

AJISS-Commentary

The Association of Japanese Institutes of Strategic Studies

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Peace Institute

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The Japan Institute of
International Affairs
(Secretariat)

RIPS

Research Institute for
Peace and Security

No. 299

6 October 2022

BUILDING RESILIENT SUPPLY CHAINS THROUGH IPEF: THE POSSIBILITIES AND CHALLENGES

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- The IPEF's intergovernmental crisis response mechanism proposed in the ministerial statement can significantly strengthen the region's supply chain resilience if adequately designed.
- On the other hand, the IPEF's mechanism is not a panacea. There may be cases where the adverse effects of supply chain disruptions cannot be mitigated.
- Moreover, it may take a considerable amount of time or be challenging to create China-free supply chains for some critical goods. Attempting to contain China through the IPEF aggressively is not constructive, even from the perspective of economic security.

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As the world experienced shortages and price spikes in critical goods such as semiconductors, medical supplies, energy and food due to increased US-China strategic competition, the outbreak of the novel coronavirus and Russia's invasion of Ukraine, the credibility of the existing global supply chains, which had been built with a priority on economic efficiency, was significantly undermined. Furthermore, increased attempts to put diplomatic pressure on other countries through economic coercion have forced governments to recognize the risks of over-dependence on a particular country, especially an unfriendly country, for critical goods.

Amidst this backdrop, ministers from 14 countries in the Indo-Pacific region gathered in Los Angeles on September 9, 2022 to declare the launch of negotiations for the Indo-Pacific Economic Framework for Prosperity (IPEF). The IPEF is an attempt by the US, which withdrew from the Trans-Pacific Partnership (TPP) in 2017, to reassert economic engagement in the region while keeping China in check. In addition to Japan and the US, the 14 members include Australia, Fiji, India, New Zealand, South Korea, and seven ASEAN countries, excluding Cambodia, Laos, and Myanmar.

The IPEF consists of four pillars: trade, supply chains, clean economy, and fair economy. The supply chain pillar, which aims to build resilient supply chains among like-minded countries, is of particular interest to the members, and all 14 countries have pledged to participate in negotiations on this pillar.

What's in the ministerial statement on the supply chain pillar?

In what way do the members intend to build resilient regional supply chains? We can deduce some of the directions they are taking from the text of the IPEF ministerial statement, which outlines the future course of the negotiations.

The most noteworthy feature of the IPEF is establishing an intergovernmental crisis response mechanism. This attempts to mitigate the impact of external shocks that could disrupt supply chains by facilitating timely information-sharing among members and the smooth movement of critical goods among them.

In the long run, the IPEF tries to strengthen industrial competitiveness in critical sectors, promote and support investments to improve infrastructure and logistics, and boost technical cooperation and capacity building to diversify suppliers in order to overcome the vulnerabilities of the region's supply chains.

One piece of good news is the commitment expressed in the ministerial statement to ensure the consistency of the IPEF with WTO rules, as "a rules-based economic order" that disregards WTO rules will not win the understanding or support of

non-member countries. On the other hand, as discussed below, there may be cases where it is difficult to build an effective (but exclusive) crisis response mechanism in the region while at the same time ensuring WTO consistency.

Another positive element the ministerial statement clearly states is that, in building a resilient and transparent supply chain, careful attention will be given to avoiding imposing unnecessary regulatory costs on micro-, small and medium-sized enterprises (MSMEs). If the costs faced by the private sector rise excessively as a price of building resilient supply chains, MSMEs will be forced to leave the supply chains and the dynamism of the supply chains in the region will be lost.

What's NOT in the ministerial statement?

What elements are missing in the ministerial statement on the supply chain pillar? First, it does not contain any remarks evoking aggressive measures against China. Judging from the ministerial statement, it is unlikely that IPEF members will introduce mechanisms to, for example, restrict imports of goods manufactured with forced labor or to collectively retaliate against those who attempt to weaponize their economic power. This is an inevitable consequence given the reality that, contrary to US expectations, many ASEAN countries do not want to be part of either the US or Chinese camp.

Second, no commitments were made regarding trade liberalization either in the supply chain or trade pillars. If intra-regional trade can be expanded through tariff reductions, this may help members reduce their economic dependence on China and diversify their suppliers. However, as anticipated, a commitment to initiate negotiations on trade liberalization was not made mainly due to political reasons within the US. Still, the supply chain pillar emphasizes the importance of promoting and supporting regional investment. If this leads to an expansion of investment in emerging members, such as some ASEAN countries and India, the long-run economic gains may outweigh those of tariff reductions.

Finally, while US Trade Representative Katherine Tai once suggested that a mechanism to ensure enforcement of the IPEF was needed, no commitment appears to have been made to negotiate provisions regarding penalties and dispute settlement procedures.

Effectiveness of the IPEF's crisis response mechanism

How well would the intergovernmental coordination mechanisms in the IPEF function in the event of supply chain disruptions due to unexpected external shocks such as pandemics, natural disasters, or outbreaks of war? Three scenarios are discussed below.

First, consider a situation where only one member faces a shortage of critical goods due to a natural disaster or economic coercion by an unfriendly country. In this scenario, the impact of the disruption could likely be mitigated, to some extent, by the IPEF's crisis response mechanism. If some IPEF members are producing or stockpiling sufficient amounts of the critical goods concerned, it would not be politically difficult for them to provide emergency assistance to the country facing shortages.

Second, consider a case in which all IPEF members, including producing and stockpiling members, face a shortage of critical goods, as in the case of a lack of personal protective equipment (PPE) during a pandemic. In such a global supply chain disruption scenario, the IPEF coordination mechanism may not function adequately. This is because it would not be easy to create political incentives for producing or stockpiling members to provide critical goods to other members on an emergency basis when they themselves are experiencing shortages.

Finally, how about the case where there is a global shortage of critical goods while an IPEF member (X) producing the goods has sufficient stocks of them at home? Suppose a non-member country (Z) offers to buy the goods at a higher price than any other country. Would X still prioritize exporting them to another IPEF member (Y)? If the market mechanism is functioning, X will likely provide the goods to Z, which is willing to pay more than any other country. Would it be possible, then, for the government of X to force its private sector to export the critical goods to IPEF member Y instead of Z?


It would not be politically feasible for every IPEF member to adopt such a system, as this would substantially restrict economic freedom. Moreover, to maintain the principle of prioritizing exports to IPEF members in the event of global shortages, exports to non-members would have to be restricted somehow. However, given that the IPEF will not be a regional trade agreement under GATT Article 24, any attempt to create rules that restrict exports to non-members in a discriminatory manner would pose a risk of being challenged in terms of WTO consistency.

Policy implications

The importance of reducing economic dependence on specific countries and strengthening supply chains for critical goods has undoubtedly increased. The IPEF's crisis response mechanism may significantly contribute toward achieving these goals. However, as discussed in the previous section, we should avoid expecting the process to be a “cure-all” remedy that works for every circumstance.

Ultimately, the IPEF's investment and technical assistance schemes may improve the capacity to supply critical goods in the region, diversify suppliers or develop alternative materials. However, it may take a considerable amount of time to create China-free supply chains for some critical goods through the IPEF. Furthermore, there may be some materials for which it is unrealistic to exclude China from supply chains even in the long run.

If these hypotheses are correct, attempting to contain China through the IPEF aggressively is not constructive, even from the perspective of economic security. It can risk costly retaliation by China before China-free supply chains have been put in place. Furthermore, the private sector would not appreciate further geopolitical confusion and decoupling of the global economy.

Granted that these considerations are woven into its design, the IPEF can better contribute to strengthening the region's supply chain resilience and ensuring the economic prosperity of its members. 

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