

*Perceptions on Free Trade: The Korean Debate
Over the Japan-Korea Free Trade Agreement.*

by
Chungsoo Kim¹

Visiting Fellow, Center for Northeast Asian Policy Studies
Senior Analyst for Economic Affairs
The Joong-Ang Ilbo

This paper analyzes the Korean public mindset on the country's external economic relations in general, and its efforts of market opening in particular, with the Japan-Korea Free Trade Area (JKFTA) as the case in point.

The study examines the way in which the JKFTA was proposed in 1998 and provides an overview of the Korean media's arguments for, and against, the JKFTA. In doing so, the study argues that Free Trade Agreements (FTA) should be realized, complementary to the multilateral trade liberalization efforts of both Korea and Japan. Until now, these efforts have been taken mostly through negotiations at the World Trade Organization (WTO) and other multilateral organizations.

The study concludes that an embarkation of official negotiations on the JKFTA would contribute to an opening of mindsets in both countries, as well as promoting stability in the region. It points to a need for concerted and steadfast efforts within both Japan and Korea that would seek to nurture and lead the discussion on the JKFTA in ways that are sensitive to the economic and political aspects of bilateral relations between the two.

1. How the Governments Have Led the Discussion

Since bilateral diplomatic relations between Japan and Korea were normalized in 1965, the exchanges between the two countries have substantially grown in trade, investment, and personnel. But the process of economic integration between the two has not been smooth. The bilateral economic relations have often been subject to trade disputes and discriminatory import regulations—as well as rocky diplomatic relations. The recent “historical legacy” debacle is a testament to such troubled waters.

The fragility of bilateral economic relations has become more conspicuous in recent years. The prolonged Japanese recession throughout the 1990s, and the economic crisis of Korea in late 1997, have left enduring marks.

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Both countries witnessed negative growth in overall economic activities in 1998. This stark reality provided sobering moments, particularly for Korea—which had never experienced a negative growth, except in the politically turbulent year of 1980, since it embarked on the course of rapid growth from the early 1960s.

In September 1998, a month before President Kim Dae Jung's first visit to Japan, the Japanese Ambassador to Korea, Okura Kazuo, proposed the JKFTA.² The idea sounded so misplaced to most Korean observers that the initial reactions of the Korean press to the proposal were lukewarm at best.

Still, President Kim's visit to Japan was well received. He proposed an "Action Plan for a New Korea-Japan Partnership for the 21st Century." Its basic message to the Japanese populace was that Koreans are ready to move beyond the mutually antagonistic historical legacy of the 20th century.

It should be noted that in the wake of the region-wide economic crisis, both Korea and Japan began to see the benefits of FTA. At the end of 1998, for example, the Korean government pronounced that: "it is not in our best interest to remain within a very small minority of economies without an FTA membership,"³ and that "it is highly critical for the Korean economy, which is heavily dependent upon international trade, to maintain stable access to foreign markets." The first official rationales for the JKFTA were in simple terms such as "everyone does it," and, it is their "insurance policy" against any potential discrimination in the markets of the region.

This is a serious departure from the long-standing orientations of Korea's international trade policies, for the country has been upholding multilateral trade policies, as opposed to bilateral or regional ones, as their guiding economic principle.⁴ However, by reiterating the official rationales of precedent FTA, both Korea and Japan began to pronounce that the efforts of market opening by FTA can be complementary to those of multilateral liberalization, and that the JKFTA would be constructed accordingly.

It was the March 1999 visit of the Japanese Prime Minister Keizo Obuchi, who proposed the "Japan-Korea Economic Agenda 21," that accorded an official blessing to discussions on the JKFTA. The two governments commissioned the groundwork research to the

² Although "both countries have been busy simply following the rules made by Europe and the United States," Ambassador Okura noted, with a JKFTA, "both countries could exercise initiatives in rule-making of the international economic community, such as those on anti-dumping measures or agricultural trades in which both share interests."

³ Of the world's major trading partners, only five economies, Korea, Japan, China, Taiwan and Hong-Kong, are not members of any RTA (Regional Trading Arrangement). Since 1948, 214 RTA have been notified.

⁴ Such turnabouts in policies have been openly encouraged and chided by the business communities in both countries. Registering complaints that "when entering markets with FTA agreements such as NAFTA, EU or Mercosur, Korean firms are relatively discriminated," they have been urging the governments "to dispel the competitive disadvantage being suffered by Japanese companies." Similar opinions, particularly by Japanese opinion leaders, tend to emerge more often in recent years.

International economic organizations or economists in non-Asian regions have expressed equally strong skepticism about the recent surge of Asian movements towards FTA or RTA.

Institute of Developing Economies (IDE) / JETRO, and the Korea Institute for International Economic Policy (KIEP). In May and September 2000, the results of their studies were published.

According to the estimates of IDE, the bilateral trade imbalance between Japan and Korea would deteriorate further under the JKFTA, mostly because of Korea's higher trade barriers and its relatively weak standing in international competitiveness. The average tariff barrier of Korea is about 7.9%, while the average barrier in Japan is 2.9%. Thus, a FTA between the two would provide greater market access to Japan than to Korea: Japanese exports to Korea would grow more (16.30%) than Korean exports to Japan (8.30%), leading to a greater bilateral trade imbalance (by 3.9 billion dollars) between the two.⁵

These estimates of the short-term effects of the JKFTA have been counter-balanced by estimates of dynamic or long-term benefits of the agreement. Although it is hard to quantify such benefits in pecuniary terms, a FTA is estimated to induce a more competitive environment as well as more secure market access for each country. More importantly, the negotiations on commercial rules and practices that usually accompany those on trade liberalization would bring the two economies closer together: not only through mutual investment, but also deeper industrial cooperation.

The study by the IDE/KIEP points to the potential enhancement of international competitiveness for both Korea and Japan under a JKFTA regime. Accordingly, both countries' exports to the world would increase (Japan by 34 % and Korea by 30%) and world trade would increase by 0.71%. As for Korea's trade balance, its short-term deficit of 1.5 billion dollars would turn into a long-term surplus by an equal amount.⁶

2. Why and Why Not JKFTA? : The Way the Korean Press Sees It

Korea Institute of Newspapers Data System (KINDS), the official database of Korean newspaper articles, reports 409 articles that simultaneously contain the key words, 'Korea' 'Japan' and 'Free Trade Agreement,' for the period from the early 1998 till the end of 2000. Among them, only those of editorials and opinion articles are analyzed. The study provides an overview of their main arguments for and against the JKFTA.

2.1 Economic Implications of the JKFTA

Free Trade Agreements directly imply not only greater market access to participating economies but also deeper and wider economic integration between them. Thus, FTA by nature are welcomed by the 'winner' sectors in participating countries.

⁵ Korean exports are expected to enjoy greater international competitiveness and easier market access in technologically lower-end products such as apparel, leather products, and agriculture/fishery products while the Japanese exports are estimated to do so in more sophisticated trades such as machinery, metal, and chemical products.

⁶ These benefits would be obtained at the expense of third parties, particularly the U.S. IDE/KIEP estimates show that the bilateral trade imbalance between Japan and the U.S. will more than double (by 122%). Similarly, Korea's trade surplus with the U.S. will increase considerably.

FTA, however, induce participating countries to adopt new patterns and practices of business and, thereby, new policies and legal institutions that are commensurate to a new regime of free trade. Therefore, FTA introduce considerable pressure of structural adjustments into the overall economy, the process of which is mostly extended and arduous. In the face of new competition and challenges, the pressures can often be so severe, particularly on some individual sectors, that FTA regimes are bound to face heavy resistance. Arguments expressing this resistance towards the JKFTA and/or arguing in support of the agreement are now examined.

“It helps to dispel the potential of an economic crisis.”

The economic situation in Korea around September of 1998 lent decisive support to this line of argument for the JKFTA. At the height of the economic crisis, Korea was under most severe economic hardships.

Although Korea’s chest of foreign-exchange reserves was rapidly being replenished by the newly earned BOP surpluses from early 1998, it was still in dear need of fresh foreign capital for both its servicing of foreign debts and the economy-wide restructuring that was in full swing. Thus, a free-trade arrangement with Japan was tantamount to a renewal of foreign capital inflow.

Japan, by contrast, was saddled with the largest foreign exchanges reserves among Northeast Asian countries while its banks were the largest foreign creditors to Korea’s financial institutions and conglomerates: “Korea could not go far with its external economic policies that are one-sidedly tilted towards the dollar and the U.S. Besides, Japan is the largest creditor to Korea.”⁷

While this argument for the JKFTA did not draw any opposing views at the time, it is not generating much interest among opinion leaders anymore, particularly because the current foreign-exchange conditions are, by any measure, considerably improved from those in 1998.

“By concentrating on the areas of its own international competitiveness based on comparative advantage, each country could allocate economic resources more efficiently and expedite restructuring in both countries” vs. “The JKFTA will transform the Korean economy into one that is permanently and structurally dependent on that of Japan.”

The proponents of the JKFTA argue that it would institutionalize the efforts and channels of economic cooperation and deepen the division of labor between the two countries. The JKFTA is expected not only to ameliorate the problems associated with the ‘unnecessary over-competition’ between the two, but also to strengthen the potential for sustainable economic growth by prompting more active restructuring.

⁷ Sang-choon Han, “Potentials of Economic Integration among Countries in Northeast Asia,” *Dong-a Ilbo*, September 25, 1998.

Instances of mutual division of labor abound. For example, if Japan transfers 'structurally problematic' businesses to Korea, "the Japanese economic system with high-price, permanent-employment and low-international production will be reformed while Korea would emerge as a supplying base of strategic parts and components."⁸ In addition, both would be able to strengthen potentials of long-term growth, "for Japan could import Korea's cadres of the relatively young work force while Korea imports Japanese capital."⁹

This is the most conventional economic argument for trade liberalization in any form, and it is logically sound. However, in the unique context of Japan-Korea economic relations, it contains seeds of contentious trade friction. More specifically, the underlying logic of 'closer' industrial cooperation between the two appears to imply more concerted efforts to reduce the extent of competition, rather than enhance it. Commercial practices of this type run directly against the norms of competition policies practiced by third parties like the United States.¹⁰

The other arguments against the deepening industrial cooperation related to Korea's economic dependence on Japan. The process of deepening the bilateral division of labor in general, or bilateral industrial cooperation in particular, is said to hopelessly subjugate the whole Korean economy to Japan.

Without preferential arrangements, Korea's industrial structure and level of technological sophistication dictate heavy reliance on Japanese supply sources—not only for capital goods, intermediate goods, parts and components, but also for core technologies. With the JKFTA, the argument of "Dependence Theory" states that Korea would be brought under the complete control of Japan: "Korea would be an economy that would not be able

⁸ Yukiko Fukagawa, "Win-win Economics among South and North Korea and Japan," *Cho-sun Ilbo*, June 6, 2000.

⁹ Youl-ki Kim, "Toward Concerted Efforts of Korea and Japan in Resolving Unemployment Problems," *Moon-hwa Ilbo*, October 16, 1998. The same article goes on to argue that such deepening of the division of labor between the two could also contribute to dispelling "the historically antagonistic relations and advance complementary relations based on mutual cooperation."

¹⁰ In fact, Korea's business community has been thinking along a similar line. When Korea began to aggressively invest in the early 1990s, the basic assumption was that overseas markets would continue to expand and that such investments would help Korea's better positioning in those new areas of international competition. However, global markets have not been expanding as fast as major competitors expected, seriously weakening the sustainable bases of Korean industries' profitability: a widespread decline in profitability has been recognized as one of the major causes of failure in Korea's conglomerates surrounding the economic crisis of 1997.

These prevalent mindsets in both business communities, therefore, are wholeheartedly ready to embrace the argument for a need to deal with over-capacities in both countries. 'Strategic alliances,' as would come about from the JKFTA, that point to overall efforts to reduce over-capacities may appear attractive to the business communities of Japan and Korea, but may also generate negative reactions from those in other countries.

For example, some U.S. industries have been alleging that the Korean government has unfairly involved itself in the restructuring process of the private industries such as iron and steel industries or semi-conductors. They contend also that arbitrary reduction of over-capacities as staged by the government is not only unfair, but that it would also make the world trading environment less competitive.

to survive a day without Japan.”¹¹ To the opponents of JKFTA, the experiences of Japanese colonialism and Korea’s chronic economic and technological dependence on Japan provide sufficient and indisputable evidence to such conjectures: “An integration between Japan and Korea would introduce such a structure of division of labor that would be identical to that of the past.”¹²

“JKFTA would eventually improve the bilateral trade imbalance because Japan’s investments to Korea as well as Korea’s exports to Japan would increase” vs. “It will only exacerbate the structural imbalance.”

The Korean leadership understands that foreign direct investments have been the major victims of the 1997 economic crisis. In other words, the return of foreign direct investment back into Korea has come to be considered a vote of confidence in Korea’s capacity to overcome the crisis and re-establish foundations for sustainable growth in the future. Proponents foresee that the JKFTA, by enhancing potential investors’ perceptions on Korea, would be instrumental in inducing investments—not only from Japan, but other countries as well.

The Japanese investments would, it is hoped, alleviate the acute problems of unemployment in Korea (In February 1999, the unemployment rate of Korea hit the historic high of 8.2%) while encouraging technology transfers from Japan. “They would upgrade the bilateral economic relations to ones of horizontal cooperation and complementarities.”¹³ Thus, “Korea’s demands for Japanese parts and components would diminish while its capacity for exports would be strengthened, and, as a result, Korea would have a window of opportunity to fundamentally rectify the bilateral trade imbalance.”¹⁴

Opponents envisage completely opposite outcomes from the JKFTA. First, in terms of technological sophistication, the Korean industries stand at such absolute disadvantages, relative to industries in Japan, that one cannot rationally expect them to be able to enhance competitiveness and improve the bilateral trade balance. A recent survey by the Bank of Korea reports that Korean exports compete with those of Japan in the world market for 67% of commodity items, but that the former enjoy stronger international competitiveness over the latter in only 8% of the world market: “While Korea’s competitiveness is intrinsically inferior to that of Japan,” “even the results produced by the government-financed research institutes indicate that the JKFTA would result in additional deterioration in bilateral trade deficit by 6 billion dollars.”¹⁵

Second, opponents of the JKFTA argue, it would take too long for Japanese investments encouraged by JKFTA to strengthen the competitiveness of Korea’s exports. “In order to rectify the bilateral trade imbalance, the competitiveness of not only parts and

¹¹ “Do not Allow the Bilateral Investment Treaty between Korea and Japan,” *Han-kyo-reh*, June 23, 2000.

¹² “Do not Allow the Bilateral Investment Treaty between Korea and Japan,” *Han-kyo-reh*, June 23, 2000.

¹³ “It Isn’t A Time for ‘Korea-Japan Free Trade,’” *Moon-hwa Ilbo*, October 2, 2000.

¹⁴ Hee-yon Song, “Japan Rises Again,” *Cho-sun Ilbo*, December 14, 2000.

¹⁵ Jong-hoon Lee, “No Reason to Hurry Free Trade between Korea and Japan,” *Dong-a Ilbo*, June 3, 2000.

components and intermediate goods but also capital goods has to be strengthened. However, it would take considerable time. Thus, the overall effects of the JKFTA would still be too early to conclude.”¹⁶

Third, recent changes in Korean trade have resulted in a deterioration rather than improvement of the bilateral trade balance. In particular, it is argued by Japan, Korea needs to dismantle import bans specifically targeting Japanese goods. As such, Japanese tariffs on certain Korea goods remain high.¹⁷

*“The impact of liberalization would not be as damaging as feared” vs.
“the benefits of free trade are not assured while its costs are clear.”*

Some argue that the impact of the JKFTA would not be considerable, and that it would not add significant restructuring pressure to Korea. This is because Korean markets have sufficiently liberalized and, even without a FTA between them, the exchanges between Korea and Japan are substantially active. For example, “the Korean market is so liberalized that acquisitions of Korean firms by Japanese interests have become normal business practices. After all, the present economic situation in Korea dictates that it should invite, rather than avoid, participation of Japanese enterprises.”¹⁸

In addition to institutional liberalization, the mutual exchanges in other areas, such as cultural or human exchanges, have so progressed over the years that the socio-economic integration between the two countries that may result from the JKFTA would not come as a shock to Korea.

But it is hard to ignore the argument that the costs of the JKFTA, including a deterioration of the bilateral trade imbalance, would “be surely and immediately arrived at” while its benefits, including the strengthening of Korea’s international competitiveness, “appear to be either questionable or would take too long a time to be
¹⁹

Opponents go one step further. Even if the JKFTA would expedite economic restructuring in both countries, it would only exacerbate the economic divide that the recent economic crisis has brought about, adding restructuring pressure to those industries that have been adversely affected by the crisis.

2.2 Implications for Regional Relations

¹⁶ Doo-hyoun Hwang, “Toward a New Horizon in Korea-Japan Relations,” *Joongang Ilbo*, November 29, 2000.

¹⁷ Jong-won Lee, “Regionalism and Korea-Japan Free Trade Area,” *Kook-min Ilbo*, June 21, 2000. Not that Korea officially ‘graduated’ from the status of a developing economy as a result of its 1996 membership to Organization of Economic Cooperation and Development (OECD).

¹⁸ Yoichi Funabashi, “Economic Cooperation between Korea and Japan Lays Foundations for the Framework of Regional Cooperation in Northeast Asia,” *Joongang Ilbo*, September 8, 2000.

¹⁹ “Pre-conditions of a Free Trade between Korea and Japan,” *Moon-hwa Ilbo*, May 17, 2000. One of the main shortcomings of the positive arguments for a JKFTA is that the estimates of benefits by Japanese investments were not based on empirical studies. For example, IDE/KIEP simply assumed certain amounts of investments would follow a JKFTA without providing reasonable grounds for such changes in behaviors on the part of the Japanese investors.

*“The JKFTA is a beginning of the Northeast Asian economic integration”
vs. “an economic bloc in the Northeast Asia as would be encouraged by
the JKFTA is neither feasible nor appropriate.”*

In recent years, there have been many initiatives and discussions on international institutions or organizations for cooperation among the countries of the Northeast Asia. After all, this is a region that will soon contain the second and the third largest economies in the world. Many analysts also envision the highest economic growth rates emerging from Northeast Asia in the near future. Thus, an endeavor such as the JKFTA, which would provide an impetus to region-wide single economic community, has come to be viewed favorably: “In view of the economic sizes and the common characteristics of market economy and democracy, the economic cooperation between Korea and Japan surely marks the first step toward the long-term goal of the Northeast Asia Economic Community.”²⁰

Second, the initiatives for deeper and wider regional cooperation and integration hit chords on a sentiment shared by the countries in the region: Northeast Asia has yet to recognize its proper place in the world economic community commensurate to its economic influence. One hears that “China, Japan and Korea, combined into one, could command a stronger voice in formulating the new rules of the global economy.”²¹

One should note that all the related arguments assume the economic integration between Korea and Japan as a springboard toward the eventual economic integration of the whole of East Asia, “If the deepened relations between Korea and Japan get expanded to trilateral relations, by adding China, and to those encompassing the economies in East Asia, then East Asia shall participate, as one of the Three Core economic powers, in the global efforts to establish the new international economic order.”²² Also, “the advancement of cooperation should contribute not only to the enhancement of bilateral interests but also to the stability and development of the whole Northeast Asia. It is, therefore, a diplomatic duty of the two countries” to proceed with the JKFTA.²³

Third, attempts to make progress in regional integration are also hoped, by the proponents, to strengthen the capability of collective response to potential region-wide economic crises. In relation, one should be able to note that most of the arguments for the JKFTA begin by paying tribute to the fact that the Northeast Asia is the only region that does not have any preferential trade arrangements.²⁴

²⁰ “Reaffirming the ‘Mutual Responsibilities’ between Korea and Japan,” *Se-gye Times*, September 25, 2000.

²¹ “Conditions of a Korea-Japan Free Trade Area,” *Han-kuk Ilbo*, September 21, 1998.

²² “Reconciliations of North and South Koreas and New Cooperation between Korea and Japan,” *Dae-han Mae-il*, September 24, 2000.

²³ “Wimp Diplomacy of Japan,” *Kook-min Ilbo*, September 26, 2000.

²⁴ One could consider APEC as a preferential trade arrangement among Asia Pacific countries. However, its plans of 2010 (for advanced economies in the region) or 2020 (for developing economies) trade liberalization are not so binding enough that one could view them as a system of trade regimes. APEC remains to be a talk shop among economic leaders of the region, who do not want to be excluded from the summit gathering.

The strong arguments for the need of a regional economic grouping are matched by equally compelling arguments against it. First, the region lacks many elements for a region to move on a integrative course. What is most clearly missing in the region is the minimum degree of homogeneity, which all other regions that have highly integrated economies, such as NAFTA or the European Union, enjoy. It is doubtful, some argue, that other countries in Northeast Asia would join with Korea and Japan even if they could form a regional grouping like the JKFTA. Furthermore, a prevalent observation notes that the region's populaces lack a sense of community or 'collectivity' that can transcend historic animosities and uneven stages of economic development among the various countries.

Second, as the concepts such as the collective influence of Northeast Asia or the arguments for a need of region's "own voice" amply suggest, there are potentially destabilizing sentiments in the region that are intrinsically exclusionary against non-regional countries. This is worrisome because "the United States, the first and foremost economic and security partner to all the economies in the region, would not want to see an exclusionary economic bloc emerge in the region."²⁵ Note that the Korean opinion leaders are ever mindful of the U.S. reaction to the idea of the JKFTA: "The U.S has been maintaining the APEC process as the main pillar that supports the momentum of economic cooperation and trade liberalization in the Asia Pacific region, thus, would not allow Japan to make such an independent move for economic hegemony."²⁶

"By agreeing to the JKFTA, Korea is de facto recognizing Japan's greater posture in the international community and its constructive roles for the regional economy" vs. "it would spark competition for hegemony"

Japan remains the main source of economic resources for the regional economies, including not only capital and technology but also markets. But its contribution to the regional welfare has yet to be recognized, which has been admittedly the long-standing aspiration on the part of Japan. Thus, if Korea agrees to a FTA with Japan, it would be de facto recognition of Japan's prominent role in the region.

This argument of a 'marriage of convenience' assumes that such 'moral' support of Korea for Japan would be reciprocated by some 'economic' support from the latter. As supporting evidence to such arguments, proponents highlight the recent changes in economic influences of major economies the Korean Peninsula: "Korea becomes more attractive to Japan as its major economic partner, as China quickly emerges as a major economic power in the region,"²⁷ and the need for the Japanese market grows for Korean exporters as the future of the U.S. economy becomes uncertain. "Korea should look away from the setting sun of the U.S. economy toward the rising sun of Japan."²⁸

²⁵ "Korea-Japan Free Trade Agreement is Too Early," *Moon-hwa Ilbo*, May 16, 2000.

²⁶ Chul-ju Choi, "The Issues Korea Should be Mindful of," *Joongang Ilbo*, December 5, 1998.

²⁷ "Transforming the Perspectives for Economic Cooperation between Korea and Japan," *Han-kook Ilbo*, September 21, 2000.

²⁸ "It Is Not All That Bad for Economy," *Dong-a Ilbo*, December 26, 2000.

However, support for deeper relations with Japan face the gravest challenges from the legacy of an antagonistic history between Japan and Korea. Due to the legacy of mutual antagonism during the period of Japanese colonialism, Japan can make no suggestion for grand integration without evoking memories of Japanese control in Korea. Many still remember all the ‘visions of Asian integration’ made by the Japanese as justification for its colonialism. The lingering suspicion about the motives behind Japan’s recent efforts to enhance its regional posture reflects the prevalent perception that the Japanese public is by nature narrow and egoistically minded. In spite of all the liberalization measures Japan asserts to have taken, many both in and out of the region still perceive that Japan has been, and remain, a closed and mercantilist economy.²⁹

There also exists skepticism on whether or not Japan could play a greater role as the main absorber of regional exports. The decade long recession of the Japanese economy speaks strongly to such skepticism. This suggests a serious need for Japan to carry out economic restructuring rapidly and earnestly before it can assume a greater role in the region, or propose new plans of cooperation, such as FTA, to neighbors. Furthermore, there is a growing concern about the heated competition, particularly between Japan and China, in initiatives for Northeast Asian economic integration. Many express concerns that competing ideas of a Chinese Economic Bloc, on the one hand, and a Yen Bloc, on the other, may destabilize the economic and security environments of the region.

Opponents view the JKFTA as potentially accelerating such a destabilizing process. They consider the JKFTA initiative as a ‘conduit to lure Korea into a regional body that Japan would dominate’, ‘an intention to diminish Korea as a part of Japan’s scheme of regional economic hegemony’, or to ‘maintain the economic leadership of Japan in face of the emerging economic influence of China as a result of the latter’s new membership to the WTO.’ Thus, some opponents, who tend to have less concern or skepticism about China, even assert, “Korea doesn’t need Japan. A new era of cooperation, that of the North-South Korea as well as that with China and Russia, is unfolding before our eyes.”³⁰

“The JKFTA would be instrumental in providing support to the changes in North Korea and, thereby, it contributes to the stability of Northeast Asia.”

This argument arises as the prospects of better relations and more active exchanges between North-South Korea have come into focus. The hope for secured and preferential access to the largest market in the region, Japan, gathers strength as the time approaches for Korea to assume the role of main provider of economic support to the survival and future development of the North Korean economy.

It is hoped that the JKFTA will contribute to the economic development of North Korea and its evolution into a stable partner of economic cooperation by promising a secured access to the common market of Korea-Japan. “The cooperation between Korea and Japan would also contribute to the improvement of Japan-North Korea relations that is

²⁹ Chul-ju Choi, “The Issues Korea Should be Mindful of,” *Joongang Ilbo*, December 5, 1998.

³⁰ “It Isn’t A Time for ‘Korea-Japan Free Trade,’” *Moon-hwa Ilbo*, October 2, 2000.

necessary to transform North Korea into a responsible member of the international community.”³¹

Practical implications that the JKFTA have with respect to the improvement of relations between the two Koreas are wide ranging. The process of the normalization of relations between Japan and North Korea and the settlement of reparation negotiations are expected to introduce a variety of business opportunities into North Korea. Therefore, the business community of South Korea will be better positioned if the JKFTA is concluded before such developments take place.

“The JKFTA, particularly an agreement on investments, would work as a buffer to the initial shock of Korean reunification. The shock of reunification would be more smoothly absorbed collectively by Japan and Korea than singularly by South Korea.”³² President Kim Dae-Jung’s comment that “the efforts of South Korea alone are not sufficient for the North Korean economy to recover” clearly indicates his wish that Japan should play an active supporting role in the process of reconciliation on the Korean Peninsula.

3 Policy Implications

3.1 A Window of Opportunity for Free Trade

Since the late 1990s, the attention of political leadership in both countries has been diverted away from furthering the cause of economic liberalization in general and mutual economic integration in particular. In fact, it is rare these days to hear a reaffirmation of commitments to economic cooperation between Japan and Korea. Similar trends can be observed by the dispirited discussions among private experts and in the press. The receding interest in the JKFTA is more clearly noticeable in Korea. Now that the economic crisis is officially over and antipathy against foreign interests is on the rise again, the supportive argument for the JKFTA is losing momentum.

However, the political leadership in both countries would be wise to revive the JKFTA. For better or worse, they should bring the issue back to the limelight of public discourse.

Before this study makes any further policy recommendations, however, a few observations are in order. First, as discussed above, the historic legacy has always been the major barrier to any meaningful at cooperation between the two countries. The JKFTA is not an exception to this rule. The discussion above and the ongoing disputes over past history suggest that moral responsibility for such agreeable developments fall mainly on Japan. The Japanese leadership must be sincere, creative, and most importantly, persistent in devising and carrying out forward-looking measures for historical reconciliation.

³¹ “Reconciliations of North and South Koreas and New Cooperation between Korea and Japan,” *Dae-han Mae-il*, September 24, 2000.

³² “Transforming the Perspectives for Economic Cooperation between Korea and Japan,” *Han-kook Ilbo*, September 21, 2000.

If the official efforts to resolve the historical issues fail or face insurmountable hurdles, one can envision a case where “a division of labor between governments and non-governmental organizations be devised where the former lead the efforts of cooperation for the future while the latter play key leading roles in resolving thorny historic issues of the past.”³³

Second, smooth progress of the bilateral economic cooperation has also been hampered by both an inferiority complex and attitude of defeatism on the part of Koreans vis-a-vis Japan. To the eyes of Korean industries, Japanese producers continue to appear insurmountably strong. To meet the challenge, Korea should strive to equip itself with such economic institutions and practices that properly reflect its economic size and level of economic development. Only through strenuous efforts for economic reforms, structural adjustments, and continuous enhancement of industrial technology bases, can the “inferiority” of Korea be overcome. Only then can Korea cooperate with Japan as a full and equal partner.

Third, the JKFTA, if realized, would fundamentally transform the mindsets of both countries on market liberalization. Both countries are known to be two of the most protectionist economies among the major trading nations. This is particularly true regarding their respective agricultural trade regimes. One should note that over its short history of market liberalization, Korea has opened its markets only at the strong urging of its largest trading partners, most often the U.S. Thus, if the JKFTA is to be successfully established, it would be the first effort of market opening that is voluntary and based on a Big-Bang approach. The JKFTA would open a valuable window of opportunity to transform the fundamental orientation of the Korean economy. It would signal to the domestic Korean population that free trade is socio-politically feasible, and even preferable.

Fourth, non-member states, such as the U.S. should support, rather than discourage, the JKFTA, despite its potential for diverting trade away from such countries. One should not fail to note that the JKFTA has wide-ranging implications for the overall reforms in Northeast Asia. The experiences with NAFTA indicate that one of the major benefits of a FTA lies in its ‘lock-in’ effects of domestic and external reforms in member countries.

3.2 Policy Recommendations

The following recommendations are suggested on the premise that Free Trade Agreements are not only beneficial to member countries, but also can and should be made complementary to the efforts of multilateral trade liberalization and the expansion of global trade. Policy makers should concentrate their efforts not in making a priori conjectures about the future idiosyncrasies of something that does not exist, but rather in devising a FTA that would not compete with multilateral liberalization efforts.

³³ Young-ho Kim, “Towards Cooperation between Civil Societies of Korea and Japan,” *Cho-sun Ilbo*, October 7, 1998.

*“Japan should play a proper role as a leader in Northeast Asia—
commensurate to its economic power—and Korea should acknowledge*

When Japan attempts to play a leading role for economic integration in Northeast Asia, based on a newly strengthened international posture, it should do so by “forwarding the paradigm of equity and openness that all the leading economies in other regional groupings have shown.”³⁴

Japan should, first, re-establish the domestic foundation of sustainable economic growth. Through continuous and aggressive economic reforms and political stability, the Japanese economy should be revived as early as possible. Second, Japan should play its proper and expected role as the leading economy in the region—which can be accomplished by overcoming its closed mindset and dispelling economic institutions and practices that go against free global competition. In October 1998, on his presidential visit to Japan, President Kim revealed his views on the JKFTA that “it would be meaningful only when Japan plays the role of the only advanced economy in Asia by adopting the economic policies that are based on domestic demands.”

“New initiatives to rectify the bilateral trade imbalance should be taken

It appears practically impossible to proceed with any serious discussion on the JKFTA before the bilateral trade imbalance shows signs of improvement. Therefore, bilateral economic interplay should be foremost directed toward reducing the bilateral trade imbalance. In relation, one can hear, in Korea, that “a separate measure should be taken that would guarantee expansion of transactions in capital and technology which could offset the expansion of bilateral trade imbalances.”³⁵ One such alternative would be to strike a deal on a Bilateral Investment Treaty (BIT) well ahead of the JKFTA so that the ensuing expansion of the Japanese investments would assure the benefits of more integrated economic relations between the two. It would set a favorable stage and dispel Korean skepticism about the JKFTA.

*“When schedules of dismantling trade barriers are ironed out with the
JKFTA arrangement, the gaps in competitiveness between Japan and
Korea, overall or sector-wise, should be duly taken into consideration.”*

Individual industries in both countries show stark gaps in international competitiveness, as revealed not only in each other’s markets but also third markets. These industries will be put under the most severe pressure of structural adjustment as a result of the JKFTA. Therefore, in order to introduce a new free-trade regime with minimum friction—economic or social—sensitivity to the needs of individual industries should be applied in both dismantling trade barriers and establishing a temporary safety net for weaker industries.

³⁴ Robert Fouser, “The Arrogance of Japan against the Tides of Globalization,” *Dong-a Ilbo*, August 18, 1999.

³⁵ Jong-hoon Lee, “No Reason to Hurry Free Trade between Korea and Japan,” *Dong-a Ilbo*, June 3, 2000.

The other aspect Korea may wish to see as an integral part of the JKFTA is the free movement of the work force, which would help to maintain the vitality of production in Japan. Another favorable aspect of the JKFTA is that the agreement is expected to bring minimal shocks to Korea's agricultural sector. Because the impact on the farmers will be slight, one should not expect strong resistance against JKFTA from this politically vital sector.

“The JKFTA cannot be anything but an open Free Trade Agreement.”

The JKFTA should be pursued with a sense of direction shared by both countries that the open characteristics in its framework and nature will be further strengthened over time. This is to avoid potential exclusion of regional allies. The fundamental rationales for both countries to keep the JKFTA open are, first, that both have greatly benefited under the multilateral trading system throughout the period of their respective economic developments, and second, that both have been repeatedly discriminated against by other economic blocs in recent years.

In addition, both have been occupying more than minor positions in furthering the cause of economic cooperation in the Asia-Pacific. However, both countries have been insistent on relatively protectionist positions, particularly in the service and agricultural sectors. Furthermore, Northeast Asia holds high potential for hegemonic competition among several players—in economic power as well as diplomatic and military power. Many Koreans are concerned with a potential breakout of hegemonic conflicts between Japan and China. Also, an imprudent move in the process of establishing the JKFTA would be to generate misunderstanding on the part of the U.S., which has been maintaining direct interest in the way economic, diplomatic, and security relations of Northeast Asia unfold. These are the compelling reasons why the JKFTA should be maintained as an open preferential trade arrangement.

The openness of the JKFTA should be also maintained with respect to new membership. As long as a third country is willing to implement a free-trade regime with Japan and Korea, its accession to the JKFTA should be encouraged. By consciously maintaining its openness, the JKFTA and the ensuing economic integration between the two countries could turn into a catalyst for region-wide economic integration. It could lay valuable foundations for deeper and wider integration so that an economic community might follow, even unto an APEC-wide FTA.

Concluding Remarks

While recognizing all the opposing views, this study has adopted as its point of departure the view that free trade is always beneficial for the public and private players involved, and that Free Trade Agreements are one of the ways that countries can expand and strengthen free trade regimes.

In consideration of the deep-rooted Korean skepticism about the benefits of free trade, an official negotiation on the JKFTA with Japan would provide a rare opportunity for Koreans to seriously review their trade policy orientations and adjust them in such a way that would fit better with the new environment of global free trade.

The JKFTA would also provide a valuable catalyst towards regional economic integration, thereby contributing to the political and economic stability of Northeast Asia.

Since the JKFTA was proposed in 1998, however, there have been signs that the narrow window of opportunity is fast closing. In the course of overcoming the economic crisis of 1997, Korea went through an acute period of drastic reforms and restructuring and its political stability faces challenges. Also, Japan is under mounting pressure to reform and restructure its economy after a decade-long recession. As a result, the leadership, both economic and political, appear to be losing interest in embarking on new initiatives of comprehensive market opening.

Nevertheless it is time for both countries to revive bilateral economic liberalization and integration. The JKFTA will be the prime vehicle for such a grand endeavor.

