Submission to the RCEP General Review[1]

Differential Effects on Incumbent and Entrant Multinational Firms

The Department of Foreign Affairs and Trade's call for submissions asks about the implementation, operation and impact of the Regional Comprehensive Economic Partnership Agreement (RCEP), as well as potential areas for improvement or expansion. This intentionally brief submission makes one point about evaluating RCEP's effects on multinational production: the response of incumbent multinational firms may be modest even when the agreement materially affects the creation of new multinational operations.

This distinction is particularly relevant to RCEP. The agreement entered into force for Australia on 1 January 2022 and complements and builds upon Australia's existing free trade agreements with the other RCEP countries. Those agreements continue to coexist with RCEP and businesses can choose between them according to factors such as tariff treatment and rules of origin. RCEP adds a common regional framework for accessing preferential tariffs, including regional rules of origin and cumulation, alongside customs and trade-facilitation provisions and commitments relating to investment. An important part of its potential effect is therefore not simply a change in headline tariff rates, but a change in the costs of organising production and trade across member economies.

The distinction between sunk establishment costs and period-by-period costs is especially important here. Not every element of RCEP affects sunk costs: tariffs, shipping costs and some customs or documentation costs affect the continuing profitability of an existing operation. But relative to the pre-existing network of trade agreements, a common regional framework is particularly relevant to costs that arise when a new cross-border production relationship is created. A firm entering a foreign market may need to learn which rules apply, choose suppliers whose inputs qualify for preferential treatment, design the supply chain and establish the necessary customs and compliance systems. These costs are paid disproportionately when the relationship is established and some are effectively sunk. An incumbent multinational has already organised its production network and paid many of these costs under the previous arrangements. Where RCEP produces only modest changes in its ongoing trade costs, the firm may therefore have little reason to abandon or substantially reorganise an existing network.

The persistence of multinational status among publicly listed United States firms illustrates the importance of this distinction. Using Compustat segment information for 1979–2017, a firm classified as multinational is around 97 per cent likely to remain multinational in the following year (Spencer, 2026). In the dynamic models of multinational activity reviewed in the same chapter, persistence of this magnitude implies a very large sunk cost of establishing a foreign operation relative to the period-by-period fixed cost of maintaining it. The figure does not identify the effect of RCEP, but it cautions against using limited adjustment by incumbent multinational firms as evidence that the agreement has had little effect.

The potentially more responsive margin is new multinational activity. A firm establishing its first foreign operation, entering an additional country or creating a new cross-border production relationship has not yet sunk the relevant establishment costs. It can choose its location, suppliers and production structure under the RCEP framework from the outset. RCEP may therefore affect the composition and location of multinational production gradually through new entrants and new operations even if incumbent firms change little in the first years after implementation.

The main evaluation implication is consequently to distinguish entrants from incumbents. The General Review should examine newly established multinational operations and new cross-border production relationships separately from the behaviour of continuing multinational firms. A small response in the existing stock of multinational activity is not by itself evidence that RCEP has been ineffective if firms establishing new operations increasingly organise them around RCEP countries. Conversely, little response on this extensive margin would be more informative about whether the agreement has materially reduced the costs of creating regional production relationships.

The practical recommendation is therefore simple: success should be assessed not only by how much established multinational firms change after RCEP, but also by whether the agreement changes the decisions made when multinational activity is created. That distinction is particularly important for an agreement that overlays an existing network of free trade agreements while providing a common regional framework for trade and investment.

References

Spencer, A. H. (2026), "Firm Dynamics and Multinational Activity", in P. Jha and D. Mitra (eds), *Elgar Encyclopedia of International Trade*, Edward Elgar, 58–63. doi:10.4337/9781035327508.00018.

[1]J.Prof. Dr. Adam Hal Spencer, University of Bonn, CESifo & Australian National University (ANU)–Centre for Applied Macroeconomic Research (CAMA). This submission reflects my own **personal** views and not necessarily those of any institution.