Unlikely Pivotal States in Competitive FTA Diffusion:
The Effect of Japan’s TPP Participation on Asia-Pacific Regional Integration

Mireya Solís
Senior Fellow, Brookings Institution
Associate Professor, American University
MSolis@brookings.edu

And

Saori N. Katada
Associate Professor, University of Southern California
skatada@usc.edu

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Abstract:

How can a state with dysfunctional trade politics spur the negotiation of major free trade agreements (FTA)? Using the case of Japan’s participation in the Trans-Pacific Partnership (TPP), we develop an analytical framework on FTA diffusion that takes into account multidimensional (economic, legal, and political) competitive pressures, and the ability of states to act as pivots in triggering FTA cascades. We disaggregate the makeup of a pivotal state into two main components—capability and credibility—and underscore Japan’s significant latent capabilities, but its serious credibility shortcomings. The TPP’s boost to Japan’s credibility raised the possibility of significant economic, legal and political externalities for specific countries which responded by reaccelerating FTA initiatives that had long stalled: the trilateral China-Japan-Korea FTA, a 16 state East Asian FTA, and the Japan-EU trade negotiations. This study extends the theoretical frontier in policy diffusion studies by clarifying the combination of factors that allows some states, but not others, to activate the externalities behind the dissemination of defensive FTAs.
Introduction

Japan is an unlikely pivotal state. After more than a decade of negotiating preferential trade agreements since 2000, it accomplished little: 13 free trade agreements (FTA) that cover 19 per cent of its exports and a stalled blueprint for region-wide integration. Japan fell behind China in exercising active FTA diplomacy in Southeast Asia and was surpassed by South Korea in negotiating with industrial giants such as the United States and Europe. Given the rather marginal role that Japan has played in the FTA movement, it is indeed striking that when it signaled its desire to join the Trans-Pacific Partnership (TPP) agreement, it triggered ‘chemical reactions’ (to use the words of former Prime Minister Noda) in regional and global FTA diffusion. Japan’s pivot towards the TPP prompted China to accelerate the joint study of a Northeast Asian trilateral FTA and helped ASEAN overcome its indecision vis-à-vis the ASEAN+3 or +6 proposals by opting instead for the ASEAN++ framework among 16 countries. Even the European Union (EU), which was not originally interested in a FTA with Japan, changed its mind. Why would a state with well-known dysfunctional trade politics exert such influence in the spread of FTA blueprints in East Asia and beyond? We find the answer to this question in diffusion dynamics centered on the notion of multi-dimensional competition triggered by pivotal states.

While the diffusion literature has alluded to the importance of trend-setting countries whose actions encourage imitation by others, we have in mind a different phenomenon. Of interest here is not which state first negotiates a FTA, but rather which state’s FTA policy triggers a competitive adjustment by peer competitors, thereby changing the viability of alternative tracks for trade integration. A state’s ability to act as such a ‘pivot’ in the FTA race hinges on its capability and credibility along three key dimensions of FTA rivalry: economic,
political, and legal. In the context of economic competition, a pivotal state with sufficient economic size (capability) has the potential to impose significant externalities on others, while its credibility hinges on how much economic liberalisation the state can endorse. In the political field, capability is power or leverage (structural or relational), while credibility is leadership. In the rule-making aspect, capability is whether a state has an advanced legal system and strong template for standard-setting, while credibility comes from the actual willingness to implement these standards internationally.

Using this analytical framework, we argue that Japan had capability in all three dimensions prior to its TPP commitment, but it was only after Japan revealed its intention to join the TPP that it gained credibility to act as a pivotal state, which triggered reaction by others. This paper is organised as follows. Section one develops the analytical framework of pivotal states and competitive FTA diffusion and contrasts it to other alternative explanations. Section two analyses the reasons behind Japan’s credibility gap, with a focus on how its political system was previously unable to overcome the resistance of vested interests to trade liberalisation. Section three hones in on the critical juncture of the regional and transregional reactions to Japan’s expressed interest in joining TPP negotiations. Section four applies our analytical framework on pivotal states and multi-dimensional competition to explain the chain reaction to Japan’s TPP announcement. The conclusion summarises our main findings and discusses the broader implications of our analysis for the conceptualization of state agency in diffusion studies.

1. An Analytical Framework for Competitive FTA Diffusion and Pivotal States

Policy diffusion has emerged as a key area for scholarly inquiry in international studies (Solingen, 2012). In large part, this is due to the realisation that policies frequently disseminate
in temporal clusters, so that specific waves of policy propagation are discernible. These policies range from broad paradigms that define the states’ roles and appropriate rules of intervention in the economy (Keynesianism vs. monetarism), to formulas for regional integration (supranational vs. intergovernmental), preferential investment and trade agreements, and taxation policies, to name a few examples.²

The cornerstone of the diffusion approach is the notion of policy interdependence where government choices are interconnected. In other words, ‘the prior adoption of a trait or practice in a population alters the probability of adoption for remaining non-adopters (Strang, 1991: 325).’ Hence, the diffusion approach moves away from the conventional political science approach of analysing varied domestic responses to common external shocks, toward studying the influence of peer pressure in propagating policy paradigms (Garret et al., 2008: 344, Braun and Gilardi, 2006).

Earlier work on policy diffusion identifies four major mechanisms of proliferation: (1) competition, as a horizontal economic process whereby states adopt policies to enhance their attractiveness vis-à-vis competitors; (2) coercion, as strong states pressure or manipulate incentives to force weaker states to adopt particular practices; (3) rational learning, as states adopt a policy after they assess its benefits, and (4) emulation, as states adopt policies they deem appropriate from socio-cultural peers (Simmons, et al, 2006, Dobbin et al, 2007). More recently, in a call to systematise the study of diffusion dynamics, Solingen (2012) has proposed four main organising concepts: stimulus, medium, agents, and outcomes. Hence, the study of diffusion requires discussion of the initial triggers and vehicles of policy dissemination, analysis of the political and social agents that help or hinder the spread of policies, and measurement of transmission results.
Taking into account these developments in the field of diffusion studies, we propose an analytical framework to explain the diffusion of FTAs in the Asia-Pacific region centered on two pillars: a multidimensional understanding of competitive diffusion dynamics and a focus on the role of pivotal states. Our formulation allows us to offer a multi-dimensional view of competition sources beyond economic rivalry and to focus on underappreciated actors who influence dissemination dynamics not through policy innovation but by imposing with their FTA policy heavy externalities on others.

Our model, discussed in detail below, offers an explanation that overcomes the shortcomings of three alternative accounts of FTA proliferation. The first alternative argument, a “no diffusion” account, argues that the decision of a government to negotiate a trade agreement is not influenced by the prior actions of other countries, but predominantly determined by domestic politics (Grossman and Helpman 1995). Consequently, in this view, we should not expect a temporal clustering of FTA negotiations. The second explanation, a “trend-setter” account, focuses on the agency of diffusion dynamics, but only trend-setting countries are deemed influential in unleashing dissemination as they influence the behavior of others through their policy innovations (Weyland 2005). The third argument, an “emulation and learning” account, posits that these are the main dissemination vehicles since governments emulate from socio-cultural peers policies they deem appropriate for them, or learn from policy experiments carried out elsewhere (Bennett 1991; Beissiger 2007; Meseguer 2005).

**Pillar One: Multidimensional competitive pressures**

Why a focus on multidimensional competition as the driver of FTA proliferation? We agree with Franzese and Hays (2008: 746) that the key transmission belt for diffusion lies in
negative externalities, whereby the actions of one actor affect the marginal utilities of possible courses of action for others, and therefore that the competitive mechanism creates the most powerful incentive to react to the prior actions of one’s competitive peers. Furthermore, we posit that externalities go beyond economics (as powerful as they may be) to include security-political and legal ramifications. We review briefly each of these rationales in turn.

**Economic competition** is paramount in policy diffusion. Baldwin’s domino effect thesis (1997) which underscores incentives for countries to join in or negotiate countervailing FTAs to neutralise trade diversion, is the most influential theory of policy diffusion in a FTA policy context. Recent elaborations on the ‘domino’ thesis start from the premise that loss avoidance generates a much stronger response from lobby groups than does profit maximisation. Katada and Solís (2010) rely on prospect theory to show that actors are more risk averse when confronted with gain opportunities and engage in bolder actions to avoid losses, and find that across different sectors in Japan such as agriculture, manufacturing, and finance, lobbying groups mobilise much more intently when their profits are threatened. Baccini and Dur (2012, 60-61) focus on the notion of uncertainty to explain why exporters will not lobby for gains as they are unsure about the market access conditions abroad and the actual benefits to be accrued through an FTA. However, exporters will lobby actively against losses because it is much simpler to calculate costs imposed by trade and investment diversion and define the strategy to restore the level playing field.

Defensive economic models of FTA proliferation focus not only on trade losses, but also on the role of investment diversion. Many North-South FTAs are driven not by trade concerns, but by discriminatory investment provisions that trigger mobilisation of multinational corporations to restore parity in investment conditions in important overseas markets (Manger
The operationalization of economic competition varies in each study, but several authors have corroborated statistically that defensive market concerns explain FTA sequencing (Baldwin and Jamovich 2010; Baccini and Dur 2012; Chen and Joshi, 2010; and Egger and Larch, 2008).

The economic and legal competitive dimensions of FTA competition are closely intertwined since FTA negotiations increasingly pursue deep integration beyond market access negotiations. For instance, in a survey of 96 FTAs, the WTO found that since the year 2000 there has been a marked increase in the number of WTO+ and WTO-X disciplines included in FTAs (WTO, 2012: 131).

Two interrelated factors seem to be driving an expansion in rule-making competition through FTAs. First, as tariff elimination has made significant progress in the world economy, non-tariff barriers have emerged as the most formidable obstacles for market access. These policy measures are non-transparent and hard to quantify, and are frequently in place for the purpose of achieving other public policy objectives. The trade agenda has become exponentially more complicated because it now revolves around behind-the-border regulatory measures which require trade negotiators to determine which policies have discriminatory intent and which ones serve legitimate social and public purposes. Second, the spread of production networks and the consequent growth of vertical trade specialisation (Manger, 2012) has dramatically changed the demand for the types of investment and trade rules. As Baldwin (2011: 3) argues that the deep integration agenda of FTAs on competition, capital movement, Intellectual Property (IP), and investment, is geared to meet the demands of fragmented production, global trade, and infrastructural services to facilitate these activities.

Whether the deep integration rules of FTAs are discriminatory or not has generated debate. Baldwin (2011: 15-19) downplays the discriminatory effect due to the public nature of
regulation (e.g. improvements in competition policy apply equally to all market participants – irrespective of the nationality of foreign companies) and the international mobility of MNCs who can use their affiliates in other countries to reap the advantages of the host state FTA network. However, as he himself acknowledges some of the disciplines can be used in a discriminatory manner (anti-dumping and countervailing duties, service liberalisation), and to the extent that firms have to adjust their foreign investment plans or are unable to open affiliates abroad, the FTA provisions can impose an additional burden.

Two main dynamics are at work in the competition over FTA rule-making: ‘standard setting’ and ‘lock-in.’ These dynamics embody the discriminatory and nondiscriminatory aspects of the FTA rules agenda. In ‘standard-setting,’ we expect governments to use FTAs to disseminate new rules that can be incorporated more widely and perhaps eventually become a multilateral standard. In ‘lock-in,’ we anticipate governments to put forward more idiosyncratic rules that apply only to their FTA network and impose a cost to countries that operate with different standards. For both strategies, early mover advantages are a powerful incentive to join the FTA race.

We should note, however, that free riding should be a more frequently observed behavior if the benign effect of FTAs is prevalent (creating rather than distorting trade). In other words, if a state expects to benefit from the rules in an FTA negotiated by other states, it has little incentive to spend resources on negotiating subsequent FTAs, since it can simply expect the benefits to trickle down. However, the clustered negotiation of FTAs seems to reflect the cascade effects that are more in accordance with the negative externalities scenario.

FTAs are useful not only to generate gains from trade and draft new economic rules, but also to achieve broader foreign policy goals. For instance, Ravenhill (2010) makes the case that
East Asian states have used FTA policy mostly as a political effort to improve relations with other states, and to avoid isolation from this diplomatic trend.

The range of foreign policy goals in areas of political and security relations that states aim to achieve through FTAs is wide and very much contingent on the power resources available to each state. Hence, most of the literature on strategic FTAs makes a distinction between the strategies of large and small powers (Stallings and Katada 2009). As Wesley (2008: 218) remarks, great powers have traditionally relied on the ‘gravitational pull’ of their economies to influence other states’ behavior. A case in point is the Bush administration’s policy of rewarding states aiding in the Washington-led anti-terrorism campaign with preferred market access to the US in the form of FTAs (Mochizuki, 2009). More generally, the fact that great powers enjoy large markets and frequently act as security guarantors for allied states enables them to use FTAs to consolidate their positions as regional leaders. By dictating the terms of economic integration, they can define the membership of regional blocs, the sequence of the integration movement, and the availability of side payments. However, a bid for leadership in the regional integration process can generate a counter-response from other great power competitors with the ensuing development of alternative and/or overlapping FTA networks (Solís and Katada 2009).

Small powers have a different political-security calculus. As Mochizuki (2009) points out, FTAs offer secondary states the ability to hedge by seeking negotiations with various large powers, which neutralises the large powers’ influence. Also, smaller states can use FTAs to reinforce security ties with existing allies. For instance, Lee (2013) argues that the KORUS FTA marked the critical transition in South Korea from a reactive and defensive FTA policy to a bolder strategy that aimed to transform the US-South Korea partnership into a comprehensive alliance. Finally, FTA diplomacy is useful to smaller trading nations to ‘punch above their
weight’ by constituting themselves as FTA hubs through the development of extensive FTA networks as seen in the examples of Chile, Mexico, South Korea, and ASEAN (Solís and Katada 2009).

In short, the range of economic, legal, and political-security interests driving FTA proliferation is wide, and the interaction of these different objectives in the design of states’ FTA policies is complex. However, not all states can activate competitive FTA diffusion dynamics among their peers. It is the notion of pivotal states that allows us to explain such ‘responsiveness differential.’

**Pillar Two: Pivotal states**

A pivotal state is a state whose actions trigger a competitive adjustment by peer competitors that may change the viability of alternative tracks for trade integration. Of interest here is not which state first negotiates an FTA, but rather which state’s FTA policy is capable of shifting the trade strategies of competitive peers to a significant degree. Some of the diffusion literature has focused on the initial triggers and in particular on the role of innovators who establish trends that other states/agents subsequently copy or counteract (Solingen, 2012: 632). However, recent work by Patel and Bunce (2012) on the spread of protest movements in authoritarian countries shows that in some instances it is the actions of pivotal states (and not the ‘early risers’ where protests initially originate) that triggers true cascade effects in the wave of anti-regime demonstrations. According to these authors, developments in these ‘late-comer’ states helped magnify the geographical scope of protest movements by demonstrating the portability of the innovation and the fact that these social movements could survive in less hospitable environments.
How and why are the actions of pivotal states in the area of international trade influential over the strategies of other states? We argue that pivotal states’ actions unleash the power of diffusion by motivating increased competition in economic, legal and political spheres as these actions tip the balance among the players in all three spheres. We attribute this diffusive power of pivotal states to a combination of capability and credibility. Only when a state has both high capability and credibility does it become a full-blown pivotal state (see Table 1). States with the requisite economic, political and legal capabilities can impose large externalities on others with their FTA decisions. In the world of trade, we expect pivotal states to be states that have large markets, act as hubs of production networks and possess related financial, technological, and managerial advantages, have well-developed legal systems and enjoy regional diplomatic clout. At the same time, pivotal states must possess the domestic and international credibility necessary to ink significant trade deals. Such credibility hinges on their past record to overcome internal opposition to market opening and to be proactive in international trade negotiations.

At the other end of the spectrum, we can identify ‘trivial’ states whose actions do not influence dissemination patterns since they have few economic or political resources, and lack trade negotiation credibility. Smaller countries that nevertheless have staked out an activist trade negotiation agenda are referred to in our framework as ‘committed states’ since they score high in their domestic and international commitment to trade talks but generate only moderate externalities on others. The ‘unlikely pivotal state’ combines the requisite economic and political capabilities, but has a poor record in overcoming domestic opposition to market liberalisation and playing a leading role in international negotiations.
Although far from an exact science, we could map states’ prospect for influencing dissemination outcomes across the two axes of credibility and capability. Figure 1 shows in broad strokes where some states in the Asia-Pacific region fall in the capability-credibility nexus. Because of their high capability and credibility, the US and China are two pivotal states whose trade policy undoubtedly impacts the FTA diffusion process. South Korea is classified as a ‘committed state’ since it has actively negotiated important FTAs (with the US and EU). Given the South Korea’s moderate capability (in terms of economic size), however, the KORUS FTA did not spur a diffusion wave of large-scale FTAs.

The unlikely pivotal state group refers to countries which have the capability to influence the course of FTA diffusion, but significantly lack credibility. As discussed below, Japan has had very dysfunctional FTA policy in the last ten years. India belongs to this group because it has significant market potential, but has chosen a defensive trade policy stance so far. The central question for this study, then, is what triggers an unlikely pivotal state to generate a FTA diffusion wave? We attempt to answer that question by looking at the leverage that Japan acquired through its bid to join the TPP.

2. Credibility Deficit: Japan’s FTA Politics 2000-2010
The evolution of Japanese FTA politics in the last 15 years underscores the credibility gaps that constrained Japan’s ability to influence FTA diffusion in the Asia-Pacific region. Having benefited tremendously from the GATT multilateral trade regime during its rapid growth era (1960s to 1980s), the Japanese government showed little interest in bilateral or regional preferential trade agreements despite the rise of trade regionalism in Europe and North America since the late 1980s (Mansfield and Milner 1999). Constrained by a globally uncompetitive and politically influential agricultural sector that constituted a key political base of the Liberal Democratic Party (LDP), the Japanese government cautiously managed the state’s trade liberalisation commitments. Japan inked its first FTA only at the onset of the 21st century, selecting Singapore first because it was easier to negotiate with a small open Asian economy that had an extremely small agricultural sector (Munakata 2006, Yoshimatsu 2005). Japan’s second FTA negotiation with Mexico (signed in September 2004) was far more challenging since agricultural commodities represented more than 20 percent of its exports to Japan (Solís and Katada 2007; 285). Since then, the Japanese government has engaged in bilateral FTAs both within and outside Asia, and has negotiated a subregional agreement with ASEAN. The literature on Japanese trade policy has identified several factors explaining why Japan became a late FTA convert.

First, as it is true for many other states, Japan’s emerging interest in FTAs relates to its concerns about the global and multilateral trade regime. Major trade players in the world have begun to see regional and bilateral preferential trade agreements as an attractive trade strategies to gain leverage in the multilateral negotiations (Mansfield and Reinhardt 2003) or establish an insurance against their possible failure (Perroni and Whalley 2000). As the Doha Round exhibited difficulties in the 2000s, a hedging strategy became necessary for Japan (Pempel and
Urata 2005; Munakata 2001). Meanwhile, the Japanese government began to prioritise control on the trade negotiation agenda over gains from trade by negotiating bilaterally with smaller countries where it could limit its agricultural concessions and avoid domestic backlash (Pekkanen, Solís and Katada 2007). Second, there was a call from Japan’s big businesses demanding that Japan not miss the FTA boat (Yoshimitsu 2005, Yanagihara 2004), especially to avoid the deleterious effects of trade diversion (Solís 2003). The peak big business lobby Keidanren managed to impose ‘naiatsu’ (internal pressure) by successfully depicting the agricultural sector as a force of resistance that placed Japanese businesses at a great disadvantage internationally by blocking FTA efforts by the Koizumi administration (George Mulgan 2005).

Despite having concluded 13 FTAs by 2012, the Japanese government has never been a dynamic or entrepreneurial FTA initiator. Its timid approach to FTAs is visible, first and foremost, in the choice of small economic partners who together only represent only 19 percent of Japan’s overall exports (Solís 2013a). Therefore, Japanese FTAs to date have had limited impact on real GDP gains (Kawasaki 2011). Japan’s FTA negotiations with a few medium size trade partners such as South Korea (6.7 per cent of exports) and Australia (2 per cent of exports) stalled for several years with no sign of a breakthrough. And the Japanese government was particularly slow in approaching for FTA negotiations the US and China, its two largest trade partners. The EU, on the other hand, was reluctant to negotiate an FTA mostly out of concern that tariff liberalization would produce a massive inflow of Japanese cars.7

Second, to judge by the trade liberalisation ratio, the quality of Japanese FTAs is low for an industrialised state since all Japan’s FTAs fall short of the WTO standard of 90 per cent of tariff lines to be eliminated ten years after agreement enactment (Solís 2012). Although the Japanese government emphasises the trade facilitation and economic cooperation elements in its
‘Economic Partnership Agreements,’ such concessions are extended often to mask the shortcomings in Japan’s agricultural liberalisation offers.

Finally, Japan’s FTA policymaking includes numerous veto players that have managed to politicise or block FTAs if they threaten to involve sensitive areas. The role of the agricultural lobby linked to Japan’s Ministry of Agriculture, Forestry and Fisheries (MAFF) is well-known, but there has also been significant opposition to the ‘movement of people’ section of Japan’s FTA with the Philippines, Thailand and Indonesia. The very institutional setup for FTA negotiation in which the involved ministries had equal status and effective mechanisms for bureaucratic coordination were lacking, made for a very cumbersome decision-making process. The strong role of the prime minister and cabinet office under Prime Minister Koizumi (2001-2006) was hard to sustain, and the subsequent sequence of short-tenured prime ministers was unable to move forward major FTAs (Solís 2010).

In short, Japan was late in joining the FTA trend, and even after it gained some experience, its trade policymaking remained highly fragmented and dysfunctional. After ten years of cautiously choosing its FTA partners and protecting its uncompetitive sectors through exemptions and managed tariff liberalisation schedules, Japanese agriculture is still highly protected and the manufacturing sector needs deregulation.


Japan’s past record in FTA diplomacy was a poor predictor of the wave of regional and extra-regional responses to Japan’s signal of interest in joining the TPP trade negotiations in late 2010. Japan’s TPP signaling opened a critical juncture in FTA diffusion both regionally and cross-regionally by accelerating the trilateral China-Japan-Korea FTA, spurring the launch of the
Regional Comprehensive Economic Partnership (RCEP), and persuading the EU to abandon its reluctance to negotiate with Japan. However, befitting its description as an ‘unlikely pivotal state,’ the Japanese government’s signaling on TPP was inconsistent, and on some occasions when it looked like its domestic constraints would prevail, the urgency of the counter-responses also diminished. All in all, the possibility that Japan could join the TPP still provided a major incentive in moving these large trade groupings forward.

The TPP’s origins date back to an agreement among four small APEC economies (Chile, New Zealand, Singapore and Brunei) that came into force in 2006. The Bush administration realised the potential of using an expanded TPP to advance its ‘gold standard’ FTA template in Asia and expressed its desire to join the talks in September 2008, and several other countries followed suit (Australia, Peru, Vietnam and Malaysia). The TPP has attracted widespread attention in the international trading system, not only because of its attempt to promote a trade grouping across Asia-Pacific, but also because of its stated commitment to avoid sectoral exclusions and to tackle non-tariff barriers, both of which have often compromised FTA quality (Solís 2012). Japan’s first signaling on TPP membership came unexpectedly when Prime Minister Naoto Kan announced his intention to join the TPP negotiations during his general policy speech on October 1, 2010. According to Sugawara (2012a) this sudden (and scarcely vetted) initiative aimed to accomplish four goals. The first was to improve the shaky US-Japan relationship after the mishandling of the Futenma base issue by the preceding Prime Minister Hatoyama Yukio. The second was to energise Japan’s stagnant FTA strategy in East Asia by strengthening its negotiation leverage vis-à-vis other countries. The third was to use the TPP as a step towards Asia-Pacific regional economic integration, which Kan would discuss as a part of the “Yokohama Vision” that he presented at the Yokohama APEC Summit in November 2010.
Finally, the TPP was considered as a way to provide ‘shock therapy’ for the recessionary Japanese economy in the aftermath of the global financial crisis.

Kan’s October 2010 speech sparked immediate reaction from both opponents and proponents of the TPP. The agricultural lobby forcefully denounced Kan’s TPP move, arguing it would devastate Japanese agriculture and lower its food self-sufficiency ratio. By contrast, the business community warmly welcomed Kan’s declaration. Kan’s own party, the Democratic Party of Japan (DPJ), quickly became polarised with opposing views on the merits of Japan’s participation. In the face of this opposition, Kan could only announce in the November 2010 APEC Summit his desire to initiate consultations with TPP countries to collect information. Nevertheless, describing the TPP as the ‘third opening of Japan,’ Kan remained committed to finding a way for Japan to join the TPP, and in January 2011 he announced that the Japanese government planned to make a decision on TPP participation by June that year. Despite delays arising from the Great East Japan Earthquake on March 11, Kan reconfirmed his intention for Japan to pursue the TPP at the time of G8 Summit in May 2011.

Nevertheless, later that summer Kan was replaced by the third DPJ prime minister in two years, Yoshihiko Noda, a move which further delayed momentum on the TPP. As the 2011 APEC Summit approached, Noda asserted his desire to secure Japan’s TPP participation, reigniting a heated political battle. MAFF and the Ministry of Economy, Trade and Industry (METI) released dramatically different estimates of the impact of TPP on Japan’s economy. The former predicted a 90 per cent contraction in rice production and 3.4 million jobs lost, whereas the latter estimated that failure to join TPP would result in losses of $128 billion dollars and 8 million job redundancies (The Japan Times, November 2, 2011). The DPJ remained unable to reach intraparty consensus, and it was also confronted with spirited opposition from both the
agriculture lobby and the medical association which claimed that the TPP would undermine Japan’s national health insurance system. Consequently, at the 2011 APEC Summit in Hawaii, Noda was only able to announce the start of consultations with TPP countries, and in the course of the following year, six TPP countries gave their support to Japan. Negotiations with the US proved particularly difficult and time-consuming as they centered on three sensitive issues: beef import restrictions, postal privatisation, and automobile market opening. In a last bid, when Noda called for an election in November 2012, he suddenly attempted to make the TPP a main election issue, but given the wide disapproval of the DPJ’s performance, the party was badly battered in the electoral contest.

Given that the LDP had taken a cautious position on the TPP, the decision on March 15, 2013, by new Prime Minister Abe Shinzo to seek TPP membership came as a surprise. The LDP’s electoral dominance, which lessened the leverage of the agricultural lobby to advance its anti-TPP campaign, as well as Abe’s own solid support ratings hovering at around 60 percent of population approving his cabinet, clearly facilitated this all-important political decision. Abe was further motivated by his desire to strengthen Japan’s relations with the US. The time was also running out if Japan wanted to influence the content of the TPP agreement as its negotiations are expected to finish by the end of 2013. With the announced launch in February 2013 of the US-EU FTA talks, Japan could be marginalised in devising the new rules on trade and investment (Nikkei News, February 14, 2013). Nonetheless, the Abe cabinet has made significant headway into making TPP a reality for Japan through several strategies aiming to marginalize the domestic opposition. First, PM Abe established a different negotiation setup for the TPP that aims for top-down leadership to overcome bureaucratic infighting and minimize the role of vested interests. Out of 100 government officials placed in charge of TPP negotiations, 30 of
them were to be deployed to diffuse domestic oppositions. Second, PM Abe has promised domestic constituents that the most sensitive agricultural commodities (so called “sacred five”) will be off limits in the TPP negotiations in order to cultivate domestic support, while at the same time exploring item-by-item concessions in these product categories to satisfy TPP demands. Finally, as a part of the “third arrow” in the Abenomics Japan growth strategy, PM Abe has pushed for agricultural reform through the newly established Regulatory Reform Council. Although the actual reach of the domestic deregulation measures and the final commitments in the TPP negotiations are not known at the time of this writing, PM Abe has certainly gone farther than most of his predecessors in pushing for more substantial market liberalization.

Though the process took over two years and often faced delays, Japan’s signaling on TPP membership nevertheless factored importantly in the evolution of three major FTA initiatives.

**China-Japan-Korea (Trilateral) FTA**

After China, Japan and South Korea spent six years conducting joint studies on the possibility of a trilateral FTA at the think-tank level, the three states’ governments agreed in October 2009 to include government agencies in their trilateral study group with the aim of producing a feasibility study by the end of 2012. In spring 2011, however, China advocated completing this feasibility study a year ahead of schedule. The pace of the CJK FTA negotiation accelerated dramatically once China’s move was confirmed by Japan and South Korea at the May 2011 trilateral summit meeting.

The CJK FTA’s acceleration was largely driven by Chinese worries over Japan’s participation in the TPP. Indeed, in the words of a seasoned Japanese trade negotiator: “as an
economist I had always believed that trade negotiations were driven essentially by economic factors. Witnessing China’s reaction to Japan’s potential TPP membership, made me realize the importance of political factors and dynamic reactions between the negotiations among countries. A central concern for China has been to prevent the TPP from becoming the central driver of Asia-Pacific trade integration. A common view in Chinese policy circles is that the TPP constitutes a ‘new tool for the United States to disturb, reshape and control Asian regional integration’ (Zhang 2011, 5), and along with the US ‘pivot strategy’ under the Obama administration, some have portrayed it as a way to contain China (Jin 2012). In that context, China sees Japan’s participation in the TPP as a crucial piece of Washington’s Asia-Pacific strategy. China is also concerned that Japan’s decision to start negotiating in the TPP ‘marks an important change in its Asia strategy’ as noted by the Director of the Institute of Asia-Pacific Studies at the Chinese Academy of Social Sciences (Yoshioka, 2011). Other Chinese scholars have worried that if Japan and South Korea join the TPP, they will be less keen to negotiate a trade agreement with China (Yonhap News, November 17, 2011). China’s response, therefore, was to accelerate its favored regional FTA initiatives, a sentiment voiced by Li Wei, president of the Development Research Center of the State Council who in a January 2012 speech urged Asian countries to focus on intra-regional initiatives as ‘close neighbors are better than distant relatives.’ In the opinion of He Liangliang, this remark is a direct reaction to Japan’s TPP policy (both statements cited in Yuan, 2012: 6).

Korea, however, has always been more reticent about the trilateral CJK FTA. Fearing an imbalance of economic benefits from tariff liberalisation (Cheong 2005), and weary of the negative impacts of the recently enacted Korea-US FTA, the Korean government was hoping to move on a Korea-China bilateral FTA first. As Japan’s TPP bid seemed to flounder in spring
2012, the announcement that Korea and China would move ahead first with their bilateral FTA came as a great shock to Japanese officials. At the time, JETRO estimated that such a bilateral FTA, in the absence of the trilateral CJK FTA, would impose market share losses for Japanese companies in China in the neighborhood of $5.3 billion dollars (Nikkei News, May 2, 2012). Because of the strong desire of both China and Japan to move forward with the trilateral FTA, however, this initiative was delayed but not abandoned.

The trilateral FTA’s high stakes were evident in the decision to launch the trade talks in November 2012 at the height of territorial disputes over the Senkaku-Diaoyutai and Takeshima-Dokto islands. Indeed, while media reports in late 2012 doubted the future of the trilateral FTA due to the uncertain diplomatic climate, Japan’s commitment to the TPP in spring 2013 cemented China’s desire to move forward. On March 19 Chinese Ministry of Commerce spokesman Shen Danyang stated that ‘concluding a FTA between Japan, China, and South Korea as quickly as possible would benefit all three nations.’ Japan’s METI Minister Toshimitsu Motegi summed up the progress on the trilateral FTA: ‘The decision to announce our entry into the TPP talks gave us some good tailwinds’ (both quotes in The Daily Yomiuri, March 28, 2013).13

Regional Comprehensive Economic Partnership

The Regional Comprehensive Economic Partnership (RCEP) among the ten member states of ASEAN and six other states (China, Japan, South Korea, Australia, New Zealand and India) was launched in November 2011 to create a ‘region-wide’ FTA. RCEP’s launch was remarkable in that it broke the stalemate that had long prevailed over two competing proposals for a region-wide FTA. On the one hand, China had proposed an East Asian FTA (EAFTA)
centered on the ASEAN+3 grouping (Terada 2010). On the other hand, the Japanese government had pursued an ‘expanded’ East Asian regional concept that included three additional members, Australia, New Zealand and India and was labeled the Comprehensive Economic Partnership of East Asia (CEPEA). Both sides insisted on the superiority of their respective initiatives. Even though in 2009 the East Asian Summit leaders mandated that the government officials of member states consider recommendations for both EAFTA and CEPEA studies, ASEAN states were hesitant to throw their support behind either of these proposals. ASEAN’s central concern was to remain in the ‘driver’s seat’ of East Asian FTA developments, and found ASEAN+1 FTAs to be the most conducive for that goal (and achieved six such deals by January 2010). Competition between China and Japan helped ASEAN maintain its centrality in the regional integration process.

China’s concern with Japan’s TPP participation, however, prompted it to suggest a joint Japan-China proposal on a blueprint for East Asian regional integration. This new Sino-Japanese consensus on a 16 nation FTA was revealed in an August 2011 meeting of trade ministers in Indonesia (Asahi Shimbun, November 11, 2011). Taken aback by China’s move, ASEAN states did not reach an agreement at that meeting on how to respond (Asahi Shimbun, November 18, 2011). However, in an effort to maintain its centrality, ASEAN announced a new approach in November 2011, an ‘ASEAN++’ formula whereby all six FTA partners were invited to join in the RCEP negotiations (Lim 2012; Pakpahan 2012). ASEAN’s goal to imbue the regional initiative with its preferred negotiating principles can be seen from RCEP’s founding document. Article 4 states that RCEP will ‘include forms of flexibility including provisions for ‘special and differential treatment’ to take into account different development levels.’
The roll-out of the RCEP coincided with Japan’s announcement at the APEC Summit that it would initiate consultations with TPP countries, and with Mexico and Canada’s declarations of interest in joining the TPP. With the TPP’s possible expansion, ASEAN feared that the US would dictate the terms of Asia-Pacific regional integration and impose a ‘high quality’ FTA with no exceptions on tariff elimination. Some voices in ASEAN also expressed concern that as some bloc members joined TPP but others did not, it could weaken regional solidarity. Japan’s potential entry into the TPP weighed heavily on ASEAN’s push for RCEP: ‘ASEAN promoted the RCEP in an effort to bring Japan back into the fold of Asian regional integration’ (Jin, 2013). The confluence of interests among all players explains the speedy launch of RCEP negotiations in November 2012. Japan was satisfied with the more expansive membership configuration, China was eager to advance the regional FTA, and ASEAN was pleased to imprint its negotiation approach on the RCEP’s blueprint. The first RCEP negotiation meeting was held in May 2013 with the aim to conclude the agreement by the end of 2015.

Japan-EU FTA

The third and final reaction to Japan’s TPP participation involved the EU. Ever since Japan’s competitor South Korea started negotiating a trade agreement with the EU in 2007, Japan attached great priority to signing a countervailing FTA that could prevent Korean companies from undermining Japanese firms’ market share in the European market. Since European tariffs on competitive Japanese sectors such as automobiles are still relatively high, there has been great concern with trade diversion. The Japanese government made entreaties to the EU for several years to no avail. The EU did not show much interest in negotiating a trade agreement until November 2010, within a month of Prime Minister Kan’s TPP announcement.
The EU then agreed to set up ministerial meetings about a Japan-EU FTA. According to a METI official, it was very clear that Europe’s attitude change toward a FTA with Japan emerged ‘because Japan announced its intention to enter TPP negotiation.’ (Asahi Shimbun November 13, 2010).

This overview of the regional and trans-regional responses to Japan’s TPP membership bid reveals the shortcomings of the alternative arguments described in section one (namely, the “no-dissemination”, “trend setter”, and “emulation and learning” accounts). The tight sequence of events as China responded to Japan’s potential TPP entry by expediting the trilateral trade agreement, as the 16 nation FTA roadmap gained the acquiescence of China and ASEAN, and as the EU reversed its position and gave the green light to trade negotiations with Japan, shows that powerful and immediate dissemination dynamics were at work. Moreover, Japan had not played a leading role in launching the FTA movement, but its TPP move was pivotal in changing the viability of different trade integration tracks in Northeast Asia, East Asia, and cross-regionally with Europe. Finally, as discussed in more detail in the next section, the range of economic, rule-making, and political competition motives behind the counter-responses to Japan’s TPP bid, puts to rest the argument that learning or emulation is the main dissemination driver.

4. The Japanese pivot: explaining FTA dissemination cascades

How can we explain the ability of an unlikely pivotal state like Japan to influence regional and transregional FTA dynamics? Our key contention is that the possibility of TPP membership helped Japan develop the credibility it was long lacking in order to act as a pivotal state.
It is unquestionable that Japan has economic heft and that it plays an important role in the spread of production networks that connect national markets through investment-production-trade links. Japan was the world’s second largest economy from 1968 through 2010. Although China overtook Japan’s position in 2010 and despite two decades of slow national growth, Japan continues to play a central role in international trade flows, a fact that is not fully captured by traditional trade statistics. Reflecting the central importance of global value chains, the WTO has released trade statistics in valued added terms which measure the value of components added in each economy and the destination of final demand. As an example of Japan’s key role in production networks, Japan’s trade balance with the US is 60 per cent larger when measured in value added terms, totaling $36 billion in 2009, than when it is reported in traditional gross exports statistics. Japan’s capability to impact Asia-Pacific trade deals is evident in projected gains from trade emerging from Japan’s TPP participation. According to Petri, Plummer and Zhai (2012), adding Japan to the current 11 TPP negotiating states would increase total income gains for the world by $149 billion per year by 2025, and almost $192 billion in export gains.

Japan is also equipped with a strong legal system. Given Japan’s interests as an advanced industrialized economy with substantial overseas investments and an active record in patent filing, it has advocated the adoption of WTO+ rules in its FTAs in the areas of services, investment, and intellectual property. Moreover, Japan has aimed to become the political leader in the regional integration process through its vision for the CEPEA.

Despite having enormous latent capabilities, Japan has been hamstrung by its own domestic constraints: strong lobbying power from liberalisation foes plus an extremely fragmented policymaking system. Dysfunctional trade politics prevented Japan from convincing its trade partners that it could offer substantial market access and partake in large-scale trade
negotiations. For these reasons, Japan sorely needed TPP participation as a commitment mechanism to fill its own credibility gaps. In the economic realm, although Japan has expressed a desire to protect sensitive agricultural commodities, the fact is that it will have to open its domestic market to an unprecedented degree in order to meet the TPP’s high liberalisation targets (expected to be around 98 per cent of tariff lines) and goals of eliminating non-tariff barriers.

In the rule-setting realm, Japan will be able to disseminate the rules it has long promoted in the region (with only moderate success) by endorsing the TPP’s ‘platinum standard.’ In the past, Japan compromised on its trade and investment rules in negotiations with ASEAN members as a part of a quid pro quo to protect its agricultural sector. For instance, in many of Japan’s bilateral FTAs in Southeast Asia, service liberalisation has been based on the positive list though Japan would gain more from a negative list; more ominously in its FTA with ASEAN, no new commitments on services and investment were even possible. Japan could therefore use the TPP to leverage its rule-making economic diplomacy in Asia.

Finally, in the political and security realm, Japan could use the TPP to strengthen its relations with the US at a time when the rise of China has generated concerns. TPP participation could also help Japan to overcome regional distrust toward Japanese leadership since the TPP is an American initiative, which allows Japan to play its traditional role as bridge between the two sides of the Pacific.

The TPP’s boost to Japan’s credibility raised the possibility of significant economic, legal and political externalities for specific states that responded by advancing FTA initiatives that had long stalled. For China, Japan’s TPP participation presents several disadvantages. In economic terms, China would suffer the brunt of trade diversion effects with an expected income loss of
$15 billion dollars. No other state would come close to experiencing such negative economic consequences (Petri, Plummer and Zhai 2012). Moreover, since the TPP is an attempt to negotiate common standards and rules for two of the world’s largest economies in the US and Japan, the possibility that China will eventually have to abide by these same standards increases. For example, as an article in Caixun (2013) notes, Japan intends to become a rule maker by joining the TPP, and China will be on the defensive if the TPP’s rules become the world standard. Finally, politically, the participation of a key Asian nation like Japan significantly strengthens the viability of the TPP as an Asia-Pacific project at the expense of Chinese leadership in the region.

For Korea, the externalities of Japan’s TPP participation are not as high as China’s. As a consequence, Korea has been less eager to move on the CJK trilateral FTA. Because Korea already has preferential access to the US, the estimated trade diversion effects of Japan’s joining TPP are much smaller: $2.4 billion dollars (Petri, Plummer, Zhai 2012). Moreover, through KORUS, Korea has already embraced many WTO plus rules, so that future adjustment to the TPP’s standards would not be onerous. In sum, Korea remains relatively unscathed by Japan’s TPP accession. Nonetheless, Korea was pressured to move forward with the CJK FTA despite its preference for the Korea-China bilateral FTA due to China’s concern over Japan’s TPP commitment.

For ASEAN, Japan’s TPP participation exacerbated old concerns: lack of cohesiveness as some members but not others want to join the TPP; loss of ASEAN centrality as big powers take the driver’s seat in the integration process; and dissemination of an alternative project that does not incorporate ASEAN’s key priorities such as flexible commitments and special and
differential treatment. As a result, Japan’s TPP participation put a premium on developing an ASEAN-centered trade grouping.

For the EU, Japan’s entrance into the TPP was a game changer. This is due to two main reasons according to Messerlin (2012). First, Japan is the most important new market that the TPP will open for the US (with a GDP equivalent to the combined GDP of the other TPP countries). Second, if the TPP with Japan on board develops new industrial, product and sanitary standards, and common rules issues including investment and services, the EU will face the burden of adjustment to these new parameters. Hence, Messerlin (2012: 6) concludes: ‘Japan is the core market in which the TPP could inflict discriminatory effect on EU exports if the EU does not conclude quickly a PTA with Japan.’

**Conclusion**

This study explains the FTA cascades that followed Japan’s moves to join the TPP. Participation in this Asia-Pacific trade negotiation has allowed Japan, unlikely pivotal state, to gain credibility and it spurred the negotiations of major FTAs including a trilateral trade deal among the three largest Asian economies (China, Japan and Korea), a 16-state FTA linking Northeast and Southeast Asia with other important economic partners (India, Australia, and New Zealand), and the EU-Japan FTA. As such, our analytical framework on FTA diffusion takes into account multidimensional competitive pressures (economic, legal, and political), and the ability of states to act as pivots in triggering FTA diffusion. By disaggregating the makeup of pivotal states into two main components, capability and credibility, the study showed how, prior to its bid to join TPP, Japan was an ‘unlikely pivotal state’ with significant latent capabilities, but with its serious credibility shortcomings. TPP became a commitment device for Japan to boost
credibility in its trade policy, which in turn raised the specter of large economic, legal, and political externalities, especially on China, but also on ASEAN and the EU.

Beyond the empirical questions, this study extends the theoretical frontier in policy diffusion studies in at least two ways. First, by explicitly focusing on the role of agents in the diffusion process, we have clarified why some states, but not others, are capable of activating the externalities behind the dissemination of defensive FTAs. By conceptualizing the two properties of pivotal state, capability and credibility, we have examined what determines the leverage of state agents in the diffusion process. Second, the study emphasises the multidimensional forces of competition as major triggers of policy diffusion, where a pivotal state can exploit, purposefully or unintentionally, negative externalities arising from its decisions. In such context, a decision made by the pivotal state tends to activate swift reaction by its competitors.

We believe that our analytical framework, highlighting the complex array of competitive forces and the fundamental factors that must combine (capability and credibility) for a state agent to unleash diffusion dynamics, could be useful in future research endeavors. For example, one direct research follow up would be to go beyond establishing Japan’s ability to influence the negotiation launch of stalled trade initiatives by joining TPP, but to examine the extent to which Japan can use its new found leverage in influencing the negotiation outcomes in these other trade groupings. Glimpses of such dynamics are already discernible even though the CJK FTA, RCEP, and Japan-EU FTA talks are in their very early stages. The Japanese government has attached utmost importance to the TPP negotiations with the intention of concluding that agreement first. This prioritization is reflected in the skewed distribution of bureaucratic resources towards the TPP, which has limited the number of staff available for the other trade negotiations and is
deemed partly responsible for the delay in those other FTA talks. The Japanese government, therefore, is employing a sequencing strategy, whereby it aims to use the more ambitious commitments of the TPP to disseminate rules on economic integration and to obtain more ambitious liberalization outcomes in the other trade negotiation fronts. As the contents of the other mega trade agreements take shape, it will be possible to offer a future refinement of our model by analyzing Japan’s level of influence in the dissemination of standards and rules across FTAs.

Endnotes

1 In contrast, the FTA coverage of exports as of 2012 for the United States is 45.3%, Mexico 92.1%, South Korea 36.5% and China 12.3% (JETRO 2012; 51)


3 As these authors note, positive externalities generate free riding as the adoption of a policy in state A (environmental control) will diminish the urgency of a response in state B (to abate the pollution problem) (Franzese and Hays, 2008).

4 Solís and Katada (2009: 15-16) rely on the concept of ‘competitive distance’ to capture the intensity of states’ competition in third markets by comparing the similarities of their export profiles by market of destination. Baldwin and Jaimovich (2010) develop a contagion index with two main components: the number of FTAs signed by a state’s trade counterparts and the rivals’ market shares in those markets. And Baccini and Dur (2012) estimate trade diversion by measuring both the amount of exports of excluded state B to state A and the degree of competition it faces in that market from states that have FTAs with A and export a similar basket of goods.
Not everyone agrees on the pull of trade diversion, however. Ravenhill (2010) doubts that an economic domino effect is at work in Asia since many FTAs in the region cover small trade amounts and preference utilization rates are lower than in Europe and North America. Freund and Ornelas (2010) point out in quantitative studies that FTAs’ trade diversion effects are relatively small and that many governments (in Latin America, for example) have negotiated FTAs and unilaterally lowered tariffs to increase FTAs’ external trade creation effect.

WTO+ commitments go beyond existing obligations at the multilateral level in areas such as government procurement, product and health standards, service liberalization, intellectual property protection, and anti-dumping and countervailing duties. WTO-X areas include issues not covered by the multilateral trading regime such as competition policy, environmental and labor standards, investment, movement of capital, and regulatory convergence.

Interview with Keidanren officials, Tokyo, June 2008.

For detailed dynamics of East Asian track and Asia-Pacific track of FTAs, and the impact of Japan’s TPP announcement, see Sugawara (2012b).

METI has emphasized the importance of this aspect of TPP from the start as seen in their supplementary document to the Report on TPP published on October 27, 2010 (http://www.cas.go.jp/jp/tpp/archive1.html). Also discussed in Sugawara (2012a, and footnote 14).

For an analysis of this decision, see http://www.brookings.edu/research/opinions/2012/11/13-tpp-noda-solis

With these items (rice, wheat, sugar, dairy and beef/pork) exempt from the tariff liberalization, Japan’s tariff liberalization ratio would only reach 93.5 percent of trade liberalized, below the 98% or higher target level that major TPP negotiating countries such as the United States and Australia are pushing for.

Interview with Japanese public official, New York, September 2013.

Another important reaction of China and South Korea to Japan’s entry into the TPP was their increased interest in eventually joining the Trans-Pacific Partnership. Obviously, for China this would be a longer term option, likely to happen only if the Chinese leadership deems TPP a useful vehicle to advance its economic reforms (Solís, 2013b). In the case of South Korea, FTA fatigue after negotiating the bilateral trade
agreement with the United States, as well as bureaucratic reshuffles introduced by the incoming Park
administration have delayed the decision on TPP membership (Solís, 2013c).

14 Kawai and Wignaraja (2008) examine welfare implication of the two schemes and concluded that
CEPEA would yield the largest gains.

15 Interview with a Japanese researcher, Tokyo, October 2013.

16 The RCEP ‘Guiding Principles and Objectives for Negotiating the Regional Comprehensive
Economic Partnership’ can be accessed at

17 ASEAN members participating in TPP include Singapore, Brunei, Vietnam and Malaysia.
Philippines and Thailand have also expressed interest in joining (ASEAN Affairs November 14-15, 2011).

18 For instance, while over a 100 public officials belong to the TPP negotiation team, the combined staff covering all
three other mega FTAs Japan is negotiating amounts to only 90 people (Asahi Shimbun, November 5, 2013).