

# Japan's FTA Drive, East Asian Regional Leadership and the China Challenge

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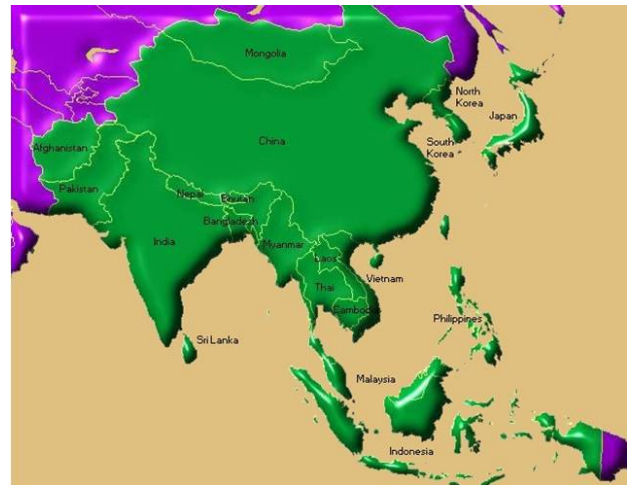
## Japan's FTA Drive, East Asian Regional Leadership and the China Challenge

By Hisane MASAKI

TOKYO - Japan is revving up its drive toward free-trade agreements (FTAs), a move largely fueled by an intensifying rivalry with China over leadership in regional economic integration and increasingly tough global competition for oil, gas and other resources.

Several years ago, Japan was not alone in East Asia in choosing to opt out of any FTAs. Other major Asian economies, such as China, South Korea and Taiwan, had declined to conclude FTAs with any of their trading partners. But Japan was even slower than its East Asian neighbors, especially China, in jumping on the global bandwagon.

This drew criticism at home that the government was allowing Japan's influence in the region, especially over economic integration, to be eroded significantly by that of China, a rapidly ascendant economic as well as military power.



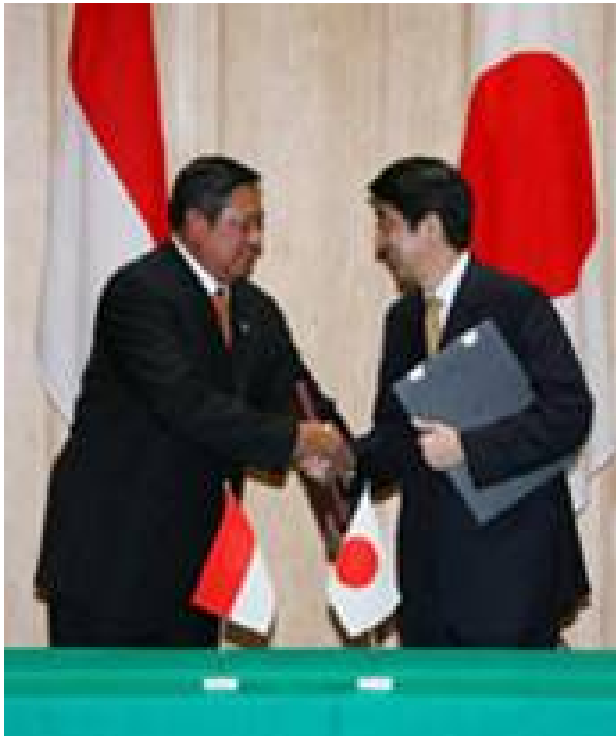
Japan and China are vying for the leadership role in the formation of an “East Asian Community.”

In a belated attempt to turn the tables, Japan is now going all out to conclude FTAs with as many countries as possible. Japan concluded its first deal with Singapore, in 2002. It signed its second FTA, with Mexico, in 2004, and a third, with Malaysia, last December.

Japan signed an FTA with the Philippines this September, and Parliament approved it this month. Japan reached a basic agreement with Chile and Indonesia in November, and then with Brunei this month. The Japanese FTAs with the Philippines, Chile, Indonesia and Brunei are all expected to go into force by the end of next year.

Under the Japan-Indonesia agreement, Indonesia will reduce tariffs on Japanese cars and auto parts. Japan will accept Indonesian nurses and care workers, following a similar arrangement between Japan and the

Philippines.



Japanese Prime Minister Abe Shinzo (right) and Indonesian President Susilo Bambang Yudhoyono shake hands at the Prime Minister's Official Residence in Tokyo on Nov. 28.

Japan completed FTA negotiations with Thailand in August 2005, but signing of the agreement, originally set for April, has been delayed because of Thailand's prolonged political instability, which culminated in a military coup in September.

Negotiations with South Korea were under way, but the two countries missed the original, end-2005 target date because of sharp differences over farm trade and also chilly political relations. The political obstacle to the proposed Japan-South Korea FTA seems to have been lifted after Prime Minister Abe Shinzo's fence-mending trip to Seoul in early October, immediately after taking office.



Prime Minister Abe Shinzo and first lady Abe Akie pay their respects at the National Cemetery in Seoul.

A free-trade agreement with the 10-member Association of Southeast Asian Nations (ASEAN) as a whole is also in the works. This month Japan and ASEAN reached a basic agreement on a plan to scrap bilateral tariffs within 10 years, a centerpiece of the negotiations. The two sides aim to bring the talks to a conclusion next spring.

In addition to fellow East Asian countries, Japan has recently begun to place priority on resource-rich countries outside of the region as a foreign-policy tool to beef up relations with them and thereby ensure stable supplies of oil, natural gas and other resources. Among those it has approached to open FTA negotiations is the oil-rich Gulf Cooperation Council. Japan opened FTA negotiations with the GCC in September.

Japan is also expected to kick off FTA negotiations early in the new year with Vietnam, India, Australia and Switzerland. Negotiations with Switzerland would mark Japan's first attempt to conclude an FTA with a European country.

Meanwhile, the Japan Business Federation

(Nippon Keidanren), Japan’s most powerful business lobby, has recently proposed an FTA with the United States, although the governments of both countries remain negative about the idea.

### The Sensitive Issue of Farmers

Despite its accelerated FTA moves, however, Japan still has a lot to do if it is to march in step in the ever-intensifying global and regional FTA competition. The biggest obstacle is Japan’s heavily protected and internationally uncompetitive agricultural industry.

Japan has refused to put many of its agricultural products on the negotiation table. Under the recent basic agreement with Indonesia, for example, Japan will cut tariffs on nearly all industrial and forestry products while removing gradually those on tropical fruits. So-called sensitive products such as rice, wheat and meat aren’t included in the pact.

Tokyo has also dug in its heels on agricultural trade in the stalled Doha talks. Japan’s plan to enter FTA negotiations with Switzerland, a close ally in the fight against farm-market liberalization in the Doha Round, is widely seen as part of its efforts to strengthen its negotiating position there.

Concluding free-trade deals is considered by some to be the best avenue to cashing in on rapid growth in other Asian economies. But many experts point out that Japan needs to reform its heavily protected agricultural market - which has been left largely unscathed despite former premier Koizumi Junichiro’s reform drive, which Abe vows to continue.

Though their influence is waning, farmers have long been part of the ruling Liberal Democratic Party’s traditional support base. Agriculture accounts for a paltry 1% of the nation’s gross domestic product (GDP), and farm households are rapidly aging and shrinking. Nevertheless, farmers have wielded disproportionately strong

political influence.

Abe’s seriousness about agricultural reform has been called in question. When inaugurating his cabinet in late September, Abe appointed Matsuoka Toshikatsu, a leader of the LDP lawmakers with close ties to the farm industry and most vocal opponent of market liberalization as minister of agriculture. Nevertheless, this month the cabinet gave the green light to entering full-fledged negotiations with Australia.



Japanese minister of agriculture  
Matsuoka Toshikatsu

They will be Japan’s first FTA talks with a major exporter of farm products. But Matsuoka cautioned, “We will enter the talks but with the commitment to defend key items.” The LDP lawmakers representing farmers are demanding exclusion of rice, wheat and sugar,

among other farm products, from any FTA with Australia.

The Council on Economic and Fiscal Policy, a top government economic decision-making panel chaired by Abe himself, decided last month to revise the current roadmap, with an ultimate goal of at least tripling the number of Japan's FTA partners within the next two years. However, Abe will need to exercise strong political leadership to overcome strong objections to liberalizing some sensitive agricultural products.

### **Regional Leadership Race**

Kicking off FTA negotiations with India and Australia early next year can be seen as part of Japan's strategic efforts to counter the influence of China in a proposed East Asian Community (EAC), one of the main issues discussed at the first East Asia Summit in Kuala Lumpur in mid-December last year. Japan has strongly advocated the inclusion of India as well as Australia and New Zealand in the proposed EAC, an idea opposed by China and some other Asian nations. Abe and his Australian counterpart, John Howard, formally agreed during telephone talks on December 12 to begin FTA negotiations next year.

Japan and China are pushing competing ideas for a regionwide FTA. In 2004, China proposed an East Asian FTA among the 10-nation ASEAN plus China, Japan and South Korea. As a counter-proposal, Japan sought an East Asian agreement that would include Australia, New Zealand and India. Japan also proposed an East Asian version of the Organization for Economic Cooperation and Development.

Making matters more complicated, the administration of US President George W Bush has recently thrown its hat into the ring in the race for regional economic integration by floating the idea of a much wider, Asia-Pacific FTA that includes the United States.

Leaders of the 21-member Asia-Pacific Economic Cooperation (APEC) forum met in Hanoi last month and issued a declaration that called for studies on the idea of creating a US-proposed Free Trade Area of the Asia-Pacific. The declaration said APEC members should report back on the findings of such studies at the 2007 summit to be held in Australia.

When combined, the APEC area forms a massive market whose gross domestic product accounts for about 60% of global GDP and where about 40% of the world's population live. APEC lumps together myriad political systems and economic powers. With some APEC members wary of the US, a regional free-trade zone is unlikely to be realized any time soon. But Prime Minister Abe said of the US initiative, "It's a significant step to study the proposal as a multi-layered approach."

The Bush administration's proposal for the regional zone apparently reflects growing concerns about the possibility of an East Asian regional economic bloc emerging without the presence of the US. The administration also apparently hopes it would help rein in China's economic clout. For the US, APEC is the most realistic vehicle to keep itself part of Asian economic integration.

Meanwhile, Indian Prime Minister Manmohan Singh made an official visit to Tokyo in mid-December, his first since taking office. During the four-day visit that ended on Dec.16, Abe and Singh agreed formally to launch FTA negotiations early next year. Japan invited the Indian leader apparently in hopes of strengthening ties with India as a counterbalance to the growing influence of China in Asia. Singh's Japan visit came three weeks after Chinese President Hu Jintao's trip to India.



Japanese Prime Minister Abe Shinzo and his Indian counterpart, Manmohan Singh, hold talks at the Prime Minister's Official Residence in Tokyo on Dec.15.

Since taking the helm of the Japanese government, Abe has described India as a “new partner in Asia” and advocated a closer partnership with two democracies - India and Australia. Abe has also proposed a four-way “strategic dialogue” among Japan, the US, Australia and India.

But India's nuclear policy remains the biggest obstacle to strengthened ties between Tokyo and Delhi. India conducted nuclear tests in 1998, sparking an outcry in many parts of the world, especially Japan, the only country to have been attacked with nuclear bombs - by the US in 1945 in the closing days of World War II.

At issue is a controversial nuclear cooperation deal signed between the US and India in March during President Bush's visit to Delhi. Japan has yet to make clear its stance on the deal. Abe told the Indian premier that Japan is still considering its position on it.



U.S. President George Bush in India in March.

The US-India agreement will give India access to US technology, although Delhi has not signed the Nuclear Non-Proliferation Treaty (NPT). It reverses US policy, which had restricted nuclear cooperation since India first tested a nuclear weapon in 1974. On December 9, only six days before the Japan-India summit, the US Congress approved legislation allowing U.S. shipments of civilian nuclear fuel to India, handing Bush a victory on a top initiative.

Critics said the measure would spark nuclear proliferation and a nuclear arms race in Asia by boosting India's atomic arsenal. The Citizens' Nuclear Information Center (CNIC), a Japanese nongovernmental organization, quickly condemned the US Congressional action as “providing an excuse for nuclear weapons programs of Pakistan and North Korea and of any other would-be proliferators.”

At present, nuclear trade with India is restricted under the rules of the 45-member Nuclear Suppliers Group (NSG) of countries. Changes to NSG rules can only be made by consensus, so if Japan opposes lifting sanctions on nuclear trade with India, the US-India nuclear deal cannot proceed. “Japan of all countries, having suffered the atomic bombing of Hiroshima and Nagasaki, must oppose this deal,” CNIC Co-Director Ban Hideyuki said before the Japan-India summit. Claiming that it



will not be in Japan's national interest to support the US-India nuclear deal, Ban said, "For the sake of Japan's security and for the sake of world peace, we demand that the Japanese government oppose lifting NSG restrictions on nuclear trade with India."

### Rush for Resources

Resource-poor Japan is also rushing to conclude free-trade deals with countries rich in oil, natural gas and other resources, in hopes of strengthening relations with them and thereby ensuring stable supplies in the medium and long terms.



Tokyo is desperate to ensure stable energy supplies.

Alarmed by stubbornly high prices for oil and the intensifying global rush for oil, gas and other resources, led by China and India, Japan adopted a "New National Energy Strategy" this year that called for, among other things, strengthening ties with resource-rich countries through such means as increased official development assistance and conclusion of FTAs.

Beneath the recently accelerated Japanese FTA strategy lies an intensifying rivalry with China over energy resources, as well as over political and economic influence in Asia. Japan has increasingly been competing over scarce

energy resources with China. The two energy-hungry Asian powers have been locked in the simmering dispute over gas reserves in the East China Sea. Furthermore, they have each lobbied hard for alternative routes for a pipeline from eastern Siberia's oilfields to Pacific Rim nations.

The Japan-Indonesia FTA, on which the two countries reached a basic agreement in late November, will contain a clause to ensure stable energy supplies. It was the first time that Japan had reached an agreement in FTA negotiations with a trading partner to include such an energy clause.

Indonesia is the biggest supplier of liquefied natural gas (LNG) to Japan, accounting for 25% of 58 million tons Japan purchased from abroad in 2005. Under the deal, Indonesia will hold prior consultations with Japan about restricting oil and gas exports in the event of a surge in domestic demand. Indonesia will also fully implement existing energy-supply contracts between the two countries even when export restrictions are invoked. In return, Japan will increase technical assistance to Indonesia in areas such as coal-to-liquid technology, energy-saving measures and the compilation of long-term supply-demand balance for crude oil, coal and natural gas.

The agreement to include an energy clause in the FTA came as Indonesia has threatened to cut in half LNG shipments to Japan from 2010 - when long-term contracts expire - to boost the availability of natural gas for domestic industries amid decreasing oil and natural-gas production at home.

This month Japan and Brunei, another oil and gas producer, also reached a basic agreement in free-trade negotiations. In addition to eliminating tariffs on most products traded between the two countries, including Japanese autos and Brunei's petroleum products, the two countries agreed to include in the pact an

energy clause similar to one in the Japan-Indonesia FTA to ensure stable oil and gas supplies.

Japan and the six-member GCC launched FTA negotiations in September. The two sides hope to conclude the pact by the end of 2007. The GCC group consists of Saudi Arabia, the United Arab Emirates, Bahrain, Oman, Qatar and Kuwait and accounts for more than 70% of Japanese crude-oil imports. In the FTA negotiations with the GCC, Japan is seeking a written pledge by the grouping to supply crude oil preferentially to Japan, even in emergencies such as war.

In addition to Indonesia, Brunei and the GCC, Japan has negotiated or plans to negotiate FTAs with some other resource-rich countries, such as Australia, Chile and South Africa. Australia is a major supplier of coal, iron ore and LNG, which together account for more than half of its Japan-bound exports. Australia is also an important country for Japan's civilian nuclear policy.

Japan's New National Energy Strategy, adopted this year, calls for nuclear-energy production to rise from the current 30% to between 30% and 40% or more in 2030. Japan is already the world's third-largest nuclear-power nation in terms of the number of civilian nuclear plants in operation. Australia has the world's largest uranium deposits. Chile is also rich in such mineral resources as copper, as well as a gateway to the South American regional trade grouping Mercosur. Japan is also eyeing FTA negotiations with South Africa, which is rich in such mineral resources as gold, platinum and diamonds.

*Hisane Masaki is a Tokyo-based journalist, commentator and scholar on international politics and economy. Masaki's e-mail address is [yi45535@nifty.com](mailto:yi45535@nifty.com).*

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*For further analysis by the author on Japan's energy strategy, see [this](#).*