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Regional Comprehensive Economic Partnership (RCEP)

Potential concerns for domestic industries

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RCEP: Potential Concerns for Domestic Industries

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Why RCEP?

The Regional Comprehensive Economic Partnership (RCEP) can be seen as opportunities for Myanmar in terms of expanding regional markets and restoring the existing markets in developing economies. Through RCEP economic cooperation, it is expected that the investment from Japan, Australia, South Korea and China are concentrated in ASEAN region under the arrangement of RCEP. Taking this advantage, Myanmar could become a host for labor intensive investment at the given low labor cost and abundant human resource. Further, with the growing young and educated population, Myanmar can be attractive to high-tech investment from the region that encourage technology spillover into the country.

Myanmar can be left behind in regional cooperation and has limited access to regional markets for its exports if it is absent from participating in RCEP. Therefore, the cost of not participating in RCEP is likely to be higher than the cost of participating in RCEP. For example, there are possible costs arising from investment and trade diversion effects (i.e. import and investment shifted from Myanmar to other countries like Thailand and Vietnam) if Myanmar is not a member of RCEP.

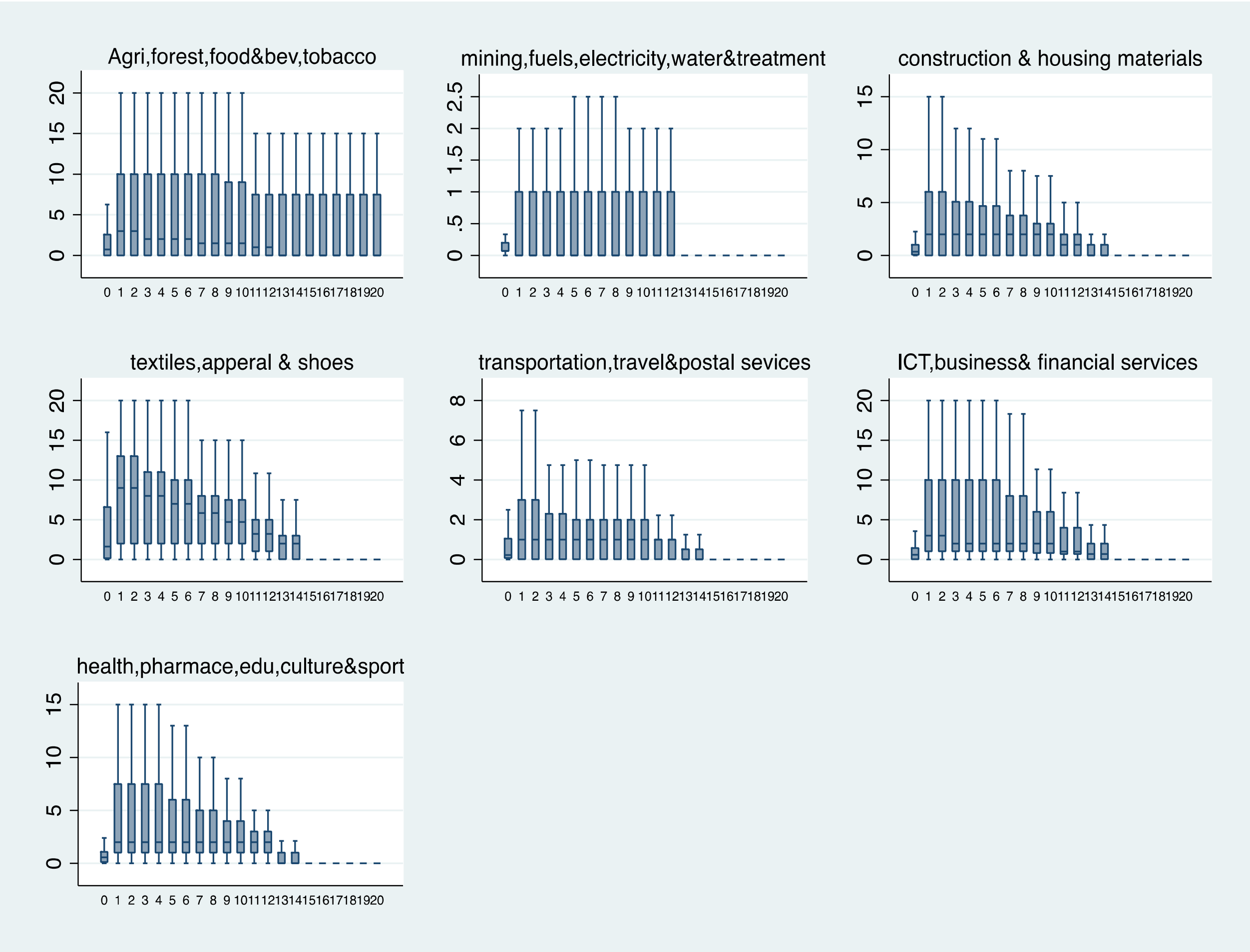
What are the Tariff Arrangements?

The RCEP member countries will eliminate tariff for 65 percent of its import product lines within 10 years and up to 90 percent in 20 years after coming into effect as ratified. However, concerning the unbalanced levels of development among members, RCEP provides special provision to the least developed members, which are Cambodia, Myanmar and Lao PDR (CML). CML countries will eliminate tariff for 30 percent of imported products from member countries in the first 10 years and 80 percent in 15 years.

The agriculture sector will remain a highly protected industry for all member countries. As for Myanmar, the tariff rates for agriculture, forestry, fishery and other food products will decrease from a maximum of 20 percent and a minimum at zero percent over the first 10 years (Figure 1). Along with the agriculture sector, the other two main sectors where Myanmar will set a slightly higher initial tariff to protect the domestic industries are: (a) textiles, apparel and shoes; and (b) ICT, computer, business and financial services.

Technically, Myanmar exporters can benefit from exporting most of their products at low tariff rates into the mega markets of RCEP region. However, there are still limited trade measures on how RCEP members will deal with non-tariff barriers, which hinder trade liberalization. For example, non-tariff barriers (e.g. restrictive rules and quota system of importing countries) are still a major obstacle for Myanmar to reap the full benefits of RCEP arrangements.

Figure 1: Myanmar tariff reduction by BEC categories



Source: author' calculation based on Myanmar Tariff schedule for RCEP.

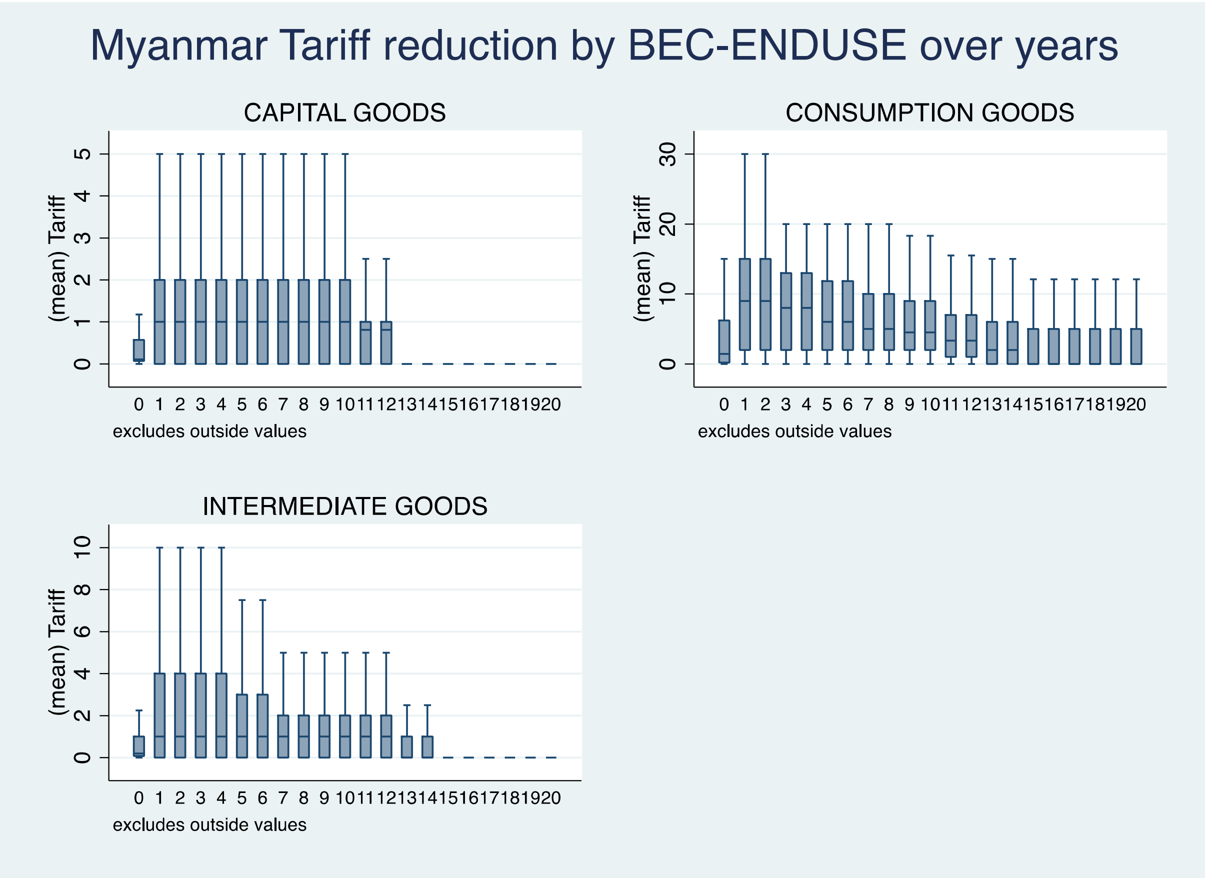
Note: Year zero in boxes represent the existing average tariff rate (i.e. middle bar) of Myanmar to RCEP members. The average tariff for year 0 is calculated based on the ongoing tariff schedule of Myanmar to ANSEAN, ANSEAN+ANZ, ASEAN+Korea, ANSEAN+China and ASEAN+Japan tariff schedule for 2020.[1] *Year 1 refers to the starting tariff rate of RCEP.*

Figure 2 shows the tariff liberalization status of Myanmar import products by broad economic category (BEC) at their main end-use under RCEP arrangements. The BEC end-use can be categorized into consumptions goods, capital goods and intermediate goods. Myanmar has a relatively protective tariff structure for consumption goods while it opens up more to the import of capital and intermediate goods (see Figure 2). Tariffs for consumption goods will decrease from a range of 0 to 30 percent to a

[1] Myanmar' existing tariff for 95% of products lines are closed to zero rate for ASEAN and China whilst it is substantialy higher for Koea, Japan and ANZ. Thus, the average tariff rate at year 0 is likely to undermine the existing high tariff rate to South Korea, Japan, Australia and New Zealand.

maximum of 12 percent over the first 15 years. Tariffs for capital goods will decrease from around 0 to 5 percent to 0 percent after 12 years, while tariffs for intermediate goods will decrease to 0 from 10 percent after 15 years.

Figure 2: Myanmar Tariff reduction by BEC end-use



Source: Author's calculations based on the Myanmar tariff schedule for RCEP

Note: Year zero represent the existing average tariff rate of Myanmar to RCEP members. The average calculation for year 0 is based on the ongoing tariff schedule of Myanmar to ANSEAN, ANSEAN+ANZ, ASEAN+Korea, ANSEAN+China and ASEAN+Japan tariff schedule for 2020. Year 1 refers to the starting tariff rate of RCEP.

Table 1 shows sectors covered under each BEC end-use category i.e. capital, consumption and intermediate goods. Generally, many countries make stringent rules—for example, higher tariff rate or apply trade defense measures—to limit the increasing imports of consumption goods (UNCTAD 2013, p.3; UNCTAD 2015, p.11). In Myanmar, 99% of domestic firms—mostly micro, small and medium size industries— are falling under the categories of consumption goods, therefore, the pro and cons of RCEP on the sector should be monitored constantly.

Table 1: Major industries covered under RCEP by BEC end-use

CAPITAL GOODS	CONSUMPTION GOODS	INTERMEDIATE GOODS
- Metals - Machinery and electrical products - Transportation - Miscellaneous and others	- Animal and Animal products - Vegetable Products - Foodstuffs - Textiles - Machinery and electrical products - Wood and Wood Products - Chemical and Industrial products - Footwear and Headgear - Metals products	- Chemical and Industrial Products - Metals - Textiles - Machinery and electrical products - Plastics and Rubbers - Vegetables Products - Mineral Products - Wood and Wood Products - Stone and Glasses

Source: Author's preparation based on Myanmar tariff schedule for RCEP

POTENTIAL OPPORTUNITIES FOR MYANMAR

RCEP involved designing a common regional value content for Rules of Origin (ROO)— i.e. the harmonized information requirements and regional content standards used to determine which products are eligible for the preferential terms of the agreement. These are slightly different under existing ASEAN + 1 FTAs with Japan, South Korea, etc. Under ASEAN+1 FTAs, exporters have to meet around 35 to 40 percent of local (or) regional value-added content to comply with the tariff concessions of those agreements. However, it is reported that meeting 35-40 percent of ROO is difficult especially for manufacturing exporters from CML countries since the local valued-added contribution from CML is very low (Kirk 2007, p.12). With the unified ROO under RCEP, the value-added content from all 15 member countries will be combined to determine regional value content, thus helping to remove the ROO barrier of CML countries in utilizing RCEP.

With such unified ROO, Myanmar's manufacturing industry can greatly benefit from fragmentation of production where developed countries with high labour costs offshoring their manufacturing production to countries with lower labour costs. Fragmentation of production is when the producers relocates their assembly operation and offshoring of parts of productions into different locations (Nunnenkamp 2006). Because the investors offshore the labour-intensive stages of productions to lower income countries, Myanmar can be an attractive location for production of fragmentation from developed RCEP member given its low labor cost and abundant young labour force. Myanmar has already attracted manufacturing from other countries (esp. garment industries),generating more than 500,000 jobs.

The German automobile industry offers an example of how fragmentation of production, by relocating assembly operations to low-wage countries in Central and Eastern Europe, can develop job opportunities for poorer countries and encourage the transfer of technology know-how. Germany is widely regarded as a leading exporter of automobiles. According to Nunnenkamp (2006), almost one-third of Germany car companies relocated their auto parts production to Poland, Hungary, Czech

Republic and Slovak Republic, which are lower income level countries with abundant labour force (p.9). For instance, Opel relocated parts of its Zafira productions to Gliwice in Poland (ibid). This happened at the same time as the region started opening up to the world market under the umbrella of the European Union, which brought about new market and profitable investment opportunities. At the same time, low wages were a major determinant for German car companies to shift their production to the region, with expectations of high economies of scale whereby they can operate at a large scale due to low labour costs and benefit from lower average costs as a result. With a massive investment by German automobile companies, Eastern European countries were able to establish an advanced domestic industry for parts suppliers, upgrading the existing suppliers and creating around 100,000 jobs in autoparts industries (ibid, p.11).

VULNERABLE INDUSTRIES AT EXPORT AND IMPORT SECTORS

As you can see in Figure 1 and Figure 2, Myanmar has already been applying low tariff rates to many import products — close to zero percent for 90 percent of tariff lines — from RCEP member countries under existing ASEAN + 1 FTA arrangements. Also, the tariff structures between the RCEP and ASEAN+1 FTA are not significantly different as both offer reduced tariff rates for intermediate and capital goods for the purpose of facilitating production and investment. While lower tariff may be beneficial for investors and manufacturers that source their raw materials aboard, lower tariffs can be harmful for domestic firms—especially SMEs—which are reliant on domestic consumers and domestic suppliers of inputs. Especially, there is a risk of local firms – in infant industries and with start-up entrepreneurs – of being crowded out by a flood of imports at cheaper prices. Therefore, this policy note identifies the potential risks for exporters and importers under RCEP tariff reductions.

a. Potential risks for export sectors

According to statistics available on Ministry of Commerce website, Myanmar exports are led by petroleum gas, garment, rice, refined copper and dried legumes in 2019 (MOC 2021). Bearing in mind that Myanmar exports its top export products to China, Thailand, Japan, Germany and etc., it is critical to investigate how RCEP can affect the Myanmar position in existing markets. This note identifies some primary export commodities and examine the potential impact for exporters regarding market share in the regional market.

i. **Rubber**: Rubber and rubber products are among the commodities promoted by the National Export Strategy to expand its exports in the international market. Myanmar is one of the main rubber producers in ASEAN following after Thailand, Indonesia and Malaysia. Myanmar exports 70 percent of raw rubber and rubber products to China, Malaysia, India, South Korea, Japan and etc. China is the main market for ASEAN rubber exporters; however, China does not offer tariff reduction for raw rubber (i.e. HS4- 4001) to ASEAN members under RCEP arrangement. The current tariff rate for raw rubber by China is 0.2 % under RCEP tariff schedule to ASEAN countries, however, it seems China still want to limit the importation of Rubber from ASEAN countries. Therefore, China exclude rubbers and its related products from normal tariff reduction schedule of RCEP as the tariff products lines for rubber was recorded as "unbound"—meaning excluded from tariff reduction schedule. This depicts the provision of RCEP has less impact for Myanmar rubber exporters while Myanmar exporters faces with price discrimination by China as Myanmar can only export raw-rubber and low-quality products. Despite the excluding concession by China, Japan and South Korea is likely to become a new market opportunity for Myanmar rubber exporter. As different members have separate tariff schedule to each RCEP member, Japan and South Korea set zero tariff rate of raw rubber (i.e. HS6- 400110, HS6-400121) for ASEAN under their RCEP tariff arrangement schedule. In fact, there was no tariff commitment for ASEAN by Japan and South Korea under respective ASEAN+1 FTA. Given same treatment with the largest rubbers' producers such as Thailand and Malaysia, Myanmar need more strategic plan to expand new international market as well as prepare to be competitive in term of quality upgrading etc.

ii. **Copper**: Myanmar is a leading copper producer in the region while copper is exported mainly to China, Thailand, Vietnam, Indonesia and Malaysia in 2019 (ODEC 2020). China have set zero tariff for imported coppers (i.e. HS2-74) from Myanmar under ASEAN+ China FTA since 2015. However, with the new arrangement under RCEP, Australia— one of the top largest copper producers— is likely to export its quality copper and related products at average zero tariff rate to China. Thus, Myanmar copper producers are likely to compete with massive copper producers and lose market share in China market.

iii. **Coffee**: Export of coffee sector from Myanmar have increased as the growing demand in the region. Top export destinations of Myanmar coffee include China, Malaysia, Singapore, South Korea and Japan between 2011 and 2017 (Basu et al 2019, p.3). Despite the substantial development in coffee export, Myanmar still hardly compete with exporters from Vietnam and Indonesia at international market. The RCEP provides new coffee market opportunities for Myanmar coffee exporter with the growing demand from South Korea and Japan. South Korea offer an average tariff rate at zero for coffee (ie. HS4- 0901) under RCEP agreement which is currently 2 percent under ASEAN+ Korea FTA. Japan, however, still set slightly higher tariff for coffee around average 8 percent in the first 10 years in RCEP. In fact, Myanmar coffee sector is at the early stage of development in term of quality upgrading and expanding international market, thus, the Myanmar coffee sector needs more state support – both technical and financial – to improve access to regional markets.

b. Potential Risk for Imports sector

Following, the note identifies three specific sectors that are vulnerable from increasing imports by experiencing potential dumping and losing domestic market share.

i. **Food and beverage industries:** Myanmar consumer behavior is noticeably changing with the growing middle-income population and their increasing purchasing power over the past few years. Deloitte's Myanmar consumer survey (2019) demonstrates that consumers are less sensitive to price; but prioritizing taste and quality in their purchasing decision (p.20). At the same time, the Myanmar Consumer Union reported that 70 percent of consumer complaints that were concerning products from the domestic food and drug industry were due to products being unhealthy/unfresh, usage of dyeing and poor hygiene, among other reasons (MCU 2017, p.28). There is thus a high risk that local food producers will not be able to withstand the growth in competition in term of the price and quality of foreign products unless they upgrade and improve the quality and packaging of the products. Currently, Myanmar imports mostly processed and/or prepared foods, prepared/preserved seafoods, beef, lamb, cheeses, processed vegetable, beer and wine from the US, Singapore, Australia and New Zealand, for example (Food Export 2020). Also, food retail sectors (e.g. bakeries, cafes and luxury restaurants) have great potential for expanding in the domestic food market, which could lead to more demand for high-quality imported products instead of locally produced products. As a result of all these factors, local food and beverage producers may struggle to survive under the RCEP regime. Bearing this in mind, programs to support quality assurance would be helpful to upgrade the quality of local products and mitigate the potential negative impacts of RCEP at the same time.

ii. **Edible Oil Industry:** With the development of the domestic food industry, the consumption of edible oil in Myanmar has been increasing rapidly since the past few years. Annually, Myanmar domestically produces 400,000 tons of oil from groundnut, sesame and sunflower oil whilst it imports around 650,000 tons of high-quality edible oil mainly from Indonesia and Malaysia to fulfil the increasing demand by domestic consumers (Global New light Myanmar 2019). According to data available from the MoC, in 2019, Myanmar imported around US$ 255 million worth of quality palm oil yearly for domestic consumption. In fact, the Myanmar edible oil industry suffers from low productivity due to the prevalence of traditional farming methods, massive usage of pesticide, the impact of rapid climate change as and low investment in the sector. Furthermore, the domestic edible oil mills are facing dumping in the domestic market, where they are losing domestic market share from increasing imports of cheap and even fake edible oil (Eleven 2020). In fact, Myanmar recently just enacted the anti-dumping law (i.e. Law to prevent an Increased Quantity of Imports) in July 2020. Under the law, the inspection committee is formed to monitor the extent of increase in import quantity and assess its impact on domestic market. Therefore, the enforcement of this anti-dumping law should be prioritised to address the current domestic edible market to withstand the competitive pressures while the systematic support is implemented to improve the productivity of edible oil crops and quality.

iii. **Furniture industry:** The furniture industry in Myanmar is experiencing both demand and supply-side constraints. A few reasons are the limited availability of raw materials and their high price (e.g. teak and timber), declining quality and limited financial capacity of domestic entrepreneurs to operate a furniture business (Myanmar Times 2018). Despite falling consumer demand for locally produced furniture owing to soaring prices, Myanmar imported around $300 million worth of furniture yearly from neighboring countries such as China (ibid). This sector is an important source of jobs for semi-skilled and skilled workers. Therefore, this is a sector that would benefit from government support to help businesses to remain affordable and relevant in an increasingly competitive market, such as policies to support the acquisition of raw materials and provide greater access to finance.

CONCLUSION REMARK

In conclusion, RCEP can be seen as presenting both opportunities and constraints for Myanmar. Importantly, Myanmar can be better off if it is attractive to investment associated with production fragmentation from more developed RCEP members. At the same time, Myanmar needs to constantly monitor the potential negative impacts on domestic industries of increasing imports and the more competitive domestic market environment. Also, it is concerning that Myanmar legal frameworks to protect domestic businesses from such a competitive environment are not fully functional. For example, although the government recently passed an anti-dumping law, IP law and consumer protection law, the enforcement of these laws are still weak—meaning the Myanmar legal system is still not effectively placed to adapt to the emerging regional economic landscape.

Furthermore, RCEP can be seen as China expanding its influence on the Asia-Pacific region, which has geopolitical considerations. Some ASEAN member countries such as Philippines, Indonesia and Vietnam have prepared specific tariff reduction schedules for China, which are lacking in Myanmar. Considering those concerns, Myanmar should closely cooperate with the domestic business institutions and develop a transparent planform of RCEP to widely distribute the information and raise public awareness on the potential impacts of such a significant trade agreement.

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