

## **The Logic of Japan's Free Trade Agreements (FTA) with ASEAN**

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*Among political scientists, Japan's free trade agreements (FTA) with member nations of the Association of Southeast Asian Nations (ASEAN) has been considered to be a political tool that can compete against China for regional leadership in East Asia. However, this paper demonstrates that Japan's so-called FTA diplomacy towards ASEAN nations serves the broad interests of Japanese actors in both the political and economic sectors. Given the attention to Japanese domestic political issues, it is argued that diplomacy primarily facilitates a need for free trade with ASEAN and ASEAN markets for Japanese corporations to compete in the global economy and for the government to nurture Japan's stagnant economy by assisting these corporations. This work also contends that the unclear function of FTA as an economic good is due to the lack of the government capacity to effectively manage FTA diplomacy. This partly results from the conventional view with regard to Sino-Japanese rivalry.*

### **Introduction**

During the rise of China, Japan's conclusion of free trade agreements (FTAs) with member nations of the Association of Southeast Asian Nations (ASEAN)<sup>1</sup> has ignited an argument with regard to Sino-Japanese rivalry over regional leadership in East Asia. An FTA is a bilateral or multilateral economic agreement that initially reduces tariffs and eliminates other economic barriers on trade in goods and services. Japan has signed a large number of FTAs with major ASEAN nations, including Singapore in 2002, Malaysia in 2005, the Philippines in 2006, Indonesia, Thailand, and Brunei in 2007, and Vietnam in 2008, as well as the Japan-ASEAN Comprehensive Economic Partnership (JACEP) (JETRO 2011). However, a view that Japan's so-called FTA diplomacy toward ASEAN nations is a primary response to China has increasingly become conventional wisdom to many political scientists. The fact that China has adopted a similar proposal towards ASEAN, along with a growing commitment to a regional cooperation or so-called East Asian regionalism, have identified FTA as a political good, rather than an economic tool that primarily promotes free trade. Many argue that Japan employs FTAs to attain greater influence in the region over China in a relative and indirect manner (Terada 2010; Prastirtsuk 2010; Sohn 2010; Yew 2008; Ravenhill 2008).

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It is worth considering, however, whether Japan's FTA diplomacy towards ASEAN is, in fact, primarily implemented to counter the rise of China. This analysis advocates that the FTA diplomacy is in response to Japan's own economic needs, rather than a reaction to the rise of China. In 2009, before the Chinese economy surpassed that of Japan in 2010, Shinzo Kobori from the Institute for International Policy Studies in Tokyo stated: "It is nonsense for us to continue talking about competing with China for sole leadership in Asia when their economy will surpass ours by next year. For Japan, Asian development must mean more than tighter economic relations with the Middle Kingdom [China]" (Forrohar 2009). Shiraishi (2003) also points out an inappropriateness of such a view of FTA in the context of power politics, indicating that Sino-Japanese rivalry and East Asian regionalism should be considered separately when focusing on the *economic* meaning of FTAs between Japan and ASEAN.

To suggest the logic of Japan's FTA diplomacy towards ASEAN, this essay develops a challenge to the popular argument of Japan's FTAs with ASEAN in the context of Sino-Japanese rivalry along with East Asian regionalism. In order to answer questions about why FTA brings Sino-Japanese rivalry to a significant height and why Japan needs to pursue FTAs with ASEAN, this work introduces Japanese domestic political issues to provide a more complete explanation of Japan's motivation to pursue regional diplomacy. The analysis maintains that Japan's FTA diplomacy towards ASEAN is likely to serve the broader interests of Japanese actors, which are mainly Japanese corporations and the government. ASEAN countries are crucial economies and markets partly as the last resort to Japan's economic distress. By promoting trade through FTA networks, Japanese corporations must explore markets outside of Japan, and the government of Japan is determined to assist them, substituting profits overseas with stagnant consumption and investment at home in order to sustain the economic growth. This work also finds that the view of FTA as a political good may be attributed to an unclear understanding of the economic function of FTA due to the lack of the government capacity to develop FTA diplomacy in an effective manner.

### **The Logic of Japan's FTA in the Context of Sino-Japanese Rivalry**

A view of FTA as a political good in the service of Sino-Japanese rivalry over regional leadership has increasingly become a mainstream idea among political scientists. A complex of China-Japan relations for centuries has underlined the rivalry, which involves mixed thoughts of "admiration, envy, and occasional hostility" (Smith 2009, 232). Military aggression during the 20<sup>th</sup> century, namely Japan's aggression against China during WWII, has impeded the development of bilateral relations. Yang (2007) notes: "The distrust [between China and Japan] is still deep and the emotions are still raw" (275). Smith (2009) adds that China-Japan relationship is "far less positive or consistent" (232), indicating that China and Japan have never been able to trust each other at a grass-roots level, even after the normalization of the diplomatic relations in 1972. Yang (2007) also points out that the relationship is almost an "exception" from others in terms of how China and Japan make policy choices towards each other (258). Whereas China and Japan have both realized their closer trade partnership in the 21<sup>st</sup> century, Bustznski (2009) adds that, regardless of their increasing economic interaction, their closer contact is "politically unprepared" (153). A recent crash between a Chinese fishing vessel and Japanese patrol ship on September 7, 2010 near the disputed area of the Diaoyutai/Senkaku Islands has demonstrated a deep divide between the two nations. The incident not only halted a national-level interaction between

China and Japan, but it also caused anti-Japan protests in China, as well as China's economic sanction on Japan by suspending an export of rare earth materials, which are critical to economic production in Japan (Zeller 2010). In short, the historical relationship has long exhibited a tendency between China and Japan to suspect events in political and economic fields as adverse actions. It has made the bilateral relations inherently nationalistic, and it is unlikely that a recent economic tie between China and Japan would ease tensions at a fundamental level.

This concept has led to a dominance of a state-centric or neorealist approach that explains China-Japan and East Asian relations. According to a well-known neorealist Kenneth Waltz (1979), as unit actors in the anarchic world primarily consider their survival and pursue power capabilities, Japan and China are determined to principally seek power in order to obtain greater influence over others in both East Asia and the international community (Yang 2007). Goldstein and Pevehouse (2008) add that power is an ability that influences another's behavior "as measured by both tangible and intangible characteristics" (38). Major characteristics include military capability, population size, economic, financial, and diplomatic capabilities. In doing so, Japan's FTA diplomacy is an economic power capability and is viewed as a counter to China's influence. (Prastirtuk 2010; Terada 2010; Yew 2008). Japan's power especially comprises what Joseph Nye (2006) calls "soft" power in contrast to hard power. The "soft" power is an "ability to set the political agenda in a way that shapes the preference of others" through non-military means (Nye 2006, 711). Scholars point out that Japan's diplomacy is a "soft balancing" act; it means that Japan attempts to balance China's influence in an economic field, which is a relative and indirect manner (Prastirtuk 2010; Sohn 2010, 497; Yoshimatsu 2008). Yoshimatsu (2008) particularly names this Japan's soft-balancing diplomacy a "patchwork realism" (150); Japan is primarily motivated to "balance China's influence in the trade field" (167) by promoting FTAs with ASEAN nations. Although Japan's action may not be well thought out, its balancing action against China is imminent and inevitable.

In addition, Sino-Japanese rivalry over a regional leadership through FTAs has increasingly become embedded into the emerging idea of East Asian regionalism. East Asian regionalism is a mutual effort and process of regional cooperation, addressing issues that are "inherently regional in scope and cannot be solved at a global or national level" (Asian Development Bank 2008, 15). It is an economically driven phenomenon, as the Asian Financial Crisis in 1997-98 revealed a lack of an economically cooperative mechanism in the region. Institutions within the region, namely ASEAN Plus Three (APT),<sup>2</sup> have valued FTAs and other projects including the Chiang Mai Initiative Multilateralization (CMIM) and Official Development Assistance (ODA)<sup>3</sup>, as important driving factors in promoting East Asian regionalism, or a multilateral framework (Chong 2010). In theory, liberals chiefly advocate regional cooperation. Both state and non-state actors play a significant role in driving a multilateral framework. The fact that East Asian regionalism particularly involves regional institutions and private firms as important actors to initiate such projects limits the neorealist argument. States are no longer solely crucial players and cannot act upon a desire simply to survive and increase greater influence on other nations (Yoshimatsu 2008). Nonetheless, many still believe that East Asian regionalism may not exactly follow the liberalist idea; neorealist notions still dominate East Asia. Poon (2001, 252) points out that, unlike the European Union, East Asian nations lack shared social and political factors that support closer linkage among the nations. When the region is culturally and politically diverse, Poon (2001) notes, "The Asian way should be viewed as a strategy to protect state sovereignty" (255). Yoshimatsu (2008) also characterizes East Asia to be evolved around "great power politics" (61) and "strong adherence to sovereignty" (8). Political tensions exist in various fields be-

tween East Asian nations, which makes states' interests more significant and crucial than a regional coherence as a society. Yoshimatsu (2008) explains, "Realist logic retains strong validity in explaining regional games in East Asia," although there has emerged a role of non-state actors, such as business networks, to embrace a cooperative mechanism in the region (9). Cooperation is exclusively limited to economic means that only serve states' own interests. When nations see cooperation as the best option to maximize their own benefits, they will cooperate (Poon 2001, 252). Hence, East Asian regionalism can be defined as, according to neorealist Robert Gilpin (2001), "an important response by nation-states...not an alternative to the nation-state, as some believe, but rather embodies the efforts of individual states to collectively promote their vital national interests and ambitions"(11). In other words, these scholars insist that East Asian regionalism primarily serves state actors' interests in obtaining greater influence in a relative and indirect manner. China and Japan, particularly, are economically powerful nations and are seen to utilize FTAs and other economic projects as their non-military or "soft" power in attaining their influence in the region.

Scholars argue that there has been a competition between China and Japan over who can make a larger contribution to the process of regionalism and who will be better accepted as a leader by other East Asian nations including ASEAN (Terada 2010; Prastirtsuk 2010; Yoshimatsu 2008; Ravenhill 2008; Hamanaka 2008). A so-called *aid war* has occurred between China and Japan over who can lead FTAs and other projects, such as ODA, and CMIM, as if they evaluate their qualification for regional political leadership based on their performance within those initiations (Rathus 2010; Terada 2010; Yew 2008). FTA is then considered to be a political good, or what Ravenhill (2008) calls "positional goods," meaning that a nation's "value [can be] maximized" (87) when others do not have FTAs. It posits Japan's FTA diplomacy towards ASEAN nations as a part of Japan's initiative in obtaining a leading role for East Asian regionalism in order to counter the growing influence of China, or its similar appeal towards ASEAN (Yoshimatsu 2008; Dent 2008). Yew (2008) states, "their [China and Japan's] contest to offer separate FTAs to ASEAN member-states and competing ideas of East Asian regionalism has enlivened the prospects of Japanese-Chinese economic competition, and possibly, regional rivalry" (88). Hamanaka (2008) also notes, "In order to neutralize the Chinese influence and to maintain its own influence in the region, Japan needed to have an FTA or EPA (Economic Partnership Agreement) with ASEAN countries" (78).

Based on this perception of FTAs, previous literature argues that Japan's conclusion of an FTA with Singapore in January 2002 chiefly influenced China to sign the ASEAN-China Free Trade Area (ACFTA) in November 2002(Terada 2010; Prastirtsuk 2010). China's conclusion of ACFTA with ASEAN is seen to trigger Japan's negotiation of FTAs with ASEAN, both bilaterally and multilaterally by 2008 (JETRO 2011; Prastirtsuk 2010; Terada 2010; Sohn 2010; Ravenhill 2008). In addition, Terada (2010) indicates the fact that China and Japan have never launched an FTA between them, although China and Japan are crucial trade partners, can explain that FTAs are more likely to be used as a political tool between China and Japan. Moreover, FTAs cause the "Asian noodle bowl," or the "spaghetti bowl" effect, which entangles different administrative procedures in the region that may raise costs for Japanese or other transnational corporations in operating business overseas (Kawai 2011; Chong 2010; Ravenhill 2008). Kawai (2011) points out, "this wave of [free trade] agreements will undermine the multilateral liberalization process," conflicting with an expected role of FTA to drive East Asian regionalism. JETRO (2011) survey reveals that most Japanese corporations have, indeed, been reluctant to apply for FTAs, partly due to the "Asian noodle bowl" effect. These views conclude that Japan em-

loys FTAs as a political response to China as one measure of its relative impact on East Asia by concluding more FTAs with ASEAN and other nations than China.

### **The Logic of FTAs in the Service of the Japanese Domestic Politics**

In contrast to the neorealist logic, an alternative discourse facilitates Japan's FTA diplomacy towards ASEAN nations as a primary response to needs and issues of Japanese domestic politics and economics. A focus on Japanese domestic politics takes parochial actors who control the FTA policy choice into comprehensive consideration. There is little attention paid to domestic politics of Japan in making a foreign policy towards China and East Asia. A principal reason is that both neorealist and liberalist approaches have predominantly formed the state-centric study of Sino-Japanese rivalry (Yew 2008). Yet the application of these ideas, which focus on a systematic, structural, and unit-level analysis at an international level, is likely to assume external factors, such as China, to be a primary determinant of Japan's policy choice (Yew 2008). In doing so, the fact that recent Japanese literature, particularly issued by economists, have looked at perspectives of Japanese corporations and the government as key factors in FTA diplomacy relates domestic politics as a variable necessary for a more complete explanation of Japanese diplomacy towards ASEAN (Itoh 2010; Okamura, Omura, and Takehana 2010; Forohar 2009). The main proposition of the domestic political approach is that Japan's FTA diplomacy towards ASEAN is likely to serve domestic or internal purposes and players. This view links FTAs to perspectives and interests of Japanese actors in the world markets and policy-making process; namely Japanese corporations and the government. These actors' various interests form an ultimate choice of getting FTAs, rather than considering Japan as a unified state that employs FTA principally in order to counter the international rise of China.

It is equally important to note that the focus of domestic politics is not to discredit Japan's security concern regarding China. In accordance with Putnam's (1988) "two-level game" concept, such an external or international concern of Japan is intertwined in the decision-making process, reflecting that domestic and international politics should not be separated, but they interact with each other in a reciprocal manner. Putnam (1988) states, "central decision-makers strive to reconcile domestic and international imperatives simultaneously" (460). Putnam (1988) emphasizes that state-centric analysis, such as neorealist and liberalist schools, overlook the "inevitability of domestic conflict about what the national interest requires," maintaining that internal and external factors equally influence policy-making process of Japan (460). Bueno De Mesquita (2002) also contends, "international relations is simply put, a venue for politicians to gain or lose domestic political advantage...the lens of domestic decision making provide a way to think about how prosperities of the international system are shaped by local considerations as part of the larger strategic fabric of politics"(7). These ideas elaborate, once again that Japan's FTA diplomacy towards ASEAN reflects broader interests of Japanese actors, rather than the rise of China's regional leadership as the only key determinant. Yew (2008) further asserts, "Foreign policy reflects the broader national interests of the Japanese state/state-elites, defined in terms of realizing an amalgam of pragmatic external goals and domestic agendas" (288). These notions understand a domestic scope of Japan's FTA policy choices as equally important as Japan's external concerns, such as China. This allows one to search various factors to explain Japan's aspiration of managing FTA diplomacy towards ASEAN at multifaceted levels. Based on these thoughts, the analysis here reveals major factors explaining why Japan has aspired to seek FTAs

with ASEAN: 1) Japan's shifted focus on FTA from the WTO accord and its protectionist attitude towards agricultural products, 2) Japanese corporations' desires to avoid the "China Risk" and advancement of "China Plus One" model that utilizes ASEAN markets, 3) the need to recover the Japanese economy from a vicious cycle, and 4) issues regarding the government capacity and behavior.

### **Japan's Shifted Focus on FTA and Protectionist Attitude on Agricultural Goods**

Firstly, Japan's initiation of FTA diplomacy towards ASEAN in the 21<sup>st</sup> century is partly attributed to Japan's shifted interest in FTAs from a strict accordance to the rules and regulations set by the World Trade Organization (WTO). Before the 1990s, Japan had been determined to follow the WTO accord, and had especially hoped for the Doha Round, one of WTO negotiation rounds that had begun in 2001, to settle agricultural issues (Hatasa 2011; Hamanaka 2008). Japan, or especially the Ministries of Agriculture, Forestry, and Fisheries of Japan, had long been concerned with a protection of Japanese agricultural products because these products, such as rice and beef, have been relatively expensive compared to that of other nations. While Japan has set tariffs on non-agricultural goods at 2.5% when negotiating FTAs with others, its tariffs on agricultural goods are set at 12 to 21% in order for Japan to preserve domestic agricultural sector (Hatasa 2011). A result is Japan's protectionist behavior, which delayed Japan's involvement in building FTA networks until Japan realized that the Doha Round was not going anywhere (Hatasa 2011).

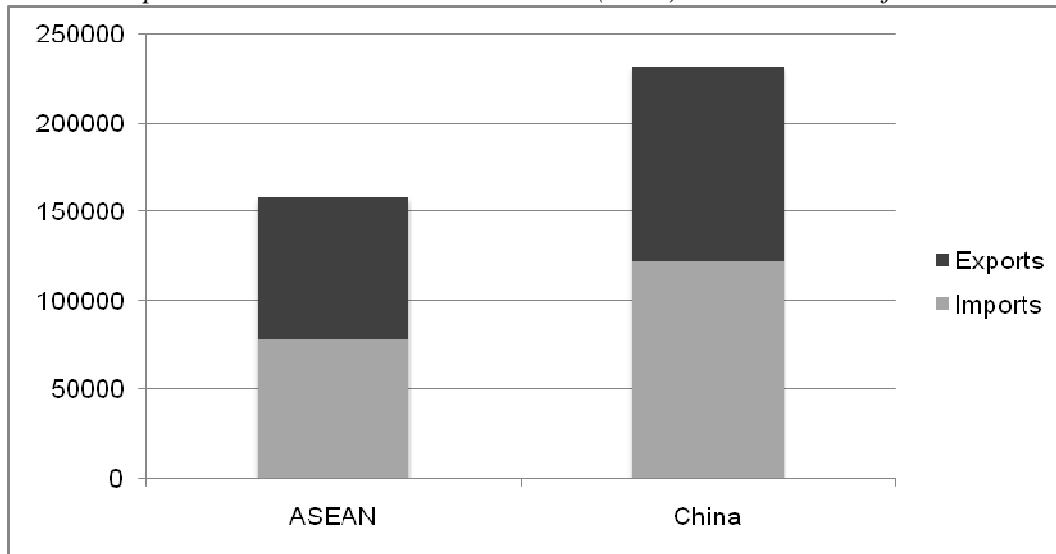
The fact that China and the U.S. are major exporters of agricultural goods is a crucial reason why Japan has not been able to sign FTAs with them (Hatasa 2011; Hamanaka 2008). As noted, it is believed that their political rivalry has impeded China and Japan from concluding a FTA between them. For example, the Northeast Asia Free Trade Area has only been under consideration, but has never practically exercised its functions (Terada 2010; Hamanaka 2008). However, a main concern still rests on their economic benefits. In short, China and Japan's production of similar agricultural products is economically competitive. FTAs can only bring burdens on their economic actors, such as their own farmers (Hamanaka 2008, 78). Hamanaka(2008) states: "The essential reason why both Japan and China are reluctant to form an FTA including the other seems to be based on the entailed economic costs (78). He further asserts that it is weak to argue political frictions between China and Japan are impediments to their FTAs. Not only does political rivalry fluctuate from time to time, but this view also leads to a controversial explanation that China and Japan are both eager to promote East Asian regionalism in the same framework that ties them in financial and monetary sectors, while they want to exclude each other only in trade or the case of an FTA (Hamanaka 2008, 78). Indeed, Japan's first FTA with Singapore was successful because Singapore, as a non-agricultural country, had minimally threatened Japan's *economic* interests in protecting its agricultural sector (Hamanaka 2008; Ravenhill 2008; Yun 2004). For the same reason, Japan was able to sign FTAs with other nations in the following years. These ASEAN countries, which will be discussed later in depth, have accepted Japan's alternate deals for high tariffs on agricultural products, such as exchanging human resources in certain fields (Hatasa 2011), making it easier for Japan to sign FTAs with them.

## **The Role of ASEAN economies and markets: “China Plus One” model**

Secondly, Japanese corporations’ desire to cultivate ASEAN economies and markets in the beginning of the 21<sup>st</sup> century significantly influenced Japan to pursue FTAs with ASEAN nations. There is no doubt that the Chinese market has currently been the biggest opportunity for Japanese corporations to explore, since it is rich in raw materials, labor, consumption, and is geographically accessible. However, Japanese corporations have become apprehensive about the so-called “China risk,” meaning that there are economic and political uncertainties for them to establish a long-term business in the Chinese market. An increasing cost of Chinese labor has rapidly become one of the biggest concerns for them (JETRO 2011; Adachi 2009). The cost of the Chinese labor has increased significantly. The average wage increase between 2004 and 2008 in four major cities of China (Beijing, Shanghai, Tianjin, and Shenzhen) indicates a rise of approximately 150%. The *2010 White Paper on Small and Medium Enterprises in Japan* issued by the Ministry of Economy, Trade, and Industry of Japan, also notes that the average cost of the Chinese labor who work in the Japanese small and medium enterprises in the Chinese market increased from 6,210 RMB in 1996 to 21,001 RMB in 2006, a 330% increase within the decade. A consequence is, according to the JETRO survey (2011), that 80% of Japanese corporations in the Chinese market are concerned with the increasing cost of labor. The political side of China-Japan relations is another risk that overshadows Japanese corporations’ ability to sustain business in the Chinese market. The former Prime Minister Junichiro Kouzmi’s visit to Yasukuni Shrine, which enshrines top Japanese officials during WWII, caused large scale of anti-Japanese protests and strikes at Japanese-owned factories in China in 2005 (Kajita 2005; SankeiBiz 2004). The aforementioned incident near the disputed area of Diaoyutai/Senkaku Islands in 2010 also caused China’s suspension of exporting rare earth materials to Japan and severely undermined Japanese production for about a month (Cheng 2010; Zeller 2010).

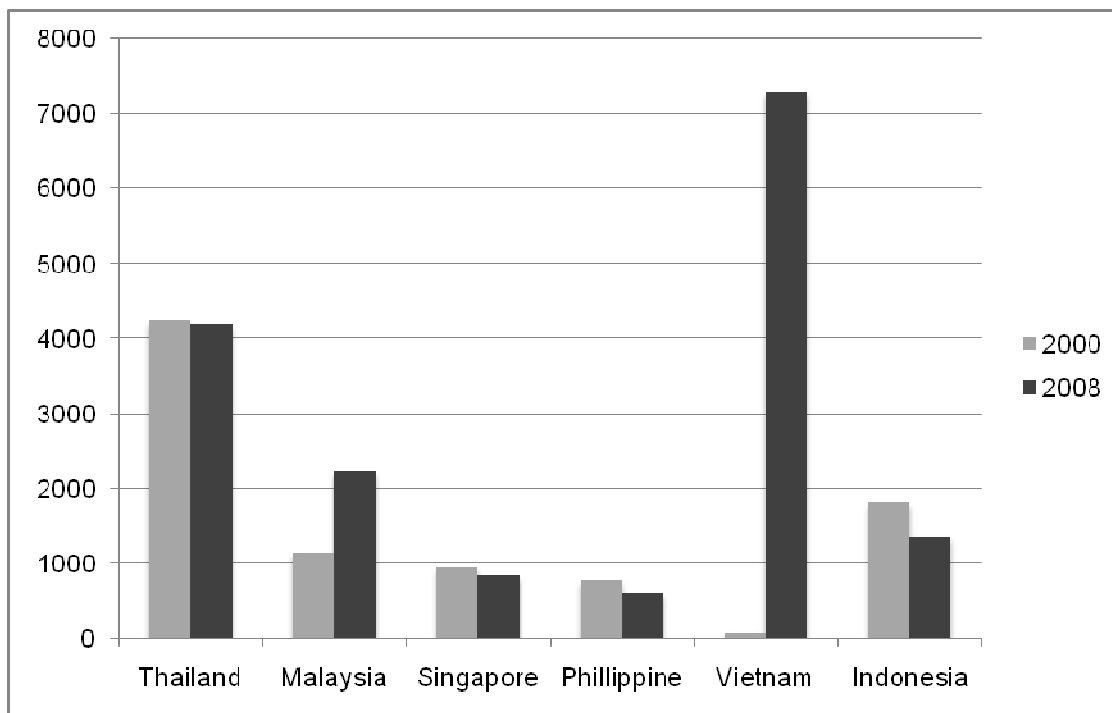
In contrast, ASEAN countries do not have as severe political tensions with Japan as does China. This has made it easier for Japan to expect a sustainable business linkage with ASEAN economies and markets. Japanese corporations’ interests in avoiding the “China Risk” and cultivating ASEAN markets as alternatives have especially generated “China Plus One” model. This model entails that Japanese corporations seek “sub” markets in ASEAN nations in order to support their “main” business in the Chinese market (Horie 2005). The JETRO survey (2011) reveals that there are risks associated with exchange rate, infrastructure, legal system, underdevelopment, intellectual property rights, increasing cost of labor, taxation, and management. The survey shows that the Chinese market has involved the biggest risks, and risks of operating business in the ASEAN markets are much lower than that of China. It is equally conspicuous that a risk of increasing cost of labor is far greater in China, compared to the ASEAN markets. Simultaneously, a function of the ASEAN markets has grown in various ways. The JETRO survey (2011) demonstrates that ASEAN markets operate as consumer markets, production grounds, a place for research and development, and export and transit points for the cheap labor-intensive manufacturing sector and other low-tech industries (JETRO 2011). Japanese corporations who responded to the JETRO survey (2011) have particularly utilized the major ASEAN markets to increase sales as with the Chinese market. Under the development of “China Plus One model,” Tables 1 and 2 also show that Japan’s trade and investment with ASEAN has grown in a rapid manner, indicating Japanese corporations’ thriving interests in ASEAN markets and economies.

Table 1. Japan's trade with ASEAN and China (2009) Unit: millions of US dollars



Source: Japanese External Trade Organization (JETRO).

Table 2: Japan's Foreign Direct Investment towards Major ASEAN countries Unit: millions of US dollars

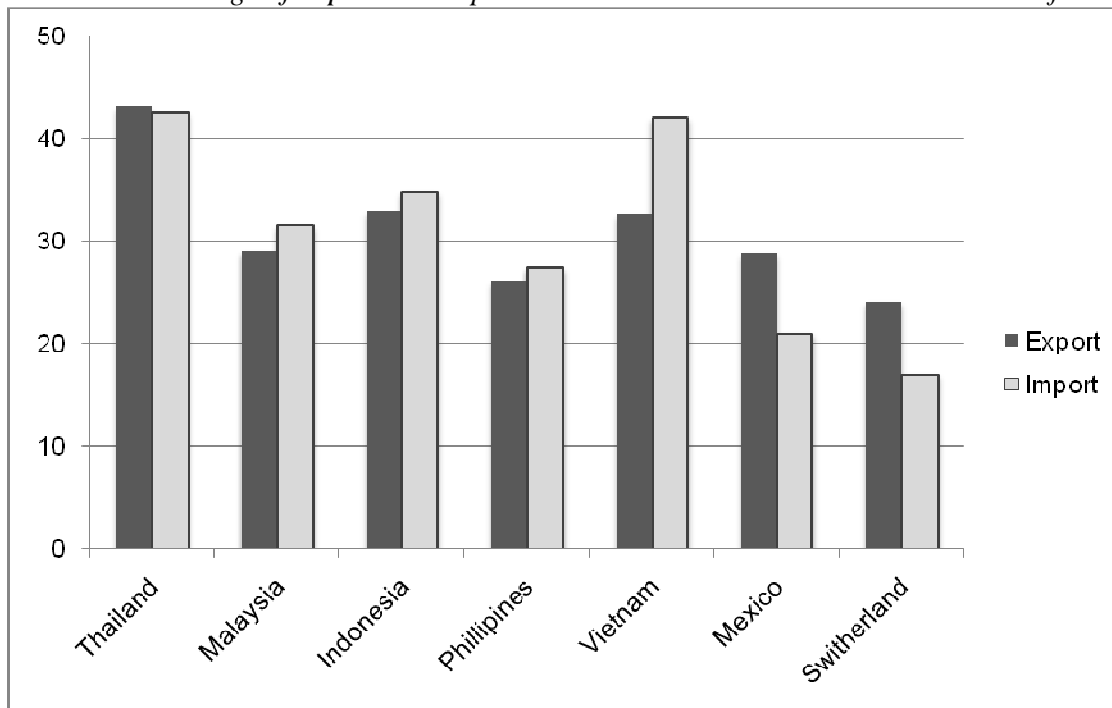


Source: Japanese External Trade Organization (JETRO).



Table 3 indicates the growing importance of ASEAN markets, in terms of how many Japanese firms have used FTAs. Whereas Japan initiated negotiations with Mexico and Switzerland in 2001 and 2005, the use of FTAs with ASEAN has significantly increased (JETRO 2011). For example, Thailand has rapidly become the second largest exporting country for Japanese corporations. Among 1,002 Japanese corporations that have responded to the JETRO survey (2011), 470 companies have already established export businesses in Thailand, while there are 570 firms in the Chinese market. In addition, JETRO reveals that FTAs between Thailand and Japan, as they went into effect in 2007, have strengthened trade relations between these two nations. The JETRO (2011) survey shows that Japanese corporations have most actively used FTAs in the Thailand market with over 40% usage (See Table 3). In 2008, 48.4% of Japanese exports and 59.5% of Japanese imports are conducted through FTAs with Thailand. Another significant case is the Vietnamese market. Its cheap labor has particularly caught the attention of Japanese corporations (Ministry of Economy, Trade, and Industry 2010). Table 2 shows a rapidly growing interest by Japanese firms in investing in the Vietnamese market. Table 3 also exhibits, as according to the JETRO (2011) survey, that Japanese corporations have implemented FTAs between Japan and Vietnam, second to Thailand, and the FTAs have been used mainly for labor-intensive manufacturing businesses, such as components for motorcycles, printers, and other small electronic products.

Table 3: Percentage of Japanese Corporations that have used/ considered the use of FTA



Source: Japanese External Trade Organization (JETRO) “平成 22 年度日本企業の海外事業展開に関するアンケート調査.” 2011. <http://www.jetro.go.jp/news/releases/20110308884-news/siryo-2.pdf> (June 10, 2011).

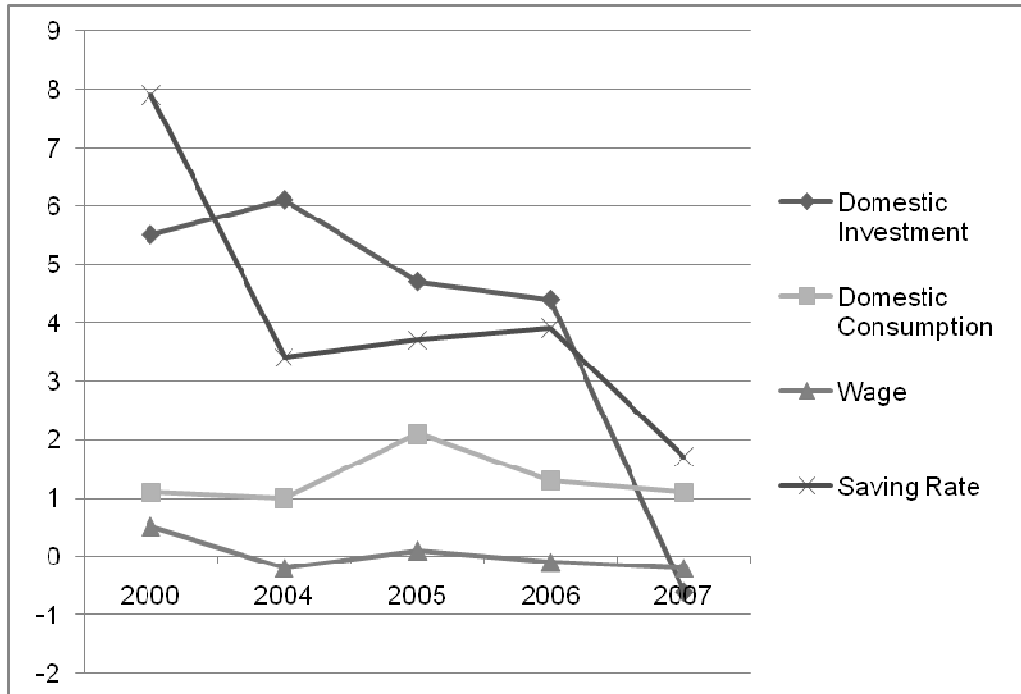
It is equally important to note that the use of FTA between Japan and ASEAN, or JACEP (the Japan-ASEAN Comprehensive Economic Partnership) has further enabled Japanese corporations to form a multilateral trade between ASEAN nations and Japan. A reduction of tariff by using JACEP between Japan and ASEAN has allowed Japanese firms to let one ASEAN nation create

components and assign another ASEAN nation to process, assemble, and export back to Japan, or sell within the market (JETRO 2011). FTAs between ASEAN and other nations, such as China, ACFTA (the ASEAN-China Free Trade Area), has also assisted Japanese firms to utilize China as a transit point or a consumer market by letting ASEAN nations to promote Japanese products. The JETRO (2011) survey reports that the consequence of using these FTAs has encouraged Japanese corporations to use more FTAs in the future. Whereas only 13.3% of Japanese corporations intended to use FTA in 2006, there were 49.7% of Japanese corporations in all sectors responding to have used or have considered the use of FTAs in 2008 (JETRO 2011). Urata (2006) adds that there has been a positive impact of FTA on the economic development of both Japan and ASEAN nations. Urata (2006) reports that the use of FTAs positively increase the Gross Domestic Product (GDP) of these nations. Although the GDP growth rate only scores 0.31% for Japan, this equals to \$118 increase in economic wealth per person. The use of FTA results in an increase of productivity in most industries. Japanese machinery and textile industries, in particular, have gained 2.6% and 2.8% increases in productivity respectively. These industries in ASEAN nations have also undergone 20% and 8.3% increases in productivity.

### **The Last Resort to Economic Distress**

An interest of the Japanese government to promote free trade with ASEAN for the stagnant Japanese economy is the third key factor in facilitating FTA diplomacy. The government is not only determined to assist the Japanese corporations who seek profits in ASEAN markets and trade with ASEAN, but it is also urged to deal with the economic distress at home. The Japanese economy has struggled to grow for over two decades (see table 4). All domestic factors necessary for the economy to grow have dramatically declined or stagnated. Domestic investment and savings have significantly dropped. Wages have stagnated since the 2000s and have discouraged consumers to spend, resulting in stagnant domestic consumption (Forrohar 2009). A declining population in Japan is another factor attributing to the economic distress. Yamaguchi (2011) indicates that Japanese population has declined by 23% between 1980 and 2009. The population of the elderly from the ages of 65 or older is expected to increase continuously, while Japan's fertility rate as of 2011 remains at 1.21, which is 219<sup>th</sup> among 223 assessed countries and entities (CIA 2011). The negative impact of the declining population and a more elderly population has not only decreased the size of the labor force in Japan, but has also reduced domestic consumption (Miyazaki 2011; CIA 2011). According to the Ministry of Economy, Trade, and Industry (2010), the labor population will decrease by approximately 8 million by 2020. Forrohar's (2009) also predicts that a ratio of working age to elderly population of Japan will fall from 8:1 in 1975 to 1:3 in 2055. This situation has added a burden on people of working age for the social security tax necessary to support the increasing elderly population. A result is less consumption and fewer profits to Japanese corporations at home, which consequently stagnates wages. Nanba (2007) also finds that the decreasing population with an increasing elderly population has been a critical cause of decreasing the savings rate of Japan (Refer to Table 4). In theory, savings is important for an economy because it allows financial sectors to lend more money and invest on business, which can increase money supply and velocity of the money flow in the economic cycle (Nanba 2007).

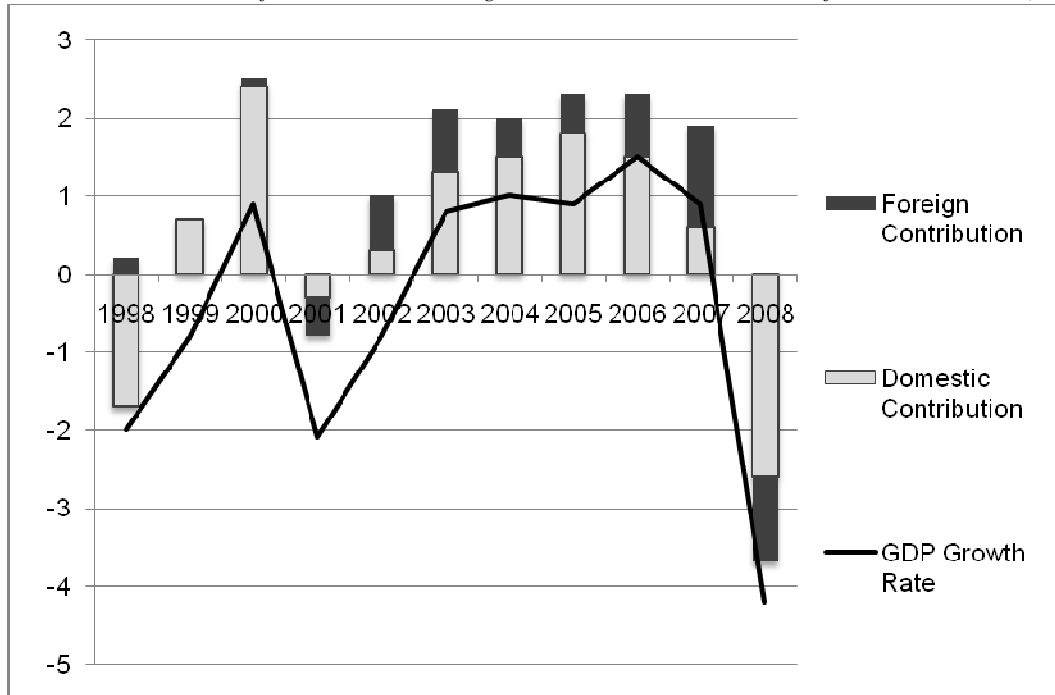
Table 4. Growth Rates of Domestic Investment, Consumption, Wage, Savings Rate, and GDP in the 2000s (Unit=%)



\*Source: Ministry of Internal Affairs and Communications of Japan

The consequence is not only the slow growth of Japan's Gross Domestic Product, (GDP) but also a harsh structural change. The economy can no longer be significantly sustained by domestic factors. Table 5 demonstrates that a foreign contribution to the economic growth has grown in the 21<sup>st</sup> century (Hasegawa 2010). Japan must utilize trade, consumption, and investment in markets overseas to maintain the Japanese economy. ASEAN countries are then one of crucial economies and markets as the last resort to Japanese economic distress. By promoting trade through FTA networks, Japanese corporations must explore markets outside of Japan, and the government of Japan is determined to assist them, substituting profits overseas with stagnant consumption and investment at home in order to sustain GDP or the economic growth (Okamura, Omura, and Takehana 2010). Economist Itoh (2010) states that it is pivotal for Japan to cultivate East Asian markets for its own economy, and Japanese corporations must accommodate Asian markets through FTA, as if these markets are their home grounds, and not just an extra opportunity. In a particular reference to the stagnant consumption of Japan, Kobori from the Institute for International Policy Studies in Tokyo has declared: "There is no viable model for increasing domestic consumption. What we need is a new model based on more regional integration. The idea is to integrate Japan into the heart of this new and growing Asian domestic market" (Forrohar 2009).

Table 5: Contributions of Domestic and Foreign Factors to Economic Growth from 1998 to 2008 (%)



Source: Calculated based on Cabinet Office, Government of Japan.

### Domestic Politics of FTA: Lack of Government Capacity

Lastly, a problematic behavior of the government to efficiently manage FTA diplomacy towards ASEAN has been a conspicuous factor that has resulted in a controversial role of FTAs. In particular, there are problems associated with the lack of government capacity to effectively promote FTAs for economic purposes. One reason why FTAs have not been effectively used for trade is an inefficient process of negotiating FTAs. Within the Japanese government, four ministries<sup>2</sup> must accommodate their ideas and visions before negotiating FTAs with other nations. However, as previously mentioned, the Ministry of Agricultural, Forestry and Fisheries has been reluctant to allow a reduction of tariff on agricultural goods, whereas the Ministry of Economy, Trade, and Investment has desired to reduce tariffs on all goods to expand *free* trade with other nations. This process then requires much more time to build FTA diplomacy than other nations, who assign one ministry or agency within their governments to initiate FTAs (Hatasa 2011). There is also a lack of collaboration between the government and FTA users, or Japanese corporations. Although the use of FTAs has gradually increased, the government has not been able to provide sufficient information regarding FTAs, resulting in less than 50% of FTA usage in most cases. Japanese corporations have responded to the JETRO survey (2011) that they have not been familiar with newly signed FTAs, questioning the ability of the government's to exercise an effective FTA diplomacy. Kawai (2011) points out: "The lack of information on the FTAs, and not the noodle bowl *per se*, is the biggest impediment to firms using FTAs."

It is equally important to realize that the government has fundamentally been incapable of carrying out practical policies. In particular, the government has lacked a consistent leadership

<sup>2</sup> Ministry of Foreign Affairs, Ministry of Economy, Trade, and Investment, Ministry of Agricultural, Forestry and Fisheries, and Ministry of Finance

(see table 6). Since 1991, there have been 13 Prime Ministers in Japan. These Prime Ministers have averaged 19 months in office (Prime Minister of Japan and his Cabinet 2011). Prime ministerial leadership change in Japan was even doubled from the economic growth era from the 1950s to the 1970s. Between 1948 and 1972, there were only 6 prime ministers in office under the same party affiliation, with an average term of four years. It is also a conspicuous leadership change compared to the U.S., which has had four presidents in the period between 1990 and 2011, and China that only has two leaders since 1990. There have been 7 prime ministers in Japan since 2000, and these prime ministers served annually for less than a year (Prime Minister of Japan and his Cabinet 2011). In doing so, the cabinet office has not been able to orchestrate FTA diplomacy. The government has been unable to unite opinions of four ministers (Ministry of Foreign Affairs, Ministry of Economy, Trade, and Investment, Ministry of Agricultural, Forestry, and Fisheries, and Ministry of Finance) into a single policy. In 2009, the government advocated signing a FTA with the U.S. However, the Ministry of Agricultural, Forestry, and Fisheries strongly resisted a possible FTA that reduces tariffs on rice and Japanese fisheries, and the government virtually deleted the policy suggestion (WAPIC 2009). Worsening the situation was a Prime Minister from Democratic Party of Japan (DPJ), Ichiro Hatoyama, who failed to execute his commitment to ameliorate a business and trade environment through FTAs. Whereas the public expected a positive change after a 50-year governance by the Liberal Democratic Party (LDP), Hatoyama suddenly stepped down in June 2010, owing to his disguised list of political contributors (Uchiyama 2009). His successor, the current prime minister Naoto Kan, has also been predicted to resign soon. Kan's sudden decision in increasing consumption tax has not only skyrocketed anti-Kan sentiment among the public, but also the loss of the DPJ control in the upper-house of the Diet, which has reduced his authority since July 2010 (*The Economist* 2011). Kan has further been criticized for being incapable of effectively dealing with the Tohoku earthquake and tsunami in March 2011 (Funatsu 2011). An April 2011 opinion poll showed only 21.8% of public support the Kan administration, already discussing the "post-Kan" government of Japan in terms of who should be the next Prime Minister and how they should take over ongoing issues (Funatsu 2011). Consequently, this repetitious leadership change has not only impeded the government to develop a long-term vision in policies, but has also hindered it from producing practical accomplishments in any policy area (Takayama 2010). *The Economist* (2010) asserts Japan has been "ungovernable" while the government has fundamentally lacked insight into and elaboration of policy choices. It is unlikely that Japan's current FTA diplomacy would be economically effective and efficient in the near future. Kenichi Ohmae, a business consultant and a professor at University of California, Los Angeles notes, "there has been no Prime Minister who has a strong leadership and clear vision since the Nakasone administration in the 1980s" Ohmae continues, "a situation of Japan would be the same, regardless of who comes in office, unless the political system will be structurally reformed" (@nifty news 2011).

*Table 6. Changes of Political Leadership since the 1990s (1989)*

Dates	Names	Actual Years of Inauguration (Approximately)	Party Affiliation
June 8, 2010-	Naoto, Kan	< 1 year	Democratic Party of Japan (DPJ)
September 16, 2009- June 8, 2010	Yukio, Hatoyama	11 months	DPJ
September 24, 2008- September 16, 2009	Taro, Aso	11 months	Liberal Democratic Party (LDP)
September 26, 2007- September 24, 2008	Yasuo, Fukuda	11 months	LDP
September 26, 2006- September 26, 2007	Shinzo, Abe	1 year	LDP
April 26, 2001- September 26, 2006	Junichiro, Koizumi	5 years	LDP
April 5, 2000- April 26, 2001	Yoshiro, Mori	1 year	LDP
July 30, 1998- April 5, 2000	Keizo, Obuchi	2 years	LDP
January 11, 1996- July 30, 1998	Ryutaro, Hashimoto	2 years	LDP
June 30, 1994- January 11, 1996	Tomiichi, Murayama	2 years	Social Democratic Party Japan
April 28, 1994- June 30, 1994	Tsutomu, Hata	2 months	Japan Renewal Party
August 9, 1993- April 28, 1994	Morihiro, Hosokawa	8 months	Japan New Party
November 5, 1991- August 9, 1993	Kiichi, Miyazawa	2 years	LDP
August 10, 1989- November 5, 1991	Toshiki, Kaihu	3 years	LDP

Source: Prime Minister of Japan and His Cabinet.

## Concluding Remarks

This work contends that Japan's so-called FTA diplomacy towards ASEAN nations primarily reflects broad interests of Japanese local actors. While many political scientists believe that Japan's FTA diplomacy towards ASEAN is a response to the rise of China, a focus on Japanese domestic politics provides that the diplomacy is likely to serve concerns of Japanese actors at both domestic and international levels, rather than solely attributing to Japan's apprehension toward the rising China in the international situation. In particular, Japan's FTA diplomacy chiefly facilitates a need for free trade with ASEAN for Japanese corporations to compete in the global economy, and contributes to governmental measures for the recovery of the stagnant Japanese economy by assisting these corporations. Japanese economists particularly emphasize the emerging importance and role of ASEAN economies and markets for *economic* purposes, and this analysis has provided less substantial grounds to concur that Japan's principal intention is to compete with China over a regional leadership. It also indicates that a view of Japan's FTAs in the context of East Asian regionalism may overlook the economic importance of FTAs, by predominantly focusing on the time frame of when China and Japan sign FTAs with ASEAN nations. Such a view based on power politics is then partly as a result of the unclear function of

FTAs as economic instruments due to the lack of the Japanese government's capacity to effectively manage FTA diplomacy.

This logic, however, does not mean that Sino-Japanese rivalry no longer exists. A complex history continues to overshadow China-Japan relations and involves the risk of affecting economic relationships negatively. Political issues between China and Japan have, indeed, affected Japanese business in the Chinese market. While this work predominantly focuses on Japan's perspectives, these factors suggest the need for a more extensive form of an analytical framework, combining studies of both China and Japan's political economies in order to revisit the preeminence of FTAs as a political instrument within Sino-Japanese rivalry. For example, Barry Buzan's security complex theory (1983) utilizes all concerns held by multiple nations in various fields and at any levels in analyzing a bilateral or multilateral relations and institutions, such as the European Union. Buzan (1983) states, "The 'national' security problem turns out to be a systemic security problem in which individuals, states and the system all play a part" (368). According to this Buzan's idea, Stone (2009) adds: "The concepts of amity and enmity cannot be attributed solely to the balance of power. The issues that can affect these feelings range from various factors, including ideology, territory, ethnic lines, and historical precedent" (6). Such an analytical framework allows one to consider the complexity of China-Japan relations in an analysis of FTAs, involving individual political, economic, societal, security, and nationalism matters. A more comprehensive and broader understanding of FTAs for China and Japan remains necessary. Nevertheless, this work proposes an important notion that Japan needs FTAs with ASEAN for its own economic survival. Power politics should not overlook the economic importance of FTAs. This also suggests that, while China has become the second largest economy ahead of Japan, Japan needs to focus on its own domestic reforms, such as its economic structure and political system. The study of the government capacity of Japan particularly reveals a fundamental issue of the government in implementing policies, regardless of who governs. Japan needs to reform its mindset and the political system to re-adopt a clear and long-term vision in managing FTAs and other policies in order to sustain the well-being of the nation in the future.

## Notes

<sup>1</sup> ASEAN groups Indonesia, Malaysia, the Philippines, Singapore, Thailand, Brunei, Myanmar, Cambodia, Laos, and Vietnam. This paper mainly deals with Indonesia, Malaysia, the Philippines, Singapore, Thailand, and Vietnam.

<sup>2</sup> APT includes ASEAN nations, China, Japan, and South Korea.

<sup>3</sup> ODA is a multifaceted aid from Japan to ASEAN nations in various ways. For example, in October 2009, Japan set up the Japan-ASEAN Integration Fund (JAIF), which pledged \$13 million for a disaster management and emergency response. In November 2009, Japan further decided to offer \$5.5 billion in total for Cambodia, Laos, and Vietnam at the first Japan-Mekong summit in Tokyo, aiming at the development of a region around the Mekong River not only for building economic partnerships but also protecting the environment, dealing with climate change, and developing human resources (Chong 2010; Prastirtsuk 2010). CMIM is a regional bilateral currency swap arrangement for APT countries in order to provide liquidity that can ease issues of balance of payments and monitor the flow of capitals (Hamanaka 2008; Wang 2008). Japan and China are main lenders, and other nations like South Korea, Thailand, Malaysia, Singapore, Indonesia, and Philippines are borrowers who alone may not be able to avoid a financial downturn (Hamanaka 2008). In 2009, APT-FMM in Bali, Indonesia, advanced the CMI into the Chiang Mai Initiative Multilateralization (CMIM) agreement. This initiates a unification of the bilateral currency swap agreements in order to avoid another regional financial crisis, which further symbolizes an improvement of political ties among the region (Rathus 2010; Terada 2010; Prastirtsuk 2010).

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