

## **Japan's Foreign Policy for Economy and Japan-Korea FTA \***

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Good morning, Ladies and Gentleman. And thank you very much, Dr. SaKong Il, for the very warm and kind introduction and, also for the fact that you have invited me, on this occasion, for me to give some words on my thoughts on the issues before us, particularly on Japan's external economic policy, and on the Japan-Korea FTA.

But let me add a few words to what Dr. SaKong Il said in my introduction. In order to give you where the Japanese Foreign Ministry stands on external economic issues as he used the word economic diplomacy, we at the Japanese Foreign Ministry, sometimes we call it Gaimusho, always have had a very strong role in formulating and executing external economic policies. I might as well use the word term econo-diplomacy, to shorten economic diplomacy, for the way we deal with these issues in international affairs.

If you really look back at the history of Japan since modernization, we have always made strong efforts trying to integrate Japan into the international economy, and of course to be a contributor to the international economy, and therefore economic issues have always been a major concern on the part of the Japanese foreign policy, and therefore, the Japanese Foreign Ministry has always emphasized the economic part.

So I've noticed, in my years of being a diplomat that there are many foreign ministries of different types, and I would say Japan, Gaimusho, is one of the strongest in the area of econo-diplomacy. I've noticed that perhaps, Brazil has an even stronger role in their formulation in external economic policies. This bears out in the fact that when we negotiate the next WTO round, for instance, most of the governments are represented by trade ministers or trade negotiators, whereas in our case, we try to have the foreign minister involved as much as possible. But since he has other issues to cover, sometimes he has to delegate the responsibilities to other people. But in the case of Brazil, the foreign minister himself is heading the WTO negotiations. As for myself, despite the very nice review of my career, I'm not, A: an academic, much less an economist; B: not

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a businessman so I don't have any feel for business; C: I'm not a civil servant, like here in Korea civil servants are very powerful, but I never had much power, but I'm a diplomat. And perhaps an econo-diplomat, which is even worse than just ordinary diplomat because I don't deal with more serious issues of security, or I have not had much experience dealing with security issues or things like that.

But anyway, if we go back into the history of Japanese diplomacy, I'll skip the prewar years, because there's too much in it to cover, but also much to cover afterwards. Because of the change from the prewar times to the post war times, the econo-diplomacy has gained in its pre-eminence, even much more than the earlier times, because after the war, as I'm sure you know, we have given up the military as being one of the important instruments for diplomacy. So the focus had to be the economic side, and of course we had to focus our energies on economic development, post-war.

The immediate focus was to joining and contributing to international economic organizations, such as the GATT, IMF and WorldBank. In this sense, it was also important to a maintain strengthen economic ties with the US; the US being the critical factor and have the pivotal role in the post-war international economic system.

I remember when I was growing up in the early post-war years (my goodness, it shows how old I am), Japan was plagued by trade deficits. And of course if you have trade deficits, you cannot pursue the economic growth policies, because you will always hit the so-called "ceiling" of the trade deficit. But around the time I was getting out of college, it turned to register surplus. That's about in the middle of the '60s. In other words, Japan became a force to be reckoned with economically in the international community at around that time, in the mid to late '60s. And then of course, our very serious trade friction with the United States started. So those are the issues in the immediate post war years, or the immediate decades after the war, on which our economic diplomacy had to focus.

Now, let's look at Japan's basic structure of economic diplomatic posture. I think it should be seen in three layers. We have the global multilateral plane, and then we have the regional arena and of course the bilateral relationships. And, as we conduct diplomacy, all these three levels are conducted, at least in theory, in a manner mutually reinforcing. First, let's look at the global and multilateral level, and particularly the system that governs the economic relations between nations. Global and multilateral

economic institutions where rules are laid down to give structure to the global economy, are the anchor of the world economy, and therefore are given priority in Japan's econo-diplomacy

Most specifically, the IMF, which provides the foundation of international financial system, is one of the most crucial. Then the WTO, not because I worked on WTO issues, but because it is one of the very important systemic organizations, is considered to be the foundation of the multilateral trading system, which provides for the rule-based free-market oriented trading system.

I've noticed, as you have, that over the past years, if not decade or so, it seems like a fashion to promote bilateral arrangements *a la* FTAs. But I must stress at this point that Japan and Japanese econo-diplomacy remains committed to the multilateral trading system, which is embodied in the WTO, as the most crucial of all economic systems. As I will talk about a little bit later, we do pursue what we call Economic Partnership Agreements; or the FTAs, but these are done with the consciousness that they should be complementing the multilateral trading system, and to create further trade rather than divert trade through those kinds of bilateral measures. So if you look at what happened prewar times where people competed by creating economic blocs and the current situation where people are trying to forge FTAs or regional trade agreements and a certain amount of competition, there's a totally different background because we have now the WTO as the multilateral trading system, which forms the floor from which we try to improve through bilateral arrangements but if we didn't have the WTO or the multilateral trading system this would be a total mess.

So that's why we attach importance to WTO. It was created in 1995, and one of the major features is its quasi-judicial dispute settlement mechanism, this has changed the nature of trade conflicts, particularly among major economies, like between US and Japan, the US and the EU, or between the EU and Japan.

The importance of rule making together with the rule enforcing mechanism of the WTO, can never be overstressed. The world economy has seen its current success because of the free trade system in which most of the national economies have subscribed to, under, initially the GATT, and the WTO at the present.

If we look at the global plane, there's another area where Japan exerts a lot of efforts.

That is the coordination and cooperation among the developed economies, such as macroeconomic policies, as well as any global economic or social issues that are crops up as the world economy grows and becomes more complicated. For Japan the G8 process, as well as the OECD where all major developed economies assemble, are two main focuses of this kind of endeavor. I might mention that at the recent G8 finance ministers meeting in Russia I understand that the finance ministers invited their Korean counterpart along with those from other emerging economies in G8 finance ministers' outreach. I think this is a welcome development just as the Korean membership to the OECD. I see a few former ambassadors to OECD from Korea in my audience today.

Now let me look at the second plane, which is the regional. As I noticed that these days, there is much talk about what should the shape of the East Asian community be? Whether it will be written with a capital C or a small C, there is much debate about the East Asian community. And many people have looked to us as to what is the Japan's position on the future of the East Asian community. If I may, I would like to put the regional integration efforts in this region in a historical and geographic perspective.

As you know Japan has always considered the East Asian neighbors, taken together, as an important element for its own prosperity. When Japan decided to proceed provision of ODA, its focus was naturally on the region in order to contribute to the region's development. Japan could only thrive if the East Asian region was prosperous and peaceful. And economic development and democratization, are the buttresses to the relations between neighbors. Of course, our focus was, on one hand, North East Asia, and the other, South East Asia, to which much of our aid went.

I remember when I was a young junior diplomat; I had to work on this forum we created in the late 1960s reaching to the free market economies of South East Asia into a forum called the "South East Asian Economic Cooperation Ministerial Meeting". That's a reflection on how much we supported this region. Of course we had always supported ASEAN from its inception. And by the 1980 we saw the emerging four tigers, or four dragons, and then came the famous concept of the flying geese pattern. I'm sure you know these terms, I won't go into them. It should be remembered, I think, that in those times China was a political issue, not yet an economic power. It should also be remembered that Hong Kong and Chinese Taipei were two of the four dragons. Any East Asian regional economic forum would not have credibility unless they were included (they being Hong Kong and Chinese Taipei), due to their economic growth but

this led to a political issue because of the Chinese concerns.

Keeping these issues in mind, and trying to see closer integration being of an informal and thus flexible approach, which manifested itself in the form of the PECC initially as a nongovernmental forum, and then APEC. As you know, APEC was formed in 1989. By the way, I might add that the efforts to bring China into the WTO were realized, along with Chinese Taipei's membership, at the same time, which was in Doha Qatar in 2001. This aspect of how to treat Hong Kong and Chinese Taipei in regional economic forums should not be lost in the whole effort for East Asian community building, or networking among the East Asian economies through FTAs, because of the economic and trade and investment realities that involve these economic entities.

ASEAN plus 3 is a grouping we also give great importance to. ASEAN itself has a long history and its ministerial meetings were always followed by what we called the "Post Ministerial Conference" (PMC) with its dialog partners, Japan, and Korea, and China some of the major dialog partners.

So Asian plus three, combining ASEAN with Japan, China, and Korea, was started as a summit meeting in 1997. It now has under the leaders forum a number of ministers on specific functional areas such as trade and finance. As we strongly support the integration efforts of Asian 10, this ASEAN plus 3 forum is considered to be very important as a very effective mechanism to link our region, which is Northeast Asia, with Southeast Asia.

In East Asia one should not fail to mention the Chiang Mai Initiative adopted by ASEAN plus 3 finance ministers meeting in the year 2000 which is designed to make a network of bilateral currency swap arrangements. The same finance minister meeting in a different year, 2003, agreed to promote the Asian bond markets initiative. These are the initiatives taken by ministers of the ASEAN plus three, and Japan supports them.

Let me turn to the current talk about the East Asian community, particularly how it was discussed at the East Asia Summit in December of last year. Some people are wondering why there is a proliferation of regional economic forums, having a bearing on East Asia. To name a few, which I already mentioned, APEC, ASEAN plus 3 and now, East Asian summit, are all more or less looking forward to the forging of an East Asian community. You can also say that FTA negotiations with ASEAN as a regional grouping by each of

the “plus 3”, which connote Japan China, Japan and Korea, are adding to the regional efforts and creating not a confusing situation by overlap and maybe some inefficiencies. I’m also aware of those who say that the region should integrate in a manner like the EU or the region will risk losing leverage in a global context. In this argument, while I am a supporter of cooperation, I would think it would be wiser not to allow political arguments to dominate in an area of economics, which could result in a situation constraining the market oriented system and defeat the gains of better coordination, if not closer integration. In other words, it would serve us well to separate economics and politics. One must not forget that the international situation in the late 1940s and 1950s was in a unique way conducive to West European integration. It was the global economic and political situation in which Europe found itself sandwiched between the US and Warsaw Pact countries under the Soviet leadership where Western European countries felt the need to integrate and thrive collectively under the free market economy or risk being marginalized separately or individually if not absorbed by the Soviet bloc. Namely the old dictum of “hang together or hang separately” applied.

If we tried to translate the geopolitical dynamics that applied in West Europe in those days, do we here in Northeast Asia or in Southeast Asia have a comparable situation, particularly in Northeast Asia? Beyond the difference between the economic and political situation between the two cases, there are many differences making integration much of a distant goal. I will only cite one today, and that is the much greater divergence among the regional economies in terms of level of develop and economic maturity as well as economic endowment such as natural resources.

Just to cite one piece of data on this income disparity: While the European union countries between the higher and lower end of the spectrum on per capita income, I think, is about 2 times in other words; the highest has about 2 times the level of per capita income compared to the lowest; but if we look at East Asia, even taking Japan out of the scene for a moment, the higher end is almost 60-70 times that of the poorest. If we include Japan it becomes 100 times difference. So on top of this, of course, I need not mention the political difference among East Asian countries, particularly Northeast Asia. This means tremendous difficulty if we try to seek real integration. So while as a politics and symbolism the notion of East Asian integration is important, one needs to assess the economic realities on the ground to see how feasible this is in the near future. So then, what is Japan’s position on the question of East Asian cooperation? We have always espoused the notion of open regionalism. Any regional integration efforts should

never undermine the international global multilateral system underpinning the international economic trade system, which brings us enormous benefits. To discard this multilateral system and give priority to integration at the expense of multilateralism would be a great disservice to our own economies if not the world economy as a whole.

To put in a very simple formulation, there are 3 pillars under which we are guided as Japan pursues East Asian community building. One as I said, is open regionalism. Two, functional cooperation: This means we should not shoot for institution building, but try to find areas where we can cooperate and build on them. Three, upholding shared values like democracy, human rights, and also international rules like those embodied in the WTO. I might also add that ensuring ASEAN's role as an organization or a regional body, as well as a continued involvement of the US in the East Asian region are further considerations we always keep in mind.

Now, let me come to the third layer of Japan's econo-diplomacy. This level comprises the bilateral approaches. Let me just quickly talk about Japan's basic policy on the FTA or how it developed. Unfortunately or fortunately, I was partially responsible, maybe some say culpable, for moving Japan away from the purist multilateral trading system only economic diplomacy policy of Japan. As I said at the outset, we give much importance to WTO and GATT preceding it, because we thought that would be the best way to produce benefits, not only to Japan, but also to the world economy. But somewhere along the line we digressed from this basic policy and pursued an FTA, first with Singapore, which was signed in 2002. I was not involved directly in the negotiations, but I was involved when we decided to seek out the possibilities of a possible FTA with Singapore in the late 90s.

At that time, (if I had time) I could recall now much difficulty trying to persuade the purists within Gaimusho, and I had lots of resistance.

But at that time, when I was in that position, I gave a few reasons why I thought FTA with Singapore it important. I'll come to that whenever necessary, but not now. At the same time, I thought the next plausible candidate would be Korea. I was involved in seeking this avenue as well. To be honest, I didn't think Mexico should be given priority. But our business people had different priorities, and business people pushed very hard for an early FTA with Mexico and now we do have, after Singapore, an FTA with Mexico. In any case, where do we stand on FTAs? Sometimes we go beyond FTAs and

we seek what we call Economic Partnership Agreements. The difference between EPA, Economic Partnership Agreement, and FTA is that we aim to create trade and economic goals transcending international borders, and much broader coverage than an FTA, going beyond the national border measures and for much more intrusive contents. I would like to cite this basic stance taken by this government in 2004 on this notion, which is embodied in a document called “The Basic Policy Towards Further Promotion of Economic Partnership Agreements.” This basic policy recognizes that against the background of globalization, EPAs compliment the multilateral free trade system centering on the WTO and simultaneously facilitate the promotion of structural reform of Japan and its partners and therefore an effective means for fostering the establishment of an East Asian community.

In addition, in identifying countries to negotiate with, based on the current state of economics relations with the proposed partners the basic policy states that the government will review possible alternative measures of economic partnership such as conclusion of investment agreement, or mutual recognition agreement, MRAs, as they are sometimes called, and an improvement of the investment environment. The basic position can therefore be seen as an attempt to formulate rules that accord with reality prevailing between countries concerned and respond with flexibility.

Let me just go down the list of negotiations which we are now pursuing in the area of EPAs or FTAs, as I said, we have already concluded one with Singapore and Mexico, and we have already signed one with Malaysia. We also have signed an agreement with the Philippines and will be signing soon with Thailand. Negotiations with ASEAN as a group are ongoing. We are now talking about the possibility of negotiating with India.

Some of you might wonder what our stance is with China. Of course, there has been much study conducted by private sector on this question. We feel that it may be more practical to first conclude an investment agreement, which would emphasize the development of business environment and liberalization of investment. We are still discussing these issues.

Now before I turn to our relations with Korea, let me quickly give you an overview where we stand in our bilateral relations with the United States. Let me just quickly introduce our experience with the Americans after the WTO was established and became a useful forum to resolve trade disputes with much less political friction.



I recall that when I was involved in the 70s, dealing with trade with the Americans, it was always a very tense and serious friction we would experience at times with the Americans over trade issues. We can remember the citrus negotiations; or beef negotiations; or TV(monitor) negotiations; or automobile negotiations. I think the automobile negotiations were the most serious, and the last before the WTO. It was resolved just as WTO was established, and the usage of the dispute settlement process was an element in the resolution of the issue.

After that, because of the WTO and its dispute settlement mechanism, much of the friction has gone from these trade issues with the US. But in the 80s, our negotiations with the Americans went beyond normal trade negotiations and became more intrusive going beyond border barriers like tariffs and IQ. And one forum was called (the name itself is almost self-explanatory): the “Structural Impediments Initiative,” meaning we were trying to resolve addressing the “impediments” of a structural nature in the economy of both sides, but from the Americans’ point of view, particularly in the Japanese economic structure.

When the Clinton administration came into office in 1993 and after a couple years of difficult times on such issues as numerical targets, most things got settled down, and people started talking in terms of deregulation dialogue, which was run in conjunction with the internal, domestic, restructuring measures in Japan. The deregulation dialogue was in fact not in fact a dialog but negotiations. It dealt with domestic regulations. I might just turn quickly to the European Union, with which we also had the deregulation dialog, but we also negotiated an MRA, Mutual Recognition Agreement. So if one looks at the areas of financial and telecommunications services, for instance, the scene prevailing at present in Japan is so dramatically different from 15 years ago. These areas have been readily been deregulated and currently many foreign companies compete with Japanese companies on Japanese soil bringing much needed efficiency to the Japanese economy.

Now let me turn to the most important question, Japan and Korea. Before exploring where we are on the FTA, let me put Japan and Korea in the context of the global and regional economic planes. In the global context, Korea is the number ten economy. And of course this ranking would go up higher if we considered the EU as one economic unit, and take away the individual EU members. Therefore Korea should by all means be an

economy taking leadership roles as it has already done in this economic scene.

Thus Korea has a great role to play in maintaining the world economic institutions, WTO, IMF etc. And I have had the pleasure throughout my career of working very closely with the Korean diplomats on WTO issues.

Japan and Korea have always worked closely, as I said, in WTO and other international economic organizations. On global issues, the emerging global issues, we have much to cooperate. In the past, Japan and Korea had a dialog forum at deputy ministers' level. The agenda of which encompassed broad issues included issues of global nature, like energy and the environment. When I came to this post, I realized that because the two governments had been working on FTA and so much human resources had been devoted on this particular element or aspect of the relationship, the broader economic dialog had practically been put on hold. When the FTA negotiation itself was put on hold, there was no longer any channel on the deputy ministerial level, to see all issues facing the two countries on a more coordinated and global fashion.

Last week on Monday June 12, our deputy foreign minister, Mr. Yamanaka, came informally to engage in talks with his counterpart. The talks between the two have been warm and forward looking and very constructive, and positive, and were very promising.

Take energy: the current focus seemed to be the supply security, but we should also work together worldwide for the efficient use of available energy by focusing on the demand side as well, and this area of energy, as well as the environment, are the areas where Japan and Korea can work closely together to contribute to the global efforts.

So there is much to be done by the two on global issues, and we can work together and also have China involved in a threesome effort in these areas. In the regional context Korea and Japan are both members of APEC, ASEAN plus 3, and the recent East Asian Summit and we have been working very closely in forging the East Asian community. If you look at the ASEAN plus three, its share of the global GDP is around 19.2%, but the share of the three Northeast Asian economies is about 17.3% (I'm using a little bit outdated '03 data). This means that the three countries' share in total East Asian GDP is about 90%. So the figure speaks for itself. Of the Northeast Asian Three, China, which is growing extremely rapidly, provides tremendous opportunities not only for East Asia, but the whole world. While in the ASEAN plus 3, East Asian Summit, APEC or other

regional forums, China has become a very active member and contributes greatly, there are still much we can do to contribute to China's smooth integration into the international economic system. Its membership in WTO in 2001 was a great step forward, in this regard. Much more can be done in cooperation with China in improving its market governance such as the question of intellectual property rights protection, and fostering a more predictable business environment for foreign businesses. Situated next to China, Japan and Korea are the most natural partners sharing basic values, basic politic system, economic structure, and you name it.

In talking about regional integration, people often compare Northeast Asia with the European Union, or say that what has been achieved in Europe should be the reference point in the Northeast Asian region. My view is that because of the similarities between the two in both the economic and political senses, it might be better to compare region of Northeast Asia with the North American experience. If you look at North America, we now see only the NAFTA, but we must remember that before Mexico became involved, the US and Canada had FTA based on the experience of the Autopact, or the Automotive agreement. So I say, wouldn't it make better sense for Japan and Korea to seek EPA or FTA, and further integration as the core of the broader regional integration? And then, can't we pursue closer cooperation, coordination on an EPA/FTA, including others?

If we keep the future East Asian community as a system based on open regionalism, then it will be important to maintain close ties with the United States as the anchor for the world economic structure. In this context, the current work by Korea on FTA with the United States is highly commendable. KORUS, as I have learned that you call this FTA, is needed not only for the two countries, particularly Korea, but would have a very positive impact on Japan-Korea economic ties, help the integration moves in the context of Northeast Asian community building, and for world economy as a whole.

In view of KORUS efforts, natural flow of thinking will come to the question of why not Japan FTA with the United States. While I do not necessarily have a determined view, as I explained above, two or three decades of Japan's trade relations with the United States, and particularly the most recent intrusive negotiations on the regulatory framework, we already have a situation normally brought about by an EPA. Add to this consideration the fact that if the two largest economies had an EPA or FTA what would become of the WTO? Because Japan and the United States are such large economies, it

is difficult to balance out new (trade) concessions to each other just between the two.

It may be more feasible to balance out in the global negotiations, i.e. the WTO trade. Japan, while needing to work more, already have a rather intrusive relationship achieved over the years with the United States, if without a formal all encompassing agreement. We will have achieved a virtual three-way FTA when the Japan-Korea FTA, or EPA, whatever the name is, is concluded. So we should not let the opportunity of a Japan-Korea FTA slip by. I am much heartened to learn that of late, business leaders of the two countries have become more vocal in calling for the early resumption and conclusion of the Japan-Korea FTA. I am hoping that these moves will soon lead to resumption of our negotiations, and lead to a result that will be beneficial to our relationship, not only economically, but econo-diplomatically as well.

Let us once again look at the global economic political structure. Based on the market mechanism, it has a three-layered structure. There is the bilateral relationship particularly between geographically close neighbors with sharing common values and perspectives. At another level, there are multitudes of regional forums, such as the East Asian summit and APEC to which Japan and Korea belong. And beyond the region there are global institutions like the WTO and IMF, and OECD. If we, Japan and Korea, see ourselves as the focal point of concentric circles, created by these layers of economic platforms, forums, organizations, and institutions, it seems obvious that strengthening economic integration with the solid framework in the form of an EPA or FTA should be the path the two nations pursue for the two to jointly contribute to the region as well as the global economic prosperity.

### Questions & Answers

**[Q]** First of all, Ambassador, thank you very much for this very interesting and informative talk. My question is a very obvious one: You made many positive observations towards the Japan–Korea FTA, but why is it stuck, what are the stumbling points, and how can they be relieved?

**[A]** The reason I didn't go into that part is because that is a very difficult and sensitive part of the whole issue. About a year and a half ago the two negotiating teams met and sort of exchanged some information as to where each side stood. And the Koreans said

our offer on agriculture is too low. Of course we have a totally different perspective, we think we had a sufficient level of ambition, a level of concessions. So we are always ready, if the Koreans are ready to come back to the table. Having had experience in trade negotiations for some years, for the past decade or so, and particularly having had the experience of working with the Korean counterparts, my very close friends in the WTO context, and we all know how agriculture is very sensitive and difficult. So my sense was that my 'good old friend' counterpart negotiators would be able to understand where we stand on agriculture, and why we are doing this, and that, when we sit down, we are willing to negotiate even on agriculture. I didn't go into the experience with Mexico when we negotiated the FTA, but at the end it became a most difficult part, when we negotiated agriculture. It went up to the ministers level, and ministers came to sit down a number of times before they reached a compromise. What I'm saying is that we are willing to negotiate even agriculture. If it takes to concede on some very important points, we will do so. But of course, it's a negotiation, so we have to sit down and make the concessions. Unless you sit down and negotiate, we cannot move. So, it is a matter of negotiation style, in my view, why we got stuck, and not of substance.

[Q] I would like to ask this question: Why is the negotiation between Japan and Korea on FTA stopped? What are the differences, and why should the negotiation begin again? What are the benefits both countries can get from restarting the FTA?

[A] As I said, the basic difficulty we are facing on surface is in the area of agriculture. But as I said, it is not necessarily that particular area, but the negotiating style, because Japan has always negotiated agriculture in the context of FTAs, or more importantly, in the context of the WTO. So when we are asked to concede in the area of agriculture upfront, it becomes difficult, but once we sit down across the table, and specifics are negotiated, I think we will be able to negotiate. Those are the sticking points. What are the benefits? I think this is very obvious. Two economies, so close, so intertwined, if we do negotiate and liberalize further in the remaining areas, the two stand to benefit. As I try to picture the whole relationship in the global context, going beyond regional context as well, we have much more to gain than otherwise if we pursue the free trade agreement.