



## **CJK FTA from a Political Economy Perspective**

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On 29 Nov, 2012, economic and trade ministers from China, Japan and South Korea announced the launch of the FTA talk among the three countries. The first round of negotiations was held in Seoul, ROK in March, 2013. The latest 5th round closed in Beijing in September, 2014. The sixth round of negotiations will be held in Tokyo in the end of this November.

At a time when China and Japan, the ROK and Japan, were still caught in the territorial disputes and historical issues, CJK's choice to stick to their original commitment and proceed with the talks as planned proves that the three countries share the same view on the importance of the FTA to their national interests and regional integration. Since the three countries account for an overwhelmingly dominant share of gross domestic product (GDP) in East Asia, once concluded, the CJK FTA will have significant implications in terms of welfare of the region and of the countries involved as well. This paper is trying to provide a comprehensive understanding of these implications from a political economy perspective.

### **I. CJK FTA is a regional boon for East Asia**

#### **CJK FTA is of crucial importance in advancing regional integration.**

East Asia so far has established a number of bilateral and plurilateral FTAs but a region-wide FTA. So far, ASEAN is the leading force in the promotion of the East Asian regional cooperation. The RCEP (Regional Comprehensive Economic Partnership), characterized with "ASEAN Centrality", is expected to demonstrate ASEAN's leadership in bringing together its own ten members and external partners to establish a region-wide FTA.

However, with the absence of the key bilateral (or trilateral) FTAs in Northeast Asia, the RCEP negotiations could hardly make breakthrough any time soon. Whether this East Asian community can be successfully established and what kind of community would be set up are still dependent on CJK cooperation because they are de facto most powerful countries in the region.

#### **CJK FTA will serve as a stabilizer of political relations in the region.**

The Germany-France case of regional integration in Europe has shown us a very good example to follow in pursuit of regional peace and stability. Considering the current tough situations of political relations among the three countries, especially the Sino-Japanese relations, it is quite

encouraging that the processes of the CJK FTA and RCEP negotiations seem not to be affected by the political tension.

## **II. CJK FTA is to the benefits of the three Northeast Asian countries**

The three countries have all adopted multi-track FTA strategy. CJK FTA, being one choice of their FTA strategies, provides both economic interests and strategic interests for the three countries.

### **Economic Interests**

1. CJK are quite geographically close, which means the largest potential trade and investment benefits simply because transportation cost and other exchange costs are lower among the three countries than with other countries. High transportation cost will make many goods non-traded even in free trade. Therefore, low cost means high efficiency (benefits).
2. CJK have a very high trade interdependence with each other. Export has long been an important economic growth factor for the three countries. Due to the weak markets in Europe and America, Japan and the ROK became increasingly dependent on Asian market, particularly East Asian market, to boost its trade and economic development. China, Japan and the ROK are now acting as one another's major export destination.
3. The three economies happen to be quite complementary. Complementarity means on one hand great trade potential, and on the other hand, huge cooperation potentials. The three countries may cooperate in many areas like new energy development and utilization, advanced electronics and IT technologies, ship building and high-end equipment manufacturing, etc.
4. CJK FTA will help strengthen East Asia's competitiveness in the global economy as the regional production networks may function more efficiently.

### **Strategic Interests**

In the background of the stalemate of the WTO Doha Round and proliferation of regional trade agreements (RTAs), more and more countries see FTAs as a strategy for them to increase their bargaining power in multilateral and regional trade negotiations, and even in other areas beyond economic issues. CJK is very important for all the three countries considering its strategic interests.

For China, as the world second largest economy, though it has signed 11 FTAs with 20 economies and is negotiating 8 other FTAs, it is currently excluded from the TPP negotiation, which, once in place, will have negative effect like trade and investment diversion.

For Japan, who is now the TPP negotiating member, and the ROK, who is willing to be the TPP member, CJK FTA will help the two countries to gain bargaining power in the TPP negotiations and other benefits considering their alliances with the United States.

### **III. CJK FTA provides different business interests for the industries within the individual countries**

The fact that each of the three countries as a whole will definitely gain from the CJK FTA does not ensure that the arrangement will be welcomed by all in terms of industries because some industries will gain while others will lose due to it. FTAs deliver concentrated economic gains to specific sectors that are highly dependent on foreign trade for imported inputs and exports of finished goods (e.g. steel, transport machinery and electronics). Therefore, business interests that represent export industries provide strong support for Japan and Korea's FTA drive. This is also the case with the CJK FTA. Such business interests like automobile and electronic sectors have played an integral role in facilitating the launching of FTA negotiations.

In contrast, the import-competing sectors generally oppose liberalization. For example, agricultural sector and small and medium-sized enterprises (SMEs) that compete with foreign companies for parts and components in Japan and the ROK tend to oppose the FTA.

Japanese and Korean farms are not competitive in international standards. Without substantial restructuring toward larger and more commercialized farms, Japanese and Korean farmers are highly vulnerable to foreign competition. More importantly, consumers in both countries exhibit strong concerns over the safety of imported food products.

China is also facing such tradeoffs when negotiating FTAs. Compared to Japan and the ROK, China retains a competitive advantage over agricultural products while a disadvantage over some manufacturing sectors like steel, machinery, chemical and automobile and even textile. Service sector is even more challenging for China. Other issues like investment, government procurement, intellectual property rights, environmental protection and technical standard are all hard to be addressed on the Chinese side because they call for deeper domestic reform. In China, there is also inter-ministerial conflicts which make it difficult for governments to liberalize sensitive sectors. As the lead agency to negotiate the FTA, the Ministry of Commerce is easily subject to pressure from other ministries and commissions to accommodate their interests.

### **IV. Can governments compensate those who lose?: Experience from the U.S. Trade Adjustment Assistance (TAA) program**

As a result of trade liberalization, some workers, firms and industries will gain while other workers, firms and industries will inevitably lose. Only when those who gain compensate those who lose will the process of trade liberalization be sustained. Without compensation, free trade will only lead to an increase in the aggregate national welfare rather than social welfare. Then losers will turn to seek protection and become barriers or obstacles to free trade. Therefore, if a government wants to maintain or even pursue a freer trade system, it must forge a domestic

political base in support of free trade. Trade Adjustment Assistance is a safety net provided by the U.S. government. TAA helps workers and firms adjust to dislocation that may be caused by increased trade liberalization. It is justified now, as it was then, on grounds that the government has an obligation to help the "losers" of policy-driven trade opening. TAA is also presented as an alternative to policies that would restrict imports, and so provides assistance while bolstering freer trade and diminishing prospects for potentially costly tension (retaliation) among trade partners. Today TAA remains important for forging a compromise on national trade policy. Similar policies can be seen in other economies like Canada, Australia, the EU, Japan and the ROK.

However, China is currently absent of such "free trade compensation mechanism". The only way to provide trade remedy is through anti-dumping and countervailing measures under the WTO.

## **V. Policy recommendation**

1. To improve bilateral ties between the three countries.
2. To strengthen connectivity among the three countries.
3. To establish an appropriate safety net in each country.