

Japan & China

In East Asian
Integration

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In East Asian
Integration

LIM HUA SING



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*This book is dedicated to my parents,
Lim Chong Leng and Yap Ah Chuan*

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Abbreviations

AA	Asia-Africa Linguistic Institute
AFTA	ASEAN Free Trade Area
AICO	ASEAN Industrial Cooperation Scheme
AIDS	acquired immunodeficiency syndrome
AMF	Asian Monetary Fund
APEC	Asia Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
CAFTA	China-ASEAN Free Trade Area
CEC	Chinese Economic Community
CEPT	Common Effective Preferential Tariffs
CER	Closer Economic Relations
CIS	Commonwealth of Independent States
CPF	Central Provident Fund
DAC	Development Assistance Committee (of OECD)
EA	East Asia
EAEC	East Asian Economic Caucus
EAEC	East Asian Economic Circle
EAEC	East Asian Economic Community
EAEG	East Asian Economic Grouping
EAEI	East Asian Economic Integration
EAMF	East Asian Monetary Fund
EC	European Community
ECEC	Ethnic Chinese Economic Community
EDB	Economic Development Board
EPA	Economic Partnership Agreement
EU	European Union (as of 1 November 1993)

FDI	Foreign Direct Investment
FTA	Free Trade Agreement Free Trade Area
FTAAP	Free Trade Agreement of the Asia Pacific
FTAs	Free Trade Agreements
FMP	Fourth Malaysia Plan
GATT	General Agreement on Tariffs and Trade
GDP	gross domestic product
GNP	Gross National Product
GPS	Global Positioning System
GSP	Generalized Scheme of Preferences
HICOM	Heavy Industries Corporation
IAFTA	India-ASEAN Free Trade Agreement
IDE	Institute of Developing Economies
IDEA	the Initiative for the Development in East Asia
IMF	International Monetary Fund
JAFTA	Japan-ASEAN Free Trade Agreement
JCCI	Japanese Chamber of Commerce and Industry
JE	Japan Embassy
JETRO	Japanese External Trade Organization
JICA	Japan International Co-operation Agency
JIS	Japanese Industry Standard
JOFTA	Japan-Oceania Free Trade Agreement
JSE	Japan Singapore Association
JSEPA	Japan-Singapore Economic Partnership Agreement
JTC	Japan Trade Centre
KAFTA	Korea-ASEAN Free Trade Agreement
LDP	Liberal Democratic Party
M&A	merger and acquisition
MD	Missile Defense
MIPRO	Manufacturers Import Promotion Organization
MITI	Ministry of International Trade and Industry
MNCs	Multinational Corporations
MSC	Multimedia Super Corridor
NAFTA	North America Free Trade Area
NAFTA	North America Free Trade Agreement

Abbreviations

NIEs	Newly Industrializing Economies
NGO	Non-governmental Organization
NPB	National Productivity Board
NTB	non-tariff barrier
NTUC	National Trades Union Congress
NWC	National Wages Council
ODA	Official Development Assistance
OECD	Organization for Economic Cooperation and Development
OEM	Original Equipment Manufacturing
OPEC	Organization of Petroleum Exporting Countries
PAS	Parti Islam
PNOC	Philippine National Oil Company
R&D	research and development
ROC	Registrar of Companies
SCCCI	Singapore Chinese Chamber of Commerce and Industry
SFCCI	Singapore Federation of Chambers of Commerce and Industry
SIJORI	Growth Triangle (Singapore-Johor-Riau Growth Triangle)
SISIR	Singapore Institute of Standards and Industrial Research
SJEZ	Sea of Japan Economic Zone
SMA	Singapore Manufacturers' Association
SMB	small and medium-sized businesses
SPC	Singapore Petroleum Company
TDB	Trade Development Board
UNCTAD	United Nations Conference on Trade and Development
UK	United Kingdom
US	United States of America
WB	The World Bank
WTO	World Trade Organization

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June 2003

Preface to the Fifth Edition

Asia is Moving Towards Closer Economic Cooperation and Integration

Since the Asian financial crisis erupted in 1997, most of the affected countries in Asia have, to some degree, miraculously recovered from the hard-hitting crisis within a year or two. Asia, as a dynamic region, has once again attracted the world's attention. Over the last few years, economic cooperation and integration have been further promoted and stimulated in the region through the signing of Free Trade Agreements (FTAs) and Economic Partnership Agreements (EPAs) among the Asian countries. The Newly Industrializing Economies (NIEs) and the Association of Southeast Asian Nations (ASEAN), together with China and India, have succeeded in a promising and sustainable economic development path. This is despite the fact that some countries, such as Thailand and Myanmar and to a lesser extent Indonesia and the Philippines, have encountered some form of social and political instabilities, which has somehow adversely affected the economic performances of these countries. Certainly, these instabilities have affected but not prevented the Asian countries from moving forward towards economic development. Asia has again, by and large, become the centre of economic development in the world.

Japan and China in Asia

Japan is a highly regulated, rigid and systematic society without much flexibility and tolerance. Japanese prefer thorough and long-term results when they conduct political, economic and social changes. It may be one of the reasons to explain why Japan takes a longer time to conduct structural reforms. Japan has to-date not completely recovered from the implosion of the bubble economy starting 1991. It has however, over the last 16 years,

conducted numerous reforms (political, economic, industrial, social and structural) with eagerness and seriousness. It is said that once Japan has returned to the right developmental tracks, economic development will be fast and impressive, compared to most of the other Western nations. Besides, economic fundamentals in Japan have been sound and have not worsened much over the last one-and-a-half decades. In the long run, however, the ageing and decreasing population problems, the reluctance of taking foreign professionals, huge fiscal deficits, and the closed agricultural and fishery market issues, will either leave Japan out from the rest of Asia, or cause Japan to develop without substance.

China, on the other hand, has developed rapidly and consistently over the last 29 years. She has become a regional as well as an international power. Within the next few decades, China will likely, together with the United States, become one of the two megapowers in the world. China, of course, is not without its difficulties. Commonly cited problems include environmental pollution, income disparity, corruption, uneven development between rural and coastal areas etc. These difficulties are likely to be solved gradually together with economic development, as the central government has implemented forceful policies to tackle them.

It is said that China's economic development is lagging behind Japan's, in terms of per capita GDP, by at least forty to fifty years. China's present economic developmental level is about that of Japan's in the 1960s or late 1950s. However, the pace of China's economic development has been much faster than that of Japan. It is possible for China to catch up with Japan and the Western nations in a shorter period. At present, as the largest developing country, China's foreign currency reserves have reached US\$1 trillion 66.3 billion (2006) and is ranked the number one country in the world. Foreign direct investments and international trade surpluses (US\$177.5 billion in 2006), together with the inflow of billions of "hot-money" due to the expectation of the appreciation of the Renminbi, have contributed to China's impressive domestic savings and capital formation. The speedy accumulation of capital and savings in Chinese banks and in central government treasury has annoyed even the Government as to how to utilize the funds for economic development purposes. Some of the measures, for instance, to increase social and industrial infrastructure spending, to increase foreign investments and foreign aids, to increase investments in education, to assist and nurture domestic small and medium-sized enterprises, and to improve and upgrade welfare system etc., have to be taken vigorously. By doing so, it will help China upgrade its economic level and international status, and to get rid of her developing country

status and at a faster pace, to become one of the newly industrializing countries (NIEs).

As an NIE, China will then, together with Japan, play a bigger role in East Asian economic cooperation and integration advancement.

From ASEAN 10+3 to ASEAN 10+3+3

China, together with Malaysia under the Mahathir administration, and to a lesser extent, Korea, were strong advocates of the ASEAN 10+3 grouping towards East Asian economic cooperation and integration. On the other hand, Japan was a strong advocate of ASEAN 10+3+3 or even ASEAN 10+3+3+1, as shown in previous Prime Minister Koizumi Junichiro's speech on the concept of "Comprehensive Economic Partnership" in Singapore in January 2002. When Dr. Mahathir proposed the concept of East Asian Economic Community (EAEC, later changed to East Asian Economic Caucus) in December 1990, obviously the countries involved were limited to ASEAN 10+3. Together with the United States, Oceania (Australia and New Zealand) was also excluded from the grouping, but the status of India was then not specifically mentioned. It seemed that the members of EAEC did not exclude India. In other words, Dr. Mahathir's EAEC concept did not have any intention to exclude India from the beginning. In that case, members of EAEC would have been ASEAN 10+3+1 (India).

In December 2005, the first East Asian Summit Meeting in Malaysia eventually agreed with the concept of ASEAN 10+3+3, despite some disagreements from the member countries. Russia was also invited to the meeting since it is a big power in Asia Pacific and also a resource rich country. Presently, East Asian economic integration has moved towards ASEAN 10+3+3, and the status of Pakistan and Bangladesh will sooner or later be put on the discussion table during the subsequent East Asian Summit Meetings. Maybe, at a later stage, some more island countries in the Pacific may wish to apply for membership. Will the EAEC then not become an entity even bigger than APEC?

The second East Asian Summit Meeting was held in the Philippines in January 2007. The ASEAN 10+3 summit meeting was held only one day before the ASEAN 10+3+3 summit meeting. Did it imply anything substantial and crucial? Did it mean the former was the core entity of the latter? Or the latter must be accomplished on the foundation of the former? Was it a temporary arrangement or was it going to be a permanent setting? So far, it has remained uncertain.

The Meaning of ASEAN 10+3+3+1 and FTAAP

The President of the United States, Mr. George Bush, had suggested the idea of FTAAP (Free Trade Agreement of the Asia Pacific), just before the APEC meeting which was held in Vietnam in November 2006. No country opposed the idea openly or officially, although some countries were skeptical and suspicious about the US's motive behind the idea. The APEC meeting in Vietnam did not discuss the idea at the meeting but had however taken the idea seriously, and it is likely that the next APEC meeting in Australia at the end of this year, will discuss the issue seriously in USA's favour.

The United States had been left out from the concept of the EAEC from the beginning, as early as in 1990. Over the last 17 years, the USA has been concerned about the development of regional cooperation and integration in the Asia Pacific region. She has so far signed or is in the process of signing FTAs with some of the Asian countries. However, unlike the China–ASEAN FTA (CAFTA), the India–ASEAN FTA (IAFTA), the Japan–ASEAN FTA (JAFTA) and the Korea–ASEAN FTA (KAFTA), the USA has not signed an FTA with the ASEAN10 as a group. Moreover, besides APEC, of which the USA has been playing a leading role, the USA does not have any formal economic relationship with the Asia Pacific region as a group. It has therefore been a main concern of the policy-makers in the USA to link with the Asia Pacific region as a group. The idea of the FTAAP has just reflected the USA's long-term concern.

East Asian Economic Community Has Become Unpredictable

*The evolution of EAEC — ASEAN 10+3 —
ASEAN 10+3+3 — ASEAN 10+3+3+1*

(FTAAP) has been a long process. Throughout this process, despite so many negotiations, disagreements and conflict of interests, East Asian countries have signed numerous FTAs or EPAs bilaterally and multilaterally, and economic cooperation and integration have been pushed forward steadily. The new framework of ASEAN 10+3+3, however, has created a new challenge to the region. It was against the wishes of China and Malaysia, but reflected the strong wish and intention of Japan. How the three new members, namely India, Australia and New Zealand, play a constructive role towards East Asian economic integration will remain one

of our main concerns. Is it necessary for the new three, India in particular, to be manipulated politically to counter balance or to dilute the increasing influence of China? As an international strategy, do the USA and Japan really need to make use of the new three to counterbalance China?

When it comes to the concept of the FTAAP, the situation in the Asia Pacific region has already become more complex. The FTAAP is no more than APEC. Is FTAAP an institutionalized and functional APEC? How can the FTAAP develop in parallel with APEC? Should the FTAAP replace APEC in the end? These are some questions which are not easy to answer now.

In any case, the fact is that East Asian economic cooperation and integration have become more complex. If the APEC members at the 2007 APEC summit meeting in Australia agree with the FTAAP, the USA, judging from her political and economic powers, will be playing an increasingly more important role in the East Asian economic integration process. Would not the USA's interest contradict with the interests of China, Japan, Korea and India? Will the America-ASEAN FTA develop with the Four ASEAN 10+1? These are some questions to be faced by countries in the Asia Pacific region, once the idea of the FTAAP has been accepted by the APEC meeting in Australia.

This is a new book based on "Japan's Role in Asia — Mutual Development or Ruthless Competition" (4th Edition), published by Eastern Universities Press, Singapore, 2003. In this new book, "Part 8 Japan and China in Asia-Pacific" has been added. Under Part 8, nine new articles are included to analyse the current economic development of the Asia-Pacific region. Special attention is particularly paid to the domestic economic development of Japan, China and India. Besides, analyses on the politico-economic relationship between Japan and China, and a comparison of economic strengths between China and India in East Asian economic integration, are examined. Finally, an overall analysis on East Asian economic integration, including some observations on the recent development and future prospects of the region, are provided.

In carrying out country research, attending international conferences and collecting data for writing these articles, the author is grateful for the generous financial support of the Ting Hsin International Group, without which this new book would not have been completed and published.

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Preface to the Fourth Edition

Forceful measures have not been taken despite favourable economic fundamentals

Japan's economic role in the world and Asia in particular, has been diminishing since the collapse of the bubble economy in 1991. Over the last 12 years, the Japanese economy has not managed to recover and her contribution to Asia (in terms of foreign direct investment, international trade, Official Development Assistance and technology transfer) is becoming less and less important.

Needless to say, the Japanese and Asian economies are interdependent as well as complementary. Japan can contribute more to Asia only when she has recovered economically. Similarly, Japan can benefit more from Asia only when Asia's economic development is on the right track. On Japan's side, despite a long period of economic sluggishness, some economic strengths have surprisingly remained unchanged. Japan is considered as number one in the following categories.

First, foreign currency reserves have amounted to US\$485.3 billion as of March 2003 (China ranks second in the world with US\$212.2 billion in year 2001). It is due in large part to Japan's international trade drive and more recently, the government's currency interference through selling Japanese yen in exchange for the greenback, in order to fulfill a weak yen policy.

Second, Japan's total net overseas assets amount to 133 trillion yen as of December 2000. Overseas assets held by Japanese banking corporations alone have amounted to 45 trillion yen as of December 2002. It indicates that Japan has accumulated a substantial amount of long term overseas capital investments as well as foreign national bonds and equities, especially in the United States.

Third, Japan's ODA during the 1991–2001 period was the largest among the DAC countries. It became the second largest since 2002 but still accounted for US\$9.7 billion (1 trillion 250 billion yen) in May 2002. The ODA budget reflects the economic strengths of a country and it has also been used to stimulate the advancement of a country's foreign business activities.

Fourth, Japanese national assets (cash, deposits, bonds, investment securities, shares, insurance and pension) amounted to 1386 trillion yen by March 2001. It reached 8275 trillion yen in December 2002, if real estate and buildings are included. The main task of the Japanese government now is to mobilize these national assets in order to expand the domestic market and to activate the economy.

Besides these economic strengths, both big and medium-small sized Japanese enterprises have accumulated world-class technologies, which guarantee Japan's industrial development despite the economic recession. Furthermore, the economic downturn over the last 12 years has created a 5.6% unemployment rate in Japan, which is still rather healthy compared to the double digits we see in some European countries. And this is the reason why Japan is not in a chaotic situation.

Very few people could have predicted that Japan's economic downturn would drag on for 12 years, with no sign of recovery. Many Japan watchers are puzzled and cannot pinpoint what exactly is wrong with the Japanese economy. Policy-makers in Japan have so far managed to identify some basic ailments of the Japanese economy: non-performing loans, deregulation, deflation, strong Japanese currency and privatization etc. However, forceful measures still need to be taken to counteract these problems and fulfill economic goals.

Asia sees Japan's economic deterioration as a burden to Asian economic development. Now, Asia is expecting Japan to emerge from the economic doldrums, hopefully in 2–3 years time, and contribute to Asia's economic development in accordance with her economic strengths.

Can Japan's Role be Replaced by China?

China has been Japan's rival in Asia, in the economic, political, military and diplomatic arena. China's role in Asia, even if we restrict it to the economic front, has been increasing and to a certain extent, has replaced Japan. In the long run, China's role will become significantly more important at the expense of Japan.

Over the last 25 years, since she started implementing a ‘reforms and open-door policy’ in 1978, China has become the first country in the world to succeed in rapid and continuous economic development. Economic development in special economic zones and coastal areas has been particularly remarkable. The per capita GNP of Guangzhou, Shenzhen, Shanghai and Beijing have already exceeded most of the developing countries in Asia. As a developing country with a 1.3 billion population, China’s economic development will continue to attract much attention.

However, together with economic development, China has encountered many serious problems — a drastic increase in income disparity between coastal and rural areas (in the year 2002, the ratio was 6:1), unemployment, expanding social gap between the poor and the rich, the 3Cs (corruption, collusion and cronyism), environmental pollution, non-performing loans and the privatization of state enterprises etc. Of course, it is unrealistic to expect China to have rapid economic development for such a long period without experiencing some serious economic distortions. The issue is whether China can solve these problems efficiently before they deteriorate farther to create political, economic and social instabilities in the country.

At current levels, the rate of economic development in China is said to be about that of Japan in the 1960s. In other words, if we assume that Japan’s economy is standing still, China will have to develop for another forty years to reach Japan’s present standard. China’s per capita GNP is US\$854 (year 2000) compared to US\$32,585 (year 2001) of Japan. The former is merely 2.6% of the latter.

China has become a “factory of the world”. Chinese manufacturing goods have penetrated into international markets and Japan, together with the Western nations, have considered China as an economic threat. However, China’s economic strengths should not be over exaggerated. Over the last two-and-a-half decades, how much technology has been accumulated by Chinese enterprises in China? How many local enterprises have been nurtured to become big enterprises or multinational corporations? How many local enterprises in China are run based on world level managerial practices? In other words, China’s economic development has been relying heavily on foreign direct investment, technology and managerial know-how.

Also, some critics claim that China’s legal system has not been developed to match domestic economic development processes, nor serve a highly developing nation such as China.

China still has a long way to go. The GDPs of China, Japan and the USA are US\$1.08 trillion (year 2000), US\$4.14 trillion (year 2001) and

US\$8.35 trillion (year 1999) respectively. The ratios are 1: 3.8: 7.7. China pledges to increase her GDP to around US\$5 trillion in twenty years, as is the Japanese standard today. Obviously, it is a very difficult task for China, but the Chinese people seem to have the confidence to fulfill it.

Some China watchers have even warned that the present bubble economy would burst sooner or later. They also claim that the “socialist market economy” (politically, it is a centrally controlled socialist system but economically, it is a western way of free competition capitalist economy) would not last very long. However, as the Chinese like to say, China has pledged to develop her economy with Chinese socialist characteristics.

Frankly, I am also rather optimistic about China’s economic development. Despite various economic distortions and contradictory economic development strategies, by the year 2008 when China hosts the Olympic Games, and by the year 2010 when China holds the World Exhibitions, China would by all means be able to develop without drastic setbacks. Even after the year 2010, say for another farther 10–15 years, it is unlikely that economic development in China will have major retrogressions caused by serious macro-economic mismanagement. In China, the following factors are contributory reasons to economic development: approximately 900 million peasants are potential industrial labourers, cheap agricultural and industrial raw materials, big domestic market with a 1.3 billion population of which the middle class population has been increasing rapidly, political and social stability, and a mechanism set in place to proceed with economic reforms and an open-door policy.

Regional Economic Integration is An Engine for Asian Economic Development Japan and China are two important players in Asia, a declining player and an emerging player (although Korea can be considered as a recovering player with economic potential). Other than the USA and the EU, Japan and China have had the most profound influence in Asia.

ASEAN 10 is a well-organized entity to which Japan and China have established increasingly important cooperation links with. In November 2001, China proposed the concept of a FTA (Free Trade Area) with ASEAN to be set up within 10 years. This concept, termed as CAFTA (China-ASEAN Free Trade Area) or ASEAN 10-plus-1, is being materialized faster than expected. Meetings and feasibility negotiations at governmental levels have been carried out frequently to expedite the process of regional economic cooperation and integration.

On the other hand, stimulated by China’s initiative, Japan has also proposed “comprehensive economic cooperation” with ASEAN in January

2002. This proposal was later termed as JAFTA (Japan-ASEAN Free Trade Agreement) or another ASEAN 10-plus-1. At the beginning, it was criticized as being without a definitive timeframe. How long was it going to take to set up? But recent sources indicate that Japan intends to realize the JAFTA within a period, which is even shorter than that of China.

Obviously, economic cooperation and integration endeavors in Asia are basically prompted by two factors. First, the formation of the EU and the NAFTA, with strong exclusive undertones, has restricted economic growth and cooperation of the Asian countries with these 2 blocs. Hence, the need exists to setup their own trading entities. Second, economic development within Asia has necessitated intra-Asia regional economic cooperation and integration, with an eye to expand into each other's trading markets.

With the initiatives of China and Japan, and most probably Korea in future, economic cooperation and integration among the Asian countries will be strengthened. Although China and Japan are rivals, they need to work closely for the benefit of Asia's economic development and infra-regional integration. Both CAFTA and JAFTA should be promoted accordingly, and eventually ASEAN 10-plus-3 (China, Japan and Korea) should be materialized under the concept of a pan-Asia regional economic integration outfit.

As an important economic power, it is hoped that Japan will move to implement economic policies more resolutely and consistently, in order to recover from her current economic downturn as quickly as possible, before its leading role in Asia is overtaken by China.

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June 2003

Preface to the Third Edition

Japan is at the crossroads of Asia. She is expected to contribute more towards Asia's economic revitalization and development, but encounters two problems. One, the Japanese economy has not bottomed out since the collapse of the bubble economy in 1991. The prolonged stagnant economy of Japan Inc. has forced her to pay more attention to domestic issues, such as deregulation, opening up of the domestic market, Big Bang programs and industrial restructuring etc. All these policies and measures are aimed at resuscitating Japanese economy but have so far not reaped any concrete results.

Two, Japan's role and initiatives in Asia have always been suspect and questioned by the Asian countries, especially by China and the two Koreas. Japan's military expansions in Asia in the 1930s and 1940s, together with her non-thorough 'war liquidation' after World War II, have always created suspicions about her motives and intentions in Asia. Japan should act collectively rather than individually, should she want to play a more active and positive role in Asia. In principal, Japan should invite China and Korea, and cooperate closely with the ASEANF 10, to find ways and solutions for Asia to achieve a stable and conducive environment for better economic development.

The economic relationship between Japan and Asia is supplementary as well as complementary. In retrospect, the stagnant economy of Japan during the 1991–1996 period can be considered as one of the important factors contributing to the Asian financial crisis. Japan's Foreign Direct Investment (FDI) in Asia decreased, exports from Asia to Japan diminished and the strong Japanese currency left Asia with highly indebted countries. All these have affected Asia's overall economic performance and have eventually led to the eruption of the Asian financial crisis. On the other hand, during the 1985–1990 period of the bubble economy, Japan invested heavily in Asia and Asia's exports to Japan as well as to other international markets recorded

phenomenal growth. The Japanese government, banking corporations and industrial enterprises extended substantial capital and loans to Asia. When the Asian countries suffered from crippling bad debts during the Asian financial crisis period, Japan suffered the most among the creditor nations. Japan will continue to suffer if the bad debt issues among the Asian countries cannot be resolved. In fact, these bad debt issues have not been resolved for many years. Needless to say, Japan will feel the impact if the debtor countries push for debt write-offs in place of good faith. One of the aims of the New Miyazawa Plan is designed to help the Asian countries settle their bad debts.

In the meantime, there is a consensus that economic cooperation among the Asian countries should be strengthened. One point in mind is to implement the New Miyazawa Plan, leading to the setting up of the Asian Monetary Fund (AMF). China and Korea had reservations about this but have become more supportive in recent months. Japan should not move as a distinct entity but should invite China and Korea to participate more actively. At the same time, close cooperation from the ASEAN 10 is also critical. In this way, Japan is expected to assist the Asian countries to recover from the Asian financial crisis and to revitalize and move forward to rapid economic development in the 21st century.

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Preface to the Second Edition

For about two months before Lee Teng Hui made the sudden “state-to-state” announcement on 9 July 1999, most of the countries in the Asia-Pacific region had started experiencing some kind of economic recovery from the recent crisis. With relatively stable currency exchange rates installed, stock and property markets improved, foreign currency reserves increased and confidence in market economy was restored — almost two years after the Asian financial crisis erupted on 2 July 1997.

On analysis, Asian countries used various policies to tackle the financial crisis. These countries can be divided into three groups. The first group, such as Korea and Thailand, resorted to the prescription proposed by the International Monetary Fund (IMF): deflationary fiscal policies, higher interest rates and thorough industrial restructuring. The second group, such as Malaysia and China (including Taiwan and Hong Kong), refused the IMF prescription and undertook expansionary fiscal policies, lower interest rates, gradual industrial restructuring and foreign exchange and capital controls. The third group, for example Indonesia, rejected the IMF prescription initially but later adopted it. The present situation in Indonesia is rather unpredictable, as the country has just held its general elections and the ruling Golkar party (which has governed Indonesia for 34 years), as generally predicted, lost ground to opposition parties. Both political and economic development in Indonesia have remained unstable, as the president in the country has yet to be elected and the country’s overall reconstruction has yet to be carried out smoothly and speedily.

Incidentally, the Asian stock markets picked up again, soon after Lee Teng Hui made his “state-to-state” statement on 9 July. Taiwan’s stock market dropped but experienced some recovery when the central bank in Taiwan interfered. The Asian stock markets have not been further jeopardized as the US, the EU, Japan and ASEAN 10 were quick to

reconfirm their “One-China” policy. The cross-strait relations are tense, but at the present time, Taiwan is totally isolated. Pressures from the People’s Republic of China (PRC) on Taiwan have been increasing but it is unlikely that the PRC will unify Taiwan by military means in the near future. The PRC prefers peaceful reunification as long as Taiwan does not proclaim “independence”.

After 21 years of rapid economic development since it first implemented the open-door policy in 1978, China requires a peaceful environment in the Asia-Pacific region to ensure the success of its “socialist market economy”. Besides, under such a severe economic environment in Asia, China has had her hands full tackling the following problems: diminishing foreign direct investment, decreasing international trade surpluses, restructuring state enterprises, rapid increase of the unemployment rate, income disparity, developmental gap between coastal and inland areas, worsening deflationary tendency and so forth. China has to solve these problems speedily and recover the 7–8% economic growth rate this year before its unemployment issues worsen. In the meantime, China not only has to strengthen its economic relationship with the West (in terms of expanding international trade and luring foreign direct investment and technology), but also with her neighbouring countries in Asia, particularly those with a significant overseas Chinese presence. Chinese economic communities in Asia will, in the long run, make a notable impact on China’s economic development in terms of capital, technology and managerial know-how.

It is fair to say that China can claim to be a stabiliser since the financial crisis erupted on 2 July 1997. On many occasions, China was under great pressure to surrender to Renminbi depreciation but managed to maintain a considerably stable exchange rate level with the US dollar throughout the period of the Asian economic crisis. China has, therefore, contributed greatly both to the stability of the Asian currencies and to the recovery of the Asian economies.

Obviously, China is a big player in the Asia-Pacific arena. However, Japan’s economic impact and influence on Asia should, without doubt, be considered with special attention. Japan’s role in Asia should be properly assessed, both as an economic superpower and the world’s second largest economy. As early as in September 1985, due to the phenomenal appreciation of the Japanese currency, Japanese companies started investing heavily in Asia, and this greatly stimulated economic development of the Asian countries. Both the supply and demand sides among the industries in

Asia were prompted by Japanese heavy investment, which had undoubtedly contributed to the creation of the Asian “economic miracle”.

However, the bubble economy in Japan burst in early 1991. Despite efforts (such as deregulation, opening up of domestic markets, financial restructuring, economic stimulus and rescue packages) made by Japan over the period 1991 till today, the Japanese economy has so far not shown any promising signs of bottoming out. The Japanese economy has been stagnant and the unemployment rate has reached approximately 5%, which is the highest since World War II.

Asia has long been expecting Japan to recover from its economic woes. Its prompt recovery would mean that Asian economies would be pulled along with Japan's due to Japan's substantial foreign direct investments in the region and Japan's importation of manufactured products from Asia. Japan should have invested heavily in Asia during the 1991–1995 period as the Japanese currency continued to appreciate, reaching its unprecedented level of 78 yen per US dollar in April 1995. However, Japan's capital investment in Asia was stagnant during this period when the yen was strong. Surprisingly, the strong yen did not stimulate exports of manufactured products from Asia to Japan. Just before the Asian financial crisis in July 1997, exports of manufactured products (machinery in particular) from Asia to Japan had in fact decreased abruptly. Japan's poor economic performance in helping Asia was basically due to her domestic economic sluggishness. To a large extent, the sluggish Japanese economy contributed adversely to the slowdown of many Asian economies, which eventually resulted in the eruption of the Asian economic crisis. Asia would not have experienced the worst of the economic crisis had Japan's economy not been in the doldrums then, as it is today.

Japan has also been seriously affected by the Asian economic crisis. As Asia imports less manufactured products from Japan, Japanese manufacturing industries in Asia are forced to reduce or to stop production; bad debts accumulate and are not recoverable due to companies' going bankrupt; and foreign debts and loans are not paid due to lack of foreign currency reserves. Moreover, Japan has been the largest official development assistance donor to the world and to Asia in particular. Japanese banks, financial institutions and private companies have extended the most loans to the Asian countries, Thailand and Indonesia in particular. Among the highly industrialized countries in the world, Japan suffered the most from Asia during the Asian economic crisis period. The crisis has in fact postponed Japan's economic recovery.

Economic relations between Asia and Japan are complementary. The New Miyazawa Plan (Shin Miyazawa Koso) planned to distribute some US\$30 billion (which has been increased to US\$80 billion to-date) to the Asian countries to help their economies recover. Loans have been extended to some of the Asian countries to develop industrial infrastructure and to nurture supporting industries; to purchase national bonds issued by cash scarce countries in Asia; and to settle bad debts incurred by banks and financial institutions in Asia. Increasingly more feasibility studies have been carried out and more useful and insightful results are expected. As a substitute to the IMF, the idea that the New Miyazawa Plan should develop into the Asian Monetary Fund (AMF) has yet to be explored. The AMF concept should, in principle, be based on the consensus involving all the Asian countries. It is advisable to set up an international institution or organization in the Asia-Pacific region to supervise capital flows and overall macroeconomic policies among member countries. Furthermore, economic co-operation among member countries in the region should be farther encouraged and strengthened in the 21st century. Japan will then be expected to play a more constructive and decisive role in this context in the Asia-Pacific region.

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August 1999

Preface to the First Edition

The increasing trauma of worldwide economic recession has generated a disconcerting tendency: short-sighted protectionist policies are being established in some major industrialized countries, at the serious expense of fruitful international co-operation, to increase world trade and development. Protectionist policies have been rationalized as important and necessary measures to protect domestic industries, to remedy chronic trade imbalances and fiscal deficit, and also to reverse the worsening of unemployment. But notable authorities have agreed that the global economic depression of the 1930s, which later led to the outbreak of World War II, is attributable essentially to the protectionism embraced by different countries in the world at that time. The Newly Industrializing Economies (NIEs) and the Association of Southeast Asian Nations (ASEAN) could continue to demonstrate, as they have been doing, the fruitfulness of a co-operative and open partnership in achieving economic affluence and progress. Other countries too can benefit from this tie, based on an open economic interdependence among the countries in the Asia-Pacific region.

Most of the countries in Asia, especially the NIEs and ASEAN, have taken a common stand strongly critical of protectionist policies and practices. Both the NIEs and the economies of ASEAN are basically outward-looking. The NIEs have succeeded in shifting the emphasis from import-substitution to export-orientation activities. The ASEAN countries are now moving towards export-orientation activities. Likewise, both the NIEs and ASEAN require an open economic environment to promote international trade and economic co-operation.

Nevertheless, among the industrialized nations, trade frictions between Japan and the Western nations (the United States in particular) have not been resolved, despite numerous negotiations at government level and between economic circles. Exports into the Western markets of Japanese manufactured goods, particularly semiconductors, automobiles, and

electronics and electrical products, have been seriously curtailed; exports of American and European goods — automobiles, machinery and equipment, electronics and electrical products, agricultural products (for example, rice, beef and oranges), and light manufactured goods (such as chocolates and cigarettes) — into the Japanese market have been alleviated. But such moves notwithstanding, the Western world continues to exert pressure upon Japan as the trade deficit, favourable always to Japan, fails to recede to an “acceptable” level.* Japan is still considered a “closed market” by the West. Trade conflicts between Japan and Western countries are likely to continue for some time.

The trade balance between Japan and the developing countries, particularly the NIEs and ASEAN, cannot be ignored either. The NIEs and ASEAN have been important customers of Japan for machinery and equipment, electronics and electrical products, base metals and various types of vehicles. At the same time, the NIEs have been important suppliers of light manufactured products and an increasing amount of industrial products (both intermediate and capital goods) to Japan. On the other hand, ASEAN has been an important supplier of mineral products and raw materials to Japan.

The NIEs have been very much geared to Japan. Their rapid economic development has been primarily reliant on the introduction of capital, technology and managerial know-how from the developed countries, and from Japan in particular. The more the NIEs develop economically, the more they have to import from Japan. Likewise, the NIEs have long been suffering trade deficits with Japan. Despite the fact that the trade relationship between the NIEs and Japan has, in recent years, been shifting significantly from “vertical” to “horizontal”, it still has not been satisfactorily rectified. This is partly due to Japan’s non-tariff barriers and “closed market”, and partly due to the fact that the NIEs’ industrial products are less competitive (in terms of quality, design and packaging).

Through most of the 1970s, excepting the years 1970, 1972 and 1974, Japan–ASEAN trade was favourable to the ASEAN countries, mainly because of the massive consumption of ASEAN natural resources and raw materials by Japan. In the 1980s, this basic trade pattern remained unchanged. In the 1990s, ASEAN’s exports of manufactured goods to Japan will probably increase substantially, but the Japan–ASEAN trade relationship will presumably remain as “vertical”. Japan is expected to open its market wider in order to reduce its trade surpluses with ASEAN.

In the 1960s, the strategy for industrial development in different ASEAN countries was based primarily on policies advocating import substitution. But in the 1970s, a general shift to export-oriented policies

occurred, triggered by two trends: import-substituting industries were becoming unattractive as they are restricted to products merely involving assembly; and some ASEAN countries were incurring serious trade deficits as a result of excessive imports of materials and accessories flooding in from industrialized nations, Japan in particular. During the first half of the 1980s, the ASEAN economies were either stagnated or recessed. ASEAN recovered only after the second half of the 1980s, when resource-based and export-oriented industries were launched, mainly to promote primary and related industries. In recent years, the ASEAN economies have been shifting gradually from labour-intensive to capital- and technology-intensive activities. ASEAN's exports of industrial products have gained momentum. Nevertheless, export-oriented industries in the ASEAN countries experienced varying difficulties in obtaining access for their products to the Japanese market. The quality and design, relatively inferior to those of Japanese products, were partly responsible. But responsible also were the Japanese non-tariff barriers and "closed market" which restricted exports of the NIEs and ASEAN manufactured goods into the Japanese market.

In general, the Japan-NIEs/ASEAN trade relationship has remained vertical and asymmetrical. The NIEs and ASEAN are likely to increase imports of intermediate and capital goods from Japan owing to their rapid industrialization and close relationships with Japan. But the Japan-NIEs/ASEAN trade relationships will be jeopardized should Japan not increase its import of manufactured goods from the NIEs and ASEAN. The phenomenal yen appreciation after September 1985 and the increase in Japanese foreign direct investment (FDI) in Asia are seen as stimulants of imports of manufactured goods, especially from the NIEs and ASEAN.

The economic performance of the NIEs and ASEAN is greatly reliant on the Asia-Pacific region. As the major economic player in this region, Japan can largely determine whether its relationship with its neighbours in the Asia-Pacific region is either (1) one of mutual development and prosperity, a symbiotic relationship, resulting in the region's countries affecting the transition from underdeveloped and developing to a developed, economically cohesive bloc or (2) one of ruthless competition, systematic underdevelopment by Japan of its neighbours and distrust of Japan by its neighbours, resulting in an economically balkanized Asia-Pacific region.

This book was published under the title *Japan's Role in ASEAN: Issues and Prospects* in 1994. The title of this edition has been altered to *Japan's Role in Asia: Issues and Prospects* as two new chapters, "Japan's Economic Involvement in Asia and Chinese Partnerships" and "Economic Superpower

and International Roles” have been incorporated as Part 4. In addition, statistical data has been updated to reflect the latest economic development between Japan and Asia.

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The author is obliged to the Institute of Southeast Asian Studies for allowing him to utilize three articles for this publication: “Japanese Perspectives on Malaysia’s ‘Look East’ Policy” (*Southeast Asian Affairs*, 1984); “Singapore–Japan Trade Frictions: A Study of Japanese Non-Tariff Barriers” (*ASEAN Economic Bulletin*, vol. 4, no. 1, July 1987) and “Japan in ASEAN: Potential Trade Frictions” (*ASEAN Economic Bulletin*, vol. 1, no. 2, November 1984). The first and third articles, with minor modifications, provide background understanding of the economic relationship between Japan and Malaysia, as well as between Japan and ASEAN. The second article, with substantial revision and updating (besides the questionnaire survey results) to incorporate the latest data on the Japan-Singapore trade relationship, analyses Singapore’s lopsided trade relationship with Japan, and the substance of Japan’s non-tariff barriers encountered by Singapore’s manufacturers and exporters. The author is also indebted to the University of Tokyo Press, for permission to republish his article entitled “Features of Japanese Direct Investment and Japanese-Style Management in Singapore” (1991), with modifications and updating, in the form contained in this book.

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* In 1991, the major Western countries “which suffered trade deficits with Japan were as follows: the United States US\$43.4 billion, UK £4.5 billion, Germany DM 23.2 billion and France F24.6 billion. In 1992, the United States and the EC suffered US\$43.6 billion and US\$31.2 billion trade deficits respectively with Japan. In 1993, the United States and the EU suffered US\$50.2 billion and US\$26.3 billion trade deficits respectively with Japan.

