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Will the Philippines benefit from the Regional Comprehensive Economic Partnership?

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The Regional Comprehensive Economic Partnership (RCEP) is a free trade area (FTA) among the 10 member-states of the Association of Southeast Asian Nations or ASEAN (i.e., Brunei Darussalam, Cambodia, Indonesia, Lao PDR, Myanmar, Malaysia, the Philippines, Singapore, Thailand, and Viet Nam) and six non-ASEAN countries in Asia and Oceania (i.e., Australia, China, Japan, South Korea, New Zealand, and India). The economies covered in the RCEP have a total gross domestic product (GDP) of USD 21 trillion in 2013, and a population of 3.4 billion.

The RCEP includes two of the world's most populated nations (i.e., China and India) and the second and third largest economies (i.e., China and Japan) (Table 1). Within the RCEP, ASEAN has a combined GDP of USD 2.6 trillion and a population of 622 million, while the six non-ASEAN countries ("+6" from here on) have a population of 2.8 billion and a total GDP of USD 19 trillion.

This *Policy Note* examines the potential effects of the reduction in RCEP tariffs and nontariff barriers (NTBs) on the Philippine economy using mathematical modeling.

ASEAN's centrality is recognized in RCEP negotiations in November 2012. One of the major points in these negotiations is the elimination of trade barriers (i.e., tariffs and NTBs). However, trade barriers continue to exist within the RCEP despite the progress achieved over the past three decades in reducing tariffs on international trade under the World Trade Organization and,

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Table 1. Population and GDP of RCEP countries, 2013

	Population (in million)	GDP (USD billion)*
ASEAN		
Brunei Darussalam	0.4	16.1
Cambodia	15.0	15.2
Indonesia	248.8	868.3
Lao PDR	6.7	10.6
Malaysia	29.9	312.4
Myanmar	61.6	80.7
Philippines	97.4	272.1
Singapore	5.4	297.9
Thailand	66.8	416.1
Viet Nam	89.7	171.2
Total ASEAN	621.8	2,460.7
"+6"		
Australia	23.1	1,468.5
New Zealand	4.5	185.8
Japan	127.3	4,898.1
South Korea	50.2	1,304.6
China	1,360.7	9,181.2
India	1,228.8	1,798.6
Total "+6"	2,794.7	18,836.8
Overall total (ASEAN and "+ 6")	3,416.4	21,297.5

* Local currency converted to USD using average USD rate; 2012 for Myanmar
Source: Asian Development Bank (2014)

subsequently, in the context of regional and bilateral preferential trade agreements. Tables 2 and 3 show that there are still notable average tariffs and NTBs in agricultural trade in the RCEP, particularly in the "+6" countries.

Simulation results

The results of the simulations using a global computable general equilibrium model indicate that the reduction in trade barriers within the RCEP will increase the total exports within the area—from 1.1 percent relative to the baseline in 2014 to 3.3 percent in 2023 (Table 4). RCEP exports to non-RCEP countries decline. Within the RCEP, the increase in exports of "+6" is higher than the improvement in ASEAN.[1]

In the Philippines, the effects on export growth of the RCEP are initially negative; these exports will improve over time (Table 5). In 2018, Philippine exports within the RCEP will improve by 2 percent relative to the baseline. In 2023, they are expected to increase by 3.8 percent. All of these effects will translate to higher Philippine real GDP growth of 3 percent in 2023, and will generate additional welfare of USD 3 billion.

Rice is the most protected sector in the Philippines. The entry of cheaper imported rice negatively affects domestic rice production, but it benefits lower-income households because rice is a major item in their food basket (Table 6). The inflow of cheaper textile imports leads to lower textile production, but it benefits the wearing apparel sector. The construction sector benefits from higher inflows of foreign investments. The output of the transportation and machinery equipment sector improves along with the increase in the construction sector. There are also

[1] The export effects vary significantly both across ASEAN member-states and "+6" (Cororaton [b]).

notable positive output effects in the services sectors, particularly in the transportation sector, which benefits from the improvement in agriculture and manufacturing.

The returns to land and in wages improve, while the returns to capital decline (Table 7). These effects are considered progressive because they favor lower-income household groups (Table 8). In turn, these outcomes decrease poverty incidence in 10 years—from the current 24.9 percent to 23.3 percent in 2023 (Table 9). Among poor households, those under extreme poverty (P2) benefit the most. Furthermore, the effects lower the Gini coefficient, indicating favorable distributional effects (Table 9).

FTA usually facilitates the inflow of foreign investment. The simulation considers only minimal investment inflows of USD 2.5 billion over a 10-year period. The gain can potentially be higher because the Philippine economy has a large absorptive capacity for foreign capital.

Likewise, the Philippines has large amounts of untapped natural (mineral) resources. A huge part of its labor force is composed of

Table 2. Simple average applied tariff rates (%)

	Agriculture and Food	Mining	Manufacturing
RCEP	18.5	4.2	6.8
ASEAN	9.1	4.4	7.2
"+6"	31.0	3.8	6.3
Rest of East Asia	3.6	1.8	2.1
North America Free Trade	7.4	1.3	3.4
European Union 25	13.3	1.1	2.6
Latin America	8.6	5.0	9.1
Africa	11.2	6.9	11.7
Rest of the world	10.8	4.7	6.6

Source: Global Trade Analysis Project (GTAP) 8 Database

Table 3. Estimates of average AVE* of NTBs in the RCEP

	Agri-Food	Crops	Cereals	Sugar	Meat	Dairy Milk	Manufacturing	Services
RCEP	11.63	17.15	20.43	17.13	12.02	16.68	2.49	28.31

Source: Cororaton (a)
*Ad valorem tariff equivalent

Table 4. Regional effects, percent change from the baseline

	2014	2018	2023
RCEP			
Total exports	0.60	2.28	3.31
To RCEP	1.87	6.97	9.89
To outside RCEP	-0.20	-0.74	-1.14
ASEAN			
Total exports	0.44	1.64	2.21
To RCEP	1.03	3.87	5.44
To outside RCEP	-0.20	-0.86	-1.73
"+6"			
Total exports	0.65	2.49	3.68
To RCEP	2.26	8.51	12.27
To outside RCEP	-0.20	-0.71	-1.00
Non-RCEP			
Total exports	-0.02	-0.09	-0.14
To RCEP	-0.26	-1.03	-1.53
To outside RCEP	0.02	0.10	0.18

Source: Author's calculations

Table 5. Philippine macro effects

	2014	2018	2023
Total exports	-0.16	1.20	2.65
To RCEP	0.11	2.07	3.76
To outside RCEP	-0.58	-0.19	0.66
Real GDP, % change from baseline	0.00	1.25	2.95
Real GDP, USD million	285.77	351.23	450.08
Equivalent variation, USD million	0.06	0.67	2.04

Source: Author's calculations

Table 6. Philippine sectoral output effects, percent change from the baseline

	2014	2018	2023
Rice	-0.91	-3.07	-4.26
Wheat and all other cereals	-0.07	0.31	0.45
Sugar	-0.22	0.31	1.13
Milk	-0.24	1.18	2.79
Oils fats	-0.42	-0.18	0.57
Meat	0.14	1.12	2.44
All other agriculture	0.03	0.91	1.41
Mining	-0.23	0.88	4.30
All other food	0.07	1.68	3.18
Textile	-0.83	-1.63	-1.28
Wearing apparel	-0.16	1.13	2.65
Petroleum and chemical products	-0.27	0.80	2.55
Metal products	-0.32	1.02	3.87
Transport and machinery equipment	0.04	2.85	7.17
Electronic equipment	-0.42	0.14	0.91
All other manufacturing	-0.33	0.69	2.36
Utilities	-0.01	1.43	3.38
Construction	2.13	5.70	11.21
Trade	0.04	1.56	3.46
Transportation	0.14	1.96	4.14
Communications	-0.02	1.53	3.43
Finance business services	-0.11	1.32	3.22
Other services	0.02	1.92	4.04
Public administration	0.01	0.34	0.72

Source: Author's calculations

Table 7. Factor price effects in the Philippines, percent change from baseline

	2014	2018	2023
Skilled wages	0.88	2.26	3.88
Unskilled wages	0.95	2.21	3.80
Returns to capital	0.77	0.27	-0.74
Returns to land	0.60	2.62	5.69

Source: Author's calculations

Table 8. Real household income effects in the Philippines, percent change from baseline

Households	2014	2018	2023
H1	0.258	2.341	5.129
H2	0.125	1.741	4.333
H3	0.133	1.787	4.404
H4	0.125	1.760	4.355
H5	0.126	1.736	4.295
H6	0.121	1.724	4.273
H7	0.164	1.761	4.312
H8	0.183	1.793	4.372
H9	0.155	1.726	4.269
H10	0.101	1.701	4.329

Source: Author's calculations

young professionals—with a high level of education—who can benefit from higher wages as a result of the RCEP.

Conclusion

RCEP can bring a positive impact on the Philippine economy. Its trade-creation effects will increase Philippine exports within the region. This higher export growth and the improvement in foreign investments will generate a chain of positive effects domestically such as higher wages to both skilled and unskilled labor, lower prices due to the reduction in trade barriers, higher household income, and lower poverty incidence.

The inflow of foreign direct investment may be enhanced with improvements in infrastructure. Significant amounts of investment are needed to improve its sorry state, which affect the country's bid to sustain its present growth trajectory.

Moreover, significant reforms in investment and corporate taxation are required to make the Philippines an attractive destination for foreign investments. At present, corporate taxes are high relative to those in other countries in the region. In this area, the RCEP could help stimulate beneficial reforms in domestic policies.

Table 9. Poverty effects in the Philippines

		End of Simulation Period: 2023	
	2012[a]	Index	Percent Change from 2012
Philippines			
P0[b]	24.85	23.29	-6.26
P1	6.84	6.26	-8.39
P2	2.68	2.42	-9.76
Urban			
P0	11.57	10.77	-6.94
P1	2.79	2.51	-10.01
P2	0.99	0.88	-11.40
Rural			
P0	35.58	33.42	-6.09
P1	10.10	9.29	-8.03
P2	4.04	3.66	-9.44
GINI coefficient	0.4713	0.4709	-0.080

[a] Family Income and Expenditure Survey (FIES)
[b] P0 - poverty incidence; P1 - poverty gap; P2 - poverty severity
Source: FIES, Philippine Statistics Authority (2012); and author's calculations

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