Shift in Japanese policy towards preferential trade agreements and its impact on foreign merchandise trade

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ABSTRACT

The article examines whether Japan's involvement in preferential trade agreements (PTAs) has benefited the country's foreign merchandise trade. At first reluctant, from the beginning of 21st century Japan has become active in signing PTAs. The research confirms positive effects of PTAs on Japan's foreign trade. After PTAs had been entered into force, Japan's exports to partner countries improved. Although Japan currently runs a trade deficit with PTA countries in aggregate, positive trends in the trade deficits with individual countries are observed. Arguably, Japan will achieve a total trade surplus with PTA countries in the foreseeable future if the positive trend continues.

Keywords: *Japan, regional economic integration, preferential trade agreement, foreign trade*

Introduction

Preferential trade agreements (PTAs) began to flourish in the 1990s. As a result of changes in foreign economic policy of countries, PTAs started to be considered as phenomena not disturbing the multilateral order in international trade but as complementary to it. Therefore, both the number and scope of such cooperation agreements began to increase among countries. At first, this type of foreign economic policy, popular in Europe and North America, was not a priority for Japanese authorities. On the contrary, Japan maintained the position that PTAs endanger the most fundamental goals of the World Trade Organization (WTO) and the former General Agreement on Tariffs and Trade (GATT), leading to discrimination. Then, a set of different external and internal factors caused a shift in Japanese policy towards PTAs. Japan did not want to lose in international competition due to not participating in such agreements. To the contrary, it wanted to benefit from involvement in closer economic relations with its trade partners.

The main objectives of this paper are as follows. First, this paper shall attempt to identify changes that took place in the economic policy of Japan towards PTAs since the beginning of the 21st century. Second, the author will illustrate the transformations that have been taking place in Japanese foreign trade with respect to PTA countries in order to understand whether PTAs were beneficial for Japanese merchandise trade, or not. The time horizon of trade analysis covers the period after 1998 when first proposals of cooperation towards Japan were formulated with Mexico and South Korea.

The goals of the paper have determined its structure. The next section discusses the historical developments of PTAs. An explanation of the basic motives, effects, and benefits of PTAs are provided next. Thereafter, issues related to Japanese policy towards PTAs are discussed, and reasons for the growing interest of Japan in such agreements are presented. Next, in the analytical part of the paper, the main trends in Japanese trade ties with PTA countries are presented. The penultimate section assesses and discusses the benefits for Japan attributable to PTAs formation. The paper ends with a summary and conclusion.

Historical evolution and theoretical background of PTAs

Despite the fact that some examples of regional PTAs were already seen in previous centuries, the proliferation of PTAs is a recent phenomenon. Until 1990 the total number of regional trade agreements notified to the GATT was only 30 (Urata, 2009). In the 1990s, the number of concluded agreements increased by 128 (to 158). As of 1 July 2016, WTO had received some 635 notifications on regional trade agreements, counting goods, services, and accessions separately (WTO, 2016). Of these, 423 agreements were in force. Among all WTO member states, only Mongolia was not a party to an agreement on preferential trade. That situation changed on 7 June 2016 with the entering into force of the Free Trade and Economic Integration Agreement between Mongolia and Japan (WTO RTA Database, 2016).

Directly after World War II, in 1947 a multilateral trade policy framework was established. However, a few years later, regional PTAs became a more popular vehicle. In the post-war period, three waves

of regionalism can be identified: (1) the late 1950s and 1960s; (2) mid-1980s to late 1990s; and (3) the beginning of the 21st century (WTO, 2011; Pasierbiak, 2015; Carpenter, 2008).

In the first wave of regionalism countries such as Belgium, Germany, Holland, Italy, Luxembourg and France played the most important role. Since 1951, these countries have been pursuing more advanced forms of economic integration. In 1957, the European Economic Community (EEC) was brought to life, in the framework of which, a customs union started to operate in 1968. In 1960, other European countries that had not wanted to integrate within the EEC framework created a concurrent organization – EFTA (European Free Trade Association). In the same period, many countries of Africa, the Caribbean and Central and South America undertook initiatives of forming regional or sub-regional economic unions, but by the end of the 1970s, most of them ceased to function (WTO, 2011). In subsequent years, regionalism consisted mainly of deepening and widening integration within the EEC. One of the examples is the United Kingdom's EEC accession and thus leaving EFTA.

The second wave of regionalism took place from the mid-1980s. At that time the EEC undertook reforms leading to the creation of a real single market and, after the collapse of the communist system, the EEC started to be involved in deeper cooperation with selected former socialist countries. During that period, the European Union signed bilateral agreements, among others, with Israel, Jordan, and Algeria. The United States also became an advocate of regionalism at that time. In 1988, the U.S. signed an agreement with Canada (Canada-U.S. Free Trade Agreement - CUFTA), which in 1994 was expanded to include Mexico. In this way, the North American Free Trade Agreement (NAFTA) was created. Integration initiatives also took place in South America. The most important example was the creation of the MERCOSUR (Southern Common Market). Argentina, Brazil, Paraguay and Uruguay decided to build a common market modeled on the European Union. In Asia, regionalization was implemented mainly by the creation of a free trade area by ASEAN (AFTA – ASEAN Free Trade Area), as well as by plans for the establishment of the Asia-Pacific Economic Cooperation. This initiative was implemented in 1989, and its purpose was pursuing free and open trade as well as investment among its twelve founding members on a non-preferential basis.

The third wave of regionalism began in the 21st century, mainly because of activities of the European Union and the United States, but also many Asian economies. Countries such as Japan, South Korea, Singapore, China, and India joined in the formation of PTAs, although by that time they had been supporting the then current multilateral order. In addition to traditional areas, such as the reduction of tariffs within the framework of the preferential areas, contemporary agreements often include issues such as services, capital flows, standards, intellectual property rights, regulatory systems, obligations with respect to labour and environmental protection. They go far beyond the scope of regulations of the World Trade Organization.

Motives, effects, and benefits of PTAs

The proliferation of PTAs indicates that there must be important reasons for countries to be involved in such undertakings.[i] These motives are both economic and political in nature. The first economic

motive is the neutralizing beggar-thy-neighbor trade policy. A protectionist economic policy's measures tend to have a positive impact on the economy of the country. However, they are damaging for other countries. This is done mainly through the so-called terms of trade effect and production reallocation effect. These kinds of effects do not occur when countries decide to co-operate, and not undertake unilateral actions.

The second motive involves the economic desire to enhance the credibility of the country. Signing and implementing an agreement may raise the credibility of the government, and make its actions to be seen as long-term and not as cyclical and short-term. Other economic motives involve, among others, benefits from extending the size of the addressable market (associated with economies of scale and the greater propensity of investors to locate their activities in a wider area) and increasing predictability of policies. These, in turn, sends positive signals to investors about economic openness and elicits greater involvement.

In addition to economic factors, there is a range of PTA determinants, which are political in nature. These include a growing significance of political integration and internal policies of countries; forms of government, institutions, and diplomacy, as well as the influence of 'power' and the idea of the formation of PTAs.

The motives mentioned above should lead to achieving far-reaching integration benefits. Without such benefits, countries would be discouraged from engaging in integrational processes. International economic integration theory confirms that involvement in regional integration brings effects (benefits but also costs). In the short-term, benefits arise mainly from the increase in trade flows, but in the long run, they rely on the growth of production, factors of production's productivity, Gross Domestic Product (GDP) and GDP *per capita* growth (Mucha-Leszko, 2012).

According to Bhagwati and Panagariya (1996) theories of international integration went through two phases of development: (1) the traditional approach with its static effects and (2) the non-traditional approach with dynamic effects of international integration. The traditional economics of PTAs are based on Jacob Viner's idea that two basic effects arise from the creation of a free trade area (customs union): trade creation effect and trade diversion effect (Viner, 1950). Countries will be interested in regional integration processes when static benefits prevail over static losses. In other words, trade creation effects should be more significant than trade diversion effects. However, there is no evidence that the creation of a customs union always leads to an increase in the world's welfare.

A changing economic and political environment brought about a concentration on the dynamic effects of the economic integration process. According to Balassa (1962), dynamic effects include economies of scale (market expansion), technological change, the impact on market structure and competition, productivity growth, risk and uncertainty and investment activity. Functioning in small markets increases costs for enterprises but also reduces the intensity of specialization. There is also a limitation of competition and weakened tendency of technological progress. These are reasons why countries will likely seek to remove such disadvantages through the integration processes. Many

authors allege the opinion of Balassa who saw pro-competitive effects of regional integration stemming from changing market structure and competition (Hosny, 2013). When monopolistic or oligopolistic structure is challenged by more intensive competition as a result of markets' integration, it can lead to increases in productivity (Urata, 2009).

Trends and tendencies in Japanese trade ties with PTA countries

Japanese approach towards PTAs

During almost the entire post-war (WWII) period Japanese foreign economic policy was based on multilateral principles formulated by the GATT/WTO and other international organizations such as the IMF and the OECD. Since 1955, when Japan became a GATT member, until the end of the 1990s it was a strong supporter of multilateral agreements (Chiavacci and Ziltener, 2008; Munakata, 2001). Participation in multilateral agreements brought to Japan a number of benefits, including easier access to member states' markets through increases in the competitiveness of industry and export expansion and independence from unilateral decisions made by its trading partners (e.g., the U.S.). By the end of the 20th century, in the opinion of Japanese decision makers, every form of economic agreement between member states other than multilateral was a clear violation of GATT/WTO principles (Chiavacci and Ziltener, 2008; Rodriguez, 2004). Non-multilateral agreements were viewed to be contributing to unjustified and undesirable discrimination between member states. At the same time, non-multilateral agreements were in conflict with the Japanese understanding of the objectives and principles set by the World Trade Organization itself.

The end of the last decade of the 20th century brought a fundamental change in the Japanese perception of PTAs resulting in a movement towards a multilayered trade policy (Sutton, 2005). Due to a number of factors, Japan started to consider such arrangements as initiatives complementary to the action of multilateral forums. First, Japan was observing integrational initiatives in Europe (the EU) and North America (NAFTA). As Japan was not involved in such initiatives before, it could not benefit from them. Second, the United States and the European Union were actively promoting open regionalism, and had concluded several bilateral agreements. These agreements guaranteed preferential market access for American and European companies, thus weakening the position of Japanese firms. A clear example of such a situation is the case of Mexico. Due to the lack of a free trade agreement between Japan and Mexico, Japanese companies had a far worse position in the market than the U.S. and the EU (both with PTAs in force).[ii] PTAs have the ability to provide expanded access to overseas markets for Japanese enterprises. Third, the difficulties with completing the negotiations under the WTO Doha Development Agenda[iii] has encouraged certain negotiating countries to be more open towards the idea of bilateral agreements. This is because such bilateral actions usually bring faster results (Yoshimatsu, 2006). In those circumstances, also Japan started thinking about expanding its exportation possibilities by creation PTAs with different partners. Fourth, PTAs could bring Japan a number of economic benefits. Beside export growth within the group (trade creation effect) and promotion of economic ties within East Asia, PTAs were to promote structural reforms that are crucial in helping the Japanese economy to recover from prolonged

stagnation (Rodriguez, 2004; Urata, 2009). Fifth, the tendency in Japan to conclude PTAs also results from the activity of its main competitors in East Asia, such as China, which has been negotiating large scale PTAs (Turinov, 2008). Both Japan and China have shown a desire to use PTAs with Asian countries to gain more influence in the region (Sutton, 2005).

All the motives mentioned above have caused a shift in Japanese policy towards PTAs. In October 2002, Japan released a policy statement *Japan's Free Trade Agreement Strategy* (Turinov, 2008) announcing its commitment to promoting and concluding economic agreements with the majority of the world's trading powers (Cheong, 2007). At the same time, Japan has undertaken internal reforms to improve its competitiveness and meet demands of the economic partnerships of this kind. A list of agreements that are already in force is presented in Table 1.

Table 1. List of Japanese PTAs in force (as of June 2016)

No.	PTA Name	Coverage	Type	Date of entry into force	End of implementation period
1	Japan – Singapore	Goods & Services	FTA & EIA	30 November 2002	2022
2	Japan – Mexico	Goods & Services	FTA & EIA	1 April 2005	2015
3	Japan – Malaysia	Goods & Services	FTA & EIA	13 July 2006	2021
4	Japan – Chile	Goods & Services	FTA & EIA	3 September 2007	2022
5	Japan – Thailand	Goods & Services	FTA & EIA	1 November 2007	2022
6	Japan – Indonesia	Goods & Services	FTA & EIA	1 July 2008	2023
7	Japan – Brunei Darussalam	Goods & Services	FTA & EIA	31 July 2008	2023
8	Japan – ASEAN	Goods	FTA	1 December 2008	2026
9	Japan – Philippines	Goods & Services	FTA & EIA	11 December 2008	2023
10	Japan – Switzerland	Goods & Services	FTA & EIA	1 September 2009	2024
11	Japan – Viet Nam	Goods & Services	FTA & EIA	1 October 2009	2026
12	Japan – India	Goods & Services	FTA & EIA	1 August 2011	2026
13	Japan – Peru	Goods & Services	FTA & EIA	1 March 2012	2026
14	Japan - Australia	Goods & Services	FTA & EIA	15 July 2015	2034
15	Japan - Mongolia	Goods & Services	FTA & EIA	7 June 2016	2037

Notes: FTA – Free Trade Agreement; EIA – Economic Integration Agreement

Source: Prepared by the author based on data from the WTO RTA Database (2016)

By July 2016, 15 agreements that Japan had negotiated entered into force, but the implementation of all commitments is spread over a period. Provisions of the agreement with Mexico were to be implemented the fastest (2015), but most agreements foresee full implementation in the third decade of the 21st century. A comprehensive assessment of the economic impact of these agreements on partners from both sides will be possible after full implementation.

The agreements presented in Table 1 relate only to those that are in force. There are also a number of agreements being negotiated. On 4 February 2016, the Trans-Pacific Partnership agreement was signed, and Japan is one of twelve signatories to this mega-FTA. Additionally, according to the Japanese Ministry of Foreign Affairs, Japan is currently engaged in a number of other PTA negotiations (Ministry of Foreign Affairs of Japan [MOFA], 2016a). Agreements under negotiation

include ASEAN (services and investment chapters), Colombia, Japan-China-ROK, the EU, Regional Comprehensive Economic Partnership and Turkey. Negotiations that have been either postponed or suspended for the moment include those with Canada, the Gulf Cooperation Council and South Korea (MOFA, 2016a).

Japan's increasing adoption of PTAs as of recent indicates that the country has changed its approach towards regional cooperation. The Japanese themselves admitted that the country "faces major changes that could be regarded as a 'watershed moment in history.' A structural transformation is taking place in the world economy in which Japan's status is gradually declining while the emerging economies are experiencing dramatic growth" (MOFA, 2016b). In pursuit of a strong and stable economy, the necessary action was to strengthen economic relations with Asian countries, emerging economies, western countries and countries rich in raw materials. MOFA argues that the Japanese government:

> "is absolutely resolved to 'open up the country' and 'pioneer a new future.' It will take major steps forward from its present posture to promote high-level, robust and long-term economic partnerships with major trading powers which can be successfully and positively measured in the competitive global marketplace. At the same time, it will first press ahead with fundamental domestic reforms in order to strengthen the competitiveness it will need for economic partnerships of this kind" (MOFA, 2016b).

Looking at the geographic spread of Japan's PTAs, it is clear that the country has the greatest interest in the East Asian region. This is natural because of the geographic and cultural proximity, especially given the significant economic growth recorded by these countries. Japan must actively look for markets for their production, especially in today's increasingly competitive international markets. PTAs can be treated as a key factor in achieving this goal. However, in its policy of promoting PTAs Japan is not limited to the countries of the region. It is now trying to establish relationships with partners outside East Asia. Agreements with Mexico, Switzerland, Peru and Australia, and negotiations with the European Union can serve as examples of such activity.

The real effects of PTAs on a country's foreign trade depend not only on the number of agreements negotiated but also on areas, they cover. Contemporary PTAs increasingly include liberalization of trade in services, foreign direct investments, as well as measures that facilitate trade and investment in addition to trade in goods. Many agreements cover such aspects of cooperation as the training of human resources and promoting economic activity among small and medium-sized enterprises. Consequently, the PTAs are becoming comprehensive agreements (so-called deep integration).[iv]

Japan has set itself the task of negotiating comprehensive free trade agreements of good quality (Turinov, 2008). This means opening up areas in the economy that had previously been considered as sensitive, such as agriculture. Although some products are excluded from liberalization[v], Japan is aware that it is increasingly difficult to negotiate PTAs that do not cover all areas of economic interests. This is reflected in the content of the concluded PTAs. Key areas of interest of selected PTAs are presented in Table 2.

Table 2. Main area covered by Japanese PTAs with selected partner countries

Goods and services	Brunei Darussalam	Chile	India	Indonesia	Malaysia	Mexico	Peru	Philippines	Singapore	Switzerland	Thailand	Viet Nam
Anti-dumping measures									G			
Balance-of-payments measures												G
Competition												G
Countervailing measures									G			
Customs-related procedures									G			G
Denial of benefits									S			G
Dispute settlement												G
Domestic regulation									S			G
Environment												
Exceptions, general or for security												G
Export restrictions									G			
Government procurement												G
Intellectual property rights												G
Investment												
Labour												G
Mutual recognition (services)												G
Rules of origin									G			G
Safeguard measures												G
Sanitary and phytosanitary measures												G
Subsidies												G
Tariff-rate quotas												G
Technical regulations, standards, technical barriers to trade									G			G

Note: G – goods only; S – services only.

Source: Prepared by the author based on the data from the WTO RTA Database (2016).

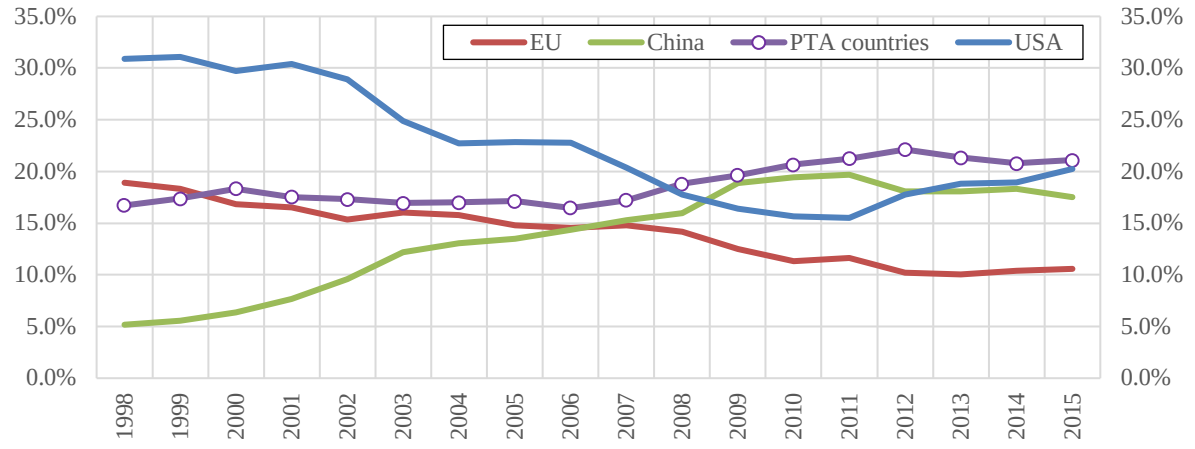
Trade of Japan with PTA countries

Figure 1 illustrates changes in trade significance of main trading partners for Japanese exports. According to Figure 1, since 1998, the importance of the United States and the European Union as exports markets has declined, and that of PTA countries and China has increased. In 1998, the share of exports to PTA countries[vi] stood at 16.7%. By 2015, it had increased to 21.1% becoming largest importer from Japan.

Figure 2 illustrates changes in trade significance of main trading partners for Japanese imports. In the case of Japanese imports, the share of imports from PTA countries is even greater than exports. In 1998, the PTA group's share in Japanese imports stood at 22.1% and in 2015, 25.2%. To a certain degree, this is because Australia, one of the most significant trade partners of Japan, entered into a PTA with Japan. It is also because the U.S. and the EU declined in importance, especially during the

global financial crisis of 2008-2009. Even the proportionate share of imports from China dropped during the global financial crisis. In 2015, the share of imports from the U.S. stood at 8.4%, the EU at 8.8% and China at 19.8%.

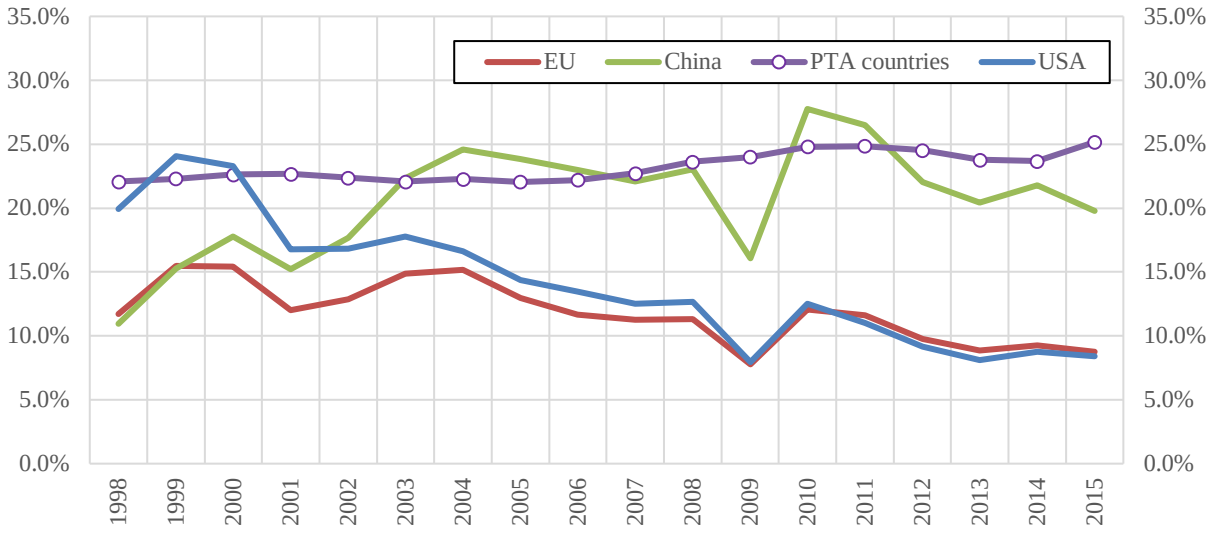
Figure 1. Significance of PTA countries in Japanese exports, 1998-2015, in %



Note: PTA countries consist of Australia, Chile, India, Mexico, Mongolia, Peru, Switzerland and ASEAN member states.

Source: Prepared by the author based on data published by UNCTAD (2016).

Figure 2. Significance of PTA countries in Japanese imports, 1998-2015, in %



Note: PTA countries consist of Australia, Chile, India, Mexico, Mongolia, Peru, Switzerland and ASEAN member states.

Source: Prepared by the author based on data published by UNCTAD (2016).

Detailed data showing the significance of PTA countries for Japanese foreign trade are provided in Table 3. It shows the shares of Japan's foreign trade with each PTA country separately. Table 3 highlights that the trade significance of some countries is quite marginal (e.g., Brunei Darussalam, Peru or Mongolia). The largest export markets for Japan are Thailand (increased from 2.4% in 1998 to 4.5% in 2015) and Singapore (decreased from 3.8% in 1998 to 3.2% in 2015). The most important

import markets for Japan in 2015 were Australia (5.6%), Malaysia (3.4%), Thailand (3.3%) and Indonesia (3.2%).

Table 3. Significance of partner countries in Japanese foreign trade, 1998-2015, in %

Specification		1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Australia	**Exp.**	2.1	2.0	1.8	1.9	2.0	2.1	2.1	2.1	1.9	2.0	2.2	2.1	2.1	2.2	2.3	2.4	2.1	2.1
	Imp.	4.6	4.1	3.9	4.1	4.2	3.9	4.3	4.8	4.8	5.0	6.2	6.3	6.5	6.6	6.4	6.1	5.9	5.6
Brunei Darussalam	**Exp.**	0.0	0.0	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
	Imp.	0.4	0.3	0.4	0.5	0.5	0.5	0.4	0.4	0.4	0.4	0.6	0.6	0.6	0.7	0.7	0.6	0.5	0.4
Chile	**Exp.**	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.2	0.2	0.4	0.2	0.4	0.3	0.2	0.2	0.2	0.3
	Imp.	0.9	0.8	0.7	0.7	0.6	0.7	0.9	1.0	1.3	1.3	1.0	1.0	1.1	1.1	1.1	1.0	1.0	1.0
India	**Exp.**	0.6	0.6	0.5	0.5	0.4	0.5	0.5	0.6	0.7	0.9	1.0	1.1	1.2	1.3	1.3	1.2	1.2	1.3
	Imp.	0.8	0.7	0.7	0.6	0.6	0.6	0.6	0.6	0.7	0.7	0.7	0.7	0.8	0.8	0.8	0.8	0.9	0.8
Indonesia	**Exp.**	1.1	1.2	1.6	1.6	1.5	1.5	1.6	1.5	1.1	1.3	1.6	1.6	2.1	2.2	2.5	2.4	2.1	1.8
	Imp.	3.9	4.1	4.3	4.3	4.2	4.3	4.1	4.0	4.2	4.3	4.3	4.0	4.1	4.0	3.6	3.5	3.2	3.2
Malaysia	**Exp.**	2.4	2.7	2.9	2.7	2.6	2.4	2.2	2.1	2.0	2.1	2.1	2.2	2.3	2.3	2.2	2.1	2.0	1.9
	Imp.	3.1	3.5	3.8	3.7	3.3	3.3	3.1	2.8	2.7	2.8	3.0	3.0	3.3	3.6	3.7	3.6	3.6	3.4
Mexico	**Exp.**	1.1	1.1	1.1	1.0	0.9	0.8	0.9	1.2	1.4	1.4	1.3	1.2	1.2	1.2	1.3	1.4	1.5	1.7
	Imp.	0.4	0.5	0.6	0.6	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.5	0.8
Mongolia	**Exp.**	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
	Imp.	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Peru	**Exp.**	0.1	0.1	0.1	0.1	0.1	0.0	0.0	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
	Imp.	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.2	0.4	0.3	0.3	0.3	0.3	0.3	0.3	0.2	0.2
Philippines	**Exp.**	1.9	2.1	2.1	2.0	2.0	1.9	1.7	1.5	1.4	1.3	1.3	1.4	1.4	1.4	1.5	1.4	1.4	1.5
	Imp.	1.6	1.7	1.9	1.8	1.9	1.8	1.8	1.5	1.4	1.4	1.1	1.2	1.1	1.0	1.1	1.1	1.3	1.4
Singapore	**Exp.**	3.8	3.9	4.3	3.6	3.4	3.1	3.2	3.1	3.0	3.1	3.4	3.6	3.3	3.3	2.9	2.9	3.0	3.2
	Imp.	1.7	1.8	1.7	1.5	1.5	1.4	1.4	1.3	1.3	1.1	1.0	1.1	1.2	1.0	1.0	0.9	1.0	1.3
Switzerland	**Exp.**	0.6	0.5	0.4	0.5	0.4	0.4	0.4	0.4	0.4	0.4	0.6	1.1	1.0	1.1	0.5	0.5	0.4	0.4
	Imp.	1.1	1.1	0.9	0.9	1.0	1.0	1.1	1.0	0.9	0.8	0.8	1.1	1.0	0.9	0.9	0.9	0.9	1.2
Thailand	**Exp.**	2.4	2.7	2.8	2.9	3.2	3.4	3.6	3.8	3.5	3.6	3.8	3.8	4.4	4.6	5.5	5.0	4.5	4.5
	Imp.	2.9	2.9	2.8	3.0	3.1	3.1	3.1	3.0	2.9	2.9	2.7	2.9	3.0	2.9	2.7	2.6	2.7	3.3
Viet Nam	**Exp.**	0.3	0.4	0.4	0.4	0.5	0.6	0.6	0.6	0.6	0.8	1.0	1.1	1.1	1.2	1.3	1.5	1.7	2.0
	Imp.	0.6	0.6	0.7	0.7	0.7	0.8	0.8	0.9	0.9	1.0	1.2	1.3	1.2	1.4	1.7	1.7	1.9	2.4

Source: Prepared by the author based on data published by UNCTAD (2016).

The impact of PTAs on Japanese merchandise trade

In an attempt to assess benefits of PTAs for an individual country we can use a number of more or less advanced measures. One such measure is a comparison of the exports and imports' growth rates corresponding to each PTA partner country during the time when the PTA was in force. If the growth rate of exports (imports) with a PTA partner country is higher than the growth rate of total Japanese exports (imports), then it can be argued that the respective PTA is fulfilling its role of stimulating Japanese trade, and is beneficial for Japan. This comparison is informed by Viner's trade creation effect.

Table 4 shows growth rates of Japanese total exports and imports as well as the difference between the export/import growth rates of Japanese trade with selected PTA countries and total Japanese exports/imports growth rates. The Table 4 highlights that after PTAs are entered into force, growth in exports to PTA countries are mostly positive, and growth in imports from PTA countries are mostly negative. Growth in exports was positive in 57 out of 101 country-years where a PTA was in force. In the import side, the number of improvements was only 43 and deteriorations 58. However, compared to the growth rate in total Japanese exports better growth rates (more positive or less negative) are recorded with individual PTA countries in an overwhelming majority of country-years. However, the opposite is true in relation to imports. Although this analysis provides mixed evidence on the benefits of PTAs for Japanese trade flows it is a positive indication that after agreements were entered into force growth rates in exports to PTA countries were more positive than the growth rates in imports from them.

Table 5 shows positive and negative changes in Japanese trade with PTAs countries at a more disaggregated level (by Standard International Trade Classification [SITC] product groups). The positive observations in each product group are the number of cases where the increase (decrease) in Japanese exports to PTA countries is higher (lower) than total Japanese exports or the decrease (increase) in Japanese imports from PTA countries are lower (higher) than the decrease (increase) in total Japanese imports. The negative observation should be interpreted in the opposite manner. In effect, if positive observations prevail over negative ones, we can conclude that PTAs are a factor leading to intensification of Japanese trade with partner countries. The analysis of the data from Table 5 confirms the previous observation that there are more favourable changes on the export side and less favourable changes on the import side.

Taking into account the export side, one notices that in each product group except SITC 4 the number of positive observations exceeds the number of negative ones. The most significant improvements due to PTAs are observed in manufactured goods (SITC 6), chemicals (SITC 5) and miscellaneous manufactured articles (SITC 8). Thus, PTAs have been beneficial for Japan in terms of exports in most product categories.

The analysis of the changes in imports from PTA countries compared to change in total Japanese imports leads to a different conclusion. In four product groups (SITC 2, 3, 4 and 7) the number of negative observations is higher than the number of positive observations (see Table 5) indicating that increments (decrements) in imports from PTA countries in these four product categories were lower (higher) than the increment (decrement) in imports from all countries. In the remaining product groups, not only the number of positive observations is higher than the negative ones but also the net positive effects are much larger compared to the ones with net negative effects.

Table 4. Growth in Japanese trade with PTA countries relative to total Japanese trade growth

Total trade (SITC 0-9)	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
	Exports																	
Japan (%)	-7.8%	7.6%	14.8%	-15.8%	3.3%	13.3%	19.9%	5.2%	8.7%	10.5%	9.4%	-25.7%	32.6%	6.9%	-3.0%	-10.5%	-3.5%	-9.4%
Australia	8.9	-2.5	-13.3	5.5	4.8	6.2	-0.8	-0.0	-8.1	3.3	12.4	-4.0	-1.9	5.1	6.4	2.6	-13.0	0.1
Brunei Darussalam	-50.8	-22.3	-7.7	14.8	468.4	-82.8	-8.5	-8.4	-11.8	11.0	37.5	15.7	-40.6	-11.2	34.0	-8.4	-26.4	22.1
Chile	-6.6	-47.4	5.3	-13.0	2.3	2.7	5.8	25.3	6.6	34.9	64.7	-25.6	69.9	-20.4	-12.1	-4.2	4.1	7.3
India	16.7	-7.1	-12.1	-6.7	-6.1	14.6	7.4	10.4	17.9	27.8	18.9	6.0	10.1	15.6	-1.4	-8.4	-1.9	9.2
Indonesia	-50.0	5.3	42.0	0.2	-5.9	1.9	6.5	-3.7	-28.7	12.4	29.4	-0.2	38.3	4.4	17.4	-5.6	-10.0	-12.2
Malaysia	-28.0	11.6	10.2	-4.9	-3.3	-11.0	-8.2	-5.5	-3.3	3.5	-0.1	3.9	4.6	-0.4	-2.8	-3.5	-3.8	-5.6
Mexico	16.6	-3.5	3.8	-5.6	-11.0	-16.9	22.7	28.3	25.2	0.1	-12.3	-5.7	7.7	-0.1	5.5	2.9	13.2	7.9
Mongolia	27.7	13.4	-64.7	47.3	-20.8	32.8	44.2	-6.0	35.9	34.7	39.8	-28.0	17.2	95.2	9.8	-2.4	12.2	-13.7
Peru	21.4	-26.5	-1.9	-5.7	-4.2	-27.9	-21.5	14.3	30.2	33.6	69.1	-15.8	41.5	-15.4	16.7	5.7	-20.9	15.2
Philippines	-8.6	12.9	2.4	-4.3	-0.1	-6.7	-13.4	-10.8	-9.3	-5.2	-4.2	8.1	2.0	-5.5	8.5	-7.9	5.5	5.5
Singapore	-19.1	2.5	13.1	-13.5	-6.8	-8.6	1.3	-2.7	-3.8	2.5	12.4	3.6	-10.8	1.1	-11.5	0.5	3.6	4.0
Switzerland	11.0	-9.2	-17.5	9.8	-21.7	8.9	-8.3	-6.7	3.5	14.5	34.3	70.5	-8.8	11.7	-49.6	-13.9	-5.1	-1.4
Thailand	-28.0	12.9	6.1	3.0	7.7	8.4	6.5	5.6	-6.7	1.4	5.5	1.1	21.5	2.8	19.5	-7.3	-9.3	-1.3
Viet Nam	11.9	14.5	6.7	6.1	16.2	10.0	1.3	7.8	6.5	26.5	28.5	9.1	-7.1	10.4	15.0	8.7	15.6	15.5
	Imports																	
Japan (%)	-17.2%	10.5%	22.5%	-8.0%	-3.3%	13.6%	18.7%	13.3%	12.3%	7.5%	22.5%	-27.6%	25.7%	23.2%	3.6%	-5.9%	0.1%	0.1%
Australia	6.4	-12.1	-6.9	5.7	0.3	-6.0	10.3	12.7	1.7	4.4	29.5	0.7	4.0	2.5	-4.1	-3.5	-5.8	-27.7
Brunei Darussalam	-9.5	-8.5	34.9	10.7	-7.1	6.8	-15.3	7.6	-10.1	-0.3	58.8	1.1	-2.5	15.6	0.8	-14.4	-15.5	-37.8
Chile	-2.5	-5.2	-9.8	-6.4	-8.3	8.8	40.3	9.2	29.4	5.0	-25.5	-5.4	20.3	3.6	-8.3	-8.3	1.4	-24.2
India	-1.0	-7.4	-5.2	-7.9	-2.2	-9.5	1.2	8.8	14.8	-4.5	3.4	-1.5	27.1	-3.5	-1.0	7.0	-1.3	-30.6
Indonesia	-8.7	5.6	7.7	-1.2	-1.3	2.5	-5.2	-2.0	3.7	2.4	0.5	-5.4	3.8	-2.6	-8.9	-4.6	-11.2	-22.9
Malaysia	-6.6	15.3	10.3	-3.3	-9.5	-1.1	-6.7	-9.4	-6.7	5.0	10.4	-0.3	10.2	11.0	4.2	-3.4	-2.0	-26.2
Mexico	-6.6	23.8	22.0	-7.9	-7.0	-14.6	3.1	3.4	-0.8	4.3	-1.8	1.0	-1.4	-8.9	7.1	2.0	1.0	11.2
Mongolia	-26.2	-89.9	-47.4	19.8	-27.9	-21.1	1.6	-34.1	16.3	85.4	101.0	-52.3	189.9	-46.4	42.6	-20.1	-10.5	217.6
Peru	-29.9	-9.6	-1.5	28.5	4.2	-12.6	39.0	-10.1	75.5	61.7	-28.0	6.2	5.5	-15.9	16.7	-0.2	-33.6	-26.9
Philippines	5.5	9.2	13.3	-2.9	5.3	-5.8	-1.6	-20.0	-8.9	2.2	-26.0	3.7	-2.0	-10.6	0.7	5.1	9.9	-12.6
Singapore	-2.5	4.7	-4.1	-8.3	-3.6	-5.1	-3.0	-6.9	-0.6	-13.1	-10.7	5.1	7.9	-17.0	-2.5	-9.0	5.6	0.2
Switzerland	4.9	1.1	-24.7	8.1	3.7	3.5	5.9	-8.5	-11.1	-5.2	0.5	25.3	-17.3	-7.9	1.1	-5.2	-1.2	2.4
Thailand	2.6	-2.1	-2.9	6.0	4.6	-0.4	-0.1	-3.0	-3.7	1.0	-9.1	4.7	5.4	-6.5	-7.3	-0.7	-1.5	-6.2
Viet Nam	-2.7	1.4	12.2	6.8	0.3	8.8	5.9	4.5	4.2	8.2	26.0	4.1	-8.2	18.1	27.0	0.3	8.2	-2.0

Note: The two rows entitled Japan shows the growth rate of Japanese total exports/imports in a given year as percentages. All other figures indicate percentage points. The figures represent the difference between the growth rate of Japanese exports/imports to a given PTA country and the growth rate of total Japanese exports/imports.
The grey fields indicate that the PTAs were in force.
Source: Prepared by the author based on data published by UNCTAD (2016).

Table 5. Comparison of trade changes by product category

Specification	Exports			Imports		
	Positive	Negative	Net	Positive	Negative	Net
0 – Food and live animals	**54**	47	**7**	54	42	**12**
1 – Beverages and tobacco	**48**	41	**7**	55	38	**17**
2 – Crude materials, inedible, except fuels	**55**	38	**17**	46	49	**-3**
3 – Mineral fuels, lubricants and related materials	**57**	44	**13**	43	45	**-2**
4 – Animal and vegetable oils, fats and waxes	**40**	43	**-3**	46	47	**-1**
5 – Chemicals and related products, n.e.s.	**63**	38	**25**	52	46	**6**
6 – Manufactured goods	**65**	36	**29**	49	47	**2**
7 – Machinery and transport equipment	**53**	48	**5**	49	52	**-3**
8 – Miscellaneous manufactured articles	**60**	41	**19**	69	29	**40**
9 – Commodities and transactions, n.e.s.	**52**	49	**3**	51	50	**1**
Total trade (SITC 0-9)	**57**	44	**13**	43	58	**-15**

Note: The grey fields show a higher number of positive effects over negative ones.

Source: Prepared by the author based on data published by UNCTAD (2016).

The observed trend in relation to both imports and exports with PTA countries indicates that PTAs have been favourable for Japanese trade. Nevertheless, the changes do not necessarily mean that final trade effect measured by trade balance is positive. The absolute value of trade flows should be examined to assess this. As a result, changes observed in the trade balance of a country before and after entering into force of a PTA can be treated as an indicator of the impact of that PTA.

For many years, Japan had been enjoying a trade surplus. However, the situation has been deteriorating in recent times. In 2011 Japan experienced a deficit of USD -32.2 billion, which later increased to USD -210.1 billion in 2015 (UNCTAD, 2016). Therefore, it can be concluded that the overall international competitiveness of Japanese trade has weakened and the weakening trend continues. This begs the question of whether the trade performance with Japan's PTA countries has also been deteriorating. The data presented in Table 6 provide some insights in this regard.

Table 6. Trade balance of Japan with PTAs countries, 1998-2015, in billions USD

Specification	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Japan	**107.5**	**107.6**	**99.6**	**54.1**	**79.1**	**88.5**	**110.5**	**79.1**	**67.7**	**92.1**	**18.9**	**28.7**	**75.7**	**-32.2**	**-87.3**	**-118.1**	**-143.9**	**-210.1**
Australia	-5.0	-4.4	-6.2	-6.8	-5.7	-5.2	-7.6	-12.1	-15.4	-17.0	-30.2	-22.6	-29.2	-38.9	-38.0	-34.1	-33.9	-22.0
Brunei Darussalam	-1.0	-1.0	-1.6	-1.6	-1.2	-1.7	-1.8	-2.2	-2.2	-2.4	-4.4	-3.2	-4.0	-5.6	-5.8	-4.6	-3.9	-2.4
Chile	-1.5	-2.0	-2.2	-2.0	-1.7	-2.1	-3.5	-4.2	-6.2	-6.6	-5.2	-4.0	-5.0	-7.5	-7.4	-6.3	-6.4	-4.5
India	0.2	0.2	-0.1	-0.3	-0.2	0.2	0.4	0.3	0.4	2.0	2.6	2.6	3.3	4.3	3.6	1.5	1.1	3.3
Indonesia	-6.6	-7.7	-8.8	-8.5	-7.9	-9.3	-9.6	-11.6	-16.8	-17.5	-20.1	-12.5	-12.4	-16.4	-12.0	-11.9	-10.9	-8.3
Malaysia	0.6	0.2	-0.6	-1.8	-0.2	-1.3	-1.5	-2.1	-2.3	-2.4	-6.7	-3.8	-5.1	-11.7	-15.1	-14.5	-15.0	-9.6
Mexico	3.0	2.7	2.8	2.1	2.0	1.9	3.0	4.4	6.5	7.1	6.1	4.0	6.1	6.2	6.1	5.5	6.4	5.7
Mongolia	-0.0	0.0	0.0	0.0	0.0	0.0	0.1	0.1	0.1	0.1	0.2	0.1	0.1	0.3	0.3	0.3	0.3	0.2
Peru	0.1	0.0	-0.0	-0.1	-0.2	-0.2	-0.5	-0.4	-0.9	-1.7	-1.1	-1.1	-1.2	-1.4	-1.8	-1.7	-1.0	-0.5
Philippines	2.8	3.5	3.1	1.8	1.9	2.0	1.3	1.4	1.0	0.7	1.6	1.8	3.1	2.3	2.5	0.4	-0.3	0.6
Singapore	10.1	10.9	14.4	9.3	9.2	9.4	11.7	11.7	11.9	14.8	18.7	14.6	17.1	18.6	14.5	13.5	13.1	11.9
Switzerland	-0.8	-1.2	-1.2	-1.3	-1.7	-1.9	-2.6	-2.9	-2.7	-2.2	-2.1	0.0	1.0	1.4	-3.8	-4.0	-4.2	-4.7
Thailand	1.2	2.4	3.0	1.5	2.7	4.1	6.2	6.9	6.0	7.3	8.6	6.2	13.2	13.0	20.1	13.9	9.6	7.6
Viet Nam	-0.4	-0.3	-0.7	-0.8	-0.4	-0.5	-0.7	-1.0	-1.2	-0.5	-1.3	-0.4	-0.0	-2.0	-4.3	-3.7	-3.6	-2.6

Note: The grey fields indicate that the PTAs were in force. Source: Prepared by the author based on data published by UNCTAD (2016).

Table 6 shows that in 2015, Japanese trade with PTA countries amounted to a net trade deficit, as the trade surpluses with some PTA countries (USD 29.3 billion) were less than the trade deficits with other PTA countries (USD 54.5 billion). The net trade deficit with PTA countries stood at USD 25.2 billion and represented a 12% share in the total Japanese trade deficit. Thus, on face value, it seems that the final effect of Japanese trade with PTA countries was a negative one. For a more accurate understanding, it is necessary to examine the Japanese trade balance with PTA countries solely within the active periods of those agreements. The data for this type of analysis is presented in Table 7.

Table 7. Japanese trade balance with PTA countries, in USD billion

Specification	Year before PTA entered into force	Most recent year of PTA functioning (2015)	Changes			Improvements		Deteriorations	
			Improvement	Deterioratrion	Neutral	Surplus increase	Deficit desrease	Surplus decrease	Deficit increase
	[USD billion]		[Units]			[USD bilion]			
Australia	-33.9	-22.0	X			-	12.0	-	-
Brunei Darussalam	-2.4	-2.4			X	-	-	-	-
Chile	-6.2	-4.5	X			-	1.7	-	-
India	3.3	3.3			X	-	-	-	-
Indonesia	-17.5	-8.3	X			-	9.2	-	-
Malaysia	-2.1	-9.6		X		-	-	-	-7.4
Mexico	3.0	5.7	X			2.7	-	-	-
Peru	-1.4	-0.5	X			-	0.9	-	-
Philippines	0.7	0.6		X		-	-	-0.2	-
Singapore	9.3	11.9	X			2.6	-	-	-
Switzerland	-2.1	-4.7		X		-	-	-	-2.6
Thailand	6.0	7.6	X			1.6	-	-	-
Viet Nam	-1.3	-2.6		X		-	-	-	-1.3
		Total	**7**	**4**	**2**	**6.9**	**23.7**	**-0.2**	**-11.3**

Source: Prepared by the author based on data published by UNCTAD (2016).

The Table 7 presents data on Japan's trade balances with the PTA countries in the year preceding the entry into force of the agreement and in the last available year of the PTAs' functioning, i.e., 2015. Japan's trade balance improved with seven out of thirteen countries analysed, deteriorated with four countries, and no changes were observed with two countries. Positive changes resulted from increases in existing surpluses and reductions in deficits with those trading partners. Similarly, the negative changes were the result of increases in the deficits or reductions in the surpluses. A comparison of the positive and negative changes highlight that the positive changes prevailed over the negative ones. The overall positive changes to the amount of USD 30.6 billion represents an increase in the surplus of USD 6.9 billion (with Mexico, Singapore, and Thailand), and a significant decrease in the deficit USD of 23.7 billion. These latter changes were connected to the Japanese trade with Australia, Indonesia, Chile, and Peru. On the other hand, the deterioration of Japanese

trade balance with the PTA countries to the amount of USD 11.5 billion was due to the reduction of the surplus or deepening of deficits with the respective PTA countries. While the surplus with a PTA country has decreased in only one case (USD 0.2 billion with the Philippines), the deficits grew larger (by USD 11.3 billion) with Malaysia, Switzerland, and Vietnam.

One could argue that a simple comparison of trade balances with PTA countries before and after PTAs were entered into force is inadequate as each PTA is different due to having its specific content and time periods of scheduled implementation. Therefore, it would be necessary to analyse each of those PTAs by considering their features to draw better conclusions. Nonetheless, the analyses presented above provide tentative evidence that PTAs have beneficial impacts on Japans' trade balance.

Conclusion

The foreign economic policies of many countries show a preference for PTAs. Although PTAs can disturb the multilateral trading system, they are created because negotiating partners see benefits in them. At first reluctant, from the beginning of 21st century, Japan has recognized the benefits stemming from PTAs. The country traditionally advocated a multilateral trading system, arguing that bilateral agreements are inconsistent with the principles of multilateral trade and thus would bring more harm than benefits for global trade. Japan's approach changed dramatically at the beginning of the 21st century when its first PTA entered into force with Singapore. Since then Japan has concluded fifteen agreements. Over the years, not only has the number of agreements increased but also their scope has expanded. Although a latecomer, Japan has developed an impressive network of trade agreements.

The analysis presented in this paper shows the influence of PTAs on Japanese trade. Japans' share of trade with PTA countries on both export and import sides is growing. This growth is most pronounced in relation to the trade with its East Asian partners. Also, the general trend in Japanese trade with PTA countries is positive. After agreements had been entered into force, positive changes prevailed on the export side while negative changes dominated the import side. The product breakdown analysis of exports and imports also supports this evidence. Despite the fact that Japan currently runs trade deficits with some of the PTA countries, improvements in the trading balances with the PTA countries since the PTAs were entered into force far outweighs the deteriorations in the trading balances with them. Noteworthy is the fact that the decrease in individual deficits with PTA countries amounted to USD 23.7 billion while individual increases in deficits amounted to USD 11.3 billion. If the current trend continues then, Japan will achieve a total surplus with PTA countries in the foreseeable future.

The findings of this study have implications for Japanese policy. First, given the evidence that Japan is benefiting from PTAs Japan should sustain its strategy of developing PTA arrangements. Second, as Japanese PTAs have achieved positive results particularly on the export side, Japan should focus on further developing of exportation possibilities of those goods having the highest significance in Japanese foreign trade. This is particularly important for groups of manufactured products that

dominate Japanese exports. Third, Japanese PTA negotiators should promote the export of products in which Japan has a comparative advantage. Fourth, Japan should also consider liberalization of trade in sensitive product categories such as agriculture) as Japan imports more agriculture goods than it exports.

The analysis presented in this paper does not provide conclusive evidence that involvement in PTAs is unconditionally beneficial for Japanese trade. This is because there are many factors influencing trade flows other than PTAs. Moreover, as some of the agreements have been in effect for only a relatively short duration of time with many still in the initial stage of implementation, it is difficult to attribute any changes observed in trade balances solely to the PTAs. Also, each of Japan's PTAs has its idiosyncrasies (e.g., subject covered), and the economic importance of each PTA partner for Japan varies. The analysis of the economic effects of PTAs will be more robust when the PTAs have been in effect for several years, and close attention is paid to the structure of the agreements. These are considerations for future research on this topic.

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Endnotes

[i] A relatively deep literature review of PTAs determinants can be found in WTO (2011).

[ii] Japanese companies exporting to the Mexican market face tariffs at an average of 16.1%. At the same time, companies from the U.S. and the EU have not been facing such elevated tariffs. In addition, Japanese companies did not have access to public procurement in Mexico, which attracted companies from the USA and the EU. (see, Urata, 2009).

[iii] This is a result of much larger number of countries participating in the negotiations, which represent many different interests and at the same time more difficult to reconcile.

[iv] In WTO nomenclature, 'deep' integration means arrangements that go beyond extending preferential tariff concessions and include areas such as investment and competition issues. 'Deep' integration differs from a 'shallow' one which can be exemplified by simple free trade agreements.

[v] For example, in the recently concluded agreement with Australia such a sensitive commodity is rice. On the other hand, Japan strongly decreased barriers for such commodity groups as wool, cotton, lamb and beer exported from Australia to Japan (news.com.au, 2014).

[vi] This includes the ten ASEAN member states plus Australia, Chile, India, Mexico, Mongolia, Peru, Switzerland.