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The multilateral context of the project of China–Japan–Republic of Korea trilateral free trade agreement

The China–Japan–Republic of Korea trilateral free trade agreement may become a critical pillar of Asian regionalism, determining future trade and political regime in the global scale. Undoubtedly, this trilateral political dialogue is to be accompanied by parallel talks over competitive, trans-regional projects involving Asia–Pacific partners, with special regard to the Transpacific Partnership (TPP) and the Regional Comprehensive Economic Partnership (RCEP). However, given the common challenges of the three analysed countries, in particular the unfavourable demographics, reindustrialization, and inefficient domestic demand, it should be noted that the said trilateral dialogue is facing very serious obstacles resulting from, among others, their historical ballast and territorial claims, as well as the intra-regional competition for leadership between Beijing and Tokyo. The aim of the article is to study both multilateral determinants and implications of the future China–Japan–Republic of Korea FTA.

Multilateralny kontekst projektu trójstronnego porozumienia o wolnym handlu pomiędzy Chinami, Japonią i Republiką Korei

Trójstronne porozumienie o wolnym handlu pomiędzy Chinami, Japonią i Republiką Korei stanowić może krytyczny filar azjatyckiego regionalizmu, determinujący przyszły ład handlowy i polityczny w wymiarze globalnym. Nie ulega wątpliwości, iż owemu trójstronnemu dialogowi politycznemu towarzyszyć będą równoległe prace nad konkurencyjnymi, transregionalnymi porozumieniami pomiędzy partnerami z regionu Azji i Pacyfiku, ze szczególnym uwzględnieniem Partnerstwa Transpacyficznego (TPP) oraz Regionalnego Wszechstronnego Partnerstwa Gospodarczego (RCEP). Mając na względzie wspólne owym trzem omawianym krajom wyzwania, związane w szczególności z niekorzystną demografią, reindustrializacją oraz nieefektywnym popytem wewnętrznym, należy mieć świadomość poważnych przeszkód dla tego trójstronnego dialogu, wynikających m.in. z zaszłości historycznych, pretensji terytorialnych, a także wewnątrzregionalnej rywalizacji o przywództwo pomiędzy Pekinem a Tokio. Celem artykułu jest przeanalizowanie multilateralnych determinant oraz implikacji przyszłego trójstronnego porozumienia o wolnym handlu pomiędzy Chinami, Japonią i Republiką Korei.

Keywords: trilateral free trade agreement, China, Japan, Republic of Korea

JEL classification: F4, F5

Introduction

The project of China–Japan–Republic of Korea trilateral free trade agreement (CJK FTA) has already been the subject of numerous economic and political analyses. Undoubtedly, trade talks among these three globally influential Asian states should be studied through the prism of a complex puzzle that covers both the regional and global context.

The future CJK FTA may be perceived as a building block boosting the regional trade regime's multilateralization. ASEAN¹ Economic Community (AEC), to be implemented by the end of 2015, cannot proceed as the core organization of the East Asian regionalism without such an impetus from the "big three". Noteworthy, the ASEAN+3² dialogue has already contributed to the steady, gradual institutionalization of the economic integration project through, among others, the Chiang Mai Initiative (CMI), the Chiang Mai Initiative Multilateralization (CMIM), the Credit Guarantee and Investment Facility (CGIF), the Asian Bond Market Initiative (ABMI), and the ASEAN+3 Macroeconomic Research Office (AMRO).

However, the "plus three" countries conduct trade talks under extremely unfavourable diplomatic and historical conditions, resulting in mutual distrust, hostility, animosities, and territorial disputes. Two of them – China and Japan, second and third largest economy in terms of the size of nominal GDP in the world – are traditionally viewed as natural rivals over the regional leadership and geostrategic influences.

The global dimension of the CJK FTA could be reflected by the US-Sino relations that translate into competitive multilateral projects of trade blocks: Transpacific Partnership (TPP) and Regional Comprehensive Economic Partnership (RCEP). The former exclude China, while engaging Japan, whereas the latter exclude United States, while potentially including Japan and the Republic of Korea. Furthermore, the slightly forgotten idea of the APEC FTA, involving the TPP states and, among others, China, Republic of Korea, and Russian Federation, remained of marginal significance.

The main objective of the article is to identify and characterize the multilateral context of the trilateral trade talks over the CJK FTA, pointing out potential correlations and mutual implications of simultaneously progressing processes of multilateralization of trade regimes in the Asia–Pacific region, legitimated by the TPP and the RCEP projects.

¹ The Association of Southeast Asian Nations.

² ASEAN (Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, and Vietnam) along with China, Japan, and the Republic of Korea.

1. The economic dimension of the CJK

The three discussed countries of Northeast Asia – China, Japan, and Republic of Korea, respectively second, third, and fifteenth largest economies in the world in terms of the size of nominal GDP – account, when combined, for more than 20% of the global and 70% of the regional product. According to data, their combined nominal GDP in 2013 exceeded the level of USD 14,3 tn, and the combined volume of their exports and imports for the same period – USD 4,5 tn [XNA, 2013]. These countries are also, respectively, first, fourth, and seventh largest exporters of goods in the world, with a total of nearly 18% of the shares in the global pool [TWB, 2014]. In the area of import, China and Japan hold analogously high positions, only the position of the Republic of Korea is slightly lower – its ninth place translates in this case into 2,8% of the shares in the world total; together, their shares exceed 17%. Performances of these three economies in the global export and import of services remain relatively modest – respectively 9,1% and 12,7% of the world total, according to the World Trade Organization (WTO) [WTO, 2014].

There is no doubt that the position of the “big three” in the contemporary global economic system is a result of, in particular, the expansion of Chinese economy – aspiring, according to Goldman Sachs, to become the largest economy in the world in terms of the size of the nominal GDP by 2030. Nevertheless, the importance of its Japanese and South Korean partners complements the vision of the enormous implications of the tripartite agreement for the entire global trading system in the context of the lowering of customs barriers and flows of foreign direct investments, deviating far from the effects of the ones already functioning, otherwise important structures, i.e. the Association of Southeast Asian Nations, the North American Free Trade Agreement (NAFTA), and the European Union (EU).

The political context must be examined from both the perspective of bilateral relations, with special regard to Beijing–Tokyo and Tokyo–Seoul, burdened with difficult historical experiences, mutual distrust, territorial resentments, and rivalry over influence in the region, and the multilateral one, at the intra- and trans-regional level. On the one hand, the dialogue concerned the institutional core of Asian integration project – the ASEAN, with the three countries of the northeast subregion, established after the Asian financial crisis 1997–1998, encouraged the mechanisms of financial and monetary cooperation which have become the impetus for economic regionalism and, consequently, for the pursuit of the institutionalized formula of economic, social, and political community; on the other hand, each of the three countries pursue its own geopolitical ambitions at the level of G20 and in bilateral relations with e.g. the United States, the Russian Federation, or the EU.

2. Asian FTAs – so far, so many...

Since the beginning of the XXI century the global trade regime has experienced expansive bilateralization, manifested through a FTA-chain reaction. According to the WTO, 583 regional trade agreements were notified³ to the General Agreement on Tariffs and Trade (GATT)⁴ or the WTO so far, under the Article 24 of GATT 1947 or GATT 1994⁵, Enabling Clause⁶, or Article 5 of GATS. Currently, 377 RTAs remain in force.

At present, the Asian region is the world leader in terms of the number of concluded FTAs (76); however, it is facing numerous challenges regarding their use, scope, and impact on regionalization trends.

According to enterprise surveys conducted by the Asian Development Bank (ADB) and the Asian Development Bank Institute (ADBI), no more than 30% of enterprises in China, Japan, Malaysia, Philippines, Republic of Korea, Singapore, and Thailand tend to utilize FTA preferences, especially because of the high fixed costs entailed, difficult to overcome by small and medium-sized enterprises (SMEs). Among other reasons, the lack of information on FTAs, low margins of preference, administrative costs, delays in export documentation, and non-tariff measures in partner economies were listed most often.

³ According to data from March 20, 2014; by 2002, 250 RTAs were notified, therefore in the period of 12 years the number of RTAs increased by 233%.

⁴ The GATT was signed on October 30, 1947 in Geneva to establish the third – after the International Monetary Fund and the World Bank – pillar of the international economic cooperation. It was expected to be a temporary agreement, paving the way to the establishment of the International Trade Organization. The lack of consensus over the ITO status has prolonged the existence of the GATT till 1994. The main priority of the GATT was to liberalize the world trade through negotiation rounds. In years 1947–1994 eight rounds were concluded, four of which were found especially important, namely the Geneva Round (1947, 7 months; 45 k tariff concessions), the Kennedy Round (1964, 37 months; anti-dumping issues), Tokyo Round (1973, 74 months; tariff reductions by over USD 300 bn), and Uruguay Round [1986, 87 months; the establishment of the WTO, the reduction of tariffs and agricultural subsidies, the agreement on free trade in textiles, the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS)]. Among the major achievements of the GATT, its reduction of tariffs in the world trade from an average 40% to less than 5% is considered to be the most significant one [Bobowski, 2011, pp. 29–32].

⁵ According to Article 24, the conclusion of RTAs is eligible to, among others, reduce trade barriers to minimize the risk of trade diversion. Addressing customs unions and free trade areas, and imposing more restrictive barriers towards third countries is forbidden; moreover, RTAs should, in perspective, eliminate tariff and non-tariff barriers to maximize the effects of trade creation while reducing negative implications for the third parties – according to the Most Favored Nation (MFN) clause. Another thing worth noting is that the obligatory notification by the Committee of Regional Trade Agreements (CRTA) is being considered.

⁶ According to the clause established in 1979, developing countries have gained the privilege of constructing agreements that do not meet the criteria set in Article 24, mainly to cover “substantially all trade”, allowing them to provide preferences for trade partners [Hoekeman, Kostecki, 2001; Ravenhill, 2003, pp. 299–317].

Another source of concern is the Asian “noodle bowl effect”, induced by multiple rules of origin and resulting in rising of the transaction costs for SMEs and distorting cross-border business strategies of larger enterprises.

Another challenge regarding Asian FTAs is the unwillingness to cover agricultural trade, induced by the pressure from powerful farm lobbies and social concerns over poverty in rural areas. Of the 69 FTAs examined, 46% had comprehensive coverage, 28% had some coverage, and 26% had little coverage of agricultural products.

The fourth issue is the trade in services, still restrictive, however progressively liberalized due to Asian FTAs and the increased regulatory cooperation. Of the 69 FTAs reviewed, 41% had comprehensive coverage, 36% had some coverage, and 23% had little coverage of services trade.

Finally, the analysed agreements differ in terms of addressing the WTO-plus elements. When studying the four “Singapore issues”, namely competition, intellectual property, investment, and public procurement, among the 69 FTAs reviewed by the ADB and the ADBI 23% had comprehensive WTO-plus coverage, 54% had partial WTO-plus coverage, while 23% excluded those components.

As it was pointed out by Masahiro Kawai and Ganeshan Wignaraja, to enhance the FTA utilization in Asia it is crucial to implement certain national, global, and regional policy agenda [Kawai, Wignaraja, 2013].

At the national level, it is necessary to strengthen the support systems for SMEs, to rationalize rules of origins, and to cover agricultural and service trade, as well as WTO-plus, with FTAs, more comprehensively.

From the global perspective, the surveillance of non-tariff measures to reduce protectionism, the WTO agenda on supply chains and FTAs to encourage convergence of regional and global trading rules were considered critical.

Ultimately, the regional context prioritize the multilateralization of Asian FTAs through liberal cumulation rules and the conclusion of larger regional agreements through the establishment and potential convergence of the Regional Comprehensive Economic Partnership and the Transpacific Partnership. However, the latter condition cannot be met without strategic consensus between Beijing and Washington.

3. To TPP or not to TPP...

Designing multilateral agreements – i.e. the Regional Comprehensive Economic Partnership and the Transpacific Partnership – to dismantle the “noodle bowl” raises huge opportunities in terms of clarifying the global trading system experiencing a strong impact of the expansion of bilateralism, although the negotiation process will be extremely difficult.

rule-making competition with the United States in terms of the degree of liberalization and integration. It must be emphasized, that the TPP is a high standard trade agreement of 26 chapters, covering, in addition to the characteristic of ASEAN+1 FTAs customs-border issues, the WTO-plus elements such as environment, labour, intellectual property rights, and government procurement. Such a “competitive liberalization”, as it was termed by C. Fred Bergsten, may discourage China from sitting by the multilateral negotiation table, also because of the restrictive clause addressing the issue of state-owned and state-supported enterprises [Bergsten, 1996]. Furthermore, it can be assumed that the TPP may enhance dynamic competition for the US market between China and the TPP members, and affect Chinese outward FDI performance, especially in Mexico – top host location in Latin America – and Vietnam, deeply engaged in vertical division of labour with China [Tso, 2012].

The entry barrier for China is therefore relatively high, however there is still some room for change. While studying Chinese strategy towards the TPP, it appears that, as for now, they stand aside, but not behind. Several important steps were already taken. Firstly, a sectoral-level dialogue between China and the ASEAN was launched in July 2011 to cover a broad range of industries [Nan, 2010]. Secondly, China concluded the Foreign Investment Protection Agreement with Canada in February 2012 [Kosich, 2012]. Thirdly, China proceeds with the FTA talks with Australia [Dobell, 2011]. And last but not least, the China–Republic of Korea and CJK FTA talks were initiated.

Admittedly, none of these initiatives were undertaken as a direct response to the TPP; that notwithstanding, contemporary multilateral context has assigned them an extra importance and a new meaning.

4. CJK FTA – a marriage of convenience?

It is worth noting that at the threshold of 2014 CJK declared to speed up the talks over the RCEP, complementary to the tripartite FTA project, having assumed the form of conversion of previously concluded ASEAN+1 FTAs into the single multilateral agreement, involving the ASEAN members as well as Australia, China, India, Japan, New Zealand, and the Republic of Korea (ASEAN+6) [Swire, 2013].

However, the tripartite CJK talks are supported by a parallel bilateral dialogue Beijing–Seoul and Seoul–Tokyo; therefore in the future – assuming the success of the project – the coexistence of China and the United States in the neighbouring, partially overlapping multilateral trading architectures – mainly because of the involvement of Japan, Australia, and the Republic of Korea – might be possible.

Moreover, parallelly to the consultation on the RCEP (third round of negotiations took place in January 2014 in Malaysia) and the tripartite FTA, China and the

Republic of Korea conduct negotiations regarding a bilateral free trade agreement (since May 2012 there have been eight rounds of negotiations), and may hold further tripartite talks involving Japan. During the eighth round of bilateral talks, in November 2013, the list of sensitive agricultural assortments was agreed on, and the statements concerning the flow of services, investments, intellectual property rights, competition, environment, and employment were exchanged. It is worth mentioning that the bilateral free trade agreement Japan–Republic of Korea was negotiated in years 2003–2004, however the following years brought deadlock – finally, in 2008, a consultation process was re-launched to provide more favourable climate for further talks. As it was announced by the South Korean Ministry of Foreign Affairs, the second negotiation round (and the last so far) at the general level took place in May 2011.

Meanwhile, Japan has decided to enter the TPP membership negotiations, perceiving such a trade pact as an opportunity to challenge deflation and stagnation of the economic growth through export expansion [BK, 2013]. In this context, the interest of Beijing – standing aside the US-backed project – in the tripartite agreement has increased, as it sought a way to counterbalance the potential impact of multilateral block, involving around the negotiating table, next to Japan, such countries as Australia, Brunei, Chile, Canada, Malaysia, Mexico, New Zealand, Peru, Singapore, and Vietnam [AFP, 2013].

On the other hand, it should be emphasized that trade negotiations are accompanied by mutual distrust and political tensions, concerning, among others, territorial disputes around the Senkaku/Diaoyu islands of the South China Sea between Beijing and Tokyo and Dokdo/Takeshima islets in the Sea of Japan between Tokyo and Seoul, as well as the “tolerant” stance of Beijing towards the North Korean nuclear program [Buckley, Jones, 2012]. Particularly strong animosities are observed between Beijing and Tokyo, as they are – as the second and third world largest economies in terms of nominal GDP – natural competitors for the leadership in the region [Haggard, 2011, p. 17].

Interestingly, recent months, abounding in diplomatic clashes, were found fruitful around the trade negotiating table – where the climate proved to be pragmatic and favourable to the bilateral economic cooperation. After in 2012 the volume of Japanese exports to China declined by 10,8%, in 2013 there was an increase of almost 18%, which translates into a value of foreign sales to the United States at the level comparable to the corresponding period. What distinguishes Japanese trade relations from the two largest Asia–Pacific economies is the fact that trade with the American partner generates significant surplus, while the Chinese rival accounts for a deep deficit that equals nearly a half of the total Japanese trade deficit [Ivanovitch, 2013].

Another thing worth mentioning is that this potential tripartite agreement paves the way to the establishment of a free trade area of East Asia, involving the

ASEAN+3 and Asia–Pacific in the grouping of ASEAN+6 (RCEP), which would translate into a perspective on the growth of mutual trade turnover with the use of the Chinese yuan as a regional settlement unit [Gill, 2012].

Conclusions

The future of the multilateral trade regime is uncertain, although at the same time it is supported by various bilateral and plurilateral initiatives. The massive expansion of bilateral FTAs, both intra- and interregional, has given multilateral projects the ability to challenge the “noodle bowl”. The disappointing Doha process has contributed to the relocation of the “liberalization race” from the WTO level to the global centres around Beijing, Brussels, and Washington. As stated by Charles Finny⁷, New Zealand’s lead negotiator of the FTAs with the ASEAN, Australia, China, and Singapore, so as it was with the Economic Partnership Agreement with Chinese Taipei, numerous FTA puzzles should finally compose two multilateral trading hemispheres: the Transpacific Partnership covering the Asia–Pacific states, including China Mainland, and the Transatlantic Partnership, based on the foundations of the future US–EU FTA. In order for that to happen, consensus regarding both the CJK and the US–Sino relations have to be reached.

The China–Japan–Republic of Korea trilateral free trade agreement may become a critical pillar of Asian regionalism, determining future trade and political regime in the global scale. However, given the common challenges of these three analysed countries, in particular the unfavourable demographics, reindustrialization, and inefficient domestic demand, it should be noted that this trilateral dialogue is facing very serious obstacles, resulting from, among others, the historical ballast, territorial claims, and the intra-regional competition for leadership between Beijing and Tokyo [Youjun, 2013].

The trilateral CJK FTA provides an opportunity for the establishment of an East Asian economic community, which could have significant effects on the global system. The three Asian members of the G20 share ambitions and trans-regional alliances, but there is no doubt that the implications of the likely compromise will extend far beyond the boundaries of these three economies. The strengthening of the economic cooperation at the level of ASEAN+3 should translate, prospectively, into the progress of the ASEAN+6 dialogue (RCEP), thus creating a “Chinese” counterweight to the TPP project, consequently strengthening the political position of the Beijing within the Asian regionalism. The relationships

⁷ Finny was consulted by the author on March 25, 2014, during his visit at the Wrocław University of Economics.

among the “big three” will determine the future trans-regional configuration of influences in the global economy.

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