

Responding to Rising Geopolitical and Economic Security Risks

By Masakazu Toyoda

This year's "White Paper on Trade", produced by the Ministry of Economy, Trade and Industry, investigates the "responses that Japan should take" during this period of turmoil in the international order, including the Ukraine crisis and the escalation of the U.S.-China confrontation. Let me follow up on some of the most interesting points.

First, the White Paper states that "Since the beginning of the 20th century, free trade and protectionism have emerged about every 20 years. The global economy is now once again facing a crisis of fragmentation." Indeed, with rising geopolitical risks induced by the Ukraine crisis, a broader trade and investment diversification must be achieved, even if it is not always optimizing or in line with market mechanisms. This is understandable, and for this reason, many companies are reassessing the location for their foreign investments. Now that China and Taiwan are labeled as high geopolitical risks, companies consider India as a promising business location. In terms of investments for the medium- to long-term (3 to 10 years), India now takes the top spot (at around 40%) overtaking China, the United States, and ASEAN.

Will we see another era of free trade lasting 20 years as the White Paper suggests? Nobody can predict but if we believe that history repeats itself, it is important for Japan to steadily advance and promote free trade where it can. One good example would be the expansion of the CPTPP (Comprehensive and Progressive Agreement for Trans-Pacific Partnership). The United Kingdom will join soon. Furthermore, some ASEAN countries are interested in joining and the US, which once withdrew from it, should reconsider and join, as suggested by a few US trade experts. If China accepts the established rules without exception, its participation in the CPTPP would be welcome. Finally, linking the CPTPP with the EU-Japan FTA would also be worth considering. These examples would sooner or later contribute to reinforcing the WTO rules.

Second, with regard to economic security, which is vague in definition, the White Paper points out that Japanese companies are lagging behind with less than 20% of them "making efforts" (11%) or "preparing to make efforts" (7%). As for specific measures, 56%, 48%, and 40% of respondents respectively selected "strengthening the information gathering function", "formulating a business continuity plan (BCP) in preparation for emergencies", and "formulating a company-wide common response policy". As for challenges in developing a system, "Difficulty in securing expert personnel" and "Difficulty in collecting relevant information" were selected by 54% and 52% of the respondents, respectively, indicating the need to find creative ways to secure personnel and collect information. Although the concept of economic security measures has just recently emerged, coordinated efforts by the public and the private sectors are urgently needed. As such, it would be necessary for the relevant ministries and agencies to hold explanatory meetings on economic

security and provide guidance to companies by dispatching specialists in the field, especially targeting the small and medium-sized enterprises (SMEs) which seem to face particularly difficult times.

Unfortunately, the White Paper does not go into sufficient depth for explaining economic security, and it is hard to identify what to watch for. For example, one country is currently presenting itself as promoting a "Dual Circulation" policy, with both "Domestic circulation" and "International circulation". "Domestic circulation" implies that the country aims to eventually produce domestically all its strategic goods, and to this end, this country strategically could utilize government procurement and subsidies against foreign companies. "International circulation" describes an increased interdependence that will eventually make the foreign country dependent and possibly subject to economic coercion.

At the end of July, the Japanese government tightened its export restrictions of semiconductor manufacturing equipment to a certain country. It is important for the Japanese people, as well as the implicated companies, to understand this background.

Third, a common international definition of "economic security" is desperately needed. The WTO has a "security" exception which means that countries do not have to abide by all the normal WTO rules. Because of the ambiguity in definition, the U.S. recently seems to have extended the meaning of this "security" exception to include "economic security". This, as well as with the WTO's over-zealous dispute settlement function, have been reasons for the U.S. dissatisfaction and the suspension of the dispute settlement function. A certain level of international common understanding on economic security is necessary. Since Japan continues to attach importance to the WTO, it should take the initiative to redefine the dispute settlement function and promote a common definition for "economic security".

Incidentally, the White Paper reminds us that there have been 131 major cases of economic coercion by China and Russia. It also mentions the agreement in the G7 Major Statement for countries to work together and establish a "coordination platform against economic coercion". This is precisely what Japan's initiative should aim for while incorporating the principles and rules of the WTO in its core.

Finally, although not mentioned in the White Paper, I would like to emphasize that in light of "economy security" it is important for Japan and the world to prevent a "Taiwan contingency" from occurring. As for specific measures to be taken on this subject, please refer to the Publishing/Chairman's Note in the March/April 2023 issue of *Japan Spotlight*. **JS**

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