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Potential Benefits of RCEP on the Philippines: Accelerating Recovery Through Trade and Other Economic Opportunities

Abstract

The Philippines, as a member of ASEAN, is part of the RCEP, which is the world's largest trading block in terms of population and GDP. RCEP was signed on November 15, 2020, by 15 member countries. This policy note discusses the potential effects of RCEP on the Philippines. Using a global CGE model calibrated to the most recent GTAP 10 database, the results indicate that the Philippines will benefit from higher exports, lower consumer prices, higher factor prices, and factor incomes of households. Among the Philippine sectors, the largest positive effects are observed in electronic equipment. Interestingly, the impact on the agriculture-food sector is also notable.

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Policy Recommendations

RCEP will have positive effects on the Philippine economy. One of the key effects is observed in the agriculture and food sectors. These are not primary commodities but manufactured products with value addition. The positive effect on these commodities is critical in the government's on-going agricultural and industrialization plan, whose key objective is to improve farmers' income. RCEP, therefore, provides an expanded market base for the Philippines. The Philippines should seize this opportunity for its exporters and MSMEs. Specifically, the different government agencies should work closely together to prepare the country for RCEP. First, the Department of Trade and Industry (DTI) should take the lead together with the Department of Agriculture (DA) and the Department of Science and Technology (DOST) to implement the completed roadmaps like those for processed fruits and nuts and other agriculture commodities. The advantage of the DTI and DA roadmaps is that they used the value chain analysis (VCA) framework, which covers the production and sourcing of raw materials up to the establishment of domestic and export markets. Second, DTI and DA should prioritize preparation of roadmaps for vegetables and fishery commodities for the international market. Third, projects like processing facilities for high-value agri-fishery products, and agri-related infrastructures and facilities should be prioritized. Examples of these projects that government can promote are the New Clark City Food Processing Terminal or the Bulacan agro-commodities and exchange center or agro-industrial business corridors.

Introduction

The Regional Comprehensive Economic Partnership (RCEP) is a regional trade agreement signed on November 15, 2020, by 15 countries, which include the 10 ASEAN member countries, Australia, China, Japan, New Zealand, and South Korea. RCEP is the largest trading block.[1] It consists of 2.26 billion population with a total gross domestic product (GDP) of US$26 trillion (Table 1).

Table 1
Gross Domestic Product and Population for 2019

Country	2019 GDP (Bn USD)	2019 Population (Mn)
ASEAN		
Malaysia	365	33
Singapore	372	6
Philippines	**377**	**107**
Thailand	544	69
Indonesia	1,119	268
Brunei Darussalam	13	0.5
Viet Nam	262	96
Lao PDR	18	7
Cambodia	27	16
Myanmar	69	54
Plus 5		
New Zealand	210	5
Australia	1,354	25
Korea, Rep. of	1,642	52
Japan	5,080	126
China, People's Rep. of	14,343	1,400
Total	**25,795**	**2,265**

Note: The GDP and population or Lao PR and New Zealand refer to 2018.
Source: Asian Development Bank (2020)

Countries in RCEP are major trading partners of the Philippines. The Philippines exports 54% of its products to the area and purchases 53% of its import requirements from these countries. The trade barriers reduction within the area due to the agreements in RCEP will certainly increase the flow of trade between the Philippines and the rest of the RCEP countries.

This policy note presents the results of a simulation analysis on the potential effects on the Philippines joining RCEP, using a global computable general equilibrium (CGE) model calibrated using the most recent GTAP 10 database.[2] The simulation analysis consists of the following trade barriers: (a) tariffs in the ASEAN Trade in Goods Agreement (ATIGA); (b) applied GTAP tariffs outside of ASEAN; and (c) non-tariff measures (NTMs) modeled as export tax, import tariff surcharge, and additional cost due to import inefficiency.[3] In the analysis, the following reductions in trade barriers within RCEP are implemented: (a) gradual elimination in tariffs (except tariffs on rice); and (b) gradual 25% reduction in non-tariff measures (NTMs) over time.

Trade agreements generate two effects, which this note will highlight with respect to RCEP: (a) trade creation that redirects trade flows to an area where trade barriers are reduced; and (b) trade diversion that generates the opposite effect, that is, trade flows out of countries outside the area. Therefore, trade expands under trade creation, whereas trade contracts in trade diversion. These effects are generated because of changes in the relative trade costs. As the reduction in trade barriers reduces trade costs, trade flows increase. As a result, economic activities expand as trade flows improve. Trade flows within RCEP will increase, which will expand economic activities within the area. Outside of RCEP, trade flows but economic activities will contract.

Simulation Results

Table 2 presents the economic impact on countries within RCEP as well as outside the area. The reduction in the trade barriers within RCEP will increase trade flows within the area, which will expand economic activities. The results are expressed in monetary value and as a percentage of GDP. In terms of monetary value, the highest positive effect is seen in South Korea, China, and Japan. In the Philippines, the positive effects are expected to increase from US$155 million in 2021 to US$281 million in 2024.

Because countries in RCEP are in different stages of development, a good indicator of economic improvement/impact is to express the effects relative to GDP. The results show that Viet Nam and Malaysia benefit the most, whereas China, New Zealand, and Japan benefit the least. The impact on the Philippines is within the mid-range, that is, RCEP increases the GDP by 0.41% in 2021 to 0.66% in 2024.

The positive effects in countries within RCEP are due to the trade creation as a result of the reduction in the trade barriers within the area. However, there is trade diversion in countries outside of RCEP such that trade and economic activities outside of RCEP contract, as indicated in Table 2.

Table 2
Change in Welfare/Economic Activities

	EV* (US$ million)				EV/GDP, %			
	2021	2022	2023	2024	2021	2022	2023	2024
Viet Nam	171	214	261	422	0.66	0.79	0.93	1.45
Malaysia	354	444	542	725	0.77	0.93	1.10	1.42
South Korea	950	1,206	1,492	2,457	0.55	0.68	0.81	1.31
Singapore	220	271	324	383	0.57	0.68	0.79	0.91
Other ASEAN	27	34	40	57	0.46	0.55	0.63	0.89
Philippines	155	193	232	281	0.41	0.48	0.56	0.66
Thailand	150	186	223	325	0.30	0.36	0.42	0.59
Indonesia	259	336	423	630	0.21	0.27	0.32	0.47
Australia	386	480	581	860	0.21	0.26	0.31	0.44
Japan	998	1,226	1,464	2,098	0.20	0.24	0.29	0.40
New Zealand	43	54	66	95	0.17	0.21	0.25	0.35
China	1,208	1,431	1,632	2,175	0.08	0.10	0.11	0.14
NAFTA**	-132	-167	-205	-275	-0.01	-0.01	-0.01	-0.01
EU28***	-96	-124	-156	-204	0.00	-0.01	-0.01	-0.01
Latin America	-59	-75	-93	-125	-0.01	-0.01	-0.02	-0.02
Africa	-72	-91	-113	-177	-0.02	-0.03	-0.03	-0.05
Rest of the world	-273	-345	-426	-658	-0.02	-0.03	-0.04	-0.05

[1] ASEAN is Association of Southeast Asian Nations.
[2] GTAP is Global Trade Analysis Project. Detailed discussion and specification of the global CGE is found Cororaton and Orcen (2015).
[3] Estimates of NTMs used were based on Kee et al. (2006). Detailed discussion of how NTMs are incorporated in global CGE is discussed in Cororaton and Orden (2016).

*Equivalent variations
** North American Free Trade Agreement
***European Union
Source: Authors' own calculations.

In the Philippines, the effects vary across sectors. Table 3 shows that the highest increase in exports is seen in electronic equipment. The increase in export of this sector improves from US$60.8 million in 2021 to US$117.7 million in 2024. These effects are expected because electronic equipment is the largest export item of the country, and RCEP is the country's major market. Therefore, agreements in RCEP will facilitate the trade flows of electronic equipment from the Philippines to markets within the trading block.

RCEP will favorably affect agriculture-food sectors in the Philippines. This impact is seen in the improvement in exports of vegetables and fruits, all other food items, oil fats, and fishing. The increase in total exports of these items will improve from US$24.4 million in 2021 to US$53.2 million in 2024. These agriculture-food products are generally manufactured and are not primary commodities, that is, they have value addition. The favorable potential effects on these products are critical as these sectors are major elements of the on-going plan of the government to modernize and industrialize agriculture in the country. Because of value addition and high labor intensity in the production of these commodities, the increase in their exports and, therefore, output will potentially improve the incomes of farmers, which is one of the major objectives of the present agricultural modernization and industrialization plan.

Table 3
Change in Philippine Sectoral Exports*, US$ million

	2021	2022	2023	2024
Electronic Equipment	60.8	79.0	98.6	117.7
Vegetables and Fruits	14.5	17.7	20.9	28.0
All Other Food	7.8	9.9	12.1	17.1
Mining	8.6	10.9	13.5	16.0
Petroleum and Chemical Products	5.1	6.1	7.1	9.2
Oil Fats	1.8	2.5	3.4	7.2
Machinery and Equipment	2.8	3.4	4.0	6.1
Iron and Steel	3.1	3.7	4.3	6.0
Wearing Apparel	1.4	1.7	2.0	2.6
Fishing	0.3	0.4	0.5	0.9
Meat	0.4	0.4	0.5	0.8
Sugar	0.3	0.3	0.4	0.6
All Other Agriculture	0.1	0.1	0.1	0.3
Milk	0.1	0.1	0.1	0.1
All Other Manufacturing	-0.5	-0.7	-1.0	0.1
Cereals	0.0	0.0	0.0	0.1
Animal Products	0.0	0.0	0.0	0.0
Metal	-0.2	-0.3	-0.4	-0.4
Textile	-0.2	-0.3	-0.4	-0.5
Vehicles	-0.1	-0.2	-0.4	-1.6
Leather	-1.2	-1.6	-2.1	-2.8

*Relative to baseline
Source: Authors' own calculation.

The reduction in trade barriers within RCEP will reduce trade as well as production costs within the area. This reduction in costs will not only reduce consumer prices, as indicated in Table 4, it will also lead to higher real factor prices, and therefore the income of households. The decline in consumer prices increases from -0.46% in 2021 to -0.79% in 2024. The increase in exports, production, and the reduction in consumer price increase factor income derived from skilled wages, unskilled wages, and returns to capital.

Table 4
Change in Philippine Consumer and Factor Prices, %

	2021	2022	2023	2024
Consumer prices	-0.46	-0.56	-0.66	-0.79
Factor Prices:				
Skilled wages	0.22	0.25	0.29	0.28
Unskilled wages	0.13	0.15	0.16	0.12
Returns to capital	0.38	0.44	0.50	0.54

Conclusion

RCEP will bring about positive effects on the Philippines. The reduction in trade barriers in the world's largest trading block will increase economic activities in the country, leading to higher income. Compared to countries in RCEP, the impact on the Philippines is within the mid-range. Viet Nam and Malaysia will benefit the most, whereas China, New Zealand, and Japan the least. The impact on the Philippines will contribute to economic recovery beginning 2021.

In the Philippines, exports of electronic equipment will increase the most. However, the improvement in exports of agriculture-food commodities is also notable. These commodities are not primary products but with value addition. The increase in exports and production of these commodities is critical in the agricultural modernization and industrialization plan of the present administration.

The reduction in trade and production costs as a result of the reduction in trade barriers will reduce consumer prices in the country. The increase in exports and production of the agriculture sector and the reduction in consumer prices will result in higher factor prices and factor incomes of households.

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