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The Indo-Pacific Economic Framework as an Economic Agreement: An Analysis

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Abstract

The Indo-Pacific Economic Framework (IPEF) focuses effort on building a compact, resilient, clean, and just economy. These four goals constitute the IPEF's four pillars. Judging from the nature of the agreement, one can understand it as a non-traditional economic agreement existing somewhere between the Belt and Road Initiative and a free trade agreement (FTA). The IPEF's impact on China will be mainly reflected by exclusionary competition in strategic industries. China has three options for dealing with the United States' exclusion of Chinese supply chains and with Sino-US technological competition. The first would be to establish international rules on supply chains; the second would be to exchange space for time, improve political relations, and strengthen supply chain cooperation; and the third would be self-strengthening in strategic industries.

On May 23, 2022, the United States and Japan announced in Tokyo the launch of the Indo-Pacific Economic Framework for Prosperity (IPEF). In addition to the United States and Japan, the IPEF also includes 11 other founding members: Australia, India, New Zealand, South Korea, Brunei, Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Vietnam. Subsequently, the Pacific Island country of Fiji also announced that it would join IPEF, so it became the 14th founding member. The IPEF is the

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economic pillar of the Biden administration's Indo-Pacific strategy; its launch has attracted much attention in various circles, and it has obvious geopolitical overtones. However, the framework is also an economic agreement, so an analysis of it as an economic agreement can help us understand the direction of US foreign economic policy.

The IPEF will focus its efforts on building a connected, resilient, clean, and fair economy. These four goals constitute the IPEF's four pillars. "Connected Economy" refers to strengthened cooperation in the field of international trade and the formulation of international economic and trade rules. It specifically includes the following areas: strengthened cooperation on digital economy, formulation of rules on the digital economy, labor and environment; promotion of trade facilitation; enhanced transparency and good regulatory practices; and corporate responsibility. "Resilient Economy" refers to improved resilience of supply chains and reduced economic losses caused by supply chain shocks. Specifically, it includes: establishing early warning systems for supply chains, finding supply distribution for key mineral supply chains, improving the traceability of key industrial production chains, and cooperation on promoting diversification of production. "Clean Economy" refers to actions taken to combat climate change, with member states stepping up cooperation on new measures on renewable energy, carbon emissions, energy efficiency standards, and curbing methane emissions. "Fair Economy" refers to strengthened cooperation in the fields of taxation and anti-corruption through, for example, exchanging tax information.

Among the four pillars above, the key focus will be on cooperation in the area of supply chains. Cooperation in the area of international trade ("Connected Economy") will be promoted by the Office of the United States Trade Representative; all other content under this pillar, apart from corporate responsibility, were covered by the Trans-Pacific Partnership (TPP) Agreement, which had been negotiated during the Obama administration. Among them, digital economy rules and trade facilitation are also included in the Regional Comprehensive Economic Partnership (RCEP) Agreement. The other three pillars are being promoted by the US Department of Commerce and are generally not included in FTAs. For example, RCEP does not have content related to these three pillars. “Clean Economy” aims to accelerate the development and deployment of clean energy technologies. This is an area that really needs international cooperation, but one should be wary of establishing new energy industry chains that are exclusive. Anti-corruption was already touched on in the TPP, and the United States has made strengthening cooperation on taxation a key area of promotion in recent years. The area of “competitiveness and business facilitation” for supply chains has already been touched on in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), but there it refers mainly to cooperation on supply chains, rather than the prevention of supply chain shocks. The reason for this development is that as a result of Sino-US economic and trade frictions and the outbreak of the COVID-19 pandemic, countries are now fully aware of the importance of ensuring supply chain security. Countries do need to strengthen cooperation on supply chains in order to improve the chains’ resilience. However, the US will be excluding China, an important player on the supply chains, promoting exclusive cooperation on the basis of decoupling. Although this may seem to improve supply chain resilience, it may not actually have the effect of ensuring supply chain security.

Judging from the nature of the agreement, one can understand the IPEF as a non-traditional economic agreement existing somewhere between the Belt and Road Initiative and a free trade agreement (FTA). The differences between IPEF and traditional FTAs are quite obvious. From a theoretical standpoint, an FTA promotes trade liberalization based on the theory of comparative advantage, and it has a market efficiency orientation, but the IPEF is based on strategic trade theory, attaches importance to government cooperation, and has a national security orientation. As for agreement content, FTAs usually include two parts, market access and rules negotiation, which are “big and comprehensive,” but the IPEF has only rules negotiation and does not include market access negotiations in areas such as trade in goods, services investment, and government procurement; it is “small and smart.” Of course, rules negotiation in IPEF goes beyond the scope of an FTA. As for the cooperating industries, the IPEF is concerned mainly with the cooperation of strategic industries, which generally belong to oligopolistic market structures; an FTA, on the other hand, is concerned with the usual industrial cooperation, which generally belongs to market structures of perfect competition and monopolistic competition. As for the form of rules negotiation, FTAs use packages of negotiations, but the IPEF uses modules, and the four pillars are divided among four agreements. Each founding member can choose to join which ones to join, which will make the IPEF negotiations go faster. As for the ratification and binding force of the agreement, IPEF is promoted in the United States by executive orders; only the president's signature is required, and no congressional approval is needed. The other members also will probably not require any domestic approval procedures as are needed with FTAs. Therefore, the IPEF will have limited binding force. However, the IPEF is also different in nature from the Belt and Road Initiative. First, the content of the cooperation in the two arrangements differs. The Belt and Road Initiative is development-oriented, while the IPEF is security-oriented. Second, the IPEF needs to be implemented, and its binding force is stronger than that of the Belt and Road Initiative. In short, the IPEF can be understood to be an intermediate arrangement between an FTA and the Belt and Road Initiative.

The IPEF has just been launched, so its prospects are not yet clear. There is some uncertainty as to whether it will absorb new members. Compared with the TPP, the IPEF adds India, South Korea, and ASEAN's Indonesia, the Philippines, and Thailand, but does not include the four North and South American countries of Canada, Mexico, Chile, and Peru. ASEAN members Laos, Cambodia, and Myanmar, having relatively low levels of development, will probably not join IPEF for the time being. Canada and the other North and South American countries are not yet brought into the Indo-Pacific region, and the United States will seek to cooperate with them under other frameworks. The United States has also made it clear that it will not include Taiwan in IPEF and will seek cooperation at the bilateral level. The IPEF is an economic agreement in which the United States has explicitly excluded China and will not invite it to join. With regard to the prospects of negotiation, some members, especially the ASEAN members, have insufficient motivation to negotiate due to the lack of market access benefits. In addition, negotiation in the fields of digital economy, labor, environment, and clean energy are difficult, so it is likely that progress in these areas will be rather small. However, in some less difficult-to-negotiate areas, including trade facilitation, transparency and good regulatory practices, corporate responsibility, supply chains, taxation, and anti-corruption, partial results may be obtained.

If the US government after the Biden administration abandons the IPEF, the IPEF will of course exist in name only, i.e., it will be difficult for the remaining member states to continue to advance. However, in the future, the United States is likely to continue a cooperation model similar to that of the IPEF and will not negotiate an FTA: first, negotiating an FTA is slow; second, the United States believes that traditional FTAs are not beneficial to itself; and third, an FTA would have difficulty winning Congressional support.

IPEF's influence on China will be mainly reflected by exclusionary competition in strategic industries. The IPEF's establishment means that the United States has established economic cooperation frameworks in the three major value chain regions of North America, the EU, and East Asia, forming a closed-loop cooperation framework in which the United States dominates strategic industrial value chains. The United States-Mexico-Canada Agreement (USMCA) in North America has been solid, and the US-EU Trade and Technology Council has been making substantial progress. The US-EU Trade and Technology Council and IPEF are regional extensions from the technological competition between China and the US in strategic industries. The fields of technological competition include the digital economy, artificial intelligence, new energy, and the semiconductor industry, among others. These are industries of systemic importance, having very large, positive spillover effects on national economies. The US government believes that if it were to rely solely on American companies to participate in the competition, winning that competition would be unlikely, so it is prepared to rely on its own strength and on cooperation with other countries to compete against China. The IPEF's impact on China will mainly depend on the amount of substantive content of cooperation within the network in the area of supply chains.

China has three options for dealing with the United States' exclusion of Chinese supply chains and with Sino-US technological competition: The first would be to establish international rules on supply chains; the second would be to exchange space for time, improve political relations, and strengthen supply chain cooperation; and the third would be self-strengthening in strategic industries. The first option—establishing multilateral international rules on export controls, sanctions, supply chain cooperation, and so on within the supply chain field, and making the United States abide by them—would be a very ideal response. This would test the wisdom of China. The United States has a very low proportion of manufacturing and relies heavily on external supply chains, but if we look around the world, who can say that other countries' supply chains are any more secure than those of the United States? The reason is that the United States has solved the problem of supply chain security through alliances. It can control its allies' supply chains. For China, strengthening political relations with major economies is still necessary and beneficial in the long run, since this will enable us to buy time for innovation at home. In comparison with the United States, China's advantage lies in manufacturing, so we can strengthen cooperation with other countries not only in strategic industries, but also in non-strategic industries. In the context of a deteriorating external environment, we should deeply realize that the most important thing to avoid is making policy mistakes under external pressure. The US-Japan trade friction of the 1980s teaches us the same lesson as we play the economic and trade game with the United States. Strengthening our technological self-reliance would be our surest answer to the United States. This requires the construction of a new national system adapted to the new era, in order to create a favorable environment and policy atmosphere for our businesses, so that they will dare to innovate and be able to innovate on their own.

Translated by Thomas E. Smith