

What Asian Economic Integration Means to China

By Jianmin Jin

China's Active Push for Regional Economic Integration/FTAs

In recent years, efforts at regional economic integration or to form free trade areas have accelerated worldwide. This is because regional economic integration can be economically significant in 1) gaining new economic benefits through market access; 2) securing market transparency, stability, and predictability by establishing common rules; and 3) offering strategic protection from the dilution of benefits already acquired or from shifts in investment and trade. In addition, regional economic integration/FTAs can also be employed as a tool of diplomatic or security policy.

In order not to fall behind in riding such global currents, both Japan and China are rushing to develop EPA/FTA strategies — regional economic integration policies — as core elements of their global strategies. While discussion in Japan is centered on whether to take part in the Trans-Pacific Partnership (TPP), which argues for a high degree of market openness, China understands the policy significance of regional integration and, in keeping with its own stage of development, seeks active participation in the process of Asian economic integration rather than the TPP.

In contrast to the lack of domestic consensus in Japan concerning participation in the TPP, in China there is little dissent to be heard concerning government efforts to promote trade liberalization. The fact that the concerns raised during the divisive debate on WTO membership — about the severe damage and swelling unemployment it was feared open markets would bring to the agricultural, automobile, and financial industries — proved unfounded, and China instead enjoys the benefits of trade liberalization through WTO membership, has done much to blunt concerns about liberalization. Accordingly, the Chinese government has been in a position both institutionally and socially to actively push free trade.

Shifting Approach: From Politics to Economy, from Regional to Global

Beginning with Deng Xiaoping's south China tour in 1992, China pursued economic reforms through the introduction of a market economy, leading to economic revitalization and large-scale investment by foreign corporations. In particular, joining the



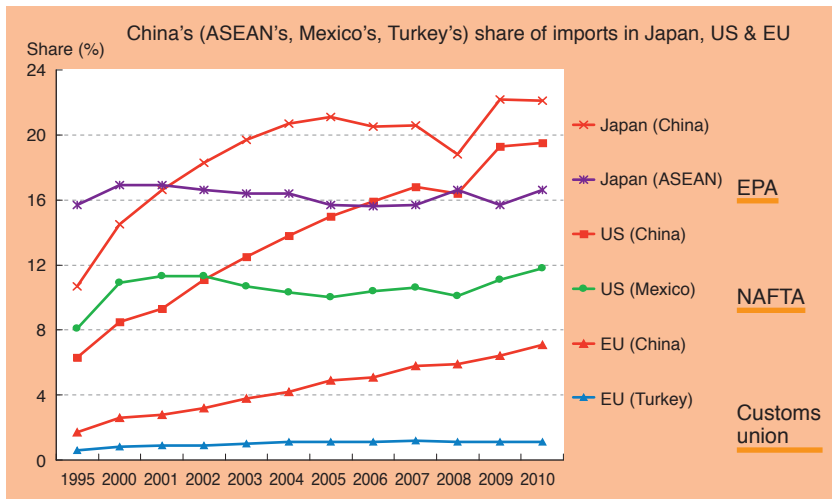
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WTO in 2001 enabled China to fully capitalize on its comparative advantages, and the presence of Chinese products in major world markets rapidly increased. As shown in *Chart 1*, China's share of import markets in Japan, the United States, and the European Union has grown to greatly exceed ASEAN's share in Japan (with which it has an EPA), Mexico's share in the US (with which it has an FTA), and Turkey's share in the EU (with which it shares a customs union). In other words, the competitiveness of Chinese products broke through the customs barriers of Japan, the US, and the EU. Seen as a matter of economics, there would seem to be little incentive, so long as the WTO framework continues to function, for China to engage in regional economic integration or conclude free trade agreements.

Nonetheless, China has actively pursued an FTA strategy since the 2000s. One reason is the rise of barriers to further expansion of Chinese trade. These include the stalled process of further liberalization under the WTO as well as the rash of anti-dumping measures aimed at Chinese products and growing resistance to Chinese investment seen in many countries around the world, particularly in Europe and North America. A more important context is China's effort to utilize FTAs not only for their economic significance but also as a tool to build stable relationships with neighboring countries, thereby alleviating their fears of a "Chinese threat" and enabling them to focus their energies on their own economic development. In other words, China's FTA strategy pursues its own

CHART 1

Competitive Chinese products break through customs barriers



Source: IMF (DTS), ASEAN Secretariat

economic benefit on the one hand, while seeking to achieve political and security goals on the other by providing or creating benefits for partner nations. This is similar to the thinking behind the FTA strategy of the US.

Specifically, given the strategic significance in economic, political, and diplomatic terms of entering into FTAs and China's circumstances, it seeks to 1) check the influence of separatist forces such as those seeking independence for Taiwan; 2) alleviate concerns about a "Chinese threat" and improve the international environment, particularly with neighboring countries; 3) secure the resources needed for its own economic growth; and 4) achieve efficiencies of scale in economic development.

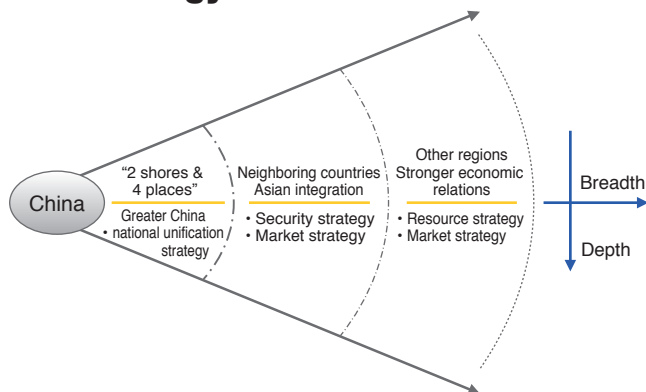
China has already concluded and moved to implement FTAs or similar agreements with 10 countries and territories. Until now, China's promotion of an FTA strategy has been weighted more toward the diplomatic and political than the economic, but from now on more attention will be paid to the economic significance of FTAs. *Chart 2* describes the multi-layered approach taken by China's FTA strategy, one that pursues both breadth and depth.

Successful China-ASEAN FTA

In recent years, and particularly in the wake of the global financial crisis, addressing imbalances and stabilizing the world economy (including the matter of governance over the global economic system) have become global issues. Given such changing conditions, China recognized the possibility that it would no longer be able to rely on the US and European markets upon which it has depended so heavily to date, and decided that such dependence on the US and European markets alone was ill advised. It adjusted its development strategy to focus on measures to expand domestic demand and diversify markets. The stirring of regional markets in Asia, in particular, has given additional impetus to its active pursuit of FTAs.

In fact, China concluded an FTA framework agreement with ASEAN as a matter of diplomacy in November 2002 and has gradually moved forward with liberalization. To alleviate long-standing concerns among ASEAN nations about a "Chinese threat" it declared that in support of

CHART 2
Multi-layered deployment of China's FTA strategy



Source: Produced by the author

ASEAN nations that had faced economic hardship during the 1998 Asian currency crisis it would not devalue the Chinese yuan, thereby offering economic stability through cooperation with the FTA. This having been received favorably by ASEAN, China then gradually expanded the scope of liberalization, moving from the framework agreement to implement an early harvest program (EHP) centered on agricultural products and to conclude agreements about trade in things, trade in services, and investment. It has also sought to build on the results by adding to the list of items to be liberalized. China also implemented voluntary export restraints in response to industrial hardships in some ASEAN countries.

After following this gradual process of liberalization, Jan. 1, 2010 brought the creation of a China-ASEAN free trade area that reduced tariffs to zero on more than 90% of imported goods, and has brought unexpected economic results. For example, as shown in *Chart 3*, the share of Chinese products among total ASEAN imports more than doubled from 6.8% in 2002 to 14.8% in 2011. ASEAN's share of Chinese imports, while not growing as much as trade in the other direction, expanded enough that in 2011-2012 ASEAN surpassed Japan to become China's second-largest regional source of imports following the EU.

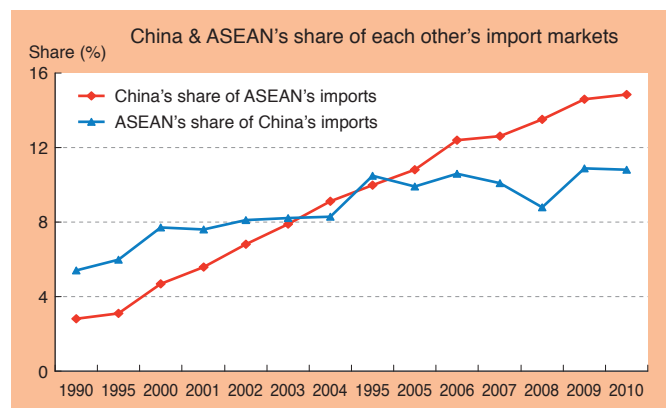
Tourism from China (from the ASEAN perspective a services export) has also increased rapidly, so much so that China is now ASEAN's largest source of tourists. In addition, direct investment from China has also increased rapidly, further deepening the close ties between China and ASEAN occasioned by the FTA.

China undoubtedly hopes to expand the success of the China-ASEAN FTA across Asia as a whole, with the conclusion of a China-Japan-Korea (CJK) FTA a particular priority.

Prioritize Promotion of China-South Korea FTA to Draw in Japan

As noted above, as China seeks to diversify markets and mold a multipolar global economy, it has pinned its hopes on a CJK FTA. China, Japan and South Korea make up roughly 20% of the world's GDP and 70% of East Asia's, yet the degree of reliance on intra-area

CHART 3
FTA brings closer ties between economies of China & ASEAN



Source: IMF (DTS), ASEAN Secretariat

Status of FTAs with related countries (as of end of 2012)

| | US | Australia | New Zealand | Peru | Chile | Singapore | Malaysia | Brunei | Vietnam | Japan | South Korea | China | India |
|-------------|-------------------|-------------------|-------------------|-------------------|-------|-----------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| US | — | ● | Under negotiation | ● | ● | ● | Under negotiation | Under negotiation | Under negotiation | | ● | | |
| Australia | ● | — | ● | Under negotiation | ● | ● | ● | ● | ● | Under negotiation | Under negotiation | Under negotiation | Under negotiation |
| New Zealand | Under negotiation | ● | — | Under negotiation | ● | ● | ● | ● | ● | | Under negotiation | ● | |
| Peru | ● | Under negotiation | Under negotiation | — | ● | ● | Under negotiation | Under negotiation | Under negotiation | | ● | ● | |
| Chile | ● | ● | ● | ● | — | ● | ● | ● | ● | ● | ● | ● | |
| Singapore | ● | ● | ● | ● | ● | — | ● | ● | ● | ● | ● | ● | ● |
| Malaysia | Under negotiation | ● | ● | ● | ● | ● | — | ● | ● | ● | ● | ● | ● |
| Brunei | Under negotiation | ● | ● | Under negotiation | ● | ● | ● | — | ● | ● | ● | ● | ● |
| Vietnam | Under negotiation | ● | ● | Under negotiation | ● | ● | ● | ● | — | ● | ● | ● | ● |
| Japan | | Under negotiation | | ● | ● | ● | ● | ● | ● | — | Suspended | In preparation | ● |
| South Korea | ● | Under negotiation | Under negotiation | ● | ● | ● | ● | ● | ● | Suspended | — | Under negotiation | ● |
| China | | Under negotiation | ● | ● | ● | ● | ● | ● | ● | In preparation | Under negotiation | — | In preparation |
| India | | Under negotiation | | | | ● | ● | ● | ● | ● | ● | In preparation | — |

Source: Compiled by the author from the WTO website and news reports

trade among these three Northeast Asian nations is lower than for the EU or NAFTA. China's degree of reliance on trade with Japan and South Korea, in particular, has fallen from 21% in 2005 to 15% in 2012. Accordingly, there is enormous potential to expand trade within the Northeast Asian area. Furthermore, concluding an FTA with the technologically superior Japan and South Korea would bring institutional security to the transfer of technology to China and to M&A activity by Chinese companies in Japan and South Korea, neither of which has made much progress to date. Japan and South Korea are high priorities in China's FTA strategy.

When it comes to Japan, however, China believes that although an FTA would have the greatest economic impact, divided domestic opinion concerning the opening of agricultural markets and consideration for US-Japan relations probably make it difficult for Japan to prioritize an FTA with China. For South Korea, on the other hand, the economic impact of an FTA with China would be greater than FTAs with either the EU, the US, Japan, or ASEAN, and consideration for the US is only a minor element as South Korea has already concluded an FTA with the US. Also, unlike Japan, South Korea has a security incentive insofar as China is an indispensable partner in cancelling out the threat from North Korea. China, therefore, has seen the conclusion of an FTA with South Korea as its highest priority for Asian economic integration.

TPP Accelerates China's Asian Economic Integration Strategy

Meanwhile, even as China has actively pursued Asian economic integration, it has also begun to be concerned that the TPP promoted by the US could generate centrifugal forces working against East Asian economic integration. In particular, both experts and public opinion in China frequently suggest that numerous provisions of the TPP are designed to make it difficult for China to participate and actually aim to achieve the goal of excluding China. Indeed, the US media has suggested that the TPP is being used to counter the economic influence of China in Asia, while President Barack Obama has declared in a campaign speech that promotion of the TPP is designed to apply pressure on China to follow the rules of international trade.

China, therefore, at the East Asian Summit (EAS) held in Cambodia

on Nov. 20, 2012, was vocal in welcoming the announcement of the launch of negotiations concerning the CJK FTA and a Regional Comprehensive Economic Partnership (RCEP) tying Asia together.

China Aiming at "Two Birds with One Stone" through RCEP

For China, which is concerned that the TPP movement could stall integration within Asia, an ASEAN-led RCEP would be a godsend, and working with ASEAN to expedite the RCEP is a natural choice. China may also be making a strategic play insofar as the RCEP, being ASEAN-led, both alleviates the need to confront the US directly and makes it more difficult for the US to object. Indeed, this may have been behind Chinese Premier Wen Jiabao's declaration at the November 2012 EAS that China would fully support the ASEAN-led RCEP and actively take part in negotiations. In this sense, China hopes the RCEP will be a tool that prevents division of the Asian region.

Furthermore, Australia, Japan, and India are included in the RCEP. China has approached each of these countries to conclude bilateral FTAs but such efforts have so far been fruitless. As shown in *Chart 4*, to enter into FTA relationships with these countries under ASEAN leadership is actually right in line with Chinese aims, and China may hope to achieve all its objectives through the RCEP in one fell swoop.

Indeed, that "recognizing the individual and diverse circumstances of participating countries" is a fundamental principle underlying the RCEP negotiations is consistent with what China has argued in its own pursuit of Asian economic integration, making it an environment in which it is easy to participate.

For China, economic integration or the conclusion of FTAs within Asia not only functions as a tool to make up for the stalled liberalization process under the WTO regime but is also necessary to promote market diversification in response to the slumping US and EU economy. In addition, it is also hoped that the process of economic integration will contribute to Asian unity and prevent regional divisions caused by a range of temptations. **JS**

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