

COMMENTARY

Japan's Asia policy must become more relevant

By Motoshige Itoh

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China's gross domestic product is predicted to surpass Japan's this year. How should Japan deal with a fast-rising China? This is a crucial and difficult issue for Japan, both politically and economically.

A decade ago, Japan's economy was overwhelmingly huge in comparison with that of China, which was only one-third the size despite being the second largest economy in Asia. The rest of the region can be better imagined than described.

What will happen to Asia's economic landscape 10 years from now? It is difficult to accurately forecast future developments, but it is projected that China's economic strength will triple that of Japan a decade from now, even if China's pace of growth slows somewhat. In this projection, Chinese yuan's possible revaluation has been taken into account. Other Asian economies also are likely to grow during the coming decade.

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Moreover, there is a possibility of China, India and the Association of Southeast Asian Nations outstripping Japan as the region's economic titans more than two decades from now. In other words, Asia will be significantly different from what we have seen to date, and Japan will no longer be a dominant regional economic power.

Rise in reliance on trade

These forecasts do not mean the Japanese economy is destined to shrink. Rather, the economic might of its neighbors is likely to become overwhelmingly large. Such forthcoming changes will inevitably compel Japan to carry out reforms. How will the fast-growing neighboring countries affect the Japanese economy? In searching for an answer, we should take a look at Germany.

Japan's exports and imports account for about 30 percent of its GDP, while the comparable figure for Germany stands at about 72 percent. Thus, the German economy's reliance on trade is more than double that of Japan. The reason for this gap is simple. Germany heavily exports goods and services to and imports from major neighboring economies, such as Britain, France and Italy.

In the field of economics, what is happening to Germany is a natural consequence of "the gravity model" of international trade. According to the model, pioneered by Jan Tinbergen, a Dutch economist who shared the first Nobel Prize in Economic Sciences in 1969, bilateral trade volumes tend to be greater when two countries concerned are geographically close to each other and their overall GDP and GDP per capita are high. The Tinbergen theory may sound obvious, but it so perfectly explains the actual trade data that the model is widely applied in various studies even today.

Let's apply the theory to Japan's trade structure. In the past, there were no large economies around Japan. Instead, the United States and Eu-

rope, located far from Japan, were its major trading partners. As a result, Japan's overall trade volume was relatively small. However, with its neighboring Asian economies experiencing robust growth, trade between Japan and the rest of Asia should rise steeply, according to the gravity model. Such a development will result in a rise in Japan's reliance on trade. U.S. President Barack Obama earlier proposed doubling U.S. exports in five years, but, considering its Asian neighbors' economic expansion, Japan is in a better position to double its overall exports—and imports as well.

'Internationalization' of Japan

Whether we like it or not, exchanges between

insights
into the
world

Japan and the rest of Asia definitely will expand—there will be increases not only in trade with the rest of the region, but also in movements of people and money as well as corporate activities and civil and cultural exchanges. Many goods will be shipped to the rest of Asia and vice versa.

Against such a backdrop, Japan should explore ways to get along with the rest of Asia that favorably affect its own future. In this sense, it is time to seriously think about Asia's future in ways that will benefit the entire region, including Japan. Therefore, it was natural for former Prime Minis-

ter Yukio Hatoyama to propose the creation of an East Asian community. Although there has been a lot of talk about it, no specific road map has been crafted to achieve such a goal.

In a related development, the Tokyo-based National Institute for Research Advancement—for which I concurrently serve as president—issued a report in September focusing on enhancing regional partnerships in East Asia. In the report, the institute touched on what should be done to promote regional cooperation in a wide number of fields, including trade, currency, civil aviation (e.g., a pan-Asian open skies liberalization proposal), education and environmental protection. All of those subjects are of great importance to Japan's future.

The key to rejuvenating Japanese society and strengthening partnerships with the rest of Asia is "internationalization" within Japan itself. Thus far, food supplies, agriculture, medical services, education, regional rejuvenation and taxation, among other areas, have been discussed solely within a domestic framework. The country's internal systems should be thoroughly reviewed, with a view to opening them up to the rest of Asia. It is pointless if Japan pursues reforms only from an inward-looking standpoint, because such an approach would only spur efforts to protect vested interests.

APEC summit and TPP

As for the definition of East Asia, an ASEAN plus Three framework, involving the ASEAN bloc, Japan, China and South Korea, is conceivable. It is important to deepen regional partnerships in conjunction with such a framework. Nevertheless, the United States and Australia should not be excluded from regional partnership efforts. Also, the existing Asia-Pacific Economic Cooperation forum, which groups the United States, Australia, Canada and other Pacific Rim countries, will remain im-

portant. Considering that no final, definitive concept of an East Asian community has been worked out, multiple approaches toward such a regional community should be pursued through the ASEAN plus Three framework, the ASEAN plus Six grouping, which also involves Australia, India and New Zealand, and APEC.

Regarding enhanced regional partnerships, the APEC summit talks in Yokohama this month and in the United States next year will be historically important to determine the structure of future regional cooperation.

Whether Japan will declare its participation in the proposed Trans-Pacific Partnership (TPP) free trade agreement is being closely watched. The TPP accord—a regional partnership arrangement distinct from the ASEAN plus Three approach—is significant for its inclusion of the United States and Australia, two Asia-Pacific powers.

Japan's participation in the TPP framework that would lead to trade and market liberalization will be the touchstone determining the country's future. If domestic factors prevent its participation in TPP, Japan will continue to be an inward-looking nation—and its Asia-Pacific neighbors certainly will look askance at this country.

Without taking part in the TPP framework, it will become difficult for Japan to enter into negotiations for other economic partnership agreements. If this happens, no country is likely to listen to this country no matter how seriously it advocates the establishment of an East Asian community. If Japan remains inward-looking in an Asia where many other countries are growing rapidly, it will find itself stalemated.

Fortunately, the APEC summit meeting in Yokohama offers a timely opportunity for Japan to declare its intention to participate in TPP negotiations. By all means, Japan should not miss this historic opportunity.