

## **PART I. Overview**

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### **Global Trend Towards Regional Trade Agreements (RTA)**

8. In recent years, the proliferation of Regional Trade Agreements (RTAs) has become a global trend. The fact that 130 RTAs, out of the 255 RTAs notified to the GATT and the World Trade Organization (WTO) to date,<sup>3</sup> have been concluded after the launch of the WTO in 1995 bears witness to this rapidly growing trend of regionalism. Existing RTAs, notably the North American Free Trade Agreement (NAFTA) and the European Union (EU), are further accelerating their course of regional expansion and integration. There is mounting widespread recognition that RTAs are in effect a constructive and reliable vehicle for facilitating liberalization of trade and investment.

9. A variety of reasons can be attributed to the rapid growth of regionalism. Most notably, major trading nations in the global economy, including the US and the EU, are proactively pursuing RTAs as an effective means of attaining trade liberalization. The successful integration of the NAFTA and the EU substantiated the great benefits that RTAs generate. In addition, countries that have not concluded RTAs are gradually encountering economic isolation and consequently increased opportunity costs, and are now endeavoring to pursue RTAs.

#### **RTAs in Asia**

10. In comparison to other regions such as Europe and the Americas, it is true that Asia manifested nominal interest in regional economic integration until the recent past. However, in the aftermath of the Asian financial crisis in 1997, North East Asian countries became aware of the need for closer regional economic cooperation. Observing the great economic benefits that a FTA may bring forth, countries in Asia, notably Japan and Korea, are pursuing FTAs in earnest.

11. As an illustration, Japan set up a working group to pursue a Comprehensive Economic Partnership (CEP) with ASEAN. A Framework Agreement on ASEAN-China Comprehensive Economic Cooperation came into

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<sup>3</sup> WTO, October 2002, Annual Report of CRTAs, WT/REG/11

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effect in July 2003. The US announced its Enterprise for ASEAN Initiative in 2002 and established Trade and Investment Framework Agreements with some ASEAN countries. India is pursuing enhancement of economic partnership with ASEAN countries. Singapore is actively pursuing FTAs with other countries and has already concluded FTAs with New Zealand, Japan, Australia, EFTA, and the US. At the ASEAN+3 Summit in November 2002, the leaders welcomed the report recommending the establishment of an East Asia Free Trade Area (EAFTA). And, ASEAN Free Trade Area (AFTA) has been virtually realized in January 2003.

### **FTA Policies of Japan and Korea**

12. Japan and Korea are two of the greatest beneficiaries of the liberalized global trade regime. The roots of their fundamental trade policies are therefore embedded in supporting a strong multilateral trading system represented by the WTO. Both countries' committed participation in the Uruguay Round (UR) negotiations and the current Doha Development Agenda (DDA) negotiations of the WTO can be understood in this context.

13. Recent endeavors to pursue FTAs on the part of Japan and Korea do not imply a shift of the focus of their foreign economic policies. In effect, their exploration of FTAs is not intended to undermine their long-standing policy of supporting the multilateral trading system. Rather, Japan and Korea are resolutely committed to continuous trade and investment liberalization, and are open to any means promoting freer trade and creating more open, transparent economies. In sum, as major global trading nations, both countries attach great importance to the complementary nature of FTAs in promoting global trade liberalization and the multilateral trading system as a whole.

14. It is true that Japan and Korea were not forerunners in the global trend of FTAs. But, by regarding FTAs as an important vehicle in carrying out their respective trade policies, Japan and Korea are now expending great efforts to conclude FTAs.

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15. In the case of Korea, in October 2002 Korea concluded its first FTA with Chile, the first trans-Pacific FTA ever. Korea has completed Joint Study with Singapore to examine the feasibility of a potential bilateral FTA. Korea is also currently pursuing FTA discussions with ASEAN and Mexico. Furthermore, Korea is exploring the feasibility of concluding a trilateral FTA among Japan, Korea, China and as well as on the EAFTA.

16. In the case of Japan, Japan signed its first FTA with Singapore in January 2002. Japan is now under FTA negotiations with Mexico, and working towards strengthening its economic partnership including a possible FTA with ASEAN countries under the Japan-ASEAN Comprehensive Economic Partnership Initiative. Under this initiative, both the regional and the bilateral approach are being sought simultaneously. Efforts for the bilateral approach are now being conducted with Thailand, the Philippines, Malaysia and Indonesia.

### **Bilateral Economic Relationship between Japan and Korea**

17. As neighboring countries, Japan and Korea are two influential economies in Asia and beyond. Aside from sharing similar heritage and cultural values, partly on account of the geographical proximity, the economies of the two countries have much in common.

18. More specifically, the two countries recorded astounding economic development by having pursued open trade policy and are now members of the Organization for Economic Cooperation and Development (OECD). Both countries adhere to the universal values of democracy and market economy principles. The two countries are also active members in the multilateral fora, such as the WTO and the United Nations (UN). In this context, Japan and Korea are pondering upon the benefits of reinforcing cooperation in the region to pave the way for an East Asia era in the 21st century.

19. Since the normalization of diplomatic relations in 1965, Japan and Korea have become mutually important economic partners. Japan is currently the second largest trading partner for Korea, while Korea is the third largest partner for Japan. Japan is also the second largest source of foreign direct investment

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for Korea, which is anticipated to increase even further since the Japan-Korea Bilateral Investment Treaty (JKBIT) came into effect early this year.

20. Bilateral trade between Japan and Korea has steadily increased over the years and reached its peak in the year 2000 by registering 52.3 billion US dollars. It is noteworthy that Korea has been recording a constant trade deficit with Japan of approximately 10 billion US dollars on an annual basis since 1994. The majority of the deficit can be attributed to imports of machinery, materials and parts from Japan.

<Table 1> Bilateral Trade between Japan and Korea

### Japan's Trade with Korea

(unit: US \$ hundred million<sup>4</sup>)

	1997	1998	1999	2000	2001	2002
<b>Exports</b>	261.9	152.5	227.9	308.2	254.0	284.4
<b>Imports</b>	146.4	120.0	159.5	205.4	172.7	154.2
<b>Balance</b>	115.5	32.5	68.4	102.8	81.3	130.2
<b>Total</b>	408.3	272.5	387.4	513.5	426.6	438.6

Source: Ministry of Finance, Japan

### Korea's Trade with Japan

(unit: US\$ hundred million)

	1997	1998	1999	2000	2001	2002
<b>Exports</b>	147.7	122.4	158.6	204.7	165.1	151.4
<b>Imports</b>	279.1	168.4	241.4	318.3	266.3	298.6
<b>Balance</b>	-131.4	-46	-82.8	-113.6	-101.2	-147.2
<b>Total</b>	426.8	290.8	400	523	431.4	450

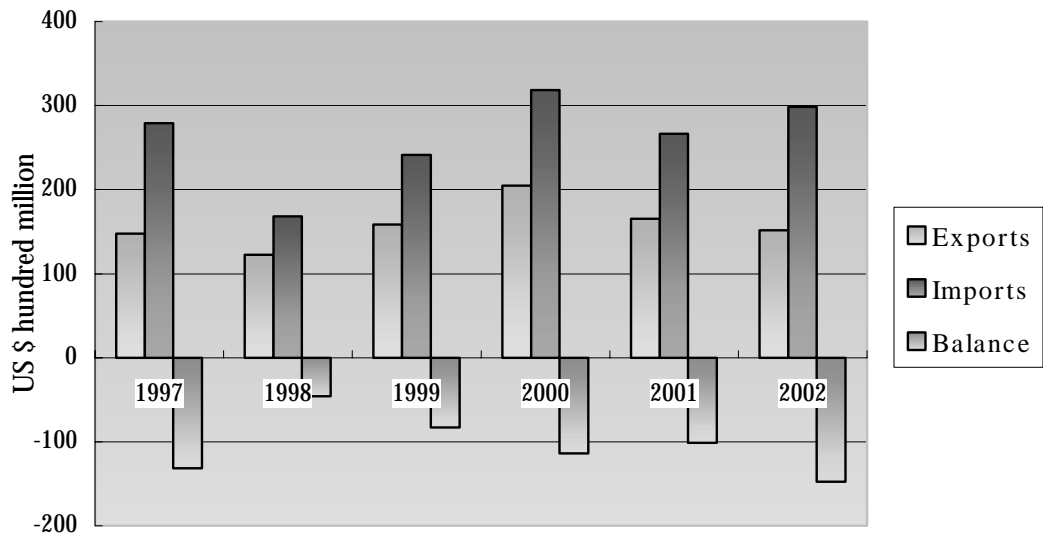
Source: Korea Customs Service

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<sup>4</sup> These figures are converted according to annual weighted average exchange rate provided by Article 4-7 of Customs Tariff Law.

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21. In the year 2002, Korea's principal exports to Japan consisted of semiconductors, textile products, oil products, computers and plastic products. Japan's main exports to Korea were semiconductors, hot-rolled steel, automotive parts, plastic products, and chemical products.

22. A breakdown of the bilateral investment demonstrates that Japan's investment in Korea sharply increased from 1999 to 2000 and peaked in 2000 by reaching 2.5 billion US dollars. In 2001, due to the economic downturn in both countries, Japan's investment declined by 68.5 percent to 770 million US dollars. Japan's investment in Korea sharply rebounded in 2002 by 81.8 percent. Japan's total investment to Korea since 1962 amounts to 13.1 billion US dollars and accounts for 1.5 percent of its total foreign direct investment, and 15 percent of the total foreign direct investment in Korea, following the US whose investment accounts for 31 percent. Japanese companies in Korea are mostly engaged in business in areas such as electronics and electric appliances, chemicals, and services.

23. The level of Korean investment in Japan, on the other hand, is relatively low. Statistics show that Korean investment in Japan stood at an average of 83 million US dollars per annum from 1995 to 2002. Korea's total investment to Japan amounts to 913 million US dollars, which accounts for 1.5 percent of its

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total foreign direct investment and 0.3 percent of total foreign direct investment in Japan.

<Table 2> Bilateral Investment between Japan and Korea

(unit: US\$ hundred million)

	1995	1996	1997	1998	1999	2000	2001	2002
<b>Japan's Investment in Korea</b>	4.2	2.6	2.7	5	17.5	24.5	7.7	14
<b>Number of Cases</b>	169	154	134	330	392	615	591	474
<b>Korea's Investment in Japan</b>	1.05	0.57	1.01	0.24	0.98	1.19	0.87	0.74
<b>Number of Cases</b>	30	25	25	20	37	135	117	82

Source: Korea EXIM Bank

(unit: hundred million yen)

	1996	1997	1998	1999	2000	2001	2002
<b>Japan's Investment in Korea</b>	438	208	558	418	1166	793	543
<b>Korea's Investment in Japan</b>	60	97	27	54	52	46	79

Source: Ministry of Finance, Japan

24. Both countries have been conducting across-the-board cooperation in a wide range of areas. Business people created an assortment of channels to search for new arenas of cooperation. For instance, Nippon Keidanren and the Federation of Korean Industries, the two major economic institutions in Japan and Korea, held 19 meetings to date, while the Japan-Korea Business Conference, composed of prominent business people from both sides, held its 35<sup>th</sup> meeting in Daegu in April 2003. Business sectors of both countries have pursued technology cooperation in parts and materials, joint development of products and cooperation in the third country market.

25. The governments of both countries have also conducted technical cooperation to promote industrial cooperation among small and medium-sized companies in the two countries. Industrial Technology Cooperation Foundation was instituted in each country to this end. Cooperation between local governments is also on the rise. The Japan (Kyushu)-Korea Economic Cooperation Conference was set up in 1993 to strengthen economic cooperation between Korea's local governments and the Kyushu province of Japan.

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26. However, it is noteworthy that there is still much room for further cooperation between Japan and Korea that would benefit both countries.