforeseen surges in imports to ensure fair competition. However, Teh, Prusa, & Budetta (2007) worry that the elastic and selective properties of trade remedies could induce undue discrimination between members and non-members, with higher trade remedy actions against non-members of the agreement. Yet another measure in the RCEP that promotes transparent, open, and fair competition, is the obligation to adopt and maintain competition laws (Jong et al., 2024). Jong et al. (2024) argue that these are expected to promote economic efficiency and uphold consumer welfare. Indeed, fair competition ensures that trading is more efficient by hindering any potential market distortions.

Innovatively, the RCEP also caters for digital trade, which is expanding worldwide, including the digitalization of trade administration and processes, cross-border data flows, and electronic contracts (RCEP Secretariat ASEAN, 2020). The appropriate legal framework to create a trade environment conducive for digitalization is also included. Undeniably, with such policies, a higher trade flow is expected in the region. Suh and Roh (2023) confirm that the presence of trade agreements that address digital trade issues will ensure that member countries experience an increase in digital trade flow. They argue that more detailed rules in the agreement will have a more intensive impact on the trade flow.

4. Impact and implications of RCEP on FDI flows in east and SouthEast Asia

This section examines whether RCEP represents a substantial transformation of the ASEAN plus system. Member countries in the RCEP are expected to experience an increase in investment flows. The actual situation in terms of Net FDI inflows and outflows as a percentage of GDP are shown in the Figures below for the RCEP member countries.[1]

An analysis of net FDI inflows in the member countries from 2010 to 2022, shows that Singapore, Cambodia, and Lao PDR are the high performers. These figures show the strong position of Singapore being a global financial hub. More so, Cambodia has a favourable investment policy with minimal restrictions on foreign investment. Laos for instance has been attracting FDI as it is endowed with natural resources and hydropower development. Countries like VietNam, Indonesia, and the Philippines show steady FDI inflows which is explained by a stable investment environment. On the other hand, member countries like Brunei and Myanmar show rather erratic investment flows which can be explained by unstable economic or political factors. Figure two shows the trend in FDI net outflows for the RCEP member countries.

Examining and interpreting the data from Fig. 1, it can be seen that high income countries like Australia, Japan, South Korea, and Singapore have had rather stable FDI outflows, reflecting their powerful economic positions and global investment strategies. Moreover, emerging markets like Indonesia, Malaysia, Thailand and Vietnam have quite slow FDI outflows reflecting restricted outbound investment capabilities. Cambodia and Lao PDR being least developed countries have rather minimal FDI outflow explained by their focus on FDI inflows rather. These ten ASEAN nations (Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, the Philippines, Singapore, Thailand, and Vietnam) plus China, Japan, South Korea, Australia, and New Zealand signed the RCEP trade agreement which is indeed the largest trading bloc in the world, covering nearly 30 % of the global economy. It is expected that this agreement will have substantial implications for FDI in East and Southeast Asia. In addition, the ASEAN Secretariat functions as the Depository for the RCEP Agreement.

Being a member of the RCEP implies investment facilitation through simplified procedures and creation of a one stop shop. Member countries who prior to the agreement did not have investment facilitation procedures, will subsequently implement such facilitation processes and institutions. Analysing the RCEP agreement, Chapter 10, discusses the matters related to FDI. The chapter includes standard provisions such as most-favoured nation treatment and fair and equitable treatment standards. Investment promotions and investment facilitation is discussed in Articles 10.16 and 10.17. Through cooperation in investment promotion agencies, the member countries are required to promote the region and there might be the formation of a regional investment promotion agency. The agreement adopts a negative list approach for the non service sectors like manufacturing, agriculture, forestry, fishing, and mining which means all sectors are open to FDI unless stated otherwise. Such liberalization will encourage more FDI as there will be less uncertainties for foreign investors. The negative list is embraced mainly by Australia, Brunei, Indonesia, Japan, Malaysia, Singapore, and South Korea. Also, the agreement makes provision for the protection of intellectual property rights mainly in the technology intensive industries. This is another factor seen to encourage FDI flows in the region. RCEP also contains some state-to-state dispute settlement mechanisms which will further boost investment confidence.[2]

Another implication of the RCEP agreement is market expansion and integration thereby attracting foreign investment. It is expected that RCEP will connect almost 30 % of the world's people and output. Computer simulations done by Brookings has shown that RCEP could add up to $209 billion annually to world income and $500 billion to world trade by 2030.[3] Similarly, the World Bank has also estimated productivity gains and FDI flows from RCEP and concluded that by 2035, real incomes could increase by 5 % for economies such as Thailand, Vietnam, and Malaysia.[4]

Trading blocs like the RCEP which harmonises trading rules and reduces trade barriers significantly will help to increase foreign investment as it becomes easier for companies to operate in multiple countries. Moreover, various hindrances to establish businesses and operate in the member nations have been removed. RCEP adopts the 'cumulation rule' whereby all the member countries are treated as one economic region. Simplified rule of origin measures in the agreement like allowing inputs from one member country to be considered as originating from another if they are used in the production process, facilitate companies to invest in the region without having to deal with complicated regulations. Hence, the RCEP agreement is seen to strengthen intra- East Asian integration, also improve the efficiency of the North and Southeast Asian economies, particularly in sectors like technology, manufacturing, agriculture, and natural resources.

This agreement can also promote the regional supply chain as the most important advantage for the member countries joining the RCEP is the tariff concessions, whereby tariffs on more than 90 % of the goods will be eliminated. Member countries will be able to procure their raw materials at a more competitive price. Also, there are provisions in the agreement for better investment protections and a more effective business environment for investors. This will surely lead to an increase in investment within the bloc as the agreement is facilitating movement of goods between member countries. RCEP is also the first trading bloc having three of the more technically advanced economies in Asia namely Japan, South Korea and China, thus potentially resulting in an

[1] Data for FDI outflows as a % of GDP for Brunei Darussalam and Myanmar are not available.

[2] https://thediplomat.com/2021/06/reconsidering-rceps-impact-on-foreign-investment/.

[3] https://www.brookings.edu/articles/rcep-a-new-trade-agreement-that-will-shape-global-economics-and-politics/.

[4] https://www.business.hsbc.co.mu/en-gb/insights/growing-my-business/how-free-trade-agreements-are-opening-opportunities-across-asia.

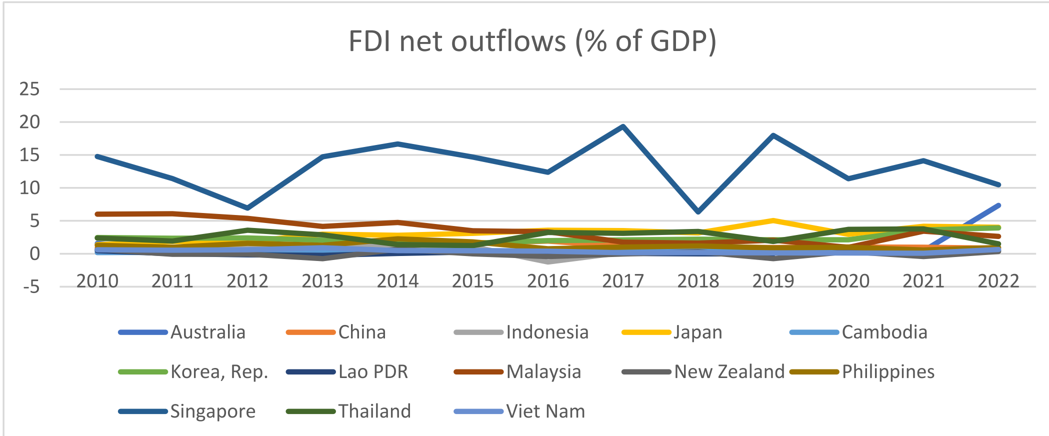

Fig. 1. FDI net outflows (% of GDP).
Source: Authors Compilation from WDI database

increase in trade and FDI. Intra-regional trade and FDI flows are likely to increase whereby countries like China and Japan may tap into new markets in the region for expansion purposes.

Moreover, the RCEP's regulatory flexibility could attract more FDI, while retaining policy control (Mishra & Valencia, 2023). Indeed, the RCEP allows countries to have more policy space and avoid stringent rules on data localization and source-code disclosures, which are attractive to certain investors.

However, it should be noted that the member countries are at different development levels with Australia, Japan, Korea, New Zealand and Singapore being developed economies, Brunei, China, Indonesia, the Philippines, Malaysia, Thailand and VietNam are developing economies, while Cambodia, the Laos and Myanmar are least developed economies. These differing development levels of the countries can impact on its effectiveness in using trade and investment policies to promote development (ESCAP, 2022). Nevertheless, provisions included in the RCEP, such as the gradual implementation and self-judging exceptions, provide a perfect solution for the diverse group of member countries. Indeed, as discussed by Mishra and Valencia (2023), it allows countries to adopt the rules that are more appropriate for them, while ensuring that even the least developed members can steer clear of any sudden regulatory shocks. Moreover, the RCEP lacks binding dispute settlement for digital trade provisions, which could potentially dampen FDI in highly regulated digital sectors as it may reduce legal certainty for foreign investors (Mishra & Valencia, 2023). However, some member governments might prefer this as it prevents claims against restrictive policies. Furthermore, risk and uncertainty might be felt by firms in Asia which are trying to expand in the high growth ASEAN region. A survey done in line with this matter shows that the major barriers for businesses to expand in the region is lack of local technological capabilities and supply chain challenges.[5] In addition to that, it is noted that the implementation of RCEP might be challenging. While the agreement makes provisions to reduce non-tariff barriers so that exporters can take full advantage of the common rules of origin and benefit from low administrative cost, the implementation might be the hard part for member countries. To fully benefit from the RCEP agreement and improve FDI stock in the member countries, the ratification and fully implementing the measures are crucial. Partial implementation will lead to smaller opportunities (Estrades et al., 2022).

5. Conclusion

The RCEP has important implications for trade and FDI in South and Southeast Asia. It represents the world's largest trading bloc and has the potential to boost the region's economic growth, enhance economic integration and benefit all the member countries. The agreement is expected to improve the regional investment climate due to the multiple measures outlined. For instance, the RCEP aims to promote predictability, consistency, and transparency in the application of customs laws and regulations, and promote efficient administration of customs procedures and expeditious clearance of goods. There is a harmonization and simplification of customs procedures for cross-border trade. Also, the agreement lays importance on consistent and transparent sanitary and phytosanitary measures to be adapted for the region. With the RCEP, there is improved information exchange. Interestingly, the RCEP agreement is more flexible compared to the relatively more aggressive tariff reduction schedules imposed by other free trade agreements. Several trade liberalization strategies are adopted by the RCEP including a reduction or elimination of customs duties and tariffs, and the possibility of initiating consultations to address adverse non-tariff measures. Market access is as well enhanced. Moreover, the RECP highlights trade remedies that cover safeguard measures and anti-dumping and countervailing duties. It also caters for digital trade, which is expanding worldwide, including the digitalization of trade administration and processes, cross-border data flows, and electronic contracts.

Importantly, RCEP can be regarded as a form of regional economic integration consistent with the framework of the WTO. In line with Article XXIV of The General Agreement, 1994on Tariffs and Trade (GATT) 1994, RCEP aims to progressively eliminate duties and restrictive regulations among its members while maintaining openness toward non-members, fulfilling the requirements set out in Articles XXIV:5, XXIV:7, and XXIV:8.

Overall, RCEP is expected to significantly boost trade and FDI in East and Southeast Asia through the creation of a larger and more integrated market, improved investment climate, more efficient supply chains and the generation of jobs. However, the extent to which RCEP will impact on the member countries will depend on how effectively the measures under the agreement are implemented and adhered to. Less developed member states may not be able to meet all the requirements of the agreement as compared to the developed nations. Moreover, the success of the agreement may largely depend on the geopolitical stability of the countries.

CRediT authorship contribution statement

Sheereen Fauzel: Writing – review & editing, Writing – original

[5] https://www.business.hsbc.co.mu/en-gb/insights/growing-my-business/how-free-trade-agreements-are-opening-opportunities-across-asia.

draft, Methodology, Formal analysis, Conceptualization. **Jeevita Matadeen:** Writing – original draft, Resources, Methodology, Investigation, Data curation, Conceptualization. **Verena Tandrayen Ragoobur:** Writing – review & editing, Writing – original draft, Methodology, Conceptualization. **Leenshya Gunnoo:** Writing – original draft, Methodology.

Declaration of Competing interest

This is to confirm that there is no conflict of interest in the above mentioned paper.

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