Mega FTAs, Institutional Balancing, and South Korea’s Middle Power Diplomacy

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Introduction

East Asia has shown a greater appetite for formal institutionalization since the first part of the new millennium. After its accession to the World Trade Organization (WTO), China has turned to East Asia in order to promote institutionalized cooperation, for reasons both economic and strategic. In the face of Chinese initiative, Japan has endeavored to fortify its existing regional and institutional leadership, although it has been ambivalent about whether and how to involve the United States. ASEAN, with its long history of building up institutions and self-confidence measures, has always attempted to position itself as the central locomotive for institutionalizing East Asia.

Seeking to multilateralize the existing bilateral FTAs, East Asian countries entered into the 2nd stage of FTAs. As demonstrated by the U.S. and Japan’s participation in TPP negotiations and the launch of long-waited RCEP negotiations, East Asia’s rush into mega FTAs testifies that the regional economic order is entering into a new territory. Departing from the era of bilateral FTAs, East Asian countries’ shift to mega FTAs is likely to result in an unprecedented stage of institutional building in the region.

I posit that the dynamics of institutional balancing is the predominant factor for East Asian countries’ drastic move to mega FTAs. It is often pointed out that a variety of factors – the limited economic benefits of bilateral FTAs and noodle bowl effects, widespread presence of transnational production networks, and structural shift in East Asia both at the regional and global level – encouraged the East Asian push for mega FTAs.¹

While I do not dismiss that these factors did indeed contribute to the East Asian rush for mega FTAs, I argue that one of the characteristics these countries have commonly shown is the

tendency to take advantage of regional institutions for dual goals: institutionalized cooperation and balancing against the target state. On the one hand, East Asian countries became more interested in institutionalized cooperation in order to effectively deal with common problems. On the other hand, they also take advantage of institutions as a means for balancing, which created a dynamic of competition for institutional building in the region. For example, China and Japan attempted to offer competing and potentially contradictory visions of regional institutional architecture: ASEAN+3 vs. ASEAN+6.

The dual dynamics of competition and cooperation have unfolded during the process of institutional building in the region. Because this transition took place under the changing regional landscape, spurred on by the rise of China and the relatively declined (yet continued) presence of the US, this tendency for competition has only intensified with the East Asian countries’ shift to mega FTAs. In addition, institutional balancing behavior is not limited to great powers; rather than unilaterally imposing their visions and preferences for regional architecture, they are likely to utilize regional institutions as a site for bargaining with small powers. Great powers will find it more convenient to strike a compromise by way of these regional institutions. From the perspective of small powers in East Asia, including ASEAN and South Korea, the regional institutions will serve as a useful means to manage unequal power relationship with great powers. It is against this backdrop that ASEAN could play a mediating role among great powers in delineating the visions of the regional order.

Under the structural shifts, East Asian countries are actively forging regional economic

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5 Paul Bowles, “Asia’s Post-Crisis Regionalism: Bringing the State Back In, Keeping the (United) States Out,” Review of International Political Economy 9, no. 2 (2002): 244-270.
order, spurred by mega FTAs, and showing no signs of hard balancing. What is the driving force behind these new dynamics of institutionalizing East Asia? I argue that the logic of institutional balancing explains East Asian countries’ heightened interest in mega FTAs. When combined, the intensified competition for institutional building between the US and China and small powers’ attempt to take initiative in institutional building generate a systemic consequence. Despite the shift to mega FTAs, East Asian countries could not succeed in merging a number of regional institutions into a single core institution that could be the institutional basis for regional cooperation. Furthermore, the coexistence of such institutions allows East Asian countries to utilize both exclusive and inclusive behaviors when building institutions.6 As a result, while some East Asian countries (such as Japan and Singapore) have overlapping membership in both mega FTAs, other countries (including the US and China) have thus far joined one of the two mega FTA deals.

**Institutional Dynamics of the Trilateral Relations in East Asia**

**Dual Transitions in East Asia**

In this section, I shift focus from East Asian countries’ shift to mega FTAs, to the way in which the dynamics of inter-institutional balancing has unfolded. In particular, I explore how and why the main focus of inter-institutional balancing has changed from a game between China and Japan to a game between the US and China, creating a competitive dynamic between the TPP and the RCEP.

The changing dynamics of inter-institutional balancing in East Asia are strengthened with

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the dual power transition. East Asia experienced a power shift both at the global and regional levels in the 21st century, as the repercussion of the global financial crisis produced profound impacts on the global economy. The rise of China and the relative decline of the US came to the fore with the outbreak of the global financial crisis. Various forecasts were published anticipating that the Chinese economy would overtake that of the US; the IMF estimated that China emerged as the largest economy in the world US in terms of GDP based on purchasing power parity (PPP). In 2014, China’s GDP reached $17.6 trillion, whereas the US GDP was $17.4 trillion.7

The global financial crisis eroded not just the hard power, but the soft power of the US in that it revealed the serious structural flaws of the global economic institutions that have been underpinning the postwar world economic order for the last six decades.8 From the mid-1980s, the US made systematic attempts to transplant the US-led neoliberal reform packages, symbolized by the Washington consensus, to developing countries in Latin America, Africa, and East Asia plagued with economic crisis. However, the sheer fact that the US became the epicenter of the global financial crisis generated dampening effects on the ideational foundation of the US leadership when managing the increasingly complex global economy.

The impact of the dual transition has materialized at the regional level. In 2010, two years after the global financial crisis, China replaced Japan as the biggest economy in East Asia, signaling that power transition would speed up at the regional level. The rise of China was sharply contrasted with the image of Japan suffering from two decade-long recession. It was a

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8 For changing dynamics in the institutional foundation of the global economy, see Alan S. Alexander and Andrew F. Cooper, eds., Rising States, Rising Institutions, The Center for the International Governance Innovation (Washington, D.C.: Brookings Institution Press, 2010).
shocking alarm not only to Japanese policymakers, but to the general public. Japanese policymakers were concerned that Japan’s strategic weight might substantially weaken in East Asia. Furthermore, since China emerged as the biggest trade partner for Japan in 2006, Japan’s trade dependence on China more than doubled from 9 percent in 1999 to 19.6 percent in 2011. This produced dual effects. On the one hand, Japan could be insulated from the repercussions of the global financial crisis as its export to China has dramatically increased in the wake of the crisis. On the other hand, increase in trade dependence would result in increase in Japan’s vulnerability, deteriorating its strategic position vis-à-vis China. Given that China could use the increased economic power to exert its influence on the newly emerging regional order, Japan needed to find an institutional means to adapt to this aggravating situation. Japan could take advantage of the TPP as a useful tool to check China’s mounting influence on the new regional order by deepening economic integration with countries in the Asia Pacific.

China and Japan also engaged in soft power competition at the regional level. China has tried to enhance its soft power in order to promote the Beijing consensus that suggests the coexistence of socialist political systems and capitalistic economic development.\(^9\) Fearing that Chinese influence grows excessively, the Hatoyama government tried to hold China in check by espousing the idea of an East Asian community.\(^10\)

\*The US-Japan Cooperation and Changes in Institutional Balancing*

The US and Japan sought to coordinate their policy stances. In cooperation with Japan, the US attempted to redesign the regional architecture that would help the US better cope with the rise

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of China, prolonging its hegemonic leadership. It is against this backdrop that the Obama administration announced the rebalancing policy in the Asia Pacific.\(^\text{11}\) Making clear that the US is an Asia Pacific power,\(^\text{12}\) the Obama government attempted to strengthen the traditional alliances with key countries in the region, such as South Korea, Japan, and Australia, as well as redesign the regional architecture in a manner that could systematically incorporate the US interests in the region.\(^\text{13}\)

Initially the rebalancing policy was formulated to address East Asian countries’ concerns that the US strategic and military commitment to East Asia was in decline because the US was trapped in Iraq and Afghanistan. However, the initial expectation of government policymakers and experts in East Asia that the US would substantially increase its military commitment in East Asia quickly evaporated. The aggravating situation in the Middle East did not allow the US to execute redeployment to the Asia Pacific immediately.

Under the circumstances, the Obama government reformulated the rebalancing policy to include both economic and strategic implications. The Obama government stressed that it was of paramount importance to connect the Pacific and the Indian, while strengthening existing bilateral and multilateral cooperation.\(^\text{14}\) In a similar vein, Secretary of State Hillary Clinton emphasized the economic and institutional aspects of the rebalancing strategy by arguing that open Asian markets would offer the US unprecedented opportunities for investment, trade, and technology, and that the recovery of the US economy hinged on the exports to the Asian economies. In reality, out of six key lines for the US rebalancing policy, three – deepening

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\(^{13}\) For a concise overview of the rebalancing policy, see: David J. Berteau and Michael J. Green, “Assessing the Asia-Pacific Rebalance,” *Center for Strategic and International Studies* (2009).

partnership with emerging powers; empowering regional institutions; helping to build a regional economic architecture that can share prosperity – are economic and institutional responses.\textsuperscript{15}

The rebalancing policy aimed to strengthen the US institutional engagement in Asia by comprehensively reformulating the existing institutional arrangements.\textsuperscript{16} US institutional engagement in East Asia was demonstrated by US participation in the East Asia Summit (EAS) and the push for the TPP; these emerged as a core of US rebalancing policy. The Obama administration in particular placed the highest priority on the TPP in order to implement economic and institutional engagement.\textsuperscript{17}

First, in terms of economic engagement, it is vital for the US to deepen an economic partnership with Asia, as it accounts for about 40 percent of global GDP and has been one of the fastest growing economies in the world. The Obama administration ascertained that it is important to tap the American economy into the Asia-Pacific region (with its high economic vitality) and to actively promote economic integration in the region.\textsuperscript{18} President Obama also urged East Asian countries to take part in TPP negotiations. In a speech delivered in Tokyo in 2009, president Obama strongly demanded Japan to participate in negotiations of the TPP.\textsuperscript{19} The Obama government’s drive for the TPP was considered the US attempt to exclude China from the newly emerging regional order in the Asia Pacific. From the perspective of the US, the TPP, if successfully completed, could be an institutional balancing act that would hold in check the ever-increasing influence of China.

\textsuperscript{15} Hillary Clinton, “America’s Pacific Century,” \textit{Foreign Policy}, November 2011.
\textsuperscript{18} The United State Trade Representative, “The President’s 2010 Trade Policy Agenda,” <https://ustr.gov>.
\textsuperscript{19} Remarks by President Barack Obama at Suntory Hall, (Tokyo, November 14, 2009), <www.whitehouse.gov>.
Second, in terms of institutional engagement, the Obama government viewed the TPP not just as trade liberalization measures, but as a way to create new rules and governance in the Asia Pacific. The Obama government promoted the TPP to redesign the economic architecture of the Asia-Pacific region. Although the US government made it clear that China would be welcome to join the TPP negotiations, the Chinese government can hardly accommodate critical issues such as regulations on state-owned enterprises (SOEs), as well as labor and environmental standards.

In short, the TPP signifies a “trade pivot” to Asia, reaffirming the Obama government’s commitment to the region. In order to pre-empt the emergence of a China-centric economic order in East Asia, the Obama government utilized the TPP to tighten economic partnership and institutional engagement to the Asia-Pacific region. The Obama government creatively reformulated the rebalancing policy to promote the TPP as an institutional channel that would substantially help the US enhance economic partnerships and institutional ties directly with East Asian countries. The TPP could evolve as a check to the ever-increasing influence of China in the region. The strategic importance of the TPP has grown stronger as China’s foreign policy has become aggressive in East Asia. On April 2015, in his speech at the McCain Institute at Arizona University, Defense secretary Ashton Carter boldly claimed that “passing TPP is as important to me as another aircraft carrier.”

From the perspective of Japan, until 2009, the Japanese government approached the TPP mainly from the perspective of economic effects. In 2011, Prime Minister Aso Taro announced the ambitious “Asia Growth Initiative,” aiming to link the revival of the Japanese economy

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23 Taro Aso, Japan’s Future Development Strategy and Growth Initiative towards Doubling the Size of Asia’s
and the sustainable growth of Asian countries. Aso noted that the TPP could connect the Japanese economy to the robust growth potential of Asian economies and help Japanese companies rebuild their supply chains in East Asia.\textsuperscript{24} Because Japanese companies built widespread production networks in East Asia, mega FTAs could substantially facilitate intra-industry trade within the production networks.\textsuperscript{25} Echoing Aso’s policy stance, prime minister Kan Naoto of the Democratic Party called the TPP the third opening of Japan.\textsuperscript{26} In short, the TPP was considered essential in creating a virtuous circle of simultaneous economic growth of Japan and Asian countries.

Against this backdrop, in November 2011, the Noda government officially announced their intention to join the TPP negotiations. However, the domestic political situation still posed a daunting challenge to the Japanese government in negotiating with major trading partners such as the US, EU, and China. The Noda government faced furious opposition not just from potential losers such as agricultural and medical sectors, but from the ruling Democratic Party. For example, about one hundred twenty Diet members, led by the former Prime Minister Hatoyama Yukio, Shizuka Kamei, and Masahiko Yamada, formed the parliamentary group opposing the TPP.

With the domestic political environment aggravating, the Abe government attempted to add strategic implications to the TPP. In March 2013, the Abe cabinet resonated with the Obama government’s rebalancing strategy as it made an official announcement of joining the TPP negotiations. Firmly believing that the TPP would become an institutional basis for new trade rules in the region, Abe adamantly argued that Japan should join the TPP negotiations.

\textsuperscript{25} Cabinet Secretariat, “Consultation with the TPP Member Countries on Japan’s Participation in the TPP Negotiations,” July 2012.
before it was too late.\textsuperscript{27} The Abe government’s decision to join the TPP negotiations sent a clear signal that it lent support to US-led trade and economic architecture in the region, as symbolized by high standards of trade liberalization. The US welcomed the Abe administration’s official announcement, saying that the US-Japan alliance returned to the core of Japan’s foreign policy.\textsuperscript{28}

Entering into the TPP is consistent with the Japanese vision of the East Asian regional order in the context of the rise of China. At the regional level, the Japanese government has responded to the rise of China in two ways. The prime objective of Japan’s strategic posture in dealing with the rise of China is to expand the geographic scope of regional integration and cooperation. It is well known that Japan has long preferred ASEAN+6 to ASEAN+3 as a basic framework for regional order in East Asia.\textsuperscript{29} Concerned that China would wield excessive dominance in East Asia if the new regional order is formed based upon the ASEAN+3 framework, Japan has consistently sought to deepen economic integration within the framework of ASEAN+6. To prevent this undesirable situation from becoming a reality, Japan has tried to attract countries with shared values of democracy and capitalism such as Australia, New Zealand, and India. In addition, Japan attempted to take advantage of US influence to hold China in check. Japan, together with India, became an active supporter of the inclusion of the US and Russia in 2011. These series of efforts underscored the Japanese effort to expand the scope of regional cooperation from the APT format, favored by China, to APT+ format.

The competitive dynamic of FTA race in East Asia was another strategic consideration that the Abe government took into account. Whereas the Japanese government attempted to enter into the FTA race in order to restore the vitality of the Japanese economy, the Abe government

\begin{itemize}
\item \textsuperscript{27} Shinzo Abe, Press Conference by Prime Minister Shinzo Abe, March 15, 2013, <http://japan.kantei.go.jp>.
\item \textsuperscript{28} Fred Hiatt, “Can Japan save itself?” \textit{Washington Post}, April 20, 2012.
\end{itemize}
adopted mega FTAs as a new pillar of FTA strategy, so as to catch up with its East Asian competitors. It is noteworthy that the Abe administration’s decision to join the TPP came just after the Korea-EU FTA and the KORUS FTA went into effect in 2011 and 2012, respectively; as well as the kick off meeting that was held for the Korea-China FTA in 2012. Concerned that Japanese companies export competitiveness would significantly erode, compared to their Korean counterparts, the Abe government decisively pushed for joining TPP negotiations. Falling behind in FTA competition in East Asia, the Japanese government thought that Japan could catch up with competitors such as South Korea and Singapore by successfully completing mega FTAs. With this strategic thinking in mind, the Abe government turned around the existing FTA strategy focusing on minor trading partners to push for mega FTAs such as the TPP, the RCEP and the Japan-EU FTA.

Of course, the Abe government took into account the economic consideration in its shift to the TPP, in order to maximize the economic effects of “Abenomics.” Unlike the first two arrows of Abenomics focusing on the improvement of macroeconomic conditions, the third arrow of Abenomics touches upon a variety of issues ranging from human capital investment, technological innovation, and local revitalization programs to the TPP. Identifying retarded FTA negotiations as one of six obstacles to impeding corporate competitiveness of Japan, the Abe government once again was spurred on by the promotion of mega FTAs. It was estimated that the market share of Japanese companies in three major exporting industries such as auto, electronics, and machinery would substantially decline in the US, EU, and Chinese markets. Specifically, with the Korea-EU FTA coming into effect, it was estimated that Japan’s GDP and employment will decrease by 1.53 percent and by 812,000.31

30 Other five obstacles are strong yen, power shortage and expensive electricity, high corporate tax, and labor and environmental regulations.

31 Cabinet Secretariat, “Estimates of Economic Partnership Agreements.”
China’s Reactions and the Evolving Dynamics of Institutional Balancing

The Obama government’s rebalancing policy and changes in Japanese strategic thinking brought about profound effects on the dynamics of institutional balancing in East Asia. Aroused by concerted efforts by the US and Japan, China grasped that the TPP could have various strategic implications, going beyond narrow economic interests. China responded to this aggravating situation in various ways. First, in November 2012, China immediately responded to the progress of the TPP negotiations facilitated by Japan’s participation. The Chinese government unwaveringly criticized the US and Japan, arguing that the TPP essentially reflected the US goals to reduce Chinese influence in the region through the method of containment.32

Second, the Chinese government solidified its relationship with neighboring countries, as demonstrated in president Xi Jinping’s speech in 2013. Suggesting that “friendship is the consistent principle of China’s diplomacy with its neighbors,” President Xi stressed that “the basic tenet of diplomacy with neighbors is to treat them as friends and partners, to make them feel safe and to help them develop.”33 Third, the Chinese government stressed that East Asian countries first seek the “unification of regional economies,” focusing on economic integration among East Asian countries. In this regard, the Chinese government argued that the RCEP would not just contribute to trade liberalization, but serve as an important step toward the unification of regional economies.34 Meanwhile, the Chinese government also highlighted that

the RCEP was more open and flexible in terms of negotiation style. By the same token, Chinese premier Wen Jiabao ascertained that whereas each country should be able to take a path commensurate to its level of development, China would support ASEAN to actively embark on the RCEP negotiations.\footnote{Ibid.} By indicating that the TPP did not correspond to the unification of regional economies, the Chinese government made clear its intention to oppose the TPP.

Recognizing that it needed to directly respond to the US push for the TPP, the Chinese government ambitiously launched a series of diplomatic drives such as the Conference on Interaction and Confidence Building Measures in Asia (CICA) and the Asia Infrastructure Investment Bank (AIIB) to tighten security and economic relationship with neighboring countries in Asia.\footnote{Zachary Keck, “China’s Growing Hegemonic Bent,” \textit{The Diplomat}, June 26, 2014.} In the area of trade, the Chinese government also sped up bilateral FTA negotiations. Even before mega FTAs emerged as a new trend, China as a global economic power has made consistent efforts to expand its own economic ties with countries such as New Zealand (2008), Singapore (2008), and Peru (2009), and negotiating new FTAs with the GCC (2005), Australia (2005), Iceland (2008), Norway (2008), and Costa Rica (2009).\footnote{China FTA Network, <http://fta.mofcom.gov.cn/english/index.shtml>.} China also concluded a bilateral FTA with South Korea and expedited the China-Japan-Korea FTA negotiation.

Among others, China effectively picked up an ASEAN-led initiative to counter the US-led TPP. The RCEP emerged as an institutional alternative for China to offer other East Asian countries. China could successfully garner ASEAN countries’ support because they made it clear that it would respect ASEAN centrality in negotiating the RCEP.\footnote{“China’s Support for ASEAN’s Centrality Lauded,” \textit{China Daily}, September 21, 2012.} The RCEP stands in stark contrast to the TPP in terms of membership and standards. Based on the ASEAN+6 framework, the RCEP explicitly seeks to form an Asia-only FTA, to rule out the US. In contrast
to the TPP aiming for a high standard FTA without exception, the RCEP is less ambitious in terms of trade liberalization and regulatory harmonization. The TPP aims to include many sensitive issues such as services, IPR protection, and regulatory harmonization, whereas the RCEP largely focuses on trade liberalization in manufacturing sectors.

The Chinese response to the shifting environments has unfolded in two ways. The Chinese approach to FTAs has become more multifaceted and flexible than in the past. After completing bilateral FTAs with its neighboring countries, China revealed its regional strategy in the process of negotiations for a Korea-China FTA, Korea-China-Japan FTA, and the RCEP. While speeding up bilateral and trilateral FTA negotiations with neighboring countries, China flexibly embraced the ASEAN+6 format as an institutional platform for regional economic integration and cooperation. It was quite a drastic turnaround because the RCEP was based on the ASEAN+6, which had long been preferred by Japan as an institutional platform for the regional economic cooperation in East Asia. Second, China took a flexible approach when creating the regional economic architecture, as demonstrated by the cases of the RCEP, the CICA, and the AIIB that would exclude the US in this process.

The shift in Chinese policy to push for the RCEP demonstrates that the Chinese approach to regional economic order became flexible. Thinking that the TPP was contradictory to its vision of regional order, the Chinese government began to seek an alternative institution. Rather than adhering to its preferred ASEAN+3 framework, the Chinese government decided to accommodate the ASEAN+6 framework that Japan has strongly preferred as a basis for regional cooperation. This sent a clear signal that China could accommodate any regional order without the US.

In a similar vein, Hu argues the “outside strategy” aiming to counter the TPP with alternative institutions such as the RCEP, China-Korea FTA, and the China-Japan-Korea FTA
is more feasible than the “inside strategy” in which China seeks to check and balance the US from within the TPP. The outside strategy would help China secure a better position in designing the regional order, as China would take the initiative in creating and developing various institutions. By contrast, the efficacy of the inside strategy is inherently constrained because China will be unable to fundamentally change the already agreed upon provisions and rules among the twelve countries, ranging from intellectual property, state owned enterprises, financial markets, and government procurement to labor and environment standards.  

China strategically respected ASEAN’s pivotal role in launching the RCEP. For ASEAN, the RCEP was regarded an alternative of restoring ASEAN centrality as it takes a form of “ASEAN+3+3.” In the past, ASEAN could play a bridging role in regional cooperation, as demonstrated by ASEAN+1 FTAs, ASEAN+3, and ASEAN+6, by consolidating its internal unity. However, ASEAN’s internal unity was on the verge of breakdown with the launch of the TPP. ASEAN has maintained its long-standing principle of joining FTA negotiations as a unit rather individual countries. But as Singapore, Malaysia, and Brunei joined the TPP negotiations and negotiations of the Korea-China-Japan trilateral FTA sped up without involving ASEAN, there was concern that ASEAN centrality would weaken in the second stage of FTAs in East Asia.  

Abe’s decision to enter TPP negotiations produced somewhat unexpected, systemic consequences in East Asia that changed the major focus of rivalry from China vs. Japan, to the US vs. China. First, China and Japan seek to implement a two pronged strategy of competition and cooperation. The emergence of the RCEP was driven by the dual dynamics of competition and cooperation. Before the launch of the RCEP, China and Japan could not settle their

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39 Yifan Hu, *China’s Strategy to Surf the New Wave of Preferential Trade Agreements*, Unpublished manuscript, December 2013.
dissenting views on the scope of regional cooperation. In the 2004 APT summit, China took initiative to create an expert group that would carry out the feasibility study of an East Asia Free Trade Area in two stages. Rather than echoing the Chinese initiative, Japan in the economic ministers’ meeting in August 2006 proposed the Comprehensive Economic Partnership in East Asia (CEPEA) among ASEAN+6 countries. The possibility of an FTA of ASEAN+3 countries and an FTA of ASEAN+6 countries was simultaneously discussed because China and Japan could not compromise on the differing views. Due to the differences, the creation of a region-wide FTA was merely discussed by expert groups without being elevated into the formal government-level negotiations. However, the rapid progress of the TPP encouraged China to shift its vision for prospective regional order. The launch of the RCEP suggests that China embraced, at least to some extent, the interests of Japan and ASEAN to promote an alternative vision of regional order.

In August 2012, under this worsening situation, ASEAN could successfully pick up the RCEP to restore its centrality. Stalled talks about a region-wide FTA could resuscitate because neither China nor Japan took initiative. Repackaging the existing discussions of regional integration as the RCEP, ASEAN could consequently mediate the rivalry between China and Japan.41 By paying deference to the centrality of ASEAN, China did not have to tangle with Japan and could sidetrack the longstanding dissents on the primary institutional platform of regional cooperation.

It is indeed obvious that Abe’s decision to join TPP negotiations was a game changer.42 However, it brought about unexpected effects. Dual dynamics of cooperation and competition has unfolded between China and Japan, whereas the competitive dynamic between the US and

41 Goh, The Struggle for Order.
China strengthened, as both countries engage in inter-institutional balancing game to create the advantages regional order of their preference. China has begun to show an inclusive posture toward East Asian countries including Japan. As its participation in the TPP and the RCEP demonstrates, Japan attempted to engage in inter- and intra-institutional balancing simultaneously. By contrast, competition between the US and China intensified, as both countries tend to seek inter-institutional balancing as a primary means to balance each other.

**The TPP and Institutional Balancing**

**The TPP and 21st Century Trade Rules**

The TPP agreement is a 21st century high quality free trade agreement (FTA) encompassing a vast range of issues, and comprised of 30 chapters. It includes most issues that any FTA would: goods, rules of origins, pharmaceutical patents, trade remedies, sanitary and phytosanitary issues (SPS), technical barriers to trade (TBT), services, intellectual property rights, and government procurement. It is a 21st century FTA, as the participating countries proclaim, because a large portion of these issues are not regulated under WTO rules and norms.

The negotiation process was arduous, as if the process reflected the partnership’s complicated issues. The US, as could be expected, held the keys. The US was the only directly involved party in the issues that presented the final hurdles, including government procurement, intellectual property rights (IPR) of new pharmaceutical products, tariffs, and quotas on dairy products and rules of origins. IPR for new pharmaceutical products, especially, was an issue where the interests of participating countries acutely collided and hampered negotiations up until the end. The US and Australia were arguing each other. The US argued for long-term
protection of IPR in order to promote technical innovation by businesses, demanding 12 of exclusive protection, while Australia stuck to five years, citing the fiscal burdens on health insurance system and patients’ rights. Government procurement was expected to be a rough area, because eight of the participating countries, including Vietnam and Malaysia, were not signatories of the “WTO Government Procurement Agreement,” which guarantees an open and transparent government procurement process. A multitude of issues lay between the US and Japan, the two pillars of the TPP. These included rule of origins for automobiles, pharmaceutical patents, IPR, and, among agricultural issues, the degree of opening of the dairy market and Japan’s five major agricultural product markets – rice, wheat and rye, animal products, dairy products and sugar. The degree of agricultural opening was a particularly difficult area, with agriculture previously an exceptional holy ground when it came to FTA negotiations.

Participating countries in the partnership proclaim the TPP could act as a standard for 21st century FTAs, considering that these various difficult issues were overcome. Nonetheless, it should not be overlooked that major issues were resolved through compromise among the participating countries. For example, the US and Australia compromised with one another on intellectual property by setting an initial protection of IPR for five years with future extension, while competing products were left under review.

Rules of origin were also a major issue as they tend to smoothen intra-regional trade, and the TPP is a mega-FTA extending the existing bilateral FTAs to a multilateral one. The parties eventually came to agree upon cumulative rules of origin, which eliminates tariffs if more than 55 percent of the parts were procured within the region. This is significant because cumulative rules of origin can resolve the noodle bowl effect. Japanese automobile manufacturers will greatly benefit from it in the US market, because they have production networks throughout
Southeast Asia and Mexico. Nonetheless, 55 percent is a relatively low figure considering the 62.5 percent cutoff in the North American Free Trade Agreement (NAFTA). The US also achieved additional victory on pickup trucks, because the agreed terms provide a longer protection period for them.

Compromise occurred between the US and Japan, as well. Their negotiations were at a stalemate until the beginning of 2015. The ministerial meetings in Tokyo between the US and Japan in April 2015 provided a venue for them to close the gaps on most issues, save some items such as rice and automobiles. Agreement became more viable as Japan decided to lower tariffs on US beef from the current 38.5 percent to around 10 percent in the coming decade. The negotiations were completed in Atlanta when Japan agreed to decrease the tariff on US beef to 27.5 percent the instant TPP is in effect and, eventually, to 9 percent within 16 years over several stages. On rice, one of the most heated issues, Japan agreed on Tariff Rate Quotas (TRQ) rather than lower tariffs, to increase quota on US rice from the current 50,000 thousand tons to 70,000 tons within 13 years. The US, on the other hand, agreed to abolish the current 2.5 percent tariff on Japanese cars and 25 percent on Japanese trucks within the coming 30 years and increase TRQ on Japanese beef from the current 3,000 tons to 6,000 tons within 15 years.

The participants, including the US and Japan, settled on the agreement by showing flexibility while still maintaining the original purpose of the TPP as a 21st century high quality FTA encompassing a vast range of issues. Strong commitment to the partnership can be witnessed by the fact that the trade ministers of the 12 countries involved in the negotiations extended the cabinet meeting deadlines. This was because the TPP will result in not just large economic effects but also strategic one.
The United States Trade Representative (USTR) that took the de facto lead in the negotiations, noted five economic repercussions of the TPP. First, it presents new opportunities and benefits to corporations, laborers and consumers because it enables comprehensive market access. Second, its regional approach to commitments promotes developments in production and supply chains, and accelerates economic integration and improves efficiency. Third, it will facilitate innovation and boost production and competitiveness as it addresses new trade challenges such as the role of state enterprises in the digitalized and globalized economy. Fourth, it seeks concrete plans to strengthen the capacity of countries at diverse levels of economic development, as well as corporations at various scales, by allowing them to benefit from inclusive trade. Lastly, it is designed to be a platform for regional trade and to include additional countries in the Asia-Pacific region.

The TPP is different from previous FTAs that aimed to abolish tariffs. It is expected to provide the basis for new trade regulations, stimulate economic integration among the members, and be the catalyst for a new regional and world trade order. Two points support these expectations. First, the TPP is a potential new trade standard. It includes a wide variety of rules and norms that are yet to be established under the WTO. These regulations are highly likely to become a new standard, or an important measure at the least, for the WTO’s multilateral FTAs as well as other mega-FTAs such as the Trans-Atlantic Trade and Investment Partnership (TTIP) or the Regional Comprehensive Economic Partnership (RCEP). In this context, the US and Japan did not officially declare China’s exclusion. However, China cannot yet fulfill the high standards of the TPP on state enterprises, environmental and labor standards, or intellectual property rights. Considering this, the intentions of Japan and the US seem to be to weave new trade rules, shaping the 21st century trade order and world economic order to benefit themselves, while excluding China from the process. This is why Abe argued that China joining
the TPP will have immense strategic meaning. China seems to be expediting the RCEP negotiation process as a short run reaction to the TPP. The RCEP is a viable alternative for China, because it will be larger than the TPP when signed, considering it has 16 members.

Second, the TPP will alter FTA competition among major actors in East Asia. It is likely to be a game changer, shifting the center of the FTA game, persisting from the late 1990s, from bilateral FTAs to mega-FTAs. The TPP will fundamentally change the nature of the game, because it will stimulate mega-FTAs in the international trade arena. Particularly, the TPP can alter Japan’s status from a follower of its major competitors, such as South Korea, to a leader. The Japanese government seems to care a lot about FTA competition with South Korea. As evidenced in their domestic announcement on sealing the TPP, they explicitly stated that the TPP is on a higher level than the Korea-US FTA. For example, the Japanese government emphasized that the TPP instantly abolishes 87.4 percent (by number of items), or 81.3 percent (by amount of exports), of tariffs, a greater reduction than that of the Korea-US FTA, which is at 83.0 percent and 77.5 percent, respectively. This competitiveness is also seen on South Korea’s side, when the Korean government emphasized just after the TPP was agreed on that the TPP only reduces US tariffs on automobiles over a period of 25 years, whereas the Korea-US FTA abolished them instantly.

Rethinking the TPP: Linking the Economy with Security

The nature of the TPP was fiercely debated upon the entrance of the US into the negotiations. The gist of the debate was whether the TPP was purely about economic benefits or whether it had security implications. However, we might fail to accurately capture reality if we approach the TPP by separating its economic and security aspects, or by focusing on only
one of the two. Focusing on the TPP’s economic effects and overlooking its security implications would amount to a misunderstanding of the nature and path of future changes in the regional and world order. The same goes for reading too much into the security concerns of the TPP. Understanding the TPP as a US tool to contain China is somewhat valid, but can be an excessive interpretation.

The key is how, not whether, the economy and security are linked. In this regard, the TPP should be understood as redesigning the global and regional architecture that encompasses the economy and security. Yet this process is not a completely open one in which the focus is to maximize economic interests, nor is it a completely closed one aimed at containing China. Major actors in East Asia are engaging in the game in order to occupy a better and more effective position for projecting their own interests on the future structure, while also forming a regional architecture. The fact that the US, which led the TPP, and China, which is leading the RCEP, did not formally exclude one another also reinforces this case.

How, then, does the TPP link security and the economy? The TPP originates from the Trans-Pacific Strategic and Economic Partnership that was signed in 2005 among the small countries referred to as P4: Brunei, Chile, New Zealand and Singapore. It took the current 12-member format as additional countries – Australia, Canada, Japan, Mexico, Peru, the US and Vietnam – joined the negotiations beginning in 2008. The TPP is not a US plot to contain China: it was the P4 who introduced a large portion of the major agenda items in the TPP negotiations. The US is not an original member nor did it take the lead in forming the TPP. It seems to be a case of the “tail wagging the dog,” at least in appearance, since four small countries provided the foundation of the largest free trade zone including the US and Japan.

What is the economic motivation of the countries involved in the TPP negotiations? First of all, the US and Japanese governments both understand the increasing need to make
connections with the Asia-Pacific region, which contains the most vibrant economies worldwide. To alleviate increasing uncertainty after the global financial crisis, the Obama administration repeatedly pointed out the need for export expansion and employment creation, and the TPP serves as a practical solution to do so. Regardless of the partial achievement of *Abenomics*, there are warning signs of the possibility of another recession. The Abe administration is emphasizing the importance of the TPP as one facet of *Abenomics*’ third arrow to improve the foundations of the Japanese economy. The Abe administration perceives the liberalization and deregulation measures that have to be implemented under the TPP as a catalyst for structural reform of the Japanese economy. This perception is aligned with former Prime Minister Naoto Kan of the Democratic Party of Japan, who first showed interest in participating in the TPP negotiations in October 2010, and whose administration referred to the TPP as “the third opening.”

Secondly, another economic factor under the purview of the TPP is related to attempts to fill the gap between 21st century type production and trade and 20th century trade regulations. In April 2013, when Japan formalized its participation in the negotiations, the number of FTAs concluded among Asian countries amounted to 76. Despite this, there were continuing criticisms that the expected economic effects of the FTAs were not occurring. Although many East Asian countries invested much time and many resources to conclude a number of FTAs, the beneficiary companies were not properly utilizing them. This was because many existing bilateral FTAs were of a superficial nature, having low convergence in rules of origin and other issues. Arguments stating that the “noodle bowl” effect should be resolved to promote practical economic integration were raised. The TPP emerged as a strong alternative to solve this problem.
While it is true that economic motives, meanwhile, strongly affected the choice of major countries, such as the US, to promote the TPP, the strategic meaning of the deal should not be underestimated. The fact that the US participated in trade negotiations led by the P4, with only limited economic effects due to trade liberalization, contains considerable strategic meaning. Also, even if the P4 started the TPP, it seems that the US participated in the TPP negotiations only after realizing its potential for the 21st century world trade order and regional architecture. The Obama government encouraged Japan’s participation not just to increase the economic effects of the TPP, but also to solidify the strategic characteristics of the TPP.

The TPP is inseparable from the America’s rebalancing policy, an attempt to shift its foreign policy focus to Asia. The Obama administration’s rebalancing policy is not simply a case of containing China or strengthening Washington’s military presence in the region, but is an effort to strengthen all elements of US power in Asia. Via this rebalancing policy, the Obama Administration is attempting to transform itself from an offshore stakeholder to an offshore leader in the Asia-Pacific region. As a result, they are strengthening traditional alliances with South Korea, Japan and Australia and participating in intra-regional multilateral systems such as the EAS. Furthermore, through the TPP, the US is seeking to take the lead in reorganizing the architecture of the East Asian region. From this aspect, the TPP is acting as a channel to closely connect the economy and security.

The Japanese government also seems be attempting to connect its economic interests and strategic objectives through the TPP. Although in the 1990s, the Japanese government successfully negotiated the first FTA among East Asian countries with Singapore, Japan had difficulties in actively promoting bilateral FTAs, considering the interests of politically strong domestic industries such as agriculture. Consequently, it realized that it has lagged behind in FTA competition with neighboring countries such as South Korea. As a measure to recover
from this in one fell stroke, it began to take notice of mega-FTAs. The Japanese government pushed for mega-FTAs as a means to catch up with competitors, overcoming its lag via parallel promotion of the TPP, RCEP, and the Japan-EU FTA. Among these, the TPP holds the highest policy priority, meant to resolve concerns that Japan will be in a disadvantageous position if it does not conclude FTA negotiations with the EU and China, especially so if it did not participate in the TPP negotiations.

The Abe administration also promoted the TPP as an aid to its policy shift. Through participation in the TPP, the economic effects of the TPP become not only tangible, but there is also a simultaneous effect wherein Japan can hold an advantageous position in the restructuring of the East Asian regional order by cooperating in the strategic plans of the Obama administration. As the importance of the TPP in Obama’s rebalancing policy increases, Japan’s participation in the TPP negotiations is regarded as a means of maximizing not only economic effects but also diplomatic security effects. This changed into a central means of not just restoring but also strategically strengthening US-Japan relations, which were tense during the government of the Democratic Party of Japan, and further strengthen strategically. From this point of view, the Abe administration also actively promotes connecting the economy and security through the TPP.

**Mega FTAs and South Korea’s Middle Power Diplomacy**

For South Korea, the TPP has become a current problem rather than a prospective one. Now South Korea has to thoroughly review not only the TPP, but also the changing direction of the world trade order and regional architecture after the conclusion of the TPP. First of all, the government seems to have decided to participate in the TPP. The important point is not the
participation itself, but the timing and conditions of participation. The economic gains and losses of participation and non-participation should be the basis of such a decision, and are a combination of tangible issues, such as tariff elimination, and intangible aspects, such as reflecting the position of South Korea in the process of establishing new regulations. The claim that the influence of the TPP can be minimized by focusing on the effects of tariff liberalization is only half-truth.

Secondly, the South Korean government should strategically review what method of participation can maximize its national interests. In order for South Korea to become the 13th participating member, it may pursue negotiations independently, or instead consider forming a group with other countries, including Indonesia, Thailand and the Philippines that have showed interest in participation.

Thirdly, the systematic prospect of the trend toward mega-FTA negotiations unfolding in the East Asian region, and a strategic approach to that prospect, should be closely examined. After conclusion of the TPP, much attention has been focused on the RCEP. Depending on the perspective, the TPP and RCEP can be seen as either contradictory or complementary. From South Korea’s point of view, focus should be put not on their contradictory nature, but on a realistic way to harmonize the two. In reality, the number of countries participating in both the TPP and RCEP amount to seven, so there is no need to prematurely conclude that the two will contradict each other. Considering that, these countries should cooperate and work to harmonize the two.

Fourth, it is clear that the conclusion of the TPP will greatly influence US-China relations. Some expect that since the TPP is indirectly connected to the response strategy of the US and Japan towards China, the US and China will redouble their efforts to independently design the regional architecture, each focusing on the TPP and RCEP, respectively. Although it is difficult
to completely deny the possibility of a US or China-led architecture, various routes toward a regional architecture are being proposed, triggered by China’s suggestion to form a Free Trade Area of the Asia-Pacific (FTAAP) at the 2014 APEC summit. South Korea should suggest a persuasive course in which the TPP and RCEP can be harmonized and, based on this, exercise a level of diplomacy that can garner cooperation from countries in the region.

Lastly, systematic process management in the dimension of domestic politics is needed. Considering the US presidential election schedule, it is expected to take 2 to 3 years for the TPP to come into effect. For South Korea, this means that there is time to prepare. One reason for South Korea’s wariness in participating in the TPP negotiations was the domestic political burden regarding the sectors that may be harmed by the TPP. The time needed for the TPP to come into effect may allow the South Korean government to not only alter their foreign policy strategy, but also to prepare to handle the domestic policy dimensions. In order to establish a domestic and foreign strategy that makes the most of the TPP, a variety of thoughts and ideas should be considered.