

# The strategic policy of Japan by referring to the regional cooperation in East Asia

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## Abstract

For a number of years, Japanese people have followed media reports and coverage pertaining to the global economic crisis with considerable trepidation and anxiety.

How do opinions on the subject diverge? What are the key points of this issue? This problem has manifested not only as a Japanese concern but a matter of Japan's role in the future economy of the Asian and Pacific regions, as well as the world. These days international market strategies including TPP have been advocated. How should future economic partnership be forged? What problems are extant and compounding today? And how should strategies be employed to remedy these concerns? The crux of these problems will be discussed and considered in this paper.

## I. Economic trends in recent years in China

In this chapter, economic trends with respect to China since 2000 will be discussed. China has continued its high growth of 10% per annum since 2000 even in spite of the economic downturn in Western countries precipitated by the Lehman Brothers bankruptcy in 2008. In 2010, China has jumped to the position of being the world's second largest GDP, recently overtaking Japan.

China consists of municipalities, provinces and 31 autonomous regions, but notable large-scale economy comparable to neighboring developed countries exists in only one province. Guangdong's gross regional production is the largest in China and is broadly comparable to Indonesia's GDP, which is largest in ASEAN.

Furthermore, China accounts for first in exports and second in imports. China's foreign exchange reserves are the largest in the world, becoming about 3 trillion 180 billion dollars at the end of 2011. In addition, holdings of U.S. Treasuries also (about 1 trillion 150 billion dollars) became the first in the world (the second in the world is Japan: about 1 trillion 60 billion U.S. dollars). Thus, China has become increasingly influential in the international community.

## **Overview of the Chinese economy**

In the Chinese economy in 2011, the suppression of inflation was a top priority of economic policy, and monetary tightening policy had been implemented. From the mid-year, exports to Europe began to slow down on account of the European debt crisis. And economic growth had slowed around the coastal areas with a high proportion of export. The actual GDP growth rate was 9.2% in the full year 2011 which saw maintenance of steady growth. However, a gradual slowing of the growth rate can be observed. Looking at the trends in quarterly, the growth rate has declined in five consecutive quarters to the first quarter of 2012.

Considering the demand of items throughout the entire year 2011, the contribution of the external demand will turn to negative (2010: 1.0% to 2011: -0.5%). Conversely, domestic demand has remained strong. The investment slowed down somewhat, but large contribution was maintained (5.6% to 5.0%) and the consumption was also expanded (3.8% to 4.8%). The social consumer goods retail total sum of 2011 was steadily changed. Looking at the different items, food and clothing sales have continued to be strong while motor vehicles and home electric appliances still were sluggish because their purchase subsidies were terminated.

### **Investment:**

Strong growth has continued in the investment of the fixed assets, but has since slowed down a little. Considering each industry, the contribution of infrastructure investment in roads and railways, etc. shrank which was activated owing to the economic stimulus package of 4 trillion Yuan implemented in 2009. In particular, the railway investment rapidly decreased after a high-speed rail accident occurred in Zhejiang Province in July 2011. On the other hand, contributions in the manufacturing investment continue to expand. Real estate investment is also strong leading to soaring house prices, as a result, creating a social problem called a housing bubble.

In the external demand side, the trade in 2011 has expanded both in import and export and a surplus of trade balance has continued. However, considering the trends in export growth in every month since mid-2011 under the influence of the European debt crisis, exports have been slowing down mainly to EU. In addition, in proportion to the slowdown in exports, imports have also slowing down since mid-year as well.

In the international balance of payments, China recorded a surplus in the current balance. In addition, high growth rates also attracted continued investment from overseas and capital balance of payments continued their inflow. Furthermore, owing to the market intervention to suppress the rise of the Yuan, the foreign exchange reserve has been increased. However, the current account surplus shrank in 2011, and net inflows of capital account decreased from the previous fiscal year in the third quarter, the fourth quarter was the outflow. Therefore foreign exchange reserves have been in decline.

### **Financial policy and prices:**

The consumer prices fell minus compared to the previous year in 2009, but rose through 2010. The deposit benchmark interest rate was also increased in early 2011, higher than the level of 4% that was the specified

suppression goal. Especially, soaring food prices that promise to impact people's lives.

After the economic downturn precipitated by the Lehman Brothers bankruptcy in 2008 the Renminbi was back in de facto dollar peg. However, China applied the Yuan exchange rate elastically in June 2010, and since then the Yuan has been rising slowly while repeating a slight up and down against the U.S. dollar. However, along with the slowdown in the Chinese economy, the constant decline of the Yuan rate is also observed recently, and anticipation of unilaterally high rates is beginning to disappear. Under such circumstances, the People's Bank of China has expanded the fluctuation range of the Renminbi exchange rate per day from 0.5 to 1 percent since April 2012.

With respect to domestic direct investment, domestic direct investment in China increased in 2010 and 2011 after the decline of 2009. Along with the increase in monetary, investment industries and regions have also spread gradually. The large investment focused industry is still a manufacturing industry. However, investment in non-manufacturing sectors such as wholesale and retail and business services, etc., in addition to real estate is expanding recently.

For foreign direct investment, from the early 2000s, the Chinese government has advocated the overseas China's active enterprise. In line with this policy under the government assistance, foreign direct investment has been expanding rapidly. The major investment target industries are leasing and business services. The finance, wholesale and retail trade are positioned at the second investment. In addition, investments are performed through Hong Kong, Virgin Islands, the Cayman Islands, etc. in many cases.

Along with the risks associated with short-term economic trend, China has also faced problems relating to medium to long term growth. China rose to second in the world of total GDP, but it is still at a low level in GDP per capita. A lot of the so-called "Middle-income trap" was indicated in the past. That is, the income levels could not be raised to the further level after the economic developing country has reached to the certain level but the economic growth has stagnated. ("Middle-income trap" has been studied in the joint research by the Development Research Center of the State Council and the World Bank. That is, developing countries can acquire a high increase of productivity by shifting from low-productivity sectors of capital and labor such as agriculture to manufacturing sectors with high productivity in the early stage of development. However, the surplus of a rural farming labor force will be exhausted soon. The labor shift between industries will be stopped and increase in wages will occur, and then the international competitiveness owing to the low wages will be lost. Therefore, it is needed to find new sources of growth by advancing the technological catch-up and increasing the productivity by innovation. As countries that rank in the high-income countries without falling into this trap, Japan, South Korea, Singapore, etc. can be indicated.) For example, there was approximately the same level in the GDP per capita from 1960 to 1980s among Southeast Asian, Korean and Latin American countries. While the rise continues in Singapore and South Korea, GDP per capita in the long Latin American countries are still paused. High interest is held whether China can continue to grow further income level.<sup>(1)</sup>

## II. Japan and TTP

Mexico and Canada successively decided to start participation in the TPP (Trans-Pacific Strategic Economic Partnership Agreement) negotiations. These two countries showed a policy to join the TPP negotiations with our country in November 2011, and received the approval of participation from all 9 TPP negotiations participating countries including the USA and Australia in the 18th and 19th June 2012 respectively. These participations ensure that all member countries of NAFTA (North American Free Trade Agreement, member countries are USA, Canada, and Mexico) will participate in the TPP negotiations. This will further enhance the political and economic value of the framework of TPP.

NAFTA is a huge and mature market of 450 million inhabitants, about 17 trillion dollars GDP. On the other hand, Southeast Asian countries among the TPP negotiations participating countries such as Singapore, Brunei, Malaysia and Vietnam are energetic and emerging growth promises markets to be the center of the world economy in the future. In addition, Australia is a unique presence that is blessed with natural resources. It can be said that the TPP integrates the nature of the framework of huge free trades of "Pacific Rim" more clearly by linking various philosophies including liberalism, compliance with fair rules, openness and transparency. Of course, the TPP also aims to oppose those forces that raise an objection against these new ideas. Ideally, all of the trade rules would be unified under the WTO-GATT system, but it's not a realistic story. From the scale of the TPP, it can be expected to be a presence that can complement and develop the idea of the WTO-GATT system in the rule making on free trade.

However, unfortunately, Japan could not acquire the approval yet and not able to participate in TPP negotiations although Japan announced the policy of participation in the TPP negotiations at the same time as Canada and Mexico announced. The biggest cause of pausing of this matter is a protectionist approach by the agricultural sectors in Japan. Former Ministers of Agriculture, Forestry and Fisheries under the government by the Democratic Party were cautious in TPP. Of course, because decision of the sensitive items is an important agenda in negotiations, protection of some of the domestic industries can be approved. However, there is no help for suspected seriousness of the attitude of Japan even if doubted. In addition, a very inward and insular attitude has been apparent in Japan after the great earthquake disaster, which also a major cause.

It will be a huge loss for Japan itself and, furthermore, for international open trade system if the TPP negotiations participation is not approved readily from the points of the scale of the economies, and because Japan is a trading nation naturally. It is necessary to perform the maximum effort to achieve participation towards the TPP negotiations. To do this, of course, strong political leadership is required. In addition, it is currently pointed out that the Obama administration in the United States has a demonstrable dearth of enthusiasm with regard to the TPP. It is inconsistent with Obama's policy as "Rebalancing to Asia" and it becomes one of the causes of doubts in Asia Pacific Ocean policies by the Obama administration. However, there is a tendency to swing in the direction of protectionism in an election year in the USA. After the election has finished, more biased policy is likely to be reinstated. <sup>(2)</sup>

TPP is a FTA negotiating in nine countries of the Asia Pacific Ocean (U.S.A, Australia, Singapore, New Zealand, Chile, Brunei, Peru, Vietnam and Malaysia). Features include high flexibility level and comprehensive subject areas. The foundation of TPP is P4 that came into effect in 2006. TPP can be said that it is expanded and developed agreements of P4. <sup>(3)</sup>

The ASEAN countries currently participating in the TPP accession negotiations are four; Vietnam, Brunei, Malaysia and Singapore. Because the TPP is a part of the FTA, Japan will conclude an FTA in triplicate. The import tariff on automobiles in Vietnam is currently 70-80%. It is difficult to abolish this tariff immediately at present. In Malaysia, the self-sufficiency rate of rice is 70% and the insufficient part is imported from Thailand. It was therefore unlikely that Malaysia would give up the self-sufficiency of rice completely in 2005 after into the negotiation in TPP. I am a trade liberalization proponent of agricultural products, similar to the other economists. However, it may be necessary to consider protecting agricultural products from outside the economic basis factors in the future.

In the aspect of effects in the FTA conclusion, trade will be expanded between the member nations. Thus, the comparative advantage sector will expand and comparative disadvantage sector such as agriculture in Japan will shrink. After the effectuation of the FTA, economic structure will change and lead to economic growth. It is so-called dynamic effects. FTA is said to be the first stage of economic integration of the 5 stages that were proposed by Béla Balassa (FTA, customs union, common market, economic union, and full economic integration). It can be translated as a first step toward economic integration since the FTA is the TPP. However, no FTA advances to the customs union have occurred recently.

ASEAN has harbored an ambition to form the ASEAN community by 2015. In the background, there is strong economic power of China. Regarding territorial issues in the Spratly Islands, it is also a political challenge for the ASEAN countries because a lot of Chinese live in each country. <sup>(4)</sup>

ASEAN is running as the first runner for the regional integration of East Asia, furthermore, the ASEAN countries consist of the majority in the framework of the cooperation and integration in East Asia. As ASEAN is composed of 10 countries, if the East Asian Community could be formed, the ASEAN countries will certainly form the majority of the community. In other words, the future advancing direction of the East Asian Community will be determined depending on trends in ASEAN. Following the completion of AFTA, ASEAN is planning the creation of the ASEAN Economic Community in 2015. The Economic Community is a composing element of the ASEAN Community along with the political security community and the socio-cultural community. The goals of the ASEAN Economic Community are the realization of "free transfer of goods, services, investment, skilled labor and capital" and cancelation of the disparities within the ASEAN regions.

The ASEAN economic community is not a common market of the EU type. Tariffs are eliminated and FTA is realized. However, a customs union is not established. Therefore, only those that meet the rules of origin can be transferred freely. For service trade, it is to be opened in all areas, but Mode 4 (cross-border service supplier) is not yet specifically determined.

With regard to the movement of people, this is presently limited to skilled workers. With regard to the investment, liberalization has progressed such as approval of the national treatment before and after the investment. The ASEAN Economic Community is "FTA+ (plus)" where the scope of EPA (Economic Partnership Agreement) of Japan, liberalization and facilitation are overlapped, but there is no plan for monetary union.

Although it is still unclear for the embodiment of the contents of the East Asian Community, the Economic Community is an essential factor, and it will serve as the economical foundation. In order to realize the economic community, it is an urgent issue to transfer from FTA, that liberalizes the trade in goods, to the liberalization of services, people and capital. In goods trade, it is essential that tariffs are eliminated, but that further trade facilitations such as simplified customs procedures and mutual recognition of product standards are achieved.

The conclusion of comprehensive East Asia FTA will be a big step towards the realization of the East Asian Economic Community. Currently the four concepts of the East Asia FTA coexist including TPP. The highest possibility among the four concepts is the TPP. For FTA with ASEAN, the United States rather requests to join the TPP than bilateral negotiations. Possibility of proceeding of the participation of the ASEAN countries will be increased. It is inevitable for Japan to consider the joining the participation and will likely do so in an appropriate time. <sup>(5)</sup>

## Conclusion

To conclude, how should Japanese economists take measures in the future to establish clue for the Northeast Asia region where political instability is ever-increasing? From what point of view should we consider this problem? This problem is actualized not only as a one specific to Japan, but is pertinent also to Asia, Asia-Pacific, and the global economic climate. How these problems should be ameliorated has been explored. In addition, how should economical cooperation be aimed at these days when TPP begins and international market opening is demanded? What kind of problems have accumulated in the present condition? What measures should be carried out?

Various cooperation among China, Japan and Korea has been observed. Especially it should be noted in this Summit that Japan attached great importance among three countries and has been taken up among three leaders was the strengthen the importance of cooperation on Maritime Search and Rescue search and rescue in 3 between it is that it has reaffirmed the of strengthening. Because it is an early stage where the maritime search and rescue basic agreement have been agreed among Japan and China just last year, the confirmation and promotion through the Summit of the three countries cooperation will have great significance for three countries.

Although embodiment of the contents of East Asian Community is still ambiguous, an economic community is an indispensable factor and TPP in economical cooperation serves will be the base of the economic community. In order to realize the Economic Community, it is an important subject to progress from FTA which liberalizes trade of goods to liberalization of service, personal and capital. In goods trade, it becomes indispensable to realize trade facilitation not only abolition of tariffs but also such as mutual recognition of product specifications, customs

formalities, etc.

Conclusion of comprehensive East Asia FTA will serve as a big step for realization of the East Asia Economic Community. However, presently four concepts coexist for the East Asia FTA including TPP. The high possibility among the four concepts will be the TPP. The USA is demanding negotiation for ASEAN and FTA to be performed not by two countries but the participation in TPP. Participation to TTP by each country of ASEAN will be progress in high possibility. It is inescapable for Japan to consider the participation in TTP and shall participate at suitable time.

Still, it is ambiguous and difficult to focus, but we would like to close observing how TTP can take any course in the future.

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