

Japanese Trade Policy and 'Economic Partnership Agreements': A New Conventional Wisdom

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Abstract

In the late 1990s, the Japanese conventional wisdom that free trade agreements were incompatible with the GATT/WTO and responsible for undermining non-discrimination was replaced by the view that free trade agreements supplement the GATT/WTO. This shift provided greater policy flexibility for Japan, especially with Southeast Asia. In light of regional economic integration pursued by North America and Europe and the costs of non-participation for Japan evident in the case of Mexico, Japan accepted Singaporean and Mexican offers to negotiate agreements. Subsequent negotiations with the Philippines, Malaysia and Thailand have furthered Japanese bilateralism. Japanese Agricultural policy was accommodated but at the cost of precluding 'comprehensive' agreements with developed countries. However, the new conventional wisdom offers a possible accommodation with North American and Europe regionalism within the GATT/WTO system.

The enemy of the conventional wisdom is not ideas but the march of events. ...the conventional wisdom accommodates itself not to the world that it is meant to interpret but to the audience's view of the world. Since the latter remains with the comfortable and the familiar while the world moves on, the conventional wisdom is always in danger of obsolescence. This is not immediately fatal. The fatal blow to the conventional wisdom comes when the conventional ideas fail signally to deal with some contingency to which obsolescence has made them palpably inapplicable. This, sooner or later, must be the fate of ideas which have lost their relation to the world.

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Introduction

The 'march of events' rendered a 'fatal blow' to the conventional wisdom in Japan on the employment of free trade agreements by the end of the 1990s. Japanese conventional wisdom was ill-tuned to the realities of a world where regional and bilateral agreements had become permanent features of the multilateral trading system embodied in the rules of the World Trade Organization (WTO). The cost of non-participation and the opportunities of using trade agreements to pursue trade, investment and aid objectives outweighed the potential discriminatory effects. The conventional wisdom that was overturned had however been resilient, dating back to Japan's accession to the General Agreement on Tariffs and Trade (GATT) in 1955. Throughout this period, Japan rejected bilateral or regional agreements in favor of non-discriminatory economic cooperation, a view culminating in the creation of the Asia Pacific Economic Cooperation (APEC) forum in 1989 and its 'open', non-discriminatory liberalization proposal. Economic cooperation embodied in APEC was the limit for the old conventional wisdom - regionalism more sophisticated than APEC would have been unacceptable for Japan.

Japan's conventional wisdom changed due to a shift in strategic, economic and historical factors. The shift coincided with a growing ease within Japan to pursue regionalism with Southeast and East Asia to a degree not possible in the past, due to the specter of the Greater East Asian Co-Prosperity Sphere. In addition, the shift reflected elements of a new approach to Southeast Asian trade, investment and aid relations in light of growing competitiveness in the region. The new policy also hints at a future accommodation of 'East Asian' regionalism within the WTO in light of the trend towards regionalism elsewhere.

The temptation at this point might be to argue that Japan's new policy undermines faithfulness to the WTO because trade agreements are discriminatory and Japan is reluctant to open its rice market beyond Uruguay Round commitments. This view ignores the accommodation of agricultural protection within the North American Free Trade Agreement (NAFTA) and the European Union (EU). In addition, this view fails to acknowledge the ambiguity of the effects of trade agreements in the mainstream economics literature. The voluminous research on regionalism has failed to produce a clear, definitive answer on whether such agreements are detrimental to world trade (Milner and Mansfield, 1999: 594; Hine, 1994: 266; Wei and Frankel, 1997: 135; Krugman, 1994: 176, Bergsten, 1997: 87). Indeed, economic analysis supporting free trade

agreements is now used to justify Japan's new conventional wisdom (MITI, 1999; MITI: 2000). Furthermore, consistent with North America and Europe, Japan's free trade agreement program sits alongside a commitment to the Doha Development Round (and non-discriminatory liberalization) the Generalized System of Preferences (GSP) for developing countries, and Overseas Development Assistance (ODA). This Japanese accommodation of free trade agreements is the genesis of the third major alignment between multilateral and regional trade policy in the GATT/WTO system, the previous alignments involving Europe and North America.

European Regionalism and the GATT

Trade agreements predated the conclusion of the Second World War and the GATT system of non-discrimination. The United Kingdom had an Imperial Preference Scheme. The United States, in order to reduce its industrial tariffs negotiated thirty two bilateral trade agreements between 1934 and 1945 (Destler, 1995: 12). Japan had ambitions for East Asia, yet its sphere of regional 'co-prosperity' remained unrealized due to defeat. The conclusion of war ushered in a new trade policy framework devised principally by the United States (Gardner, 1969) ostensibly to encourage freer trade on an innovative, non-discriminatory basis, a vision that was marred in two respects. The British were strongly opposed to the elimination of Imperial Preferences and negotiations between the UK and the US failed to bring about abolition (Gardner, 1969: 356-359). More seriously, the original US vision for the post-war world was for an institution of trade to sit alongside the International Monetary Fund (IMF) and the Bank for Reconstruction and Development (World Bank). The International Trade Organization (ITO) was an ambitious multilateral treaty, but drenched with compromises was eventually rejected by the original sponsor – the US (Ostry, 1997: 67).

Most Articles on the construction and operation of customs unions and free trade areas included in the ITO were not included in the GATT except what would become Article 24 which is the legal accommodation of customs unions, free-trade areas or interim agreements. The negotiators for the "ITO (and therefore the GATT) did not see any tension between regional groupings and multilateral exchange" (Marceau, 1994: 173). Historically, non-discrimination in trade policy was a GATT creation as the GATT "did not codify an existing international custom of non-discrimination" (Marceau, 1994: 179). Indeed, trade

negotiators in this period agreed “the MFN clause was not of a customary nature” (Sauvignon quoted in Marceau, 1994: 179). Contracting Parties to the GATT believed they had a right “to form regional arrangements and their subsequent practice confirms that they consider Article XXIV of the GATT as providing guidelines for such successful arrangements” (Marceau, 1994: 180).

The decision to include Article 24 in the GATT was fortuitous in light of the realities of post-war Europe. In April 1948, the Organization for European Economic Cooperation (OEEC) was established to oversee European recovery and reconstruction and in particular administer the US Marshall Plan. The OEEC also had the objective of promoting European trade by tariff reduction and consideration of the possibility of a European free trade area or customs union. Under US pressure, sixty percent of intra-European private trade was liberalized and eighty four percent was liberalized by 1954, covering food, raw materials and manufacturing. In 1950, the OEEC proposed a European Common Market, but by 1952, with the end of the Marshall Plan, fell victim to Cold War security and was eventually restructured to become the Organization for Economic Cooperation and Development (OECD). The last major achievement of the OEEC was the negotiation of the European Free Trade Agreement (EFTA) (OECD, 2000). The formation of the European Coal and Steel Communities, the Treaty of Rome and the European Economic Community (EEC) all featured in the 1950s.

GATT law on regional integration is a departure from Article 1 on non-discriminatory trade liberalization for the purpose of intra-regional liberalization. Three forms are permitted: a customs union, free trade area and interim free trade area (Article 24.5). Participants are not prohibited from raising tariffs, provided compensation is paid (Article 24.6, Article 28). The purpose is to increase “freedom of trade by the development, through voluntary agreements, of closer integration between the economies of the countries party to such agreements...(and)... to facilitate trade between the constituent territories and not to raise trade barriers to the trade of other contracting parties with such territories”. The remaining trade barriers “shall not on the whole be higher or more restrictive than the general incidence of the duties and regulations of commerce” before the establishment of the agreement. In addition, “substantially” all trade should be free between the members. Article 24 is mild on discrimination compared with other GATT articles. Trade discrimination and various legal but subtle derogations from Article 1 have dominated post-war GATT trade policy. For example, Waivers, countervailing duties, antidumping, voluntary export restraints (VER), quarantine regulations and product standards all feature in the

GATT/WTO system (see Krueger, 1995).

The WTO and the March of Events

Until 1998, Japan rejected free trade agreements (Yamamoto and Kikuchi, 1998: 192). The official conventional wisdom was that free trade agreements possessed adverse effects for non-members and these effects needed to be 'reined in' abroad through forums such as APEC or GATT/WTO. This policy suited Japan's agricultural policy which was to resist liberalization beyond GATT negotiations which would involve a considerable period of time to finalize. At the same time, Japanese companies investing overseas were to be protected and assisted by overseas development assistance (ODA) - an acceptable departure from non-discrimination.

There were several reasons for the Japanese position. Japan had for a number of years suffered trade discrimination from GATT contracting parties despite GATT membership, until the 1960s (Yamamoto and Kikuchi, 1998: 209 footnote 2; Asakura and Matsumura cited by Ogita, 2002: 3). At the establishment of the EEC, the Europeans employed a number of trade barriers that resulted in adversely affecting Japanese exports to Europe (Stewart et al, 1993: 1840). Almost thirty countries at one point used Article 35 of GATT to discriminate against Japan. Later Japan experienced the effects of quantitative restrictions and 'voluntary' export restraints (Kojima, 1977: 32-3). Japan was also aware that trade agreements with Asian neighbours would trigger memory of Japan's wartime aggression and the Greater East Asia Plan (Munakata, cited by Ogita, 2002: 4, Funabashi, 1995: 187).

The Uruguay Round (1986-1994) therefore afforded Japan with a unique opportunity to push for reform of Article 24. Japan argued that Article 24 did not legitimise adverse effects accruing to non-members of the regional grouping (Japan, quoted in Stewart et al, 1993: 1841). Such agreements had potential adverse effects on non-participants such as threatening export markets in both North America and Europe (Preeg, 1998: 82; Croome, 1995: 99). In addition, intra-regional free trade among members of a FTA could lead to a reduction in trade with non-members (Stewart, 1993: 1839; Croome, 1995: 99). Japan proposed the creation of a mechanism where the adverse effects accruing to non-members such as market access could be compensated (Japan, quoted in Stewart et al, 1993: 1844, footnote 132). Japan also insisted that members to an FTA extend a portion of the liberalisation to non-members and that interim agreements have a

definite time-limit (Croome, 1995: 100, 219).

In part to bolster its position in the GATT, Japan was also sponsoring its own version of regionalism in APEC that it did not feel inconsistent with its stand on Article 24. APEC permitted grand visions but difficult decisions could be postponed either until a new trade round or the distant target of 2020. The weaknesses of APEC did not prevent frequent exaggeration by Japanese leaders. Japan announced in 1995 that trade discrimination was obsolete (Murayama, 1995a, 1995b) and that the voluntary (and yet untested) APEC liberalisation strategy was an alternative to the GATT/WTO method of negotiation (Hashimoto, 1995, Kono, 1995). Since the heart of GATT/WTO cooperation is the negotiation of trade barriers by the principle of reciprocity this comparison made little practical sense. APEC was also said to be 'open regional cooperation' and non-discriminatory, "complementing and strengthening" the GATT/WTO (Kono, 1995a, 1995b). Ironically, the term 'complement' is now used in Japan to describe the relationship between free trade (discriminatory) agreements and the WTO. At the time Japan believed that some regional agreements "have raised barriers to trade with non-member countries, and that they have effectively weakened the free, non-discriminatory, and open multilateral system formed under the WTO" (Japan, 2000: 10). Japan was adamant that free trade agreements could minimize their negative impact on non-members by being open "so as to supplement and reinforce the...WTO and contribute to the further liberalization and stimulation of world trade" (Japan, 1995). Since such agreements would divert focus from WTO liberalization, APEC was essential to ensure liberalization that would benefit non-members (MITI, 1998).

Japan's protest in the GATT and its model of open regionalism in APEC was largely rejected. Regionalism was reaffirmed in the 1994 "Understanding on the Interpretation of Article 24 of the GATT", imposing stricter guidelines for completion of an agreement to ten years. Preferential rules similar to Article 24 of GATT were also applied in the General Agreement on Trade in Services (GATS). The General Council of the WTO in 1996 established a research committee on Regional Trade Agreements. Just as Article 24 and GATT was written amid the pragmatic realities of the need to reconstruct Europe on the basis of a common market, the World Trade Organization was created amid the pragmatic realities of building a regional market in North America, the completion of the European Single Market and the formation of the ASEAN Free Trade Area (AFTA). Uruguay Round negotiators felt that little needed changing in the rules of Article 24.

There were obvious reasons in favor of the status quo – the world trading system had encouraged underlying dynamics that settled in favor of regionalism. First, trade agreements could benefit from legal status and the discriminatory effects would provide stimulus for GATT negotiations. Regionalism could 'stimulate' the world trading system and the GATT could 'discipline' regionalism through Article 24 (Marceau, 1994:172). The creation of the EEC in part motivated the US to support the Dillon Round (MITI, 1999). Furthermore, the negotiating modalities employed in the 'Kennedy Round' were forged in the pragmatic US concession that product-by-product negotiations would not work against the common European external tariff (MITI, 1999). The growth of the EEC to include Ireland, the UK and Denmark in 1973 preceded the Tokyo Round (Marceau, 1994: 172). The Uruguay Round was concluded following the creation of the European Single Market, the North American Free Trade Agreement and the ASEAN Free Trade Area (AFTA).

Secondly, crises in the GATT have stimulated the growth of regionalism. The failure of the 1982 GATT Ministerial contributed to the 1984 agreement between Australia and New Zealand. It was also an important motivation in the negotiation of the 1988 Canada-United States agreement (Krueger, 1995; Preeg, 1998: 48). The difficulties in the Uruguay Round were instrumental in the establishment of the Asia Pacific Economic Cooperation Forum (APEC) in 1989 and influenced North American and European regional negotiations. The failure of the 1990 GATT Ministerial during the Uruguay Round helped to encourage a shift to regional agreements such as the EU which in turn helped to prompt ASEAN and AFTA (Hatekeyama, 2002a). The collapse of the 1999 Seattle Ministerial was influential in stimulating the proliferation of bilateral agreements among APEC members such as Singapore, New Zealand, Japan and Chile. At the conclusion of the failed Cancun WTO Ministerial, the METI Vice Minister for International Affairs Tadakatsu Sano remarked 'Japan will now shift a major portion of its focus to FTAs' (JETRO, 2004).

Thirdly, trade agreements are a laboratory or test-bed for new ideas, innovations and approaches that are applied and adopted in the WTO (OECD, 1995; WTO, 1995; APEC Economic Committee: 1997; Lawrence, 1997: 24-5). Regional pacts have contained provisions that were promoted in GATT negotiations and subsequently adopted as part of the 1994 WTO Agreements. For example, the Australia-New Zealand, NAFTA and EU Chapters on trade in services (Bergsten, 1997; 86; footnote 6; Marceau, 1994: 172) and the US-Canada bilateral pact on dispute settlement (Marceau, 1994: 172).

Fourthly, regionalism also begets regionalism. Since the formation of the Single European Market, many countries on the edge of 'the EU' have sought membership. Regional pacts have stimulated regionalism elsewhere by countries concerned about preventing a loss of their bargaining position, markets and competitive position (Mansfield, 1998: 524, 527; Lloyd, 2002; Perroni and Whalley, 1996: 57). The European Single Market influenced creation of NAFTA and NAFTA helped to influence arrangements in the Asia Pacific (Mansfield, 1998: 527). The creation of Europe in the late 1950s inspired Kiyoshi Kojima's Pacific Free Trade Area (PAFTA) in the 1960s which in turn stimulated discussions on Pacific regionalism.

Fifthly, regionalism privileges and intensifies relationships with other countries, usually neighbouring countries. Filters for regionalism could be culture, history, language, economics or politics. European regionalism for example originally involved the joining of Western European countries with a common history and experience (the devastation of war), similar culture and religion, and antipathy for Eastern European communism. ASEAN established AFTA as a 'defensive measure' to expand the ASEAN market in face of competition from North America, Europe and a growing China (Urata et al, 2005: 10). In recent years, the US has pursued the Free Trade Area of the Americas (FTAA) in part to balance on one hand judicious access to the US market and on the other to bolster institutional respect for human rights, democratic opinion and discredit views antagonistic to the US. This privileging and intensifying can also reduce political tension, insecurities and misunderstanding among neighbouring countries.

Resisting the March of Events

There were proposals for regionalism in earlier years such as the Pacific Free Trade Area (PAFTA) in the 1960s and the Organization for Pacific Trade and Development (OPTAD) in the 1970s. The Economic and Social Council for the Asia Pacific (ESCAP) oversaw the negotiation of the Bangkok Agreement in 1975 a preferential agreement involving Sri Lanka, Bangladesh, China, India, Laos and Korea. Japan also played a crucial role in the formation of the Pacific Trade and Development Conference (PAFTAD) as well as the Pacific Economic Cooperation Council (PECC). Another grouping, the Asia Pacific Council (ASPAC), began in 1966 with Japan, South Korea, Australia, New Zealand, Thailand, South Vietnam, the Philippines, Taiwan and Malaysia but collapsed in

1975 due to the admission of China, and controversy over Taiwan.

However, it was the Japanese/Australian proposal of the Asia Pacific Economic Cooperation (APEC) forum around which considerable official enthusiasm coalesced from 1989 until the mid-1990s. APEC was to include the United States, Canada, Mexico and Chile alongside East and Southeast Asian nations, Australia, New Zealand and Papua New Guinea and later China. It was an 'Asia Pacific' grouping. For example the Pacific Trade and Development Conference (PAFTAD), the Pacific Basin Economic Council (PBEC) and the Pacific Economic Cooperation Council (PECC) all stressed 'Pacific' rather than 'Asia Pacific'.

US involvement in APEC was vital for Japan. While Japan in 1988 discussed a free trade agreement with the US, it decided in favor of US engagement "a strategic move to prevent the US from disengaging with Asia, and entrenching itself in the Western Hemisphere" (Funabashi, 1995: 201-2). As Funabashi writes "Perhaps there was no other viable alternative to regionalism for Japan to counteract and prevent the potential balkanization of the world trading system and exclusive blocs precipitated by the seclusion of Western Europe and the United States in their respective regions. Asia Pacific regionalism was the best insurance policy against the emergence of regional blocs"(Funabashi, 1995: 201). APEC did embrace technical cooperation (loosely 'aid') as well as trade facilitation (customs procedures and standards) and oversaw the proliferation of many bureaucratic networks. Much of this institutional fabric still exists, though it was overshadowed by the focus on trade liberalization. An alternative 'East Asian' proposal was Malaysia's 1990 East Asian Economic Group (EAEG) proposal devised to restrain the influence of APEC and the United States and Australia (McKay, 2005: 1). Under US pressure, Malaysia revised the EAEG to become the East Asian Economic Caucus, subordinate to APEC (Funabashi, 1995: 68-9). Malaysia's 1995 suggestion of an ASEAN Economic Ministers Meeting plus Korea Japan and China received the same reception from Japan (Funabashi, 1995: 207).

The APEC/EAEC was a side-show to the real rift which was the Uruguay Round of trade negotiations, commenced in 1986. The 1990 GATT Ministerial was a disaster and therefore APEC until 1994 was overshadowed by the profound complexity and difficulties in expanding trade rules to agriculture and services in GATT. APEC is said to have played a role in the final deal with the US threatening to form an APEC pact if GATT failed (Bergsten, 1994: 218). APEC also boldly declared free trade and investment by 2020 in 1994, but ironically failed to properly oversee the negotiation of a minor and entirely unnecessary

liberalization proposal (1997-8) with Japan's policy on fish and forest products widely viewed as the chief stumbling block.

APEC laid the foundations for East Asian regionalism in two ways. First, because Japan's fish/forest position is said to have undermined the 1997/1998 initiative, it could hardly appeal to further application of 'open regionalism' without having to revisit the issue of fish and forest products. Second, since APEC appeared to offer a different regional method – open regionalism – and appealed to GATT consistency, APEC members could not oppose regional arrangements that were in fact ostensibly themselves GATT consistent. APEC liberalization would be 'not to the detriment of other parties', 'a powerful complement to multilateral trade liberalization', and a "model of open regional cooperation". In the mid-1990s, Japan could defend its agricultural position (WTO-based liberalization) and avoid any substantial trade discussion that might challenge that position through appeals to voluntarism. Given that the Uruguay Round had recently been concluded and Japan was in no mood for further liberalisation, the APEC model based on 'voluntary liberalisation' was seen by Japan as the "the only practical and effective means for advancing liberalization in this diverse region" (Murayama, 1995a, 1995b).

This meant however that Japan could do nothing against sub-regionalism in APEC such as NAFTA, the EU or AFTA. These agreements were also GATT consistent and have contributed to GATT liberalization. Both the US and EU supported multilateral efforts alongside the 'creation of large scale regional frameworks' (MOFA, 2002a). Both the US and the EU continued this policy suggesting that "[t]he current round of WTO negotiations (Doha Development Round) could be the last multilateral trade negotiations prior to the creation of these large-scale regional frameworks" (MOFA, 2002a). In other words US engagement in Asia and US WTO policy was sustainable alongside a vigorous free trade agreement program in North and South America. Elsewhere, a commitment to 'open regionalism' was not inconsistent with participation in a trade agreement. Indonesia and Thailand, strong supporters of 'open regionalism' are members of the ASEAN Free Trade Area (AFTA). During this period Japan admitted that trade agreements brought economic benefits and could "contribute on the whole to an expansion of world trade and to eventually extend their benefits to contracting parties outside the arrangement" (Japan, quoted in Stewart et al, 1993: 1839, 1841).

While "open regionalism' (was) a failure as a strategy to counter the effects of the formation of more and more RTAs (regional trade agreements)" (Lloyd, 2002:

6), APEC continues to tackle economic, political and security issues. However, APEC has become impotent as a vehicle to restrain regionalism in the Asia Pacific. The rise of 'East Asian' arrangements are rearranging the 'Asia Pacific'. It is too early to say whether APEC is an idea whose time has come and gone. However, an Asia Pacific without East Asian 'sub-regionalism' is increasingly unlikely.

Japan's fish and forest products policy in APEC however was itself overshadowed by the fallout of the 1997 Asian Financial Crisis. Due to ill-feeling towards the US and the IMF there was a revival of interest in 'East Asian' cooperation. Japan's Asian Monetary Fund (AMF) proposal was firmly rebuffed by the United States and the International Monetary Fund (IMF). However, the behavior of the IMF created frustration and disappointment with 'western' engagement in East Asia so instead of being a mechanism to bring stability "the crisis appears to have presented the IMF with the opportunity to force open East Asian economies" (Higgott, quoted in McKay, 2005: 2).

Due to the Asian financial crisis, the ASEAN+3 meeting began in 1997 (McKay, 2005: 1). The perception of crisis-induced 'economic diplomatic isolation' was crucial in informing this interest in 'East Asian' free trade agreements (Drysdale and Xu, 2004: 14). The 1998 ASEAN+ 3 summit established the "East Asia Vision Group" (EAVG). EAVG in 2001 proposed the creation of an East Asia FTA, a proposal to date that has not been adopted (Urata, 2004, 1). The ASEAN+3 meeting in 2000 discussed the idea of an East Asian free trade and investment agreement (Soesastro, 2001: 2). By December 2001, China had successfully acceded to the WTO, followed by Taiwan in January 2002. In November 2001, China and ASEAN agreed to proceed with the negotiation of a free trade agreement. Like Japan, China views free trade agreements as instruments to advance its trade and investment policy within the region.

Did Japan simply follow China to support free trade agreements? One view sees Japan's promotion of 'East Asian' regionalism as a reaction to China's ability to more swiftly construct mutually satisfactory arrangements with ASEAN, notably the ASEAN-China FTA (Drysdale and Xu, 2004: 15-16). Following the Chinese-ASEAN FTA move in November 2002 Japan proposed a broader more ambitious agreement to cover Australia, New Zealand, Southeast Asia, but instead has continued to pursue negotiations on a bilateral basis. In part to allay fears from ASEAN, China proposed the ASEAN-China FTA with a pledge for prior tariff commitments ahead across a range of commodities (Yun, 2002). The agricultural commitment to ASEAN was well received (Miyazaki, 2004) as was

the anticipation for greater export opportunities available to ASEAN in the Chinese market (Urata et al, 2005: 11).

In 1999 the US proposed the Pacific 5 grouping an agreement to be between the US, Singapore, Australia, New Zealand and Chile (Barshefsky, 2000, DFAT, 2000). At the time Chile, Singapore, New Zealand, South Korea and Mexico were at the forefront of proposing various bilateral trade agreements (Groser, 1999: 12-13) capturing the APEC liberalization goals by claiming the FTA method as a more efficient way to hasten realization. The 'Pacific 5' group originated with the prior President Bush to link Asia with North America" (Matsukata, 2005: 1). This proposal faded away but the United States concluded free trade agreements with Australia and Singapore and launched an initiative with ASEAN. Recently, the US seems focused on solidifying the Free Trade Area of the America's (FTAA) due to the passage of the Central American and Dominican Republic Free Trade Agreement (CAFTA). While the US continues to register protest against the concept of an East Asian Community, the role of Australia and New Zealand in the region (due to Japanese and perhaps conditional ASEAN support) may temper East Asian regional identity. However, former deputy secretary of State Richard Armitage has claimed that the present Bush Administration is losing influence in Asia to China, indicated by the decision not to include the US in the December 2005 East Asian Summit (Hartcher and Banham, 2005).

Contingencies and Obsolescence (1998-1999)

With the immediate context of the Asian financial crisis in 1997 and the fragmentation of APEC, Japan in 1998 began its reevaluation of trade agreements (Kojima, 2001). Mexico a member of NAFTA and recent beneficiary of an interim free trade agreement with the EU in 1997 would provide the catalyst for change. Mexico and Chile both withdrew from the APEC liberalization program in 1997 but are keen supporters of bilateral agreements. In August 1998, Mexico officials discussed an agreement with Japan (through JETRO). Japan argued that a Mexico-Japan agreement would contradict Japan's stance in both APEC and WTO. The Ministry of International Trade and Industry (MITI) argued that adopting an FTA would radically alter Japanese policy so an FTA-study team was created in MITI's International Trade Policy Bureau (Hatekeyama, 2002a). The influential report concluded Japan should pursue the FTA alongside WTO efforts (Hatekeyama, 2002, Munakata, cited in Ogita, 2002: 4). Japan feared isolation in a world where most had free trade agreements (Hatakeyama, 2002b). In November

1998 the Mexicans formally proposed a FTA with Japan (METI, 2001: 235).

At the same time, the business association Keidanren argued that a free trade agreement with Mexico would prevent discrimination against Japanese companies investing in Mexico due to their country's non-participation in an FTA (Keidanren, 2000: 18). Due to NAFTA and the EU-Mexico trade agreement, EU and US goods could be exported to Mexico at lower tariff rates than exports from Japan (Hatekeyama, 2002b; Urata, 2001; Yun, 2002). Other countries face similar problems. Chile has argued that free trade agreements are vital to 'reduce the external vulnerability of the economy' (Chile, 2003). One trade policy objective of Switzerland "is to ensure that the conditions of access to foreign markets for its exporters are equivalent to those for their competitors. Often, the only possible way of eliminating discrimination against Swiss exports – which is the result of preferential agreements concluded with third countries – is to sign free trade agreements" (Switzerland, 2004).

Importantly for Japan, an FTA with Mexico would not require the liberalization of agriculture as the EU-Mexico interim-free trade agreement in 1997 agreed substantially less in terms of commitments on agriculture (Urata, 2001, Europe-Mexico FTA, 1997). While MITI was surprised that this 'fake FTA' was possible, the Mexican model offered the precedent to justify the exemption of comprehensive agricultural liberalization. Keidanren also argued Japan could "follow the examples set by ...other agreements and exempt certain products from the agreement or establish a longer liberalisation timetable for them, until the results of WTO negotiations concerning the liberalisation of agricultural products are known" (Keidanren, 2000) The view that Japan's rice policy is the 'Achilles Heel' in the FTA program (Japan Times Editorial, November 22, 2002) is unsustainable given the variety of options for agricultural management available in the context of a free trade agreement.

The Mexican negotiation however, demonstrated the potential difficulties with such agreements both in terms of sensitive items and bargaining strategy. Negotiations eventually centred around the sensitive and unresolved issues of oranges, pork, beef, chicken and oranges, steel, automobiles and leather (The Japan Times, February 25, 2004). The negotiations with Mexico met with a crisis in October 2003 concerning pork and orange imports. On the last day of talks Mexico changed its request vis-à-vis orange exports to Japan. While Mexico accepted Japan's proposal for a tariff-free quota on orange juice, Mexico surprised Japan by demanding for a greater volume (The Japan Times, Oct 17, 2003). Japan made concessions such as the removal of tariffs on 300 items,

excluding pork, in opposition to Mexico's demand for 485 products (The Japan Times, August 28 2003).

The final value of the agricultural concessions was contested. A senior negotiator at the Trade Policy Bureau in METI stated "What is most important is that for the first time, Japan was able to free so many farm and industrial products" (The Japan Times, February 25, 2004). However concessions are not sufficient evidence of a shift in thinking on Japanese agriculture. Indeed, prior to the Mexican treaty, Japanese agricultural policy in the Singapore-Japan negotiations was greatly influenced by the decision of the Liberal Democratic Party's Research Commission on Trade in Agriculture, Forestry and Fishery Products on 3rd September 2001. This stated "a) Japan must be careful not to have negative impacts on domestic agricultural, forestry and fishery industries; b) as a specific issue, tariffs on agricultural, forestry, and fishery products are not to be further curtailed or revoked under the two-country agreement, because this subject has to be discussed in the WTO; c) similar bilateral agreements which will be negotiated in the future are to be dealt with under the same policy" (Kagami, quoted in Soesastro, 2003).

The Singapore 'partnership' discussion began in October 1998, when Japan had discussions with Singapore on the FTA issue (Kojima, 2001). Before the late Keizo Obuchi and Goh Chok Tong met in December 1999, the latter promoted the idea of a 'New Age FTA' to both JETRO and Keidanren (Allison, 2001). Singapore was a developed country, and eager for agreements (Ogita, 2002: 11). Singapore is also the headquarters for many Japanese companies operating in ASEAN and assuming an important role for "Japanese corporation's manufacturing networks in the ASEAN region" (Yun, 2002). Agriculture consisted of only 1.7% of bilateral trade (The Japan Times, October 23, 2000). The agreement covers 98% of bilateral trade volume including some agricultural forestry and fisheries products (METI, 2002a: 15), specifically 486 of 2,277 products, 428 products whose tariffs had been subject to previous WTO elimination and 58 products with a tariff rate of 0 (Ogita, 2002: 13). The Ministry of Agriculture, Forestry and Fisheries that agriculture ensured that agriculture would be largely excluded (Masaki, 2000a). The Japan-Singapore Economic Partnership Agreement (JSEPA) was signed 13th January 2001, covering tariffs, services, investment e-commerce, and employment mobility. METI argued that "the agreement would be, a valuable model case for Japan to become proactive in bilateral and regional agreements" (METI, 2002a: 18).

The year 1998 also saw the commencement of discussions with Korea. In

September 1998, Japan proposed an FTA with Korea (Asakura and Matsumura, cited by Ogita, 2002: 4). In October 1998, Korea proposed a Japan-Korea 'Action Plan' for trade and investment and a study group to consider an FTA between Korea and Japan. An interest in negotiating with Korea was an important context for the original Japanese shift to accepting the free trade policy as a supplement to WTO policy (Hatekeyama, 2002a). However, the Korean – Japan negotiations have been fraught with difficulties and to date remains incomplete, in part due to unresolved political grievances, a variety of disputes and the problem of agricultural liberalization.

The New Conventional Wisdom

As Galbraith argues, ideas that are no longer valid in a changing world are discarded. In Japan, a new conventional wisdom emerged on free trade agreements, revising in particular Japan's approach to Asia. Agreements could advance Japan's economic interests. For instance agreements on intellectual property rights could underpin innovation in Japan and secure the offshore activities of Japanese companies (METI, 2002a: 44). Agreements could be essential for "Japan to strengthen its economic ties with East Asia as a means of gaining access to East Asian growth factors and stimulating the Japanese economy" (METI, 2002a: 47). Trade agreements could also "increase Japan's bargaining power in WTO negotiations, and the results of FTA negotiations could influence and speed up WTO negotiations. The deepening of economic interdependence gives rise to a sense of political trust among countries that are parties to these agreements, expanding Japan's global diplomatic influence and interests" (MOFA, 2002). The focus, despite Mexico is Northeast Asia "the only area in the world which has shown little interest in regional cohesion or integration, applying itself with greater vigour to the development of regional cohesion" (MITI, 1999). Finally, bilateral negotiations can establish "the lead in the creation of multilateral rules in new areas. Such FTAs basically aim to establish de facto trade standards....ultimately to play a central role in developing multilateral trading rules originating from rules of that country's creation" (METI, 2001: 204).

While some proposals have been ostensibly regional, such as the Japan-ASEAN "Framework for Comprehensive Economic Partnership" (2004) the thrust of substantial Japanese negotiations is bilateral. A Ministry of Foreign Affairs (MOFA) report argued that while an ASEAN-Japan FTA is the final, longer term

objective, in the immediate term, Japan should “rapidly make efforts in creating bilateral economic partnerships...with major ASEAN states” subsequently “expanding those agreements” to an ASEAN-wide arrangement (MOFA, 2002). Japan is wary of large initiatives because the prospects for settling a negotiation among many members is often more difficult than between a few (METI, 2001: 181).

With the shift in conventional wisdom Japanese trade policy could engage with the traditional methodology and language of WTO regionalism. Choosing terms familiar in other countries, Japan advocates a “Multi-layered Trade Policy” where regional and bilateral activities would be pursued as a “supplement” or ‘complement’ to the multilateral sphere, with the “baseline of Japan’s policy (being) the strengthening of the multilateral trade system, centred around the WTO” (MITI, 2000; METI, 2002a: 47; Japan, 2000: 10). Agreements are “good precedents for the WTO and complement it, thereby spurring greater liberalisation, strengthening rules, and expanding the scope of international trade activities” (METI, Multilateral Trade System Department, 2001). Alongside the new methodology Japan devised the criteria for participation – consistent with Article 24, comprehensive, yet flexible; acceptance of some trade diversion; able to stimulate Japanese economic reform; and with a focus on East and Southeast Asia where the highest tariffs for Japanese exports are found (MOFA, 2002).

Just as the Europeans created the Common Agricultural Policy and the US its own agricultural subsidies program, Japan’s new conventional wisdom needed adjustment. The world had moved on, but the bold rhetoric from METI needed to be fine tuned. From the outset, METI promoted the idea that such agreements (and external economic policy) could prompt regulatory reform in Japan (METI, 2001, 139; 147; METI, 2002a: 44). This assumed that developed countries in the region due to their similar level of development would be first to harmonise their regulations (MITI, 1999) leading to “comprehensive rules for global economy activity” (MITI, 1998). METI has argued that regional trade agreements can “contribute to multilateral rule-making in new areas such as investment and competition” (METI, 2002a: 6). This view was influenced by the failure of the multilateral agreement on investment in 1998 and that investment negotiations in the Doha Round were also “likely to be severely hampered by conflicts of interest” (METI, 2001: 159 footnote 44).

Therefore, Japanese agreements were to go beyond the ‘traditional’ view of agreements to include services, investment, labour markets, and economic policy

(METI, 2000; JETRO, 2000: 28). An earlier similar proposal in APEC was termed the 'open economic association' (Yamazawa, 1995: 210). This approach might have opened the possibility of complementing the US Pacific Five proposal. However, despite proposals from Australia, New Zealand, Canada and even the EU (The Japan Times, February 27, 2001), the problem of agriculture would prevent negotiation of treaties with Australia, New Zealand, Canada and the EU. Many APEC developed countries are also agricultural exporters. Indeed, the 1998 New Basic Law on Agriculture reaffirmed Japanese commitment to multifunctional agriculture (Japan, 1999a), the "coexistence of the various types of agriculture" (Japan, 1999b) and in the WTO Japan argued for no additional agricultural, fisheries or forestry liberalization outside a new trade round (Japan, 2000: 8; Hanai, 2000).

In September 2000, a classified report written by officials in MOFA and METI argued that Economic Agreements or other arrangements be negotiated with developed countries to avoid the agriculture problem, but free trade agreements be pursued with developing countries. Developed countries had low tariffs with Japan (except in agriculture) and such Economic Agreements ought to be negotiated to "establish a comprehensive framework for harmonising various economic systems, regulations and standards between Japan and other industrialised countries" (Masaki, 2000b). Trade agreements would hasten reform and bring competition, as well as increase bargaining power. However, they would be strongly resisted by agricultural, chemical and textile industries (Masaki, 2000b). Thus by 2000, Japan resolved agriculture and made trade agreements more palatable.

The Ministry of Foreign Affairs soon became supportive of free trade agreements, a commitment that solidified in 2001 (Kojima, 2001) arguing that WTO consistent agreements could be a "driving force for open trade" and a 'complement' for the world trading system (MOFA, quoted by Ogita, 2002: 7). Agreements could also stimulate reform, bypassing traditional mechanisms for foreign pressure (Tanaka, quoted in Kojima, 2001). At the end of 2002, the Ministry was "at the vanguard" of FTA policy (The Japan Times, October 14, 2002, Editorial) promoting special criteria for future agreements. MOFA argued that FTA negotiations will concentrate not on issues that can be resolved in the WTO, such as agriculture and liberalisation, but on "advanced liberalisation" or "WTO Plus" areas (MOFA, 2002b), echoing the 2000 compromise position. This position in spirit undermines the rationale for WTO consistency which presumes 'substantially all free trade' in goods as part of a free trade agreement. Australia,

New Zealand, and even Korea are among the countries that oppose this interpretation of FTA coverage and have challenged the 'wisdom' of this position.

Japan's view of the vital role of overseas development assistance also passed into the new conventional wisdom unchanged. For Japan, trade, aid and investment are inextricably linked. For example, the 1988 New Asian Industries Plan from MITI emphasised the links between trade investment and aid (Yamamura and Hatch, 1996: 120; Yamamoto and Kikuchi, 1998: 194). Strategically for Japan, accommodating free trade agreements within the overall Japanese policy for economic cooperation in East Asia is vital. The chairman of the METI Study Group on Technical Cooperation argued "The main pillars of East Asian economic integration that Japan aims to bring about are not only the promotion of free trade but also the establishment of harmonised and integrated intra-regional institutions to promote domestic and international investment, as well as cooperation in (various) sectors" (Hara, 2003: 4-5). The 2005 Japanese Economic and Industrial Policy statement remarked that Economic Partnership Agreements go hand in hand with the "construction of common systemic infrastructure in areas such as intellectual property systems, standards and conformance assessment systems and trade control systems" to realize an 'Asian Economic Zone' (METI, 2005b: 13). This is more explicit in the Industrial Competitiveness Strategy Council's report on "Six Strategies for Greater Competitiveness" when it remarked that in order for Japan to realize the East Asian Free Business Area it ought to 'implement economic agreements and make strategic use of ODA" (METI, 2002a).

In all the ASEAN negotiations, agriculture is only one of several sensitive issues and that the negotiations link trade, aid and investment. Malaysia and the Philippines signed a framework agreement (FA) with Japan that side-lined some of the most sensitive issues. The Philippines-Japan FA did not resolve the number of nurses that would be permitted to work in Japan, a major issue for the Philippines, but not for the other ASEAN partners. The deal also saw the elimination of 60% Japanese steel import tariffs and elimination of tariffs in the automobile sector. Japan made concessions in pineapples and some other agricultural commodities, but the sugar sector was too controversial. The Malaysia-Japan FA removes tariffs on imported Japanese automobile parts, with some exceptions to protect Malaysia's local car production. Japan also made a variety of agricultural concessions but excluded sensitive products such as rice, beef and pork. Japan will provide technological exchange ostensibly to allow Malaysia to develop production of automobile components and parts. In the

Japan-Thailand FTA, Japan will also provide technical assistance and training ostensibly to enable Thailand to become the 'Detroit of Asia', exporting high value manufactured goods. Thai automobile tariffs will be reduced gradually with exceptions. Despite pressure from Thailand, an exporter of rice, the Japanese Prime Minister Koizumi intervened in the negotiations to insist that rice would never be included (Japan Times, October 13, 2004).

These 'sweeteners' demonstrate the links between aid, trade and investment in the new Japanese conventional wisdom. The recent literature on Japanese FTA policy has focussed on trade, neglecting the relationship between aid and 'economic partnerships'. Japan's new approach to free trade agreements has exposed the vulnerability of Japan's position on rice and other special commodities. Of course 'rice' is a crucial policy issue, but so is Japan's 'overseas development assistance' relationship with Southeast Asia. What role Japan's 'partnership' agreements will have in fostering a new 'Asia Strategy' remains to be seen, particularly in managing Chinese ASEAN ambitions. However, the new conventional wisdom on free trade agreements enables Japan to more flexibly establish closer economic relations with Southeast Asia and China offers the possibility of a viable starting point for negotiations with developed countries in the Asia Pacific region.

Conclusion

Japan's shift to free trade agreements represents a shift in conventional wisdom. In particular Japan realized the prior policy could not halt the growth of regionalism elsewhere and could not resolve the costs of non-participation. To date Japan has approached the issue bilaterally, leading to framework agreements with Malaysia and the Philippines and agreements with Mexico and Singapore. Negotiations continue with Thailand, Indonesia and Korea. Agreements do not seem to be a 'testing ground' for wider liberalization, reflected in the accommodation of agricultural protection especially rice. Developed APEC members have been excluded, Japan's strategy has an Asian focus and aside from Singapore, all the countries are developing countries. If Japan's program with ASEAN countries is successful, then perhaps the Japanese conventional wisdom is filtered primarily through the lens of a redefinition of Japan's 'Asia Strategy' rather than 'complementing' the WTO. Such a redefinition of Japan's approach to regional integration to fit within the post-war GATT/WTO model may offer greater flexibility in negotiating with other countries. However, accommodating

Japan's new conventional wisdom alongside the aspirations of ASEAN and China remains a significant challenge.

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