

## ANALYSIS OF JAPAN'S EXISTING AND FORTHCOMING FREE TRADE AGREEMENTS IN THE ASIA – PACIFIC AND GLOBAL CONTEXT

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### Abstract

*The paper analyzes the rise of interest for free trade agreements and economic cooperation agreements following the failure of Doha Round and the different impact of the economic crisis on various countries and regions, focusing on the participation of Japan to such agreements. Given the high economic dynamism of the Asia – Pacific area the interest for finding operational solutions for trade facilitation is even higher than in other parts of the world economy. More initiatives that aim at supporting trade and cooperation among the countries in the area are under way and they contribute in various forms to the economic integration of the participants. The conclusion of the paper is that the current trend towards free trade agreements does not represent a dispute between multilateralism and bilateralism in international trade but an imperfect quick fix for something too important to be postponed (that is the regulation of international trade). In our opinion is that despite a certain level of duplication of efforts these initiatives represent in fact building blocks for a future multilateral framework with global scope.*

**Key words:** free trade agreements, economic cooperation agreements, world trade, post Doha Round, Regional Comprehensive Economic Partnership (RCEP), Trans – Pacific Partnership (TPP), ASEAN plus Three – APT, Free Trade Area Asia – Pacific (FTAAP).

**JEL classification:** F13, F42, F53

### The global economic context and its implications on trade

The current decade (2011 – 2020) of the world economy has started under less auspicious signs of an ongoing crisis although the scope and significance of that crisis give way to numerous interpretations. While such interpretations on the economic crisis are not the subject of this paper, suffice is to make two comments. **The first comment** result from the analysis of the International Monetary Fund data for the world domestic product year on year change during the 1980 – 2013 period. This

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analysis reveal that during a time span of 34 years in just only one year there was a negative growth: in 2009. And even in 2009, at the level of world economy as a whole the negative growth was of only - 0.59 % in constant prices and a bit higher in market prices: - 2.151%<sup>2</sup>. Under such circumstances one can hardly speak about a crisis at the level of the whole system of the world economy. At the same time, the projections of the International Monetary Fund from 2014 till 2018 indicate for the world domestic product a continuation of growth in the range of 4.404 – 4.489 % .

**The second comment**, which is based on the first one, refers to the rather differentiated economic dynamics of the main groups of countries within the world economy, differentiation that has led to changes at least in the global balance of economic power. This comment is supported by the fact that even in 2009 when the world domestic product expressed in constant prices contracted with 0.59 %, the developed countries contracted with 3.47 % and the Euro zone with 4.387 %, while the developing countries registered a growth of 2.668 %<sup>3</sup>.

The conclusion based on these two comments is that in the long run and also in perspective the world economy is functioning well. At the same time, the relative importance of the main players is changing. In this context it is noteworthy that in 2010, just at the time border between the first and the second decade of the 21st century a change took place in the sense that China became the second largest economy, thus replacing Japan that had hold the second position for almost 40 years, since the 1970s<sup>4</sup>. The spectacular evolution of China's position in world output has been matched by its position in world exports: from 1 % in 1980 to 11 % in 2011. Also as result of the changes in the economic balance of power of the world, by the end of 2010 China became the 3<sup>rd</sup> largest member country in the IMF and four emerging economic powers (Brazil, China, India and Russia) are among the top 10 largest shareholders in IMF<sup>5</sup>.

The change in the relative importance of global players can also be found in international trade. In 1980 the developing countries represented just 34 % of world exports while in 2011 their share rose to 47 %.

As regards the correlation between the economic output of the world economy (expressed by GDP) and the evolution of international trade we can note that in the past 27 years there a permanent growing trend of the ratio of world exports to world GDP, trend interrupted only in 2009. After 2009 world trade returned rather fast to the pre-crisis levels. The growing trend of ratio of world exports to world GDP is reflected in Figure 1.

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<sup>2</sup> International Monetary Fund, World Economic Outlook Database, April 2013, at <http://www.imf.org/external/pubs/ft/weo/2013/01/weodata/download.aspx>

<sup>3</sup> Idem.

<sup>4</sup> David Barboza, China Passes Japan as Second Largest Economy, The New York Times, August 15, 2010

<sup>5</sup> Factsheet IMF Quotas, March 31, 2013 at <http://www.imf.org/external/np/exr/facts/quotas.htm>

**Figure 1. Ratio of world exports of merchandise and commercial services to world GDP, 1980-2012 - ratio of current \$ values**



**Source:** World Trade Organization, World Trade 2012, Prospects For 2013, Press Release PRESS/688, 10 April 2013

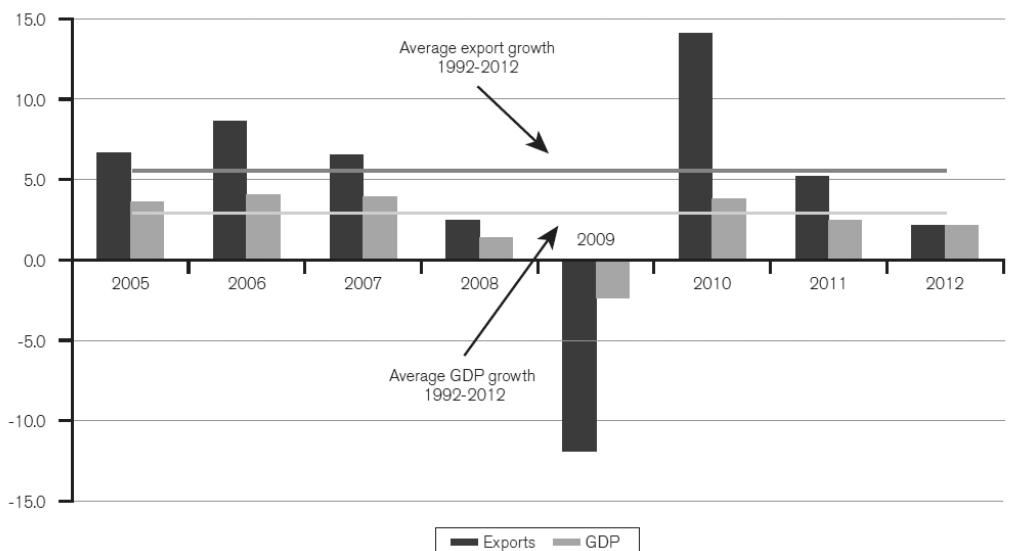
The growing trend in the ratio of world exports to world GDP was possible due to the much faster growing rate of world trade as compared to world GDP. According to World Trade Organization, for the period 1980 – 2012 world trade has grown on average twice as fast as the world GDP. This very impressive evolution materialized into an average annual growth rate for trade in goods of 7 % for the period 1980 – 2011 and even higher, of 8 % for the average annual growth for the trade in services<sup>6</sup>.

This phenomenon is explained by the elimination of numerous tariff and non-tariff barriers from the international trade flows but also by the impact of globalization, and particularly by the impact of the activity of transnational corporations that allowed the connection to world economy economic circuits almost all parts of the globe.

At the same time, this faster growth of world trade as compared to world GDP made much larger the amplitude of variations for the year on year evolution of the trade flows as compared to GDP levels. This is particularly evident in case of decline registered in 2009 by both world trade and world GDP and the subsequent resuming of growth. This difference is reflected in Figure 2.

<sup>6</sup> World Trade Report 2013 – Factors Shaping the Future of World Trade, World Trade Organization, [www.wto.org](http://www.wto.org)

**Figure 2. Growth in volume of world merchandise trade exports and GDP for the period 2005 - 2012**



**Source:** World Trade Report 2013 – Factors Shaping the Future of World Trade, World Trade Organization, [www.wto.org](http://www.wto.org)

### **World trade: from the Doha Round to a growing interest for free trade agreements**

The dynamics of world economy represents a mirror reflection of the state of the world trade and, at the same time, of the state of globalization. If globalization is ever more present and world trade grows also, then the world economy is growing too. The correlation among the three elements is direct and evident in all directions. A logical result of this correlation is that international cooperation in one form or another is needed in order to find the dynamic balance of interests among numerous and diverse participants<sup>7</sup>.

Therefore the well functioning of world trade presents a keen interest for all participants as the well being of the vast majority if not all of them depends in various degrees on the world trade. The participants to world trade are of various economic sizes and they may have different perspectives and interests but all these refer more to the “how” of participating to international trade, rather than to the “why” of participating to it.

Under these circumstances, the launch of the Doha Round of trade negotiations in 2001 was accompanied by ambitious goals referring at the same time at the large scale liberalization and regulation of international trade<sup>8</sup>. According to some

<sup>7</sup> World Trade Report 2013 – Factors Shaping the Future of World Trade, World Trade Organization, 2013

<sup>8</sup> Doha WTO Ministerial Declaration, WT/MIN(01)/DEC/1, 20 November 2001

estimates made during the negotiations the success of Doha Round would have generated at a global level potential gains of about 280 billion \$ per year<sup>9</sup>.

While such an association of terms may seem absurd (“liberalization” and “regulation”) in fact it is not while the “liberalization” part refers to eliminating obstacles from the normal flow of international trade, while the “regulation” part refers to the common understanding of terms and procedures as well as to common approaches to various trade issues.

But 12 years later it is a common fact that the Doha Round failed for many reasons among which there are often mentioned the large number of participants as well as the strict observance of the principle “Nothing is agreed until all is agreed”. Given the diversity of participants to negotiations the combination of the two aspects has been an almost perfect recipe for failure.

Despite the failure of Doha Round, the world trade continued and all participants are looking for alternatives for world trade regulation that maybe less ambitious but anyway operational.

More and more a partial solution emerges internationally under the form of **Free Trade Agreements**. Although free trade agreements have been traditionally bilateral agreements, in practice one can find two situations:

- **Free trade agreements as such** that involve usually two parties (two economies). There are cases when there are more than two parties involved but each of them is an economy. Examples of this type can be: the Japan – Mexico free trade agreement in force since April 2005; the United States – Singapore free trade agreement in force since January 2004. An example when there are more than two participants but all of them are countries is the North American Free Trade Agreement where the participants are the United States, Canada and Mexico.

- **Free trade agreements where at least one of the parties is represented by an organization of economic integration that includes several countries**. In such a case the agreement is still bilateral from a theoretical and legal point of view, but, at the same time, the agreement is multilateral so far as the number of involved parties is concerned. Examples of this type can be: The Free Trade Agreement China – ASEAN, in force since January 1, 2010 which is on the 1<sup>st</sup> place in the world as regards the number of population involved and on the 3<sup>rd</sup> place in the world as regards the cumulated GDP of the participating countries. Another example is the Free Trade Agreement European Union – South Korea in force in a provisory format since July 1, 2011. This agreement is on the 2<sup>nd</sup> place in the world after the North American Free Trade Agreement – NAFTA from the point of view of the cumulated GDP of the participating countries.

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<sup>9</sup> Workshop On Recent Analyses Of The Doha Round, 2 November 2010, Geneva, at [http://www.wto.org/english/news\\_e/news10\\_e/dda\\_brochure\\_nov10\\_e.pdf](http://www.wto.org/english/news_e/news10_e/dda_brochure_nov10_e.pdf)geneva

In 2013 there is an increasing number of negotiations under way regarding free trade agreements. What is of particular importance is that these agreements involve the largest players from the world economy. As result it is expected that the outcomes of such agreements will significantly influence the whole world economy. Among the most important of these agreements currently under negotiation there are:

- \* European Union – USA;
- \* European Union – Japan;
- \* European Union – India;
- \* European Union – MERCOSUR;
- \* Regional Comprehensive Economic Partnership;
- \* Trans - Pacific Partnership.

### **The position of Japan vis-à-vis regional and world wide free trade agreements**

As an important economic player in the world economy Japan granted particular attention to improving the international trade regulations that may influence its export and import performance. This is why Japan has free trade agreements with its economic partners and participate in negotiations for multilateral free trade agreements in its region and world wide.

As of August 2013 Japan had numerous free trade agreements (FTA) and economic partnership agreements (EPA) which can be classified into three categories<sup>10</sup>:

- **Concluded** with Singapore, Mexico, Malaysia, Chile, Thailand, Indonesia, Brunei, ASEAN, Philippines, Switzerland, Vietnam, India, Peru,
- **Under negotiations** with Australia, Mongolia, Canada, Columbia, Japan – China – Republic of Korea, European Union, Regional Comprehensive Economic Partnership (RCEP), Trans-Pacific Partnership (TPP), Gulf Cooperation Council (GCC) - suspended.
- **Pre-negotiating** with Turkey.
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The geographical distribution of these free trade agreements (FTA) and economic partnership agreements (EPA) of Japan as of July 2013 is presented in Figure 3.

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<sup>10</sup> Ministry of Foreign Affairs of Japan - Free Trade Agreement (FTA) and Economic Partnership Agreement (EPA), July 2013, at <http://www.mofa.go.jp/policy/economy/fta/index.html>

**Figure 3. Free trade agreements (FTA) and economic partnership agreements (EPA) of Japan**



**Source:** Ministry of Foreign Affairs of Japan, July 2013

### **The importance of Japan – ASEAN free trade agreement**

From the point of view of the concluded free trade agreements of Japan the one with ASEAN is of particular importance due to the current economic significance of ASEAN in the Asia – Pacific context and particularly due to the prospects of further free trade agreements that include ASEAN.

The Association of South East Asian Nations (ASEAN) has been established in 1967 and include a free trade area - **ASEAN Free Trade Area (AFTA)**. ASEAN has now ten member countries: Brunei, Indonesia, Malaysia, Philippines, Singapore, Thailand, Vietnam, Laos, Myanmar, Cambodia. Besides economic integration and cooperation ASEAN has other two objectives related to security and socio-cultural integration.

The cummulated population of ASEAN countries in 2012 was of 615.6 million people (8.8 % of world population) while the combined nominal GDP was of about 2400 billion US \$. In 2012 if ASEAN would have been a country, it would be ranked four in the world after USA, China and Japan<sup>11</sup>.

ASEAN has concluded free trade agreements with its main economic partners from the region:

- Japan (in 2008);
- Australia and New Zealand (in 2009);
- China, India, South Korea (in 2010).

Given the high economic dynamism of the countries in the Asia – Pacific area new and more flexible forms of trade related consultations have been established. One of them is the so called **ASEAN Plus Three – APT** forum that reunites ASEAN countries plus China, Japan and South Korea.

<sup>11</sup> Based on data from International Monetary Fund database.

ASEAN Plus Three forum started its activity in December 1997 and has been institutionalized in 1999. The meetings of the Forum are attended by prime ministers, ministers and other officials from the member states that consult each other and aim at coordinating the activities in an ever growing number of fields among which energy, transport, information technology and communications.

In 2012 an even more complex and large free trade agreement initiative has been launched in the Asia – Pacific area. The project that has been launched in December 2012 is called **Regional Comprehensive Economic Partnership (RCEP)** and it is expected to become the largest free trade area in the world. The negotiations involve the 10 ASEAN member states plus the states which already have free trade agreements with ASEAN, namely Japan, Australia, New Zealand, China, India, South Korea. The negotiations started in 2013 and are expected to finish in 2015.

The RCEP project has been launched in 2011 based on two different proposals for regional free trade agreements that existed at that time:

- The **East Asia Free Trade Agreement** that was supported by China and included the ASEAN member countries, China, Japan, South Korea;
- The **Comprehensive Economic Partnership in East Asia** that was supported by Japan and included ASEAN member countries, Japan, India, Australia and New Zealand.

In order to reconcile the two proposals and to start negotiations, ASEAN (which was a member in both proposals) suggested the RCEP and this has been accepted by all parties.

The importance of RCEP is given by a number of economic data:

- The cumulated GDP of the member countries is of about 17000 billion US\$;
- The cumulated population is of about 3 billion people;
- The trade carried out in the area represents 40 % of world trade;

At the same time, the RCEP has a substantial significance for the world economy as it is much more than a free trade agreement. RCEP includes trade with commodities and services, but also investments, technical and economic cooperation, intellectual property competition issues as well as dispute settlement.

At the same time, another characteristic which is very important from an operational point of view is that RCEP provides for a flexible approach which allows members (particularly less developed countries) to avoid or postpone the regulations that are not in their favor.



The role of Japan in the establishment of RCEP is more than its simple presence as a member state or because it is a developed country. The role of Japan is also conceptual in the sense that the first proposal for the establishment of a **Trans-Pacific Free Trade Agreement** was made by the Japanese economist Kiyoshi Kojima in 1966. Although that idea was not accepted at that time, it had a major contribution in the establishment of the **Pacific Trade and Development Conference** in 1980 and then of the **Asia Pacific Economic Cooperation (APEC)** in 1989.

It is interesting to mention that RCEP is not the only initiative for a free trade area and economic cooperation in the Asia – Pacific region. Another current initiative is that of the **Trans – Pacific Partnership - TPP**.

The starting point for the Trans – Pacific Partnership as a project was represented by the **Trans-Pacific Strategic Economic Partnership Agreement** (known also as **TPSEP** or **P4**) which is a free trade area having as members Brunei, Chile, New Zealand and Singapore that started in 2005 and in force since May 2006.

Since 2010 a larger number of countries than the members of TPSEP started negotiations on TPP. The countries involved are: Australia, Brunei, Chile, Canada, Malaysia, Mexico, New Zealand, Peru, Singapore, USA, Vietnam. Japan joined the negotiations since April 2013. Different from RCEP, the TPP has very comprehensive and ambitious goals which lead to the conclusion that this project can not be finalized in the near future.

Because all the countries in the Asia – Pacific are aware that the more comprehensive the proposed agreements are, the more difficult is to finalize them, there is even a third project, besides RCEP and TPP, which is larger as number of countries involved and less ambitious as goals and there easier to be achieved.

This third project is proposed by the Asia – Pacific Cooperation Forum (APEC). The importance of APEC which has started in 1989 and has now 21 member states comes from the fact that it represents 40 % of world population, 56 % of world GDP and 48 % of world trade. The APEC member states are: Australia, Brunei, Canada, Chile, China, Hong Kong, China, Indonesia, Japan, South Korea, Malaysia, Mexico, New Zealand, Papua New Guinea, Peru, Philippines, Russian Federation, Singapore, Chinese Taipei, Thailand, United States, Vietnam.

This third project is called the **Free Trade Area Asia – Pacific (FTAAP)**. The interest for this project has been determined by the failure of Doha Round but also by the fact that in the Asia – Pacific region there are in force 60 free trade agreements and 117 under negotiation. This huge number of agreements as well as the complex economic interactions generated by transnational corporations and globalization determine many overlapping and contradictions (the so called spaghetti bowl effect) that negatively affect business in the region.

## Conclusions

The free trade agreements, most of them established on a regional basis (that is involving countries located in the same geographical region, even in a broad sense, such as Asia – Pacific area) have increased their importance in the past years.

This trend can be, at least partially explained, by two factors that relates to the importance of international trade for most economies and to the different impact of the economic crisis that started in 2008 on the economies of the world.

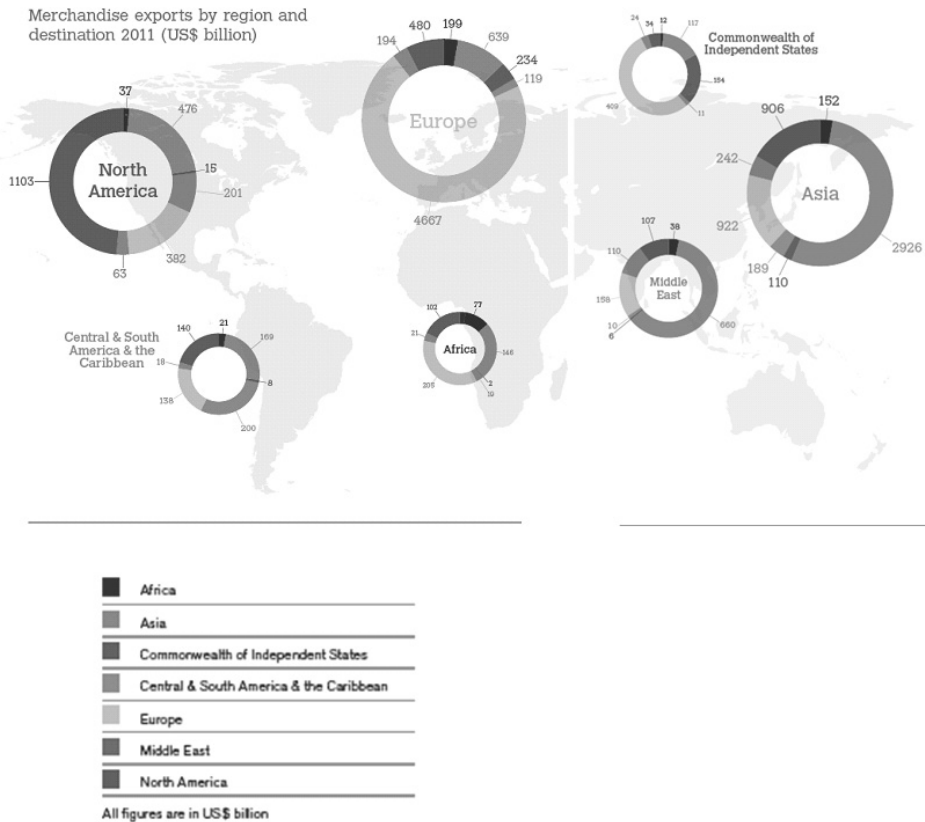
The first factor is represented by the failure of the Doha Round. As world trade is a very intense and large scale economic activity, vital for the well being of the vast majority of economic actors from the world economy, solutions for the support of further development of world trade are continuously searched. For purely pragmatic reasons this activity is carried out both within the framework of World Trade Organization and on a bilateral or multilateral basis, involving either countries located in the same region or countries with intense trade relations. In this respect one can note that the more intense the trade relations among certain economic partners the more likely the establishment of various formats of free trade agreements and economic cooperation agreements. Although some authors<sup>12</sup> present this trend towards free trade agreements as a weakening of the World Trade Organization and multilateral regulation of international trade in our opinion there is no real confrontation between multilateralism and bilateralism in international trade. In our opinion the current trend towards using free trade agreements is just a quick fix for something (that is international trade) too important to be postponed.

The second factor that currently supports free trade agreements is represented by the impact of geographical proximity on the intensity of trade relations. One reason for this is obvious, it refers to distance: it is easier and cheaper to trade on short distances rather than on very long ones. The other reason refers to the (usual) higher economic, political, social compatibility of economies situated in the same region. As region is an ambiguous term we can speak about narrow and large defined regions. Examples of narrow defined regions that led to free trade agreements or even customs unions are: Benelux (involving Belgium, the Netherlands and Luxembourg) or NAFTA (involving Canada, United States and Mexico). Examples of large defined regions that led to free trade areas or customs unions are: ASEAN, European Union, Asia – Pacific free trade agreements such as Japan – India. This significance of the regional dimension of international trade as compared to the extra regional trade has been presented by the World Trade Organization in the International Trade Statistics 2012<sup>13</sup> and it is reflected in Figure 4.

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<sup>12</sup> Corina Berceanu, Why has the unsuccessful Doha round resulted in bilateral and inter-regional FTAs and what are the consequences for global trade?, January 16, 2013, [www.geopolitics.ro](http://www.geopolitics.ro)

<sup>13</sup> International Trade Statistics 2012, World Trade Organization, [www.wto.org](http://www.wto.org)

**Figure 4. Merchandise flows within regions outperform flows between regions**

**Source:** International Trade Statistics 2012, World Trade Organization, [www.wto.org](http://www.wto.org)

From Figure 4 results in a very graphical manner that in North America, Europe and Asia the trade flows within regions are larger than flows between geographical regions. This very factor influences in our opinion the establishment of free trade areas or economic cooperation agreements based on regional economic flows.

In our opinion, gradually globalization will led to the increase of trade flows between regions and that, in its turn, will lead to more free trade agreements between partners located in different regions.

This aspect can be clearly seen in we take the case of European Union. As of August 1, 2013 European Union has been involved in 27 free trade agreements negotiations which are in various stages, among them with USA, Canada, Japan, India, MERCOSUR, Andean Community<sup>14</sup>. A map of the European Union existing and pending free trade agreements is presented in Figure 5.

<sup>14</sup> European Commission, Overview of FTA and other trade negotiations, updated as of August 1, 2013, at <http://ec.europa.eu/trade/policy/countries-and-regions/agreements/>

Figure 5. European Union Free Trade Agreements as of August 1, 2013



**Source:** European Commission, Overview of FTA and other trade negotiations, updated as of August 1, 2013, at <http://ec.europa.eu/trade/policy/countries-and-regions/agreements/>

The interest for free trade agreements is the more so important in the Asia – Pacific region, an area which is particularly dynamic from an economic point of view. The area was much less affected by the economic crisis that started in 2008 and it is regarded as the most important economic area in the world economy for the next 50 years. The fact that the regions include China, India, but also United States and Russian Federation explain why the economic center of gravity of world economy has shifted from the Atlantic to the Pacific area. The Asia – Pacific area will represent a major area for the world economy of the 21<sup>st</sup> century, based on a multi-polar model. This high economic dynamism is also reflected in the number and scope of discussions in the area related to establishment of free trade areas.

In the context of Asia – Pacific area Japan plays an important role both as an economic power (now on the third place in the world) but also as the member and conceptual founder of the existing or under negotiations free trade agreements. Japan has already in force free trade agreements with its economic partners in the region

(ASEAN, India, Philippines, Thailand, Indonesia, Malaysia) and is negotiating agreements with other key player both in the Asia – Pacific area (China, South Korea, Australia) or in the world (with European Union, Canada).

Japan is also part of all free trade and economic cooperation multilateral initiatives in the region: ASEAN Plus Three – APT, the Regional Comprehensive Economic Partnership (RCEP), the Trans – Pacific Partnership – TPP, the Free Trade Area Asia – Pacific (FTAAP).

The numerous and young population in the Asia – Pacific region, the huge reserves of economic growth, the natural resources as well as the geographical proximity make the area and its countries the natural partners for Japan.

Together with Japan an important role for the development of trade and economic cooperation in the Asia – Pacific region is played by ASEAN which has the advantage of being a mature organization (established in 1967), with experience in economic, social, political and cultural cooperation. Due to its experience ASEAN can act as a catalyst for the establishment of the new free trade and cooperation structures, particularly in the case of the Regional Comprehensive Economic Partnership - RCEP.

In our opinion this project is the most likely to succeed in the medium term as compared to the Trans – Pacific Partnership (TPP) or the Free Trade Area Asia – Pacific (FTAAP) because has much less ambitious goals and provides for a flexible approach that can accommodate the different interest of the participants.

The fact that the same countries in the region take part in parallel to similar free trade area and economic cooperation projects is not, in our opinion, a disruptive or inefficient process because the very fact of having some of the same partners allow for “recycling” already agreed upon terms and clauses from one project to another.

At the same time, despite the failure of Doha Round, the proliferation of regional and even global in scope free trade agreements can be seen as an intermediate stage of creation of building blocks for a world wide agreement that will take form at some point in time.

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