East Asia in 2013

A region in transition
# East Asia in 2013:
## A Region in Transition

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Foreword

White Rose East Asia Centre

The White Rose East Asia Centre (WREAC) is an international Centre of Excellence on China and Japan established by the Universities of Leeds and Sheffield under the umbrella of the White Rose University Consortium.¹ The National Institute of Chinese Studies (based at Leeds) and the National Institute of Japanese Studies (based at Sheffield) together constitute the Centre. It was funded from 2007-12 by the Higher Education Funding Council (HEFCE), the Economic and Social Research Council (ESRC) and the Arts and Humanities Research Council (AHRC) and is funded from 2013-16 by the AHRC and the British Academy. It undertakes world-class research and provides advanced research training in Chinese and Japanese Studies as part of a government drive to strengthen the United Kingdom’s specialised research capacity in the area.

Covering the arts and humanities as well as the social sciences and business studies, WREAC is equipped to pool the expertise on East Asia in the two universities in order to produce research on a wide range of topics, many of which are important outside of the university environment. The International Advisory Board (IAB) supports WREAC in expanding the range, reach and significance of the research produced in order to generate impact by contributing to debates in the wider community.

These briefing papers are targeted at the policymaking debate. Their production is based on seminars presented by WREAC staff in May and June 2013 at the Foreign and Commonwealth Office (FCO) for participants from across Whitehall. Their aim is to contribute to the enlargement of knowledge and understanding of key issues in East Asia for the policymaking community.

As Executive Director of WREAC, I would like to thank the FCO for the support offered and express my hope that the briefing papers contribute to the policymaking debate on these important topics.

Professor Caroline Rose
Executive Director of WREAC

¹The Universities of Leeds, Sheffield and York constitute the White Rose University Consortium. The white rose is the symbol of Yorkshire, where the three universities are located.
Foreword
Foreign and Commonwealth Office, Research Analysts

The Foreign and Commonwealth Office’s Research Analysts have close working relationships with academics and other non-government experts. We value their original research, rigour and the unique perspectives which can come from long term, on-the-ground engagement with overseas societies and institutions. Including such perspectives in the policymaking arena means we have a stronger and more informed debate and, we hope, better policy and better implementation as a result.

The papers here demonstrate the breadth of UK-based expertise on East Asia as well as the diverse range of regional policy issues which underlie continued prosperity and security. They do not represent British government stances and are very much the independent views of UK-based scholars. But their existence is the fruit of cooperation between Research Analysts and scholars in the White Rose East Asia Centre who, in the summer of 2013, got together to run a seminar series giving Whitehall officials the chance to discuss policy with leading academics, on topics as diverse as trade, climate change, corporate management and welfare.

My thanks go the Centre for stimulating and informing those talks.

Dr Cornelia Sorabji CBE
Head of Research Analysts, Foreign and Commonwealth Office
Overview

In recent years, East Asia and the Asia-Pacific has been the most dynamic zone of Free Trade Agreement (FTA) activity in the world. Figures 1 and 2 show the development of FTA projects through their progressive stages – proposed, studied, negotiated and concluded/signed. In 1998, the Asia-Pacific was largely devoid of such agreements compared to other regions but by the early 2000s an increasing number of Asia-Pacific countries had active FTA policies. By mid-2013, the Asia-Pacific was host to 107 free trade agreement projects, seventy-five having reached the signed or in force stage.

Of these, only four were strictly regional FTAs (ASEAN Free Trade Area (AFTA), North America Free Trade Agreement (NAFTA), Central America Common Market (CACM) and Pacific Island Countries Trade Agreement (PICTA)), and a small number of others being ‘quasi-regional’ arrangements where a regional group has an agreement with a third party country, mostly ASEAN’s separate pacts with Japan, China, South Korea, Australia and New Zealand. Thus, FTA activity in the Asia-Pacific has been predominately bilateral, accounting for over 90 per cent of all agreements concluded to date.
The proliferation of FTAs has become a key defining feature of the regional political economies of East Asia and the Asia-Pacific for the following reasons. First, these agreements have recast the macro-structure of the regions' international economic relations, as well as the trade policies of all major countries towards a specific preferential approach and away from multilateralism. A growing preoccupation with FTAs has, for example, inevitably meant that less trade diplomatic time and resources have been spent on WTO negotiations at a time when the future of the global multilateral trade system is in the balance.

Second, FTAs have the potential to significantly affect regional trade and investment flows through the reduction of conventional barriers (e.g. import tariffs and quotas) and changes to commercial regulatory environments, such as rules on intellectual property rights (IPR), investment and government procurement. Third, after the hitherto dense pattern of bilateral FTAs, many countries in East Asia and the Asia-Pacific have most recently advocated harmonising or merging these agreements into consolidated regional FTAs. As we later discuss, there are currently two major ‘grand regional’ FTAs in negotiation – the Trans-Pacific Partnership and the Regional Comprehensive Economic Partnership – which have become the main focal points for regional economic relations in East Asia and the Asia-Pacific. The future implementation of any such pact could have significant implications for regional integration and regional community-building, as well as Europe’s relationship with this strategically important part of the world.

*Figure 2* Asia-Pacific FTA Projects (by end of mid-2013)
Understanding FTAs

Free trade agreements are notably heterogeneous: it very much depends on what kind of agreement is signed. The preferred FTA model adopted by developed market-liberal countries like the US, Canada and Australia include complex and lengthy provisions on commercial regulatory areas such as IPR, the individual chapters on which can be longer than the entire text of simpler FTAs preferred by China and all ASEAN countries with the exception of Singapore. The underlying philosophies of FTAs can also be very different. For countries like the US they are perceived essentially as behind-the-border market access deals and politically marketed as ‘platinum standard’ or ‘high quality’ agreements that extend beyond current WTO accords on international trade and investment regulation. By contrast, East Asian countries generally – including Japan – conceive FTAs as not simply about market access but more broadly about fostering closer international ‘economic partnerships’, where provisions on economic co-operation and development capacity-building are incorporated into the agreement text. Generally speaking, East Asian centred FTAs tend to emphasise regulatory co-operation compared to the Anglo-Pacific preference for regulatory rights. Thus, for most East Asian states, ‘free trade’ is embedded in a broader international economic pact or bargain, and to some extent may be explained by East Asia’s developmentalist political economic tradition although the actual substance behind co-operation provisions the region’s economic partnership agreements (EPAs) can be lacking.

More technically, FTAs can vary enormously at the article-level, this relating to the specific measures, provisions and rules covering the 10,000 plus harmonised tariff schedule (HTS) product lines concerning phase-in liberalisation periods, exemptions, rules of origin percentage thresholds and formulae, modes of liberalisation, adherence to certain technical standards, and so on. The article-level structure and content of FTAs is largely determined by what is politico-economically feasible or aspired to in the negotiations process, and that take into account lobbied interests. All governments face a particular set of constraints when dealing with their respective domestic constituency groups (e.g. business, farmers, labour, and various civil society organisations) and domestic legislatures. Lower income countries in East Asia and the Asia-Pacific also face certain development capacity constraints arising in technocratic, institutional, regulatory and industrial contexts. For example, most ASEAN countries would find it extremely difficult if not impossible to implement the legislative commitments encoded within the standard IPR chapter found in a United States FTA. With these points is mind, FTAs are essentially the bespoke outcomes of politico-economic interactions between negotiating parties, and the diverse nature of the East Asia and Asia-Pacific regions fundamentally explains their high level of FTA heterogeneity compared to most other regions.

In sum, what has thus far developed in East Asia and the Asia-Pacific is a dense region-wide pattern of heterogeneous bilateral FTAs. Many observers make the mistake of equating this trend with regionalism per se. One may make the case that FTA bilateralism has fractured trade relations in both regions into a complex array of preferential trade relationships that actually work against the development of regionalism and regional community-building. Compliance to various trade and investment rules embodied in these bilateral agreements also poses the so called spaghetti or noodle bowl problematic for firms. Business has long complained about the issue and governments from the region have tried to address it through proposed regional FTAs that aim to harmonise sets of bilateral deals into unified singular agreements.

Early Quests for Regional FTAs

The idea of establishing a regional FTA in East Asia and the Asia-Pacific is not new. Japan’s early initiatives on Pacific community-building in the 1960s included a proposal to create a Pacific Free Trade Area (PAFTA) although this never progressed. The aforementioned establishment of AFTA, NAFTA, CACM and PICTA were to follow in the 1990s, yet these were either on a small sub-regional scale or involved just a small number of nations. Proposals for grander-scale regional FTAs arose on the crest of the new bilateral FTA wave.
The East Asia Free Trade Area (EAFTA) project was ASEAN Plus Three membership (ASEAN plus China, Japan and South Korea) based and principally advocated by China, whereas the Comprehensive Economic Partnership of East Asia (CEPEA) was championed by Japan and comprising the original membership of the East Asia Summit group, i.e. APT plus India, Australia and New Zealand. Meanwhile, an APEC membership based Free Trade Area of the Asia-Pacific (FTAAP) project was initially suggested by the APEC Business Advisory Council group in 2004, later championed by the United States from 2006 onwards under the Bush Administration.

United States led diplomatic efforts on pushing the FTAAP proposal failed owing to resistance from many East Asia states who were more interested in the EAFTA and CEPEA proposals, and who were at the time wary of entering into negotiations on a regional FTA that would be primarily driven and shaped by the US commercial regulatory interests. Washington's aborted bilateral FTA projects with three Southeast Asian nations around this time (Malaysia, Philippines and Thailand) due to irreconcilable differences over certain areas of commercial regulation was instructive to other East Asian states on the challenges of negotiating with the US. To date, the only Asian nations with which Washington has successfully brokered free trade agreements have been the advanced economies of Singapore and South Korea. It is also worth noting that the US’s parallel proposal on creating a Free Trade Area of the Americas (FTAA) with Latin American countries had similarly faltered because of frictions arising between the US and Brazil, with each championing their own preferred FTA model.

**The Trans-Pacific Partnership (TPP) Project**

With FTAAP proposal floundering, the Bush administration took a different tack and in 2007 announced the US would be joining the expanded negotiations of the Trans-Pacific Strategic Economic Partnership Agreement (TPSEPA), a unique quadrilateral FTA signed by Singapore, New Zealand, Chile and Brunei that had been in force since 2006. Being omitted from the initial agreement, negotiations on financial services and investment commenced in March 2008, with the US joining as a fifth negotiating party on these sectors. The arrangement was then recast in November 2008 to negotiations on a Trans-Pacific Partnership (TPP) agreement that in addition to the original Pacific-4 nations and the US also included Australia, Peru and Vietnam. Malaysia joined the TPP talks in October 2010, then Canada and Mexico in October 2012, making eleven participating countries in total by the time. Successive Japanese governments had long dithered about whether or not to join the TPP but in March 2013 Tokyo announced its intention to finally join the negotiations, bringing the number of TPP parties to 12. South Korea has too been asked to join TPP talks but has thus far declined the offer mainly due to concerns over the potential adverse effects of a US-led regional trade pact on China.

Whereas the TPP had progressed to full negotiations by 2010, both the EAFTA and CEPEA proposals were stuck at the feasibility study stage. However, TPP negotiations have been long, difficult and complex. The 19th round of talks was held in August 2013. Indications from TPP talks date suggest that the most likely outcome of any concluded deal will be a matrix of new separate bilateral deals packaged within a very generic TPP agreement comprising some common non-legally binding provisions (e.g. a review process), basic principles of trade policy adherence and statements of future intent to build a truly harmonised agreement in years to come. If this transpires then what value-added benefits will a final negotiated Trans-Pacific Partnership actually bring in addition to the 38 existing bilateral FTA links (out of a possible 66) already in place? The remaining 28 bilateral links do include some important trade partnerships (e.g. US–Vietnam, US–Malaysia) but it all depends on the substance of the deal(s) brokered, and how coherent the package of bilateral deals are if the ultimate goal is to forge a completely harmonised and converged regional FTA.

For those countries that already have a strong majority of agreement links with fellow TPP members in operation (e.g. Chile 100 per cent, Singapore 82 per cent), their motive for engagement lies in upgrading existing bilaterals and any generic TPP ‘package’
arrangement successively negotiated. There is also the question of how these two sets of agreement – the bilateral and the generic regional – will work alongside each other, if indeed there is any significant overlap in terms of provisions, rules and standards of compliance.

If any TPP deal is eventually achieved then what kind of ‘regional’ agreement will it create? Figure 3 shows that the pattern of TPP membership involves a geographically dispersed network of countries across East Asia, Oceania and Pacific America rather than a contiguous regional community. From an Asia-Pacific perspective, it would constitute a firmer foundation on which a Pacific economic community could further build, and possibly be the initial first stage for realising the APEC-based FTAAP some years in the future. However, that would mean the Asia-Pacific’s second largest economy, China, acceding to a free trade agreement largely shaped by US politico-economic interests. Given current realities, such an outcome is unforeseeable. Furthermore, APEC’s fourth (Russia), seventh (South Korea), eighth (Indonesia), ninth (Taiwan) and tenth (Thailand) largest economies are not TPP parties, which along with China means that six of the top ten Asia-Pacific’s economies would be left outside any final agreement as things presently stand. South Korea, Taiwan and also Japan would find it difficult to sign any future TPP deal that required them to open up their agricultural sectors in any significant way. Russia, Indonesia and Thailand would be averse to signing up to any rigorous commercial regulatory commitments on areas such as IPR, should the US manage to succeed in substantially incorporating these into any final agreement.

Figure 3 Regional FTA Projects in East Asia and the Asia-Pacific
The Regional Comprehensive Economic Partnership (RCEP) project

Attention on future regional FTAs has most recently swung back to an East Asia-centred arrangement. Japan’s CEPEA proposal was rebranded in late 2012 as the Regional Comprehensive Economic Partnership (RCEP), comprising the original 16-nation East Asia Summit membership with the first round of talks held in May 2013. The ASEAN group is the hub of this newest regional project and based on its separate existing radial FTA links with China, Japan, South Korea, Australia, New Zealand and India. These are relatively simple, conventional free trade agreements that by and large reflect developing country level interests. While this tighter regional grouping of countries with a much stronger set of lowest common denominator interests and politico-economic backgrounds have arguably much better chance of realising a final agreement than the TPP’s disparate membership, similar problems are likely to be encountered in forthcoming negotiations. The main problem lies with forging a deal between the ‘plus 6’ countries outside the ASEAN collective. Notwithstanding parallel efforts to negotiate a Northeast Asia trilateral FTA, the first round taking place in March 2013, Japan and South Korea’s bilateral FTA talks have been stalled since 2005, regular high-level diplomatic spats between China and Japan make it difficult to foresee the two nations ever signing a common free trade agreement, and separate bilateral talks between South Korea and China – in their fifth round by April 2013 – have made slow progress, hindering by differences of stance over agriculture and labour-intensive manufacturing sectors.

Australia’s bilateral talks each of the Northeast Asian three (NEA-3) countries have meanwhile experienced similar challenges. Although by 2013 it was close to signing a deal with Japan, negotiations with China were running into difficulties by mid 2013 over unresolved issues on agriculture, investment and other areas of commercial regulation. Consequently, Canberra had to scale back its ambitions for signing a ‘comprehensive’ market access deal with Beijing. The Australian government’s talks with South Korea had too hit a wall over negotiations on liberalising politically sensitive farm products such as beef around the same time. New Zealand signed a relatively basic bilateral FTA with China in 2008 but a similar long-standing project with South Korea has long floundered, and a deal with Japan has been informally discussed but never officially proposed. India meanwhile has managed to sign ASEAN-level FTAs with ASEAN itself, South Korea and Japan, and is negotiating with Australia and New Zealand but not with China.

Difficulties in bilateral FTA negotiations amongst the ‘plus 6’ RCEP countries will inevitably reappear at regional-level talks if the same problematic sectors are on the agenda. Realistically speaking, any final RCEP deal would have to substantially exclude agriculture and include only rudimentary coverage on commercial regulation. This would be especially hard for Australia and New Zealand to sell to its domestic constituencies but politically feasible. Such an arrangement would be unacceptable to US Congress and American lobby interests by comparison. At the same time, if an RCEP agreement is signed it will most likely incorporate a range of measures on enhancing economic co-operation and a broader economic partnership, this being consistent with the generic East Asia FTA model. It remains to be seen whether provisions on such areas, if included, will lead to substantive regional-level co-operation and integration yet this could be a vitally important contribution that the RCEP could make to East Asia-centred regional community building.

However, the future prospects of the RCEP ultimately depend on the maintenance of good diplomatic relations amongst its negotiating parties. In recent years, these relations have been notably tested by various bilateral counter-sovereignty disputes over certain territorial zones in East Asia. Many of these concern China’s claims in the South China Sea and East China Sea. For example, in April 2012 there was a naval standoff between the Philippines and China over the Scarborough Shoal. China and Vietnam became embroiled in a similar dispute in the Paracel Islands in March 2013, while China and Japan have also recently come to loggerheads over the Senkaku/Diaoyu Islands further north. Japan has also been involved in disputes with South Korea and Russia over sovereignty of Dokdo/
Takeshima and the Southern Kuriles/Northern Territories. Meanwhile, Malaysia has objected to the Philippines’ reactivation of its historic sovereignty claim over Sabah on the island of Borneo. Interestingly, these spats compelled the Philippines, Vietnam, Japan and South Korea to all reaffirm the importance of their security ties with the United States that seemed to consequently bring some justification to the Obama administration’s new ‘pivot to Asia’ strategy.

China’s more assertive foreign policy in the region has been attributed primarily to domestic politics in the run up to both installing and consolidating the new leadership over 2012/2013. East Asia is also generally a region where historic animosities have prevailed for some time amongst many of its constituent nations, and it is therefore quite remarkable that inter-state regionalism has progressed to its current state given such long-standing conflicts. What essentially coheres and holds the East Asian region together is economics, and in particular economic interdependence. It is revealing that through the turbulent intra-regional diplomacy of the early 2010s that trade ties between East Asian nations nevertheless continued to thrive. The fact that RCEP member nations still agreed to proceed with talks on forming a regional FTA to bind them closer together economically (and also whereby diplomatically) whilst these territorial disputes continued to rumble on was testament to the importance afforded to managing their regional economic interdependence. Yet just as has transpired previously at the bilateral FTA level (e.g. Japan and South Korea), the flaring up of serious diplomatic disputes could still jeopardise future RCEP talks.

**Summary**

Since the late 1990s, there has been a proliferation of bilateral free trade agreements (FTAs) in the Asia-Pacific that have had profound impacts on economic relations within the region. However, dissatisfaction over the fractured system of trade and other commercial rules this so called ‘spaghetti bowl’ of highly diverse agreements have caused have led to a push for harmonising regional FTAs. The two current contenders are the Trans-Pacific Partnership (TPP) led by the United States and which has already been in negotiation for many years, and the much more recent Regional Comprehensive Economic Partnership (RCEP) that is East Asia centred and based on a simpler FTA negotiating modality. Whereas the TPP stresses broad commercial liberalisation in close alignment with US market access interests, the RCEP is conceived more as an economic partnership deal that more strongly combines trade liberalisation with economic and technical co-operation. The prospects for these regional FTA talks ever concluding are uncertain. The TPP looks likely to miss its third deadline (end of 2013) for reaching a final deal, due mainly to persisting disagreements over sensitive economic issues such as intellectual property rights and agriculture. Historic animosities and current security-related disputes among East Asian states could unravel future RCEP talks, or at least seriously push back the present deadline of 2015 for concluding an agreement significantly beyond this. It is a little reported fact that FTA negotiations often fail to reach conclusion, especially when the aims are ambitious and involve a diverse set of countries. Any future TPP or RCEP deal concluded will very much depend on what compromises are willing to be made, and what kind of FTA is deemed politically possible. In the meantime, the dense pattern of bilateral FTAs in the region will continue to function, and some may transform into broader economic agreements in the longer-term.

**Further Reading**


Christopher M. Dent is Professor of East Asia’s International Political Economy in the White Rose East Asia Centre and Department of East Asian Studies at the University of Leeds. He may be contacted at c.m.dent@leeds.ac.uk
Overview

Negotiations to agree the Trans-Pacific Partnership (TPP) amongst Australia, Brunei, Canada, Chile, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States and Vietnam were joined by a new participant at the eighteenth round of talks in July 2013: Japan. The inclusion of the world’s third largest economy means the successful conclusion of the negotiations by the now twelve partners will lead to the creation of a group accounting for approximately 40 per cent of world gross domestic product and over 30 per cent of world trade. Whilst the US is clearly playing the leadership role in promoting the TPP and remains open to new members from the Asia Pacific region joining the negotiations in the future, increasing the global size and reach of the group even further, no official text detailing the negotiations has been released. However, the available information and commentary indicates the TPP’s overall aim is to bring the domestic legislation and policies of the member economies into conformity in areas such as the liberalization of investment, elimination of tariffs, protection of intellectual property rights and the standardization of regulatory frameworks. In this sense, the TPP is wider in scope than simply promoting free-trade and market access, but the exact nature of the final agreement will not be known until the conclusion of the on-going negotiations amongst the current and potentially new members of the group.

The Democratic Party of Japan prime ministers Kan Naoto and Noda Yoshihiko had both expressed an interest in joining the TPP, but the decision to take part in the negotiations had to await the election of the new Liberal Democratic Party Prime Minister, Abe Shinzo, who within a few months of taking office had overcome the resistance in the party and resolved to join the TPP negotiations. This briefing paper outlines the background to Abe’s decision to seek admission to the group and explores the domestic support and resistance to the TPP in order to illuminate the impact of international and domestic forces on the foreign policy-making process.

Prime Minister Abe and the TPP

The TPP can best be understood in the international as well as domestic context of Prime Minister Abe’s decision to join the negotiations. The international setting is twofold: the bilateral relationship with the US in the context of a rising China, on the one hand, and the multilateral relationship with other states involved in negotiating economic partnership agreements, on the other. The Abe government has made a strong commitment to the bilateral relationship with the US, not just economically, as seen in the TPP, but militarily under the US-Japan security treaty as well. The strengthening of Japan’s commitment to play a greater role in the alliance goes hand in hand with the strengthening of economic ties through the TPP. The two lock together in Japan’s concern over the growing military as well as economic power of China, which is not included in the TPP. With the US as the first and Japan as the third most important economies in the world, the TPP for these two giants is akin to a bilateral economic partnership agreement. The reinforcement of the alliance and China’s non-participation in the TPP serves to consolidate their bilateral relationship both economically and militarily. In essence, the liberalization of trade and investment together with the deregulations and structural reform of the Japanese economy will move Japan much closer to the kind of intimate relationship enjoyed with the US in the security sphere.

But the TPP is not the only economic partnership agreement Japan began negotiating in 2013: the first meeting with China and South Korea to discuss a trilateral free trade agreement also got underway in the same year as did the start of negotiations with the European Union (EU) as well as those to establish the Regional Comprehensive Economic Partnership (RCEP) agreement. As these latter negotiations are led by the Association of Southeast Asian Nations
and aim to establish a free-trade agreement with ASEAN partners, including Japan, we can see how the Abe administration is promoting trade agreements on different spatial scales, trilateral with China and South Korea, inter-regional with the EU and regional with ASEAN and the other ASEAN partners. What this means for Japan is the potential to hedge amongst different groups and for trade negotiators to be able to deploy learning from one negotiation process to another. Whilst the stronger economies may not always achieve their negotiating goals, Japan can expect pressure from the US to cut tariffs, deregulate and restructure the economy during the TPP negotiations as the government puts similar pressure on the weaker economies in the other economic partnership negotiations. In this way, Japan can be expected to benefit from more than one agreement and negotiating the TPP may add to the skill set of Japanese negotiators in the setting of other negotiations.

Domestically, the Abe administration is committed to revitalizing the Japanese economy through what has become known as a policy of ‘Abenomics.’ The policy has ‘three arrows’: monetary easing to target deflation; fiscal stimulus, including government spending on public works to the tune of ¥10 trillion; and the promotion of sustained growth in the long term by the implementation of deregulation and structural reform of the economy to improve competitiveness. Whilst the current administration has trumpeted a number of successes attributable to Abenomics, as evidenced by the fall in the value of the yen and the boost the lower-valued currency has given to the exports of the internationally competitive sectors of the economy, such as automotive and electronics, the aim is to make the economy as a whole more competitive, including currently uncompetitive sectors.

The TPP is closely aligned with the third of Abe’s three arrows to carry out structural reform and deregulation to improve competitiveness. In the face of a declining population as well as an aging population, the Abe administration hopes to be able to shake up and revitalize the economy with the aid of the TPP. To start with, the TPP is expected to contribute to structural reform of the uncompetitive sectors of the economy. As in the case of the agricultural sector, however, these sectors are often precisely those the Liberal Democratic Party relies on for votes. This creates a dilemma for the government. It has promised to negotiate with a view to protecting certain sacrosanct products, without specifying concretely how this will be achieved. The countries taking part in the negotiations have categorized all products into those where the tariff can be immediately abolished, gradually reduced, and pending, with Japan including agricultural products in the ‘pending’ category with a view to seeking their exception from tariff elimination. This reflects the resolution of an LDP Panel in March 2013 to negotiate exceptions for tariff elimination in five areas: rice, wheat, beef and pork, dairy products, and plants for making sweeteners (sugar cane and sugar beet). More broadly, the TPP is expected to contribute to the deregulation of the economy, but this is not simply in order to improve competitiveness; it also implies the erosion of the mode of capitalism at the heart of the Japanese political economy. In other words, although the final outcome of the TPP negotiations must still be awaited, and agreeing the concessions needed to reach the final outcome will be fraught with difficulty, the negotiations so far suggest the direction of travel will be to move the Japanese political economy towards a more neo-liberal model of capitalism than at present. It is this dual implication of structural reform and deregulation which engenders both support and resistance for the TPP within Japan.

Domestic Support for the TPP

The TPP is expected to bring benefits as well as costs to the Japanese economy and citizens and this divides opinion on the TPP. On the popular level, surveys point to a majority in support of joining the TPP as measured by public opinion polls. The public’s support for the TPP increased from a 2010 poll showing 46.6 per cent of the pollees in favour of Japan joining the TPP negotiations (38.6 per cent opposed) to a 2012 poll showing the support had grown to 63 per cent (27 per cent opposed). After the Abe government decided to join the TPP in March, a poll in June 2013 by the newspaper, Asahi Shinbun, showed only 53 per cent supported joining the TPP, although 71 per cent were positive about Prime
Minister Abe’s decision to take part in the TPP negotiations. This latest poll demonstrated the support for the TPP was in line with the Abe government’s focus on revitalizing the economy, with 65 per cent agreeing Japan’s participation in the TPP would benefit the country economically.

Apart from these positive sentiments on the popular level, the TPP is supported by a range of businesses likely to benefit from the TPP. The business community, as represented by the Japan Business Federation, or Keidanren, represents the voice of these economic groups, most prominently the larger multinational corporations at the top of the economy. Keidanren was a major force in supporting the government in joining the TPP negotiations and produced a brochure in 2012 outlining the benefits of Japan joining the TPP and the costs of not joining. These include the benefit of revitalizing the regional economy by exporting agricultural products compared with the cost otherwise of the decline of the agricultural sector; the benefit of the growth of web business compared with the cost of limitations on developing web businesses; the benefit of the export of Japanese infrastructure overseas compared to the cost of being shut out of the foreign infrastructure market. These and other benefits led the Federation to call on the government to promote economic growth and employment by the realization of the following seven points through joining the TPP: elimination of tariff, such as the US tariff of 2.5 per cent on automobiles and 5 per cent on flat screen TVs; speeding up of custom’s clearance for imports and exports; tackling piracy and fake goods; facilitating recovery of payment for intellectual property rights; liberalization of services on the internet; opening of the government procurement market; and elimination of discrimination on foreign investments. If Japan is successful in achieving these goals, then a range of businesses can be expected to benefit from joining the TPP.

**Domestic Resistance to the TPP**

At the same time, though, certain groups fear the costs rather than the benefits of Japan joining the TPP, not least Liberal Democratic Party politicians with rural electoral districts. As one of the central aims of the TPP is the comprehensive elimination of tariffs, strong resistance has been mounted by these rural, agricultural communities, which represent one of the weaker sectors of the economy protected by tariffs. Despite the Keidanren’s rosy picture of the TPP offering the opportunity to export agricultural products, street protests by farmers and their support organization, the agricultural cooperatives, suggest many are still to be convinced of the benefit of the TPP or of the ability of the government to gain agreement on key agricultural products being exempt from the abolition of tariffs. The protection offered to different types of agricultural products highlights the reason for their concern. We saw above how Keidanren viewed the elimination of tariffs of 2.5 per cent and 5.0 per cent would help Japanese exporters, but should the Japanese government not be able to negotiate an exemption for agricultural products, then the tariff rate potentially up for elimination is 778 per cent on imported rice; 252 per cent on wheat; 360 per cent on butter; 328 per cent on sugar, 38.5 per cent on beef and 4.3 per cent on pork. Whilst the government is expected to fight for protection of these products, the potential for success is constrained by the TPP’s goal of comprehensively eliminating tariffs. The difficulty of such negotiations can be seen from the US-Peru Free-Trade Agreement, where the percentage of products exempted from tariff abolition was only 1 per cent. In the case of the five agricultural areas in question, these in aggregate would equate to a 5 per cent exemption. Given that Australia, New Zealand and the US are all major exporters of agricultural products, the ability of the Japanese negotiating team to achieve these exemptions remains to be seen.

If, instead, these key agricultural tariffs are eliminated, then questions as to the viability of Japanese farmers becoming internationally competitive and the potential for regional disparity to grow between the rural and urban areas of Japan will become critical. It is clear from a comparison of the average size of farms in Japan and the US, 1.9 hectares versus 198 hectares, that increasing competitiveness in at least some areas of agricultural production will be difficult. Deregulation could promote the creation of larger farms, or up-market quality products could be exported, as Keidanren
envisions, but farmers are still to be convinced and remain resistant to the TPP. For some, the TPP is a tool from outside of Japan to deal with the intractableness of the agricultural sector inside Japan. From the perspective of the farmers, however, the abolition of tariffs will not only make their products uncompetitive in the market, but more widely will destroy their income, community, and way of life, with an increase in regional disparities an inevitable result.

The potential exacerbation of regional disparities is illustrated by the case of sugar. Although 70 per cent of sugar is imported, the remaining 30 per cent is produced domestically from sugar beet and cane and these two sources meet an annual per capita consumption of approximately 18 kilograms, compared with 32 kilograms for the US. Japan produces these two types of sugar in different regions of the country, sugar beet in Hokkaido and sugar cane in Okinawa and Kagoshima. Hokkaido produces about 80 per cent of national output with the other two prefectures producing the remaining twenty per cent: Okinawa accounts for 59 per cent and Kagoshima 41 per cent of the cane. Should the 328 per cent tariff on sugar be simply abolished without countermeasures, the farmers of Hokkaido, Okinawa and Kagoshima will face difficulty in surviving. This is particularly the case in Okinawa, where sugar cane is produced by 80 per cent of the farmers on the main and outlying smaller islands and the processing, transportation and sale of sugar is an important part of the island economies. It is thus no surprise to find the farmers of these prefectures continuing to protest in order to resist the TPP.

**Summary**

The Abe government’s decision to join the TPP demonstrates the prime minister’s resolve to move Japan closer to the US economically as he has done militarily as well as to implement Abenomics. That is, the decision was made taking account of the international a well as domestic contexts:

- The rise of China and the non-participation of the Chinese government in the TPP negotiations has reinforced the Abe administration’s commitment to the alliance and the strengthening of economic links with the US through the TPP.
- The start of negotiations to agree partnerships with China and South Korea, the EU and the RCEP demonstrate how Japan is hedging among different groups and can be expected to learn negotiating skills in the process.

But the outcome of the negotiations will be influenced by the results of the third arrow of Abenomics in the domestic environment, too:

- Supporters of the TPP in the business community will continue to push for the successful conclusion of the negotiations in order to benefit from the agreement.
- The weaker sectors of the economy such as agriculture will continue to press for their exception from tariff elimination with their allies in the Liberal Democratic Party.

Finally, should the TPP negotiations lead to the comprehensive elimination of tariffs, along with the deregulation and restructuring of the economy, then neo-liberalism will gain further ground and the Japanese model of capitalism will be transformed as result of the Abe administrations foreign and domestic policies.

**Further Reading**


Glenn D. Hook is Professor of Japanese Politics and International Relations in the National Institute of Japanese Studies and School of East Asian Studies at the University of Sheffield. He may be contacted at g.hook@sheffield.ac.uk
Overview

Since the 2008 global financial crisis there has been a growing interest in China’s state capitalism from academia and international media. Initially, the dramatic reversion of the economic deceleration as a result of the massive stimulus programme introduced by the Chinese government to offset the impact of the crisis on China’s economy reignited the debate whether the state capitalism with state-owned enterprises (SOEs) playing a heavy role could be an alternative to the market capitalism. The aggressive expansion and increased visibility of China’s state-owned ‘national champions’ further heightened the interest. However, as the effect of the stimulus programme tapers off and the economy slowdowns significantly, there emerges a serious concern whether China’s economic growth is sustainable and a suspicion whether the state-led development model viable. Economists and policy advisers inside and outside China urge the Chinese government to renew SOE reform and different suggestions are made on how to further the reform. In all these suggestions privatisation is a key component of reform. It is either said that privatisation is ‘the only way-out’ and ‘best cure’, or suggested that SOEs should retreat from non-natural monopolistic sectors. But little attention has been paid to the possible risks associated with privatisation and how the risks can be avoided or minimized.

An overview of SOE reform in China

SOE reform in China can be roughly divided into two stages since 1978 when the ‘Reform and Opening-up’ programme was launched: the pre-1992 stage and the post-1992 stage. During the first stage, reform efforts were limited to separating business from governments, allowing SOE management more operational autonomy and offering managers and employees pecuniary incentives in the forms of profit retention, performance contracts, bonuses, etc. After Deng Xiaoping’s ‘Southern Tour’ in 1992, corporatisation became the guiding policy for SOE reform. At the macro level, the Chinese government adopted the ‘grasping the large and letting go of the small’ policy, allowing local governments to sell off small SOEs. At the micro level, medium and large SOEs were converted into corporations and listed on stock exchanges. But this process of corporatisation and listing is not privatisation in that existing shares were not sold but only new shares were issued, and the newly-issued shares normally accounted for only 1/3 of the total shares of a listed SOE. Consequently, governments still hold effective control over listed SOEs. Meanwhile, tens of millions of SOE employees lost their job as SOEs were restructured and downsized. Governments also set up an agency to take over the administrative and supervisory responsibilities previously shared by a myriad of government departments, and the jurisdiction over specific SOEs were clearly demarcated between the central and local governments.

Today, the landscape of SOEs has changed dramatically. The relative size of the SOE sector as a whole has decreased considerably, by 2010 accounting for only 4.5 per cent, 42.4 per cent, 26.6 per cent, 19.4 per cent and 15 per cent of the total in numbers, net assets, outputs, employment and exports, as far as the industrial sector is concerned. More than 90 per cent SOEs have been converted into corporations and listed SOEs own 57.7 per cent of the total net assets and contribute 88.1 per cent of the total profits, as far as SOEs controlled by the central government are concerned. SOE managers have acquired a considerable degree of autonomy in managing their companies and SOEs are no longer a mere implementer of governments’ economic plans.

The performance of SOEs

The performance of SOEs as a whole has also changed dramatically. The total assets of industrial SOEs increased from RMB7491.6
billion in 1998 to RMB28167.4 billion in 2011, almost 4 folds, and the total profits increased from RMB52.5 billion to RMB1645.8 billion during the same period, more than 30 folds. The ratio of return over equity (ROE), an indicator of profitability, increases from 2.2 per cent in 1996 to 15.7 per cent in 2007, but drops to 10.9 per cent in 2009. Labour productivity increases 5.6 per cent annually between 1999 and 2007, higher than that of the private sector which recorded an annual increase of 3.6 per cent in the same period. In 2012 there were 54 SOEs in the list of Fortune Global 500, compared with only 6 in 2003. The days when SOEs were like beggars have gone and many of SOEs are making huge profits and flooded with cash.

However, these huge amounts of profits do not mean that SOEs are in a good health and the management of SOEs has truly improved. On the one hand, profitability as measured by ROE is still much lower than private enterprises or the international peers, as is the total factor productivity. On the other hand, much of the increased profits are due to monopoly and government subsidies. First of all, the bulks of the profits are contributed by SOEs enjoying monopoly or oligopoly in the industrial sectors where they operate. For example, one research found that, in 2010, 67.5 per cent of the total profits made by the SOE sector were contributed by SOEs under the central government’s control and the top 10 SOEs enjoying monopoly or oligopoly, such as PetroChina, Sinopec, China Mobile, China Telecom etc., accounted for 70 per cent of the total profits made by central SOEs. Two companies, PetroChina and China Mobile, alone contributed more than 1/3 of the total. Second, SOEs are exempted from paying land rentals for the lands that they occupied before the system of paid use of state-owned lands was introduced, saving industrial SOEs RMB2578.7 billion cost between 2001 and 2009; rates of resource rent are very low in China, meaning that the natural resource exploiting sector like mining and oil extraction, which is dominated by SOEs, receives a huge amount of benefits from the state; unlike in most countries, telephone operating companies in China, which are all SOEs, are not required to pay for using the radio spectrum. Third, due to the implicit guarantee from governments, SOEs have been able to receive cheap credits from banks, and one study found that SOEs would need to pay RMB2753.9 billion more interest between 2001 and 2009 if market interest rate were charged. Lastly, governments at different levels still hand out explicit subsidies in different names to SOEs or exempt them from paying taxes. If all these saved costs, received benefits and subsidies are added, SOEs would incur a huge amount of loss, instead of making profits.

SOEs are not just less efficient, the prevalence of SOEs in the economy has also a serious negative effect on the macro economy and social welfare. First, monopoly or oligopoly results in high price and low quality of products or services provided by SOEs. Second, SOEs explain much why China has a prolonged problem of production overcapacity. SOEs are less profit-oriented, receive cheap credits from banks, pay out little dividends, and market discipline is less effective for SOEs. Third, SOEs also contribute to the unbalanced economic structure and investment-driven growth model. On the one hand, SOEs have a strong preference for investments. On the other hand, low interest rate is wealth transfer in nature from depositors to business and low payments of dividends by SOEs mean people’s income from capital gains is limited, both of which lead to low consumption capacity. Fourth, SOEs also underscore the severe income equality in China. It is found that the average income of SOE employees is 63 per cent more than that of employees of private enterprises. Because SOEs pay little dividends to the governments, the ability of the governments to provide social service and welfare to the people is reduced. Lastly, it is claimed that compared to private enterprises, SOEs are less effective and efficient in innovation. Hence, despite the call by the government to develop an economy based on innovation to move up the value chain of production and sustain economic growth, the prospect is not optimistic, as long as the innovation system is led by governments and dominated by SOEs.
Privatisation, property right illegitimacy and corporate governance

There is no doubt that SOE reform has to be pushed forward. Various suggestions have been made on how to further the reform and privatisation features heavily in these suggestions. Some scholars and policy advisers argue that privatisation is ‘the only way out’ or ‘the best cure’. Even the less radical policy advisors recommend that SOEs should retreat from the non-natural monopolistic sectors. However, little attention has been paid to the possible risks associated with privatisation in China and how these risks can be avoided or minimised.

First of all, it should be established that the purpose of privatisation is to improve the corporate governance of privatised SOEs and make them more efficient. Although the prevalence of SOEs in the economy has a serious negative effect on the macro economy, micro issues of corporate governance and firm performance should still be the primary consideration of SOE reform. If these issues are not taken into account and privatisation is undertaken only for the sake of macroeconomic considerations, the governance and performance of privatised SOEs could deteriorate, and the effect on the macro economy may actually be opposite. In fact, if privatisation is undertaken hastily and recklessly, the consequence could be disastrous for the whole economy and society.

How can privatisation improve the governance of privatised SOEs? The accepted theory is that the property right is key to good corporate governance and privatisation creates the property right. However, under current social conditions in China and if privatisation is not carefully designed and implemented, the private property created by privatisation may become illegitimate. First, this illegitimacy could be a result of corruption during the process of privatisation. Corruption can be in different forms. For example, a top manager of SOEs may steal the assets or shares of an SOE or engage in self-dealing to acquire state-owned assets or shares cheaply; bribes may be offered to people who have the decision-making power in privatising a SOE and hence the SOE is cheaply sold. When corruption such as these happens in privatisation, ownership in the privatised SOEs acquired by people will lose legitimacy. Second, income inequality is now a serious problem in China. If privatisation leads to worsened income inequality, there is a danger that the privatisation as a whole would be regarded as illegitimate. It is not difficult to image that income inequality may deteriorate as a result of privatisation. For example, governments may favour rich people and large businesses in selling SOEs.

What are the negative effects of illegitimate property right on corporate governance? First, the right of illegitimate property will not be secured, as the public may demand correction or even reversion of a privatisation. Because of this insecurity, people who have acquired a SOE may liquidate and attempt to launder clean their ownership rather than focus on improving performance of the privatised SOEs; worse still, they may attempt move their wealth out of the reach of the country, i.e. capital flight. Second, even if unsecured property right is not a problem, people who acquire an SOE in an illegitimate way may have a less strong incentive to improve the governance and performance of the privatised SOE, because what they have paid is less than the real value of the SOE and thus they may less value the SOE that they have acquired. Third, it is widely recognized that privatisation alone will not necessarily improve corporate governance and much depends on whether privatisation could improve the rule of law in the country, the key to good corporate governance. However, instead of improving the rule of law, corrupt privatisation may have an effect to weaken the rule of law, as those who benefits from the corrupt privatisation may have an interest and strong incentive to prolong the state of weak law.

As illegitimate property has negative effects on corporate governance, a core consideration in privatisation should be on how to ensure that the ownership created by privatisation is legitimate. Based on this requirement, some provisional suggestions on the design of privatisation could be made. First, a hasty or ‘big bang’ privatisation should be avoided. It is very possible that such a privatisation may create a chaotic situation where cleanliness in selling SOEs is difficult to achieve. Second,
selling SOEs should be equitable and the public should be able to benefit from the selling. Favours rich people and big businesses should be avoided in order to ensure that privatisation does not widen the income gap. Third, transparency, competitiveness in selling and public participation should be the core principles of privatisation to ensure that privatisation is clean and equitable.

Summary

Economic reform in China has come to a new stage and the furtherance of SOE reform is critical to sustaining the economic growth in China. Privatisation in larger or smaller scale is a key component of reform. However, little attention has been paid to the risks associated with privatisation and the issue of how to avoid such risks. Under current circumstances in China, there is a danger that private property created by privatisation may become illegitimate. This could either be a result of corruption during the process of privatisation or an inequitable outcome of privatisation. Property right illegitimacy has serious negative effects on corporate governance and it is essential to ensure that private property created by privatisation should be legitimate. To achieve that end, a hasty or ‘big bang’ privatisation should be avoided and transparency, competitiveness and public participation should form the core principles of privatisation.

Further Reading


Zhong Zhang is a Lecturer in Chinese Studies in National Institute for Chinese Studies and the School of East Asian Studies at the University of Sheffield. He may be contact at zhong.zhang@sheffield.ac.uk
Overview

‘Zimbabwe’, is how Michael Connors of Hermes, a British pension fund manager, compared Japan’s shareholder democracy to an African dictatorship in 2008. Five years later, many foreign observers remain critical of Japanese corporate governance practices and alleged failings to secure shareholder value. Recent scandals, such as the one at Olympus, a well-established camera manufacturer, seem to prove their point. Olympus had systematically covered up losses amounting to over a billion dollars dating back to the 1990s, which were exposed only after its new British CEO, Michael Woodford, took the helm in September 2011. Woodford had become aware of unusual financial transactions and when adequate explanations and information were not forthcoming, called on the board of directors to resign. However, the board fired him instead, citing “differences in managing style”, and a costly financial settlement followed. Even though some of the real culprits, including a former chairman, were subsequently issued with suspended prison terms and the company was ordered to pay seven million dollars in fines, the scandal highlights again the alleged deficiencies of Japanese corporate governance practices.

This briefing paper argues that there remain unquestionably numerous problems in Japanese corporate governance, but foreign criticism is all too often based on a narrow understanding of the purpose of corporate governance. Corporate governance can be defined as set of institutions and rules which determine what a corporation or its agents do and who profits from the value added by a corporation’s activities. Corporate governance is thus an institutional element of a nation’s business system and hence reflects economic and social structures as well as norms. Foreign observers tend to neglect these complexities and take it for granted that ‘shareholder value’ should be the only rationale of corporate governance in Japan. A more nuanced understanding of the interdependencies between corporate governance, strategic investment, intercompany relations and education and training is also needed if UK policy makers are to succeed in reviving British manufacturing industries.

Whose company is it?

From an Anglo-Saxon perspective, the essence of the corporate governance ‘problem’ is how to manage the principal-agent problem which stems from the separation of management and ownership (shareholders). Following Adam Smith’s classical argument of the invisible hand, the allocation of economic resources will be efficient if firms maximize the wealth of their shareholders and individuals pursue their own interests. ‘Shareholder value’ should thus be the ultimate rationale of corporate governance. Comparative research confirms that managers in the United States and the United Kingdom have long subscribed to this view, but according to data from the mid-1990s a majority of Japanese and, for that matter, German managers replied that firms exist for the interest of all stakeholders, including shareholders, employees, other firms, and customers, and that job security was more important than dividends. While we do not have recent numbers on such attitudes, media statements of Japanese managers suggest that they continue to hold more complex views about the purpose of a firm.

Foreigners at the gates

Were Japanese stock markets as insular as the country, these different perceptions would perhaps not be a source of much trouble. However, following the bursting of the so-called bubble economy in the 1990s, Japanese companies and banks dissolved large parts of their shareholdings in other companies, while foreign institutional investors engaged more in the Japanese stock market. With 28 per cent...
of all stock holdings, foreigners are now the largest group of stockholders on the Tokyo Stock Exchange, followed by Japanese financial institutions and business corporations. Foreign institutional investors, alongside some important Japanese investors, such as the Pension Fund Association, have been calling for a stronger shareholder orientation and criticize other practices. A list of typical complaints includes:

- Companies are not prioritizing ‘shareholder value’ and do not pay sufficient attention to dividends and stock prices;
- Companies have insulated themselves from potential hostile takeovers through cross-shareholdings and ‘poison pills’;
- There is no adequate separation of management and supervision: chairman and board members are frequently long-term company employees or employees of stable shareholders;
- Statutory auditors (despite their legally powerful authority) are often selected by the president whom they are supposed to monitor;
- External auditors (who are prescribed by law) are often chosen from affiliated companies;
- 42 per cent (2012) of shareholder meetings are held on the same day, preventing shareholder activism;
- Whistle blowers, such as recently Michael Woodford, are not taken seriously;
- Companies do not actively seek out and incorporate outsider views or promote diversity in top management.

Recent changes

Despite the continuing problems listed above, Japanese laws and company policies with regard to corporate governance have changed considerably over the 2000s. The introduction of consolidated accounting in 2000 ruled out the hiding of unprofitable businesses in privately held subsidiaries. In 2001 mark-to-market evaluation of corporate stock holdings was introduced, so that companies are no longer able to declare large shareholdings at possibly high purchase prices. As part of the revision of the Commercial Code in 2002 companies were given the option to opt for a new governance structure with three board committees (audit, nomination, compensation). Shareholder rights were substantially improved by the 2006 Corporation Law, according to which managers can be held liable for their actions through derivative lawsuits brought by shareholders on behalf of the company. Such lawsuits have increased in number. Moreover, changes to companies’ bylaws require now a two-thirds majority vote of the shareholders, which need also to approve budget and balance sheets, executive compensation and stock options, mergers and acquisitions, hostile takeover defense mechanisms and the appointment of directors. Even though these changes might look standard from a Western perspective, except for the appointment of directors, all of these issues had previously been decided by management only. Companies have also substantially reduced the size of their board of directors and pay now closer attention to measures such as return on equity and profit margins.

This author’s recent research on UK institutional investors’ attitudes towards Japanese equities shows that most observers acknowledge these improvements, but cite also continuing corporate governance deficiencies for an overall low enthusiasm in Japanese equities. Foreign investors tend to invest in Japanese companies that adhere to Anglo-Saxon governance principles as measured by the ‘Japan Corporate Governance Index’. The JCG-index confirms that firms with a high score tend to have larger percentages of foreign ownership and higher export/sales ratios. By investing predominately in large export-oriented firms, UK pension funds do not only circumvent problems in Japan’s domestic economy, they ensure also that these companies subscribe more strongly to Western concepts of corporate governance.

Not deviant but different

What makes Japanese managers hesitate to follow primarily a shareholder value approach in their management? The primary reason is that corporate governance is a subsystem of the Japanese coordinated market economy
where the different elements are dependent on and complement each other. For example, even though cross-shareholdings have declined substantially since the bursting of the bubble economy in the 1990s, some Japanese companies continue to value non-profit oriented shareholdings in supplier companies or major customers as a measure to reinforce their mutual business ties. They are thus somewhat insulated from stock price fluctuations and possible hostile takeovers and can engage in more long-term strategic investments, without worrying too much about short-term shareholder value demands. Note, for example, that Japanese spending on research and development is at 3.5 per cent of GDP, substantially higher than in liberal market economies such as the UK (1.8 per cent) or the US (2.8 per cent). Long-term employment practices continue also to be important - albeit for a shrinking group of core workers - as the internal training and job-rotation of these workers supports crucial features of the Japanese production system, such as just-in-time and total quality control. Contrary to Western approaches, reductions in headcounts are thus not necessarily the first measures in an economic crisis and shareholder demands are not always primary concerns of Japanese managers.

Such interdependencies between corporate governance and intercompany relations, strategic investment and education and training are most important in manufacturing industries. The manufacturing share of GDP in Japan remains at 21 per cent substantially higher than in the UK (under 10 per cent) and the US (about 13 per cent). If we are prepared to recognize Japan’s competitive advantages in many manufacturing industries, especially in advanced materials, its corporate governance practices can be seen in a more favorable light as they:

- facilitate long-term strategic investments in manufacturing industries;
- support long-term employment practices which enhance skills development for manufacturing industries;
- allow long-term R&D strategies to maintain manufacturing competiveness;
- limit income and wealth inequalities;
- and sustain the Japanese form of capitalism.

As the Japanese economy has to confront increasing international competitive pressures and companies are facing demands for short-term profit maximization, managers are seeking new forms of corporate governance to satisfy both shareholder and company strategic needs. What happens in Japanese corporate governance over the next decades is thus a good indicator of what happens to the Japanese coordinated form of capitalism. Will it converge towards more liberal market practices or will it maintain its distinct coordinated character? Only the future will tell. However, in light of the current UK government’s aim to bolster British manufacturing, a nuanced understanding of the interdependencies between corporate governance, strategic investment, intercompany relations and education and training is highly desirable. A careful analysis of these interdependencies can either facilitate the development of meaningful policies to revive British manufacturing or might lead to the conclusion that the existing liberal market institutions of the UK’s form of capitalism are not, or no longer, compatible with a revival of these industries.

**Summary**

This paper has argued that Japanese corporate governance practices need to be understood as an expression of different corporate values and as an integral part of a different ‘variety of capitalism’. Moreover, recent changes in Japanese corporate governance highlight tensions in the country’s evolving capitalist system. On the one hand are the demands of a liberal, market-based Anglo-Saxon style of economic management, on the other hand, are the prevailing practices of a coordinated market economy with internal labour markets, long-term financing, employment, and intercompany relations.

To summarize the main points of this paper:

- Japanese laws and corporate governance practices have changed considerably over the 2000s, but Japanese managers appear by and large not to subscribe to a simple shareholder value view of the firm.
Changes in Japanese corporate governance must be seen in relation to other practices such as long-term financing, intercompany relations, long-term employment and the production system.

A nuanced understanding of these interdependencies would help UK policy makers to analyze the preconditions and develop the necessary policies for a successful revival of British manufacturing.

Further Reading


Harald Conrad is Sasakawa Lecturer in Japan’s Economy and Management in the National Institute of Japanese Studies and School of East Asian Studies at the University of Sheffield. He may be contacted at h.conrad@sheffield.ac.uk
Overview

While population ageing is now a common feature of many societies, research has tended to concentrate on western contexts with ageing in developing countries receiving less attention. In China, the challenge of population ageing is an emergent area of concern with significant implications as the country enters a period referred to by some as ‘super ageing’ (Joseph and Phillips 1999). In 2012 the number of people in China who were 60 years old and over had reached 185 million, comprising 13 per cent of the total population. It is estimated that by 2053, this number will exceed 487 million, constituting 35 per cent of the population. Among the ageing population, the majority (it is estimated to be two thirds) of older people live in rural areas. In China the position of the older people in rural areas is complicated by the fact that since the 1990s there has been a large-scale migration of younger workers from rural to urban areas (it is estimated that as many as 144 million rural residents are now working in towns and cities) and this has geographically separated many adult children from the ageing parents.

The household registration system introduced in 1958 effectively divided the Chinese population into two different kinds of citizens (either rural or urban). Ever since, rural residents have been deprived various entitlements and welfare provisions that are only available to urban residents. This lack of state support, combined with a recent relaxation of urban-rural migration rules, has challenged existing social norms and caused a disjuncture in what is expected in later life and what is now currently possible.

Research background

The research was funded by the Economic and Social Research Council 2011-13 (RES-000-22-4031) to examine the impact of adult child migration on ageing and intergenerational relationships in rural Chinese families. The research sought to redress the absence of qualitative in-depth research on rural families and on experiences of growing older in rural China. The project ran for 16 months and utilised qualitative in-depth biographical research methods. The fieldwork took place in 2011 and involved myself as principal investigator living with local families for two months in two different villages. Seventeen families took part in the project, nine in Village One and eight in Village Two. Sixty interviews were conducted in total across at least two (and sometime three) generations in each family and with both male and female family members.

Main findings

Resilience of familial support system

Unlike the western modernization thesis which anticipates the decline of family ties in the face of migration and urbanization, the data demonstrated the continuing significance of family and kinship in shaping people’s lives in rural households. For example, villagers often reported how family members introduced jobs to them or how they followed their relatives to a particular migration destination. Not only were people’s migrating livelihoods secured within the family network, the household acted as a safety net for all members. It was a common theme in all interviews that, whenever people ran into difficulties, monetary or non-monetary, it was family members who they turned to for help.

Migration choice was often made in a household context. Frequently, it was found to be a strategy to enhance the collective welfare of the household and positively accepted by the older generation. Despite geographical distance, different family members worked together to pool resources for the collective welfare of the household. For example, in terms of the support for the older generation, migration enabled a division of labour between children who migrated to offer financial support and the children who stayed behind to offer instrumental support. Among the families in the village where all offspring had migrated,
other more distant relatives stepped in as a wider kinship support network is a common characteristic of many Chinese villages (indeed, many villagers shared one of a handful of surnames, which means their ancestors were generally related within five or six generations). In this sense, it would be over simplistic to suggest that migration is always detrimental to the older generation who stay behind.

**Changing intergenerational contract**

Traditionally the Chinese value of filial piety emphasized a deference of the needs of children’s generation to the will and welfare of parents and other seniors in the family. The study indicated a shift from this traditional pattern of filial piety to a model which is based upon reciprocity and interdependence. Unlike the victimized image of the ‘left-behind’ in the Chinese media, the older generation were active support providers in their family. For example, the younger generation’s migration was enabled through the older generation’s support in raising grandchildren and looking after farm work. The older generation took on these talks as their duty and believed that their support would be reciprocated when they need it in later life.

Whilst interdependence is the dominant feature of relations between older parents and their children, a principle of ‘tiered egalitarianism’ persists in the relationships of reciprocal obligations and duties. That is, parents still prioritize sons’ family needs over daughters’ family needs and then between sons, the support from parents is provided equally. Any perceived non-compliance with this principle would cause damage to the interdependent networks within the family. Interviewees reported that perceptions of unequal childcare support and property division from parents were an important source of family discords between parents and children and between siblings. These conflicts in the household usually led to the breakdown of the webs of interdependence and reciprocity, with detrimental effects upon old age care for the seniors in the household. Therefore, the way in which migration affects care and support for older people is shaped by the conditions embedded in the reciprocal relations between older parents and adult children prior to and during migration.

**Gender dynamics**

Gendered division of labour resulted in older women carrying the main burden of care and farm work. In particular, their care work was critical in facilitating the bonds between generations. However, when the care is performed in a private sphere, it is often constructed as non-work. Indeed, because of the lack of formal recognition of women’s care work within the domestic sphere, interviewees only referred to this work as ‘women’s errands at home’. This gendered division of labour and the feminized notion of care work contributed to the reproduction of gender inequalities within the household.

Traditionally the care of parents was primarily the concern of sons. That is to say, because of the patrilocal marriage practice, a daughter moved to her husband’s family to take up her place in his household and look after his family. As a result, daughters were only required to make contributions to their natal families as long as they remained unmarried. However, migration seems to have put daughters who stay-behind in a central role in providing support to their parents. The study found that the burden on stay-behind married daughters has increased as they have become an important source of emotional and instrumental support to their parents as a result of their brothers’ migration.

Associated with the changing role of daughters in old age support is the part a daughter-in-law plays in the household. As noted above, traditionally sons were considered the main providers of support for parents, it was their wives who undertook the daily care work. Today, the daughters-in-law’s filial obligations towards the in-laws still remain but some care responsibilities have been transferred to the daughters. For many village interviewees, washing parents’ dirty clothes and bed sheets had become a taken-for-granted daughter’s job. The decline in support provided by daughter-in-laws may reflect a decline in the power of the mother-in-law, in that traditionally she was the immediate, unchallengeable supervisor of her daughter-in-law’s work and life. This research found that the power of mother-in-law had diminished significantly and this reflects a gradual disappearance of the traditional hierarchical family authority.
Despite the fact that daughters play an increasing role in caring for their parents in the context of migration, the patriarchal practice that only sons inherit the parental home still persists. The persistence of gendered arrangements and tradition such as patriarchal property inheritance affords sons more symbolic status and material benefits.

**Insufficient welfare provision**

The public pension in China is available to all urban residents who have undertaken paid employment. In contrast, the state pension is only available to small proportion of rural residents and the level of financial support is much lower. One of the two villages used in this research benefited from the rural pension provision, and it should be noted that it is official government policy to considerably extend coverage by 2020.

Participation in the pension system is voluntary; any citizen who is aged over sixteen is eligible to participate and required to make an annual contribution to their pension fund for a minimum of fifteen years; reaching sixty, he/she will receive a monthly pension (the rate of 2011 was 55 yuan or 5 pounds approximately). The pension system was universally welcomed by all the interviewees as they felt they still could rely upon the government as a last resort. However, the rural pension system is household-based rather than citizenship-based, that is, in order to receive a pension, all the other adult household members must participate in the pension system. This premise causes financial constraints upon older generation if they have a distant relationship with their adult children. For example, as her children did not want to make any contribution to their own pension fund, an older interviewee had to pay for additional contributions on behalf of her sons and daughters-in-law in order to receive her own state pension.

The single biggest concern of rural villagers was the cost of medical treatment. Whilst state medical care insurance was introduced to rural areas in 2003, and it was officially estimated by 2012 that 96 per cent of the rural population was covered, the scheme only provides subsidized treatment if hospitalised. Most villagers complained that this arrangement was of little value to them since they hardly ever became hospitalized and could not use the contribution to offset the cost of their medicine expenses (which comprised a large proportion of their medical treatment costs). This was an acute problem for those who suffered from chronic disease and had to rely on medicines for a long-term treatment. Another problem with the system was that cover could not be transferred to other regions, meaning that villagers who migrated could not benefit if they received hospital treatment in their migration destinations. Tragically, there have been newspaper reports of rural residents committing suicide when they become ill so as not to burden their family with the cost of their treatment.

**Summary**

To summarize the main points of this research:

- The research reveals the two-way flow of intergenerational support in Chinese rural households and its resilience in the face of outward migration.
- In contrast to their stereotyped image as receivers of care, the older generation are active support providers to their family; older women, in particular, play a vital role in enabling the migration of their adult children.
- Despite the challenge to existing stereotypes, the research highlights the necessity of a state intervention into care for the older people as family relations can turn sour and become unstable.
- Chinese family relations have undergone a shift from traditional filial piety to an intergenerational contract based upon reciprocity and interdependence.
- The traditional hierarchical family authority structure is gradually disappearing. However, the patriarchal/patrilineal structures in Chinese rural families remain largely un-impacted by migration.
Further Reading


*Jieyu Liu is Lecturer in Chinese Studies at the University of Leeds. She may be contacted at j.y.liu@leeds.ac.uk until December 2013. From 2014, she will join the School of Oriental and African Studies, University of London as a Senior Lecturer in Contemporary Chinese Studies.*
Overview

Japan is one of the most rapidly ageing and depopulating countries in the world. Government projections indicate that Japan may shrink 32 per cent from the high of 128 million in 2008 to approximately 87 million by 2060, due to a sustained fall in rates of human reproduction. Whereas in 1947 each woman expected to give birth in her lifetime to 4.54 children, this had dropped below the population replacement rate of 2.1 children per woman by 1974, and remained at below replacement to stand at 1.39 children in 2010 (Figure 1).

Figure 1. Actual (1960-2010) and Projected (2020+) Population of Japan (left hand scale, millions) and by Age Group (right hand scale, %). (Source: Japanese government websites).

Overall, population reduction is probably good news for Japan, and possibly other countries too, in that it provides opportunities for reconfiguring living conditions and it may help to reduce human pressures on the natural environment. Nevertheless, ageing and depopulation bring with them consequences for affected regions, and policies may need to be developed to deal with these. What is interesting about Japan’s situation as a pioneer shrinking society is how the outcomes of these processes and policies might inform us about the prospects for other East and Southeast Asian countries such as China, South Korea, and Thailand in the years and decades to come, as they too experience similar developmental pathways.

In this briefing paper I will outline the ways in which Japan’s demography has been changing and make comparisons with China and South Korea. I will then describe some of the impacts in Japan’s non-metropolitan regions, focusing on the issue of over-capacity. I will conclude by looking to the future.

Japan's Changing Age Structure

Japan is in the midst of a dramatic century-long shift in the age structure of the population, from being a young country in 1960 to an old one in 2060 (Figure 1). Demographers have come to call these circumstances either a ‘demographic dividend’, due to the potential for a young population to deliver rapid economic expansion, or a ‘demographic burden’, because of the high economic costs of maintaining a hyper-aged society. Japan, moreover, is in a particularly difficult position, given that national debt in 2013 stands at approximately 240 per cent of GDP, with debt servicing swallowing around a quarter of the national budget, and an annual budget deficit of around 6 per cent.

When we compare demographic change in Japan with that of other countries in Asia such as China and South Korea, UN Population Division data, which are more conservative than the Japanese government’s, show Japan growing by 82 per cent in the 75 year period up to its population peak in 2010, and project a 26 per cent shrinkage by 2085. The UN forecasts similar paths for South Korea and China. South Korea is projected to grow and shrink 138 per cent and 26 per cent in the 75 and 70 year period either side of its expected peak in 2030,
and China by 154 per cent and 33 per cent in the 75 year periods either side of its peak in around 2025.

In all three countries projections for the dependency ratio between working and non-working people point to worrying consequences for the long-term stability of each nation’s finances, for the continuation of growth-oriented economic regimes, and for maintaining community stability and resilience. In Japan the dependency ratio reached its most economically advantageous position in 1990, just as the economy tilted into the long stagnation known as the ‘Lost Decade(s)’. Thereafter the proportion of the population dependent on working people has steadily risen and is expected to reach about one worker per dependent in 2055. China will reach its most advantageous ratio in around 2015 and South Korea in 2025.

The Changing Spatial Distribution of Japan’s Population

Alongside ageing has occurred a dramatic shift in the population's spatial distribution due to the familiar processes of agricultural transformation, industrialization, and urbanization that accompany modern economic growth (Figures 2 and 3). Whereas 41 per cent of the population lived in urban areas in 1960, by 2010 this had increased to 67 per cent, with an increase in the total population over the same period of 73 per cent. This has placed enormous pressures on urban areas in accommodating ever rising demand for housing, infrastructure, and services. Less noticeable has been the stresses that population loss have placed on rural regions.

In general, internal migration in Japan can be understood as a movement by predominantly younger adults from rural to urban locations in search of more plentiful, varied, and higher quality educational, employment, and social opportunities, and producing urbanization at four levels of geographical scale or distance:

- inter-regional (to metropolitan centres; Tokyo, Osaka and Nagoya);
- inter-prefectural (to regional centres; e.g. Fukuoka, Sapporo and Sendai);
- inter-municipal (to prefectural capitals and core cities);
- and intra-municipal (to the municipal urban zone).

Within this spatial redistribution of population can be discerned some generalizable patterns, with similar patterns having been experienced in South Korea and China thus far.

First, rural locales are now widely recognized as being hyper-aged societies lacking the means to sustainably reproduce their own populations such that communities are declining in vitality and, in increasing numbers, even collapsing and disappearing. Second,
while urbanization was taking place against the backdrop of an expanding national population, metropolitan centres and prefectural capitals in particular expanded very rapidly, to some extent at the expense of rural shrinkage, such that there is now over-crowding in some urban districts. However, and third, with depopulation now taking place at the national level nearly all settlements are now shrinking. Consequently, depopulation can no longer be considered an unfortunate rural expression of successful national economic development, as it once was, but also as an urban phenomenon and a condition affecting settlements of all sizes and concentrations. Accordingly, and fourth, depopulation is experienced spatially as a retreat from the peripheries of the archipelago, with the most remote hamlets collapsing first, and progressively larger settlements being drawn into a recursive spiral of ageing, depopulation and decline, until almost the entire land area of the country experiences the impacts in some form or another.

Impacts of Ageing and Depopulation in Rural Japan

Ageing and depopulation are being felt in all areas of Japan’s social, economic, political and cultural life. In this section I will focus on some of the more significant issues that rural communities have faced and which, with some reservations, as processes of ageing and depopulation become more widespread and severe in the near future, may also occur in urban settlements in the rest of Japan, as well as in other East and Southeast Asian countries.

In Japan a large number of rural communities are in decline and some are collapsing. This is what Japanese social scientists mean when they describe ‘genkai shuuraku’, or ‘communities on the edge’. In these there is virtually no economic activity between residents, few children are being born, an increasing proportion of the built environment is empty, idle and deteriorating, agricultural land is being abandoned, and forests are encroaching on human settlements. Such communities have little attraction for reinvestment or in-migrants and, in the course of time, some will disappear entirely. What are some of the conditions of living in such communities?

Beginning with employment, which is the foundation for any stable local economy, well-paid secure jobs that do not require physical labour is in short supply in rural Japan. Traditional routes into employment for eldest sons and daughters wishing to remain living in the family holding and care for ageing parents, such as family commercial enterprises, municipal administration and school teaching, are fast disappearing as economic functions in rural communities decline, and where public and private services are in retreat. For example, over-capacity in educational infrastructure due to fewer school age children means that schools are merging or closing down, leading to fewer teaching opportunities; and increasing numbers of empty school buildings dot the landscape, reminding residents of once thriving communities (Figure 4).

Similarly, rationalization of local authorities has led to a wave of municipal mergers. Few job openings are appearing in public administration or essential services as organizations remove duplication and slim workforces through retiree attrition. Moreover, the preference among urban Japanese for holidays overseas means that seasonal tourism related work is thin on the ground in previously popular domestic rural destinations, leading to the closure of hotels, facilities and shops (Figure 5).
Municipal mergers have encouraged local centralization of administration, which has caused the closure of public facilities in outlying areas. This has produced various consequences. First, services have become more distant from users; yet, reductions in subsidies combined with reduced demand means public transport is also being cut. Residents feel forced into cars, which disproportionately affects older people living alone, who require frequent and easy access to services, but who may not be able to drive. Second, office and facility closures reduce overall demand in surrounding neighbourhoods, damaging a community’s economic vitality. Third, younger and middle-aged people remaining in rural communities spend increasing resources and time helping and caring for elderly relatives and neighbours in compensation for reduced formal service provision. Although such kindness is admirable, it reduces the opportunity that economically able citizens have for productive activity.

Nevertheless, overcapacity is a serious issue in non-metropolitan regions, as communities empty out. Provincial real estate markets are failing as houses remain empty, and occupancy rates in apartment blocks reach low levels. Property reinvestment is disappearing and the built environment looking shabby and derelict, further depressing prices, and causing remaining residents to leave, if they can. Empty houses, or akiya, are becoming uninhabitable and unsellable due to colonization by fauna and flora (Figure 6). Ransacking and defacement by monkeys is a familiar blight. Although land prices in central Tokyo are rising again, this belies a collapse in market conditions in many rural areas.
heating oil deliveries, and emergency services travel longer distances per client. Such a phenomenon, if generalized out across China and the rest of Asia, may have important consequences for the transition to a low carbon economy and society.

The Future for East Asia

While the future is always uncertain, China and South Korea will probably experience many of the outcomes of ageing and depopulation currently being faced by Japan, due to their similar patterns of demographic and economic change. Later in the century other countries in East and Southeast Asia, such as Thailand, Malaysia and Indonesia may follow.

East Asia will remain an economically dynamic world region. However, a deep cleavage is appearing there, between the large, vibrant, energetic and young metropolitan centres, such as Tokyo, Shanghai, Seoul, and Bangkok, and an increasingly old, shrinking, depressed and struggling regional periphery. Metropolitan centres are pulling away from the regional hinterland on which their continuing dynamism ultimately depends. How the tension between urban dynamism and rural decay will unfold is unclear. But the potential for disruption is present and, I argue, increasing. For example, even as urban demand for food expands, rural agricultural production decreases, leading to higher prices.

Not only is the number and size of marginal regional communities increasing, their exposure to risks is also expanding. Whereas in previous decades in Japan only the most peripheral hamlets were under threat, in the 21st century even provincial core cities are losing their vitality. With more than 90 per cent of Japan’s municipalities now shrinking it is certain that the impacts of ageing and depopulation will spread to large regional and metropolitan settlements. For example, health and welfare costs are rising and the central government wishes to pass some costs on to local authorities, with the result that the most vulnerable municipalities will bear a disproportionate economic burden.

Importantly, the March 11, 2011 tsunami in Northeastern Japan has shown how vulnerable ageing marginal communities are to extreme environmental disturbances. Climate change theory predicts extreme weather events of increasing frequency and intensity, and the Northwestern zone of the Pacific Ring of Fire appears to be experiencing an increase in seismic intensity. As East Asia develops, it is possible that extreme disturbances will also destabilize industrial facilities such as power stations and chemical plants, such as occurred at Fukushima in Japan.

It is my belief that a careful study of how economic and demographic change interact in present-day Japan will provide essential knowledge for responding to similar circumstances in the rest of East and Southeast Asia. In particular, how Japan responds to the intersection between the long-run endogenous ‘disaster’ of rural decline and the sudden exogenous ‘disaster’ of the 2011 Tohoku tsunami and nuclear crisis will be especially instructive for other regions in Asia as they traverse their paths through industrial and post-industrial development.

Summary

• Japan is in the midst of a dramatic century-long shift in the size, age structure and spatial distribution of its population.

• The impacts of ageing and depopulation are being felt in all areas of social, economic, cultural and political life.

• While community decline was confined to the most peripheral villages, even regional cities are now losing some of their vitality.

• Due to similar patterns of economic development and demographic change, what is currently occurring in Japan will likely occur in future in other countries in East and Southeast Asia.

• Although East and Southeast Asia will remain economically dynamic, a deep cleavage is appearing between still vibrant metropolitan centres and a struggling rural hinterland.

• Issues to watch: regional socio-economic sustainability, rural-urban bifurcation and disruption, health and welfare provision,
resource consumption patterns, agricultural self-sufficiency ratios, potential impacts of extreme environmental disturbances.

**Recommended Reading**


Peter Matanle is Senior Lecturer in Japanese Studies in the National Institute of Japanese Studies and School of East Asian Studies at the University of Sheffield. His research interests are in the social and cultural geography of Japan and East Asia. He may be contacted by e-mail at: p.matanle@sheffield.ac.uk, or through his personal website: www.matanle.net
Overview

Long-term observers of China-Japan relations will be familiar with sporadic incidents relating to the disputed Senkaku/Diaoyu islands, beginning in 1978 on the eve of the signing of the Peace and Friendship Treaty and breaking out intermittently in the 1990s and first decade of the 21st century. However, since 2010, ongoing tensions over the islands appear to have developed the potential to escalate further than in the past, raising fears and speculation in some quarters about the possibility of war between the two countries. This narrative stems from a common view that a power shift is underway in East Asia, with an aggressive rising China attempting to face down a Japan in decline. Such assessments tend to overlook the otherwise robust trade and investment links shared by the world’s second and third largest economies, and reject the view that economic interdependence might mitigate against conflict. They also downplay what lies behind the political posturing and rhetoric from both sides, and the symbolism with which the territorial dispute is imbued.

This briefing paper considers what has changed since 2010 in the way the dispute has been played out, and what factors might explain such changes.

Background

As Zhou Enlai and Deng Xiaoping wisely foresaw in the 1970s, the territorial dispute would be better left to future generations to resolve. Yet an amicable solution still seems a remote possibility, and over the years the islands have attracted the attention of nationalist groups (whether independent of the state or state proxies) on all sides (including activist groups from Taiwan, which also lays claim to the islands, and Hong Kong), prompting diplomatic spats and (in China) anti-Japanese demonstrations. Until 2010, however, both the Chinese and Japanese governments adhered to the status quo put in place by the agreement to ‘shelve’ the territorial issue and managed to prevent an escalation of tension. The turn of events in 2010, however, when a Chinese fishing boat collided with the Japanese Coast Guard leading to the detention of the Chinese crew for an extended period (rather than immediate release as had been the case in the past) signified a change in the status quo. The (mis?)-handling of the dispute by the Democratic Party of Japan (DPJ), perhaps caught off-guard in the midst of a leadership election, prompted a fierce diplomatic response from a ‘shocked’ China and sparked anti-Japanese protests across major cities in China.

Furthermore, hard-liner Maehara Seiji secured an assurance from US Secretary of State Hillary Clinton in October that the islands were subject to US protection in the case of armed attack, under Article 5 of the US-Japan Security Treaty. Tensions temporarily relaxed until spring 2012 when controversial Tokyo Governor Ishihara Shintaro announced plans that the Tokyo Metropolitan Government aimed to raised funds to purchase three of the privately owned islets. Tension escalated through to summer, with visits to, or attempted landings, by various activist groups on the islands. Prime Minister Noda Yoshihiko’s decision to purchase and ‘nationalise’ the islands, thereby scuppering Ishihara’s own plan, nonetheless ignited another summer of anti-Japanese demonstrations in China. While the demonstrations subsided soon after the usual round of anniversaries was completed (in particular September 18th, which marks the beginning of Japan’s invasion of Manchuria in 1931), the high-level political posturing on the Senkaku/Diaoyu dispute continued, taken up enthusiastically by the new leadership in both countries. In late 2013 the issue continues to occupy a fairly central space on the diplomatic agenda. The next sections explore what is different about the 2012-13 instalment of the Senkaku/Diaoyu issue, and why this might be.
Re-presenting the Territorial Dispute in 2012

One of most striking differences in the 2012-13 instalment of the Senkaku/Diaoyu dispute compared with previous incidents is the way in which the history of the dispute has been recounted to the domestic and international audiences. In the Chinese narrative, the Diaoyu dispute has become firmly embedded into the story of Japan’s imperialist history of invasion. This has not been done to such an extent before, and the Diaoyu dispute has thus been incorporated into one of the other major recurring problems in Sino-Japanese relations – the ‘history problem’. On the other hand, the Japanese official narrative is at pains to completely decouple the history of the acquisition of the islands from Japan’s imperialist past.

In the Chinese discourse, Japan’s capture and illegal occupation of the islands is traced back to the unequal treaty of 1895 (Treaty of Shimonoseki) after the first Sino-Japanese war (1894-1895), from whence a straight line can be drawn through to the second Sino-Japanese war (1937-1945), about which the Japanese do not hold a ‘correct’ view, which is why the Chinese need to remain vigilant about a possible resurgence of Japanese militarism, evidence of which can be seen in the sort of behaviour being demonstrated around the Diaoyu islands today. Chinese media reports on the dispute in 2012 and 2013 made direct links with the ‘history problem’, criticising Japan’s official stance on the Diaoyu as representing a denial of the outcomes of the global anti-fascist war (in which the Chinese were victorious alongside the allied powers).

In the Japanese discourse, the standard explanation is that there is no territorial dispute, although much effort is expended on providing evidence as to why that is the case, including lengthy accounts (for example on the Japanese Ministry of Foreign Affairs website) of the historical origins of Japanese claims to the islands. The Japanese approach is to remove the issue from the sensitivities of history (that is, Japan’s imperialist past) and to deal with it instead from the point of view of international law and security, stressing Japan’s democratic and peaceful credentials.

In both China and Japan, the telling of the Senkaku/Diaoyu story can be seen as a re-nationalising of history; in each case it is an immutable, indisputable story with one, and only one, version. Furthermore it seems to resonate very strongly with the public, and plays well to the sorts of domestic audiences that leaders Abe Shinzo and Xi Jinping are trying to attract, and from whom they gain their legitimacy. These are unifying discourses in each country. In Japan, the ‘traditional’ left-right split, not least on interpretations of the past, disappear into a national consensus on the Senkaku issue. In China, where multiple and contested histories have been emerging in recent years, the Diaoyu ‘story’ becomes a reminder of the Chinese people’s struggle to overcome national humiliation at the hands of the imperialists.

Appeals to international audiences have been important in this round of the dispute too, and both sides have attempted to garner support, through the use of international media and proactive public diplomacy for their respective arguments. This marks a shift away from dealing with the dispute as a purely bilateral issue, though the effect such international public relations campaigns seems somewhat limited. The DPJ’s success in bringing a hitherto reluctant US off the fence in 2010 to pronounce on the issue was an important milestone, although Prime Minister Abe did not get the support he was hoping for from President Obama in 2013. The Chinese courted Papua New Guinea in September 2012 and gained their ‘understanding’, but were less successful in securing similar support from Germany during a visit by Li Keqiang in May 2013.

Political Transitions and Legitimacy Issues

Putting aside any economic value and the (slightly separate) issue of gas and oil deposits in the East China Sea, it could be argued that the ongoing tension has considerable political value. Barring the potential for mishap or miscalculation since September 2012 (and of course this can’t be ruled out), the stand-off has not been damaging to, and could be said to have positively enhanced, the domestic political agendas for the leaders in China and Japan in the context of major political transitions in both cases.
In the summer of 2012 China was preparing for the handover of power from the Hu Jintao/ Wen Jiabao period to Xi Jinping and Li Keqiang ahead of the 18th Communist Party Congress to be held in November. As the Senkaku/Diaoyu dispute developed over subsequent months, Xi Jinping was still building and consolidating his power base. Even though he was Hu’s protégé, which carries a certain amount of authority, he did not have Hu’s physical support since he had stood down from all senior posts (previous leaders tended to remain in top posts). This in turn meant that Xi had to ensure that he had firm control over all areas of government. This included the need to send strong and clear signals on foreign policy in order to placate the People’s Liberation Army, in addition to having to deal with potentially de-legitimising and destabilising legacy problems from the Hu-Wen era (in the form of corruption, social unrest and so on). A tried-and-tested foreign policy issue such as the Diaoyu island dispute was arguably a useful distraction at this point and would enable him to take a strong stance against Japan.

Political change was also afoot in Japan with the collapse in support for the DPJ by the summer of 2012, a general election on the horizon and the resurgence not only of the Liberal Democratic Party, but Abe, who took up position once again as prime minister by the end of the year, and had much to prove. Unusually, foreign policy ranked fairly high up the agenda during the election campaign and Abe promised to take a firm stance on the Senkaku issue, not least to contrast the DPJ’s bungled handling of the 2010 instalment. On taking office, Abe adopted a fairly pragmatic position on China (as he had done during his first stint as prime minister), but he remained committed to policies which were clearly aimed at checking China’s rising power (for example, by strengthening the role of the Japan Maritime Self Defense Role to counter China’s naval build up), and remained constant in his assertive tone on China. Mindful of the need to prove himself in the Upper House elections of July 2013, Abe had to ensure not only the success of Abenomics but he also had to remain true to his general election pledges to ‘take back the country’.

In both countries, the Senkaku/Diaoyu dispute, and its timing in 2012/13 presented certain opportunities for the new leaders to legitimize their positions and build their domestic support base by proving their nationalist credentials. This in turn presents a certain risk or escalation if not managed carefully, but it should be noted that, compared with the 2010 incident, there were much greater dispute management mechanisms in place in 2012 through both informal and formal channels (for example through friendship diplomacy and through Ministry of Foreign Affairs links). Anti-Japanese demonstrations in China, almost a regular feature in the Sino-Japanese calendar, are also of concern. But self-regulation was in evidence in the summer of 2012 where bloggers, and the official media, admonished those who showed the ‘wrong’ sort of ‘irrational’ patriotism.

**Summary**

- The Senkaku/Diaoyu dispute has long held a symbolic value to nationalists in both countries and has been of sporadic use to the Chinese and Japanese governments at various points from the 1970s to the early 21st century; on the whole, however, both governments had tacitly adhered to the agreements of 1972 and 1978 to shelve the issue for future generations.

- The nature of the Senkaku/Diaoyu dispute changed in 2010, perhaps as a result of DPJ mishandling, but this has had implications in terms of taking the issue ‘off the shelf’ and producing a recalibration of the positions of both sides. This partly explains the instability of the current situation as a new status quo emerges.

- The 2012/13 instalment of the Senkaku/ Diaoyu dispute is noteworthy because it has remained high on the diplomatic agenda for longer, and both sides have maintained a fairly regular drum beat of high level political rhetoric. This can be explained partly by the need for the new leadership on both sides to consolidate domestic support after a period of political transition.

- Dispute management mechanisms are in place, but need to be used carefully to avoid any further escalation of tension.
Further Reading


Caroline Rose is Professor of Sino-Japanese Relations in the Department of East Asian Studies at the University of Leeds, and Executive Director of the White Rose East Asia Centre. She may be contacted at c.rose@leeds.ac.uk
Overview
The terms of the Diaoyu/Senkaku Islands territorial dispute are shifting and at times unpredictable. In mid-2013, it was possible to view Sino-Japanese exchanges over the islands as an ongoing war of words rather than a potential war of military hardware; with the establishment of the ‘Air Defense Identification Zone’ (ADIZ) over the East China Sea in November (including, but not confined to, the vicinity of the islands), the stakes might easily appear higher and the possibility of escalation more real.

The view that tensions may result in the near future in military conflict is not new: an article in *The Economist* September 2012 asking rhetorically if China and Japan would go to war over the islands concluded that, after all, they might not – but academics in the Anglophone academy have been warning of the possibility of renewed East Asian conflict for a number of years. This position may be supported to an extent by a literal reading of the Chinese official press coverage. It is generally, however, far more productive to assume that the Chinese official media is designed to influence its audience rather than to deliver bald statements of practical official intentions, and that approach shows a rather more complex picture.

It is fair to assume that neither the Chinese nor the Japanese authorities have any serious expectation that a sustainable and amicable solution to the dispute can be reached in the foreseeable future: as Caroline Rose points out, both Chinese and Japanese leaderships have too much invested in maintaining quite narrowly conceived national interests in the wrangling over the islands’ status. Arguably, therefore, the central priority on both sides is to manage perceptions of the dispute – and their own response to it – on the part of domestic and foreign audiences. In this context, though, where perception management appears to be the only game in town, we should not dismiss the efforts made to that end as merely hollow words: the legitimacy that Beijing and Tokyo seek to generate through those words is not only the sole gain available at the current stage of the dispute, but is also crucial to regimes that, for different reasons, sorely need to build support at home and overseas. It is worth, therefore, taking the rhetoric of the dispute seriously, and asking how the different voices represented therein work together.

In Search of the ‘Official’ Voice
Some of those voices are very loud indeed, as *The Economist* article noted, and the islands dispute is the subject of intensive and assertive coverage in the Chinese press. For example, a simple search of the online *People’s Daily* for the term “Diaoyu Islands” generated 4,312 hits in English and 92,850 in Chinese in November 2013, up from 3,599 and 74,385 in mid-June of the same year, and the dispute also receives regular (though less intensive) attention in provincial titles.

That said, it is worth considering carefully what meaning can be extracted from those rising levels of noise. On one hand, while content in the mainstream media is far more varied on many questions than was once the case, and while studies of the relationship between the state and the media suggest that the state is becoming more responsive to public opinion, there is still much less variation in discussions of sensitive issues. On the other hand, the very assumption that press coverage of those sensitive issues is heavily influenced from above does not of itself suggest that press commentary is a reliable guide to official intentions. It is striking that much of what is written refers to Chinese understandings and entitlements and to the actions of other powers, rather than to any possible consequences of those; rather than committing
the authorities to any specific course of action, it has the cumulative effect of legitimising a range of possible ways forward.

This apparently carefully orchestrated media coverage, however, was not matched by an equally assertive presentation in the official netscape. True, the Ministry of Foreign Affairs website carries a collection of documents on China’s claims to the islands and commentary on the developments of 2012, accessed via a dedicated button on the Chinese-language and English-language homepages. However, these pages are apparently quite static, neither having been updated or extended since end 2012; the dedicated link appears in neither French or Spanish homepages – that collection is displayed for specific audiences; and more recent coverage of the islands issued in, for example, regular press conferences, appears in English but not in Chinese.

The Ministry of National Defense, while relatively muted in its discussions of the islands in mid-year, referring more often in general terms to activity and capability in the East China Sea, was far more direct in treatment of the ADIZ in November, both in Chinese and in English. However, the primary message of the English-language content was that the ADIZ was neither an unusual measure nor one that should – if properly handled – cause any rise in regional tension.

Additionally, both official sites make considerable use of material drawn from the mainstream press. While this confers a degree of recognition on the selected articles, it also has the effect of re-presenting a version of developments produced at one remove from official circles, both ministries appearing thereby to delegate commentary on developments to the media, rather than producing a narrative explicitly marked as official.

Themes and Variations in the Press

That is not to say that media coverage has differed visibly from the essence of the official position. In summer 2013, much press commentary focused self-consciously both on Chinese official narratives of legitimate possession of the islands and on Chinese official efforts – sober and determined, we are told – to convince and remind third-party governments of the rightness of the Chinese position. These articles therefore treated the dispute variously as the subject of Sino-American discussions in which Xi Jinping was able to impress on US officials the validity of Chinese claims; of Sino-Japanese talks in which Japan was lectured on the error of its own understanding of the issue; and as a question of shared cross-straits interest and co-operation. The introduction of the ADIZ in November introduced a new focus into the press coverage, most early reports solemnly asserting China’s responsible management of the zone.

It is also central to this coverage that the islands are not just a matter of high-political concern. References to the growing archive of documents, maps and photographs generated by cultural institutions – museums, libraries and archives – have underlined the historical roots to Chinese claims, adding scholarly authority and considerable weight of archival evidence to the official position. There are also efforts to emphasise and encourage popular engagement with the problem of the islands. The People’s Daily interactive page (advertised in the provincial media) allows readers across the world to register support for Chinese sovereignty over the Diaoyus and to plant a virtual flag on the islands. It currently records over 53 million flags and 131 million declarations of support (disclosure and note: two of each of these hits were produced in the writing of this piece; there is no apparent barrier to multiple entries in either feature).

Elsewhere, the Guangming Daily has featured primary school classes on the islands, in which smiling children in Henan produced pictures and maps marking the islands as China’s, domesticking the issue and underlining its status as one of everyday concern for Chinese citizens of every age and status, in inland as well as coastal provinces. And China’s claims to the islands appear in cartoons and body art – this has become a matter of popular culture, as well as politics.

While all this commentary points broadly in one direction, it is still possible to register modest variations on that central theme. In November 2013, the relatively independent
Southern Weekend reported on the translation and publication in China of a Japanese work on the history of Diaoyu/Senkaku issue, and carried an interview with its author, the Japanese scholar Murata Tadayoshi. This work had attracted controversy in Japan for its rather sympathetic treatment of the Chinese position, and to that extent was supportive of the Chinese official line on possession of the islands. However, by noting diversity of opinion within Japan on the status of the islands, it admitted more openly than much other public discussion the possibility of a negotiated settlement and portrayed the dispute in more complex terms than the more common, one-dimensional picture of a beleaguered China confronted with the legacies of twentieth-century Japanese expansionism. It also invited a more reflective approach to the dispute, by pointing to shifting post-war Chinese rhetorics of nationalism and patriotism and explicitly distancing academic research from national interest.

Reader comments on the article were also less bellicose than one might expect. While some commenters appeared suspicious of Murata’s standing and motives, or repeated the familiar exhortations to defend every inch of territory, others compared the work favourably to Chinese scholarship on the same question and noted drily that no work questioning Beijing’s official position in similar ways could have been published in China.

The article and its comments do not represent dramatic departures from the official insistence that the islands belonged unquestionably to China. However, they do show that the dispute can at times be talked about as something other than a black-and-white confrontation, based on immutable interests and principles, between ‘China’ and ‘Japan’ as homogeneous entities; that evidence-based academic research can be detached from national interest; and that the political and rhetorical stage on which these tensions played out was itself subject to change and redesign. These are not alien ideas in the China of 2013; but their implications for a dispute which is elsewhere discussed in terms of unquestioned and unchanging claims and rights are potentially unsettling.

Summary

- Chinese press coverage of the Diaoyu/Senkaku dispute varies in tone and intensity with practical developments in Sino-Japanese interactions; the level of variation in media coverage appears higher than in official – Ministry-level – web coverage;
- Orthodox press coverage – in People’s Daily, Guangming Daily and many provincial titles – appears designed to emphasise that Chinese interests and ownership of the Diaoyu/Senkaku islands is beyond question, and is of immediate, daily concern to all Chinese, regardless of age, profession and place of residence;
- Despite the orthodox treatment of the status of the islands as a pressing and immutable national concern, there is still some limited space for the discussion of alternative perspectives;
- Media commentary does not commit the Chinese authorities to any specific course of action, but rather supports a range of possible responses to developments.

Further Reading


Marjorie Dryburgh is Lecturer in Chinese Studies in the School of East Asian Studies at the University of Sheffield. She can be contacted at m.e.dryburgh@sheffield.ac.uk.
East Asia’s Energy Security and Diplomacy
Christopher M. Dent

Overview

East Asia is having an increasingly profound impact on global energy security.1 Spurred by rapid economic development, the region’s energy consumption levels rose five-fold over 1970 to 2012 while the average world energy consumption rate only doubled. In 1970, East Asia accounted for just an eighth of world energy consumption but by today this share had grown to a quarter of the world total, and current estimates predict the region’s share will rise to well over a third by 2030. This is being particularly driven by China’s growing energy demand requirements, which already accounts for over a half of East Asia’s primary energy consumption.

We may expect East Asian states to afford increasing priority to tackling energy security challenges for the following general reasons. First, China’s dynamic economic growth will continue to impel the region’s own future economic development, manufacturing industry-driven and high energy-intensive process, and hence a burgeoning demand for energy resources. Furthermore, many parts of the region are still poor and under-developed, and the socio-political pressures on East Asian governments to raise levels of energy service provision will remain strong for some time to come. Second, East Asia’s own conventional energy resources are fast depleting, thus requiring its states to increasingly seek resources from outside the region. East Asia now consumes three times more oil than it produces, and the region is more dependent on oil imports than any other in the world. As a result, East Asian countries will become increasingly dependent on international energy partners and stable energy governance in the global system.

Third, competition for conventional energy fuels (oil, gas and coal) is intensifying globally as stocks of these fuels dwindle and access to known reserves have become either restricted or logistically difficult to secure. Presently, every three years a new Saudi Arabia is required in production terms just to maintain oil consumption rates at current levels. The explosion of the BP Deepwater Horizon rig in April 2010 was indicative of existing pressures to push out exploration and production frontiers into areas of increasing operational difficulty and risk: positioned 1,260 metres above the seabed, the rig drilled the deepest oil well in history to a vertical depth of 10,683 metres. Fourth, pollutant emissions from energy consumption is the prime known cause of climate change, and East Asian states will come under increasing international pressure to address the environmental risks associated with their intensifying demand for fossil fuels.

As an important consequence of the above, East Asian states are affording greater priority to energy security objectives in their foreign policy and development strategies, and will adopt more proactive energy diplomacies over forthcoming years. We may also expect a stronger conflation between their energy and environmental diplomacies as global concerns regarding climate change grow, leading to expanding international dialogues on implementing green energy technologies and practices. While there will be intensified competition amongst East Asian states over securing access to energy resources, their energy diplomacies will too be oriented by the imperatives to internationally cooperate given the interdependent nature of many energy security predicaments and challenges confronting them.

East Asia and Energy Security

The perceptions and objectives of energy security have changed significantly over time. As a general principle, energy security concerns come into sharper focus during

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1 East Asia refers to Northeast Asia (China, Japan, South Korea, North Korea, Mongolia, Taiwan) and Southeast Asia (Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand and Vietnam, which comprise the membership of the Association of Southeast Asian Nations (ASEAN)).
periods of acute crisis, such as the oil shocks of the 1970s and more recent turbulent events in the Middle East. Increasingly, however, energy security is a permanent foreign policy priority given that conventional fossil fuel sources are becoming critically depleted. Generally speaking, we may define energy security in terms of risk, namely the securing of energy supplies (minimising supply or quantity risk) at stable and affordable prices (minimising price risk), and taking into account the environmentally damaging effects of energy consumption (minimising environmental risk), especially from the combustion of fossil fuels.

East Asia, like Europe, is a major net energy importing region. Its conventional energy resources are concentrated in Southeast Asia and China, whereas Northeast Asia’s developed economies – Japan, South Korea and Taiwan – have extremely scarce energy resources and have long maintained very high-level dependencies on energy imports. On specific fossil fuel sectors, East Asian states are among the world’s largest: oil (China ranked 2, Japan 3, South Korea 6, Singapore 8), coal (China 1, Japan 2, South Korea 4, Taiwan 5), liquefied natural gas (Japan 1, South Korea 2, China 4, Taiwan 7). Securing the necessary levels of energy inputs (increasingly from foreign sources) to maintain the momentum of the region’s burgeoning economic development has become a challenge for all East Asian countries.

Furthermore, huge flows of energy supplies shipped into the region are funnelled through a series of narrow sea-lane ‘chokepoints’ that are highly susceptible to blockade and piracy, the most important being the Malacca Straits that at its narrowest point is only around 1.5 miles wide but through which a quarter of world trade (approximately 100,000 ships per year, including around half the world’s oil-tankers) passes. Energy and other resource imports are also transported through other chokepoints such as the Sunda Strait between Java and Sumatra, the Lombok Strait between Bali and Lombok, and the Makassar Straits between Borneo and Sulawesi. In addition, territorial and sovereignty disputes persist amongst a number of countries over zones in the South China Sea (Spratly Islands and Paracel Islands) and the East China Sea (between China and Japan) through which this energy trade passes, and where there is thought to be potentially significant oil and gas reserves located. These factors create a strong maritime dimension to East Asia’s energy security interests and energy diplomacy.

Renewable and other alternative energy sources are being increasingly viewed in East Asian countries as a key long-term solution to national energy security predicaments. Renewable energy sources (hydro, wind, solar, geothermal, tidal, etc) are inherently indigenous as well as replenishable and abundant. The region has become the world’s largest investor in renewables, the biggest producer of renewable energy products such as solar panels and wind turbines, and no other part of the world generates more electricity from renewable energy sources. China has the world’s highest level of installed hydropower and wind energy, and its solar photovoltaic (PV) sector is now growing at an astonishing rate. The country also now manufactures around two-thirds of the world’s solar panels. However, there are significant challenges regarding the scaling up of every renewable energy sector, including spatial or equipment material constraints, intermittency problems, infrastructural connectivity problems and others.

After the March 2011 Fukushima disaster in Japan, the future of nuclear power in East Asia and globally has been uncertain. The industry has been relatively static worldwide before Fukushima. In 2002, total world nuclear power capacity stood at 362GW from 444 reactors, rising by just 13GW by 2010 at a total capacity of 375GW that year. However, this level had fallen to 364GW and 427 reactors worldwide by 2012. Most of this drop is attributable to Japan’s post-Fukushima energy policy but many of the world’s 31 nuclear power producing countries have also been decommissioning old reactors and plants and not replacing them. Only four East Asian economies have nuclear power capacity: Japan (38.0GW in 2013), South Korea (20.7GW), China (13.8GW) and Taiwan (5.0GW). Although there are plans in East Asia to construct new reactors in the future (China 28, South Korea 4 and Taiwan 2), renewables have nevertheless gained ground over nuclear as the most viable
long-term alternative energy source to fossil fuels. By the mid-2010s the combined installed generation capacity of solar PV (102GW) and wind energy (283GW) alone was greater than that of nuclear power. Even if China successfully achieved its target of having 58GW of installed nuclear power by 2020, this is likely to be just over a quarter of the planned installed wind energy target of 200GW by that same year.\(^2\)

**East Asia’s Energy Diplomacy**

**Markets**

The nature of the world’s energy markets, and East Asian countries situation regarding them, varies from sector to sector. The world’s *oil market* is the most globalised and integrated of all, and current structures of global energy security are more dependent on oil than any other fuel source. Around 60 per cent of the Middle East’s oil exports go to East Asia, and approximately 70 per cent of East Asia’s oil imports come from the Middle East – 90 per cent for Japan, 70 per cent for China, 95 per cent for the Philippines. China is the region’s largest and world’s fifth largest crude oil producer but in 1993 it became a net oil importer. Over the last decade, it has accounted for half of world growth in oil consumption. East Asia’s other major oil producers in order of significance are Indonesia, Malaysia, Vietnam, Brunei and Thailand. However, only Brunei, Malaysia and Vietnam are the region’s only net oil exporters.

Unlike oil, the *natural gas market* is regionalised or localised rather than globalised. Whereas oil is mostly distributed by tankers by sea, most gas is transported by land-based pipeline networks. This limits the geographic scope of sourcing natural gas for importing countries as they are reliant on gas supplier nations in their regional neighbourhood. Furthermore, pipelines are extremely expensive to construct, thus presenting additional supply constraints. The regionalised fragmentation of the natural gas market also limits the degree of competitive contact amongst suppliers at global level.

Prices for internationally traded natural gas are far more static than for oil as agreed fee rates of supply are set under inter-state contracts as part of the terms of constructing international pipelines. Arguably the most recent significant development in global energy markets has been the emergence of the ‘unconventional’ or *shale gas* industry. This energy source is produced by the hydraulic fracturing (use of pressurised liquids) of natural gas-permeable shale rock that recent technological advances have enabled to be extracted in commercially viable quantities. The United States has pioneered the industry’s rapid development and is thought to have enormous shale gas reserves, as are many others including East Asia and Europe that have also invested significantly in exploration.

*Liquefied natural gas* (LNG) is a small but fast growing sub-sector of the gas market. LNG is produced by super-cooling natural gas until it reaches a temperature of -162 degrees Celsius, liquefying it and thereby reducing its volume by a ratio of 600:1. Thermally insulated tankers are used for transportation to special facilities where it is reconverted into natural gas and thereafter distributed by pipeline or other means. LNG infrastructure costs are huge but industry expansion and scale economies are helping reducing average unit costs in this sector. Although LNG only accounts for around 7 per cent of total world demand for gas, it is fast becoming a globalised market and is by far the most traded form of natural gas in East Asia. Up to the mid-2000s, the region had both the world’s largest exporters and importers of LNG. Indonesia, Malaysia and Brunei, as well as Australia, are the major suppliers of LNG to Northeast Asia: Japan, South Korea China and Taiwan together accounted for around 60 per cent of the world’s total LNG imports in 2012.

Once a relatively localised industry, the *coal market* has become increasingly internationalised. Like oil, it is a comparatively easy and cheap fuel material to transport, and therefore trade. It was noted earlier that East Asian nations dominate the world coal import market, and in 2011 Indonesia became the world’s largest exporter overtaking Australia. China maintains a heavy dependence (70 per

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\(^2\) This wind energy target is ‘unofficial’ but most experts believe China will exceed this. In 2012, it stood at 75GW. In 2005, it was only 1GW.
cent) on coal for electricity generation and is the world’s largest coal producer by far with a 42 per cent share and possesses around 40 per cent of known global reserves. Over the last 20 years, international trade in coal has increased by an annual average of 7 per cent. Australia sends the majority of its traded coal to East Asia, while Russia, South Africa and Canada are other major foreign sources for the region. Despite the announced plans of East Asian governments to reduce CO₂ emission levels, many countries in the region are relying increasingly on coal (the most carbon-intensive fuel) in their energy mix given concerns over high and volatile oil prices, comparatively limited natural gas reserves, persisting fears over using nuclear power and the challenges involved of scaling up renewables.

The inherent indigenous nature of renewable energy sources means that the international market for sectors such as wind, solar, hydropower, geothermal and biomass is primarily concerned with technology and equipment, although there is a growing global market for biomass pellets. The wind and solar energy industries are fast becoming mainstream energy markets on these fronts. However, due to China’s expanding domestic production capacity and the increasing scale of wind turbines (with towers now up to almost 200 metres tall and blades exceeding 80 metres in length) the market has become more localised and less internationalised. China also has some 90 turbine producers, four of these (Sinovel, Goldwind, Guodian United Power, and Mingyang) in the world top ten largest. These mainly serve the domestic Chinese market, which with an installed capacity of 75.4GW in 2012 (up from just 1.1GW in 2005) represents over a quarter of the global total. Chinese, Japanese and Korean turbine makers are looking to increase exports and overseas operations: Samsung has recently installed one of the world’s largest offshore turbines off the east coast of Scotland. In 2004, China produced just 5 per cent of the world’s solar panels but by 2012 its share had risen to 65 per cent. The US and EU have both taken China to the WTO in a dispute over the alleged ‘dumping’ of cheap (or affordable, depending on your viewpoint) solar panel imports from Chinese manufacturers.

International trade in the nuclear sector meanwhile is largely confined to sales of reactors and other technological components. As a highly capital-intensive energy industry, only very small amounts of the fuel derivative, uranium, are required in nuclear power generation. Thus, international energy security issues in this sector centre more on dependencies on foreign technology rather than foreign material resources. However, we have seen the growth of foreign direct investment in the nuclear industry, as most recently shown by the investment deal between the British government and two Chinese state-owned enterprises (China National Nuclear Corporation and China General Nuclear Power Corporation) to build the new Hinkley Point C plant in Somerset. China itself has plans to construct 28 new nuclear plants and quadruple its nuclear power capacity from 2011 to 2020. South Korea also has ambitious plans for expansion, to construct another 17 plants by 2030 and become 59 per cent dependent on nuclear by 2030. Even after Fukushima, nuclear cannot be ruled out as being integral to Japan’s long-term energy strategy. Many Southeast Asian nations are also considering nuclear in similar terms although the region still has no nuclear powered electricity at present. The domestic markets

**Multilateral Economic Cooperation and East Asia**

Multilateral energy cooperation frameworks remain generally under-developed in comparison to its international trade, finance, regional integration and other economic-related equivalents. The Organisation of Petroleum Exporting Countries (OPEC) was the first substantive multilateral energy grouping, formed in 1960 by Iran, Iraq, Kuwait, Saudi Arabia and Venezuela. Responses to the 1973/74 oil crisis are also cited as an important landmark of multilateral energy cooperation, being instrumental in not only creating the IEA but also the G7 grouping in 1975 with Japan as an original member of both. As host of the G8 summit in 2000, Japan proposed the establishment of a multilateral, multiple agency task force on promoting renewable energies development. At the 2008 summit, also hosted by Japan, G8 leaders agreed to adopt in the United National Framework
Convention on Climate Change (UNFCCC) talks the commitment to reduce global carbon emissions by at least half by 2050. In addition, G8 leaders invited China, South Korea and India to join the International Partnership for Energy Efficiency Cooperation. Japan and South Korea are currently Asia’s only IEA members but the organisation works at a certain advisory level with key non-members such as China.

Regional-level energy cooperation in East Asia began with relatively low-level ASEAN-led endeavours dating back to the 1970s, starting with the creation of the ASEAN Council on Petroleum (ASCOPE) in 1976 as a forum for discussing oil and gas industry matters and later developing various analytical functions. Subsequent initiatives included the ASEAN Petroleum Security Agreement and ASEAN Energy Cooperation Agreement (signed in 1986), the more programmatic five-year ASEAN Plans of Action on Energy Cooperation (APAEC) from the 1990s onwards, and an ASEAN Centre for Energy established in 1999. However, it was not until the 20th ASEAN Ministers of Energy Meeting held in July 2002 that high-level consultations on advancing regional energy cooperation occurred, that in turn led to a common understanding on ‘Energy Cooperation among Japan, China, Korea and ASEAN’ being signed at the ASEAN Plus Three (APT) Energy Ministers Meeting, this comprising a five-point initiative: (i) the creation of a energy emergency network; (ii) development of a strategic oil reserve; (iii) joint studies on the ASEAN oil market; (iv) improvement of natural gas development; and (v) improvement of energy efficiency and renewable energy.

These are all still works in progress, partly managed through six APT energy working groups, namely: energy security, national gas, oil market, oil stockpiling, renewables, and nuclear safety. Under the larger regional membership of the East Asia Summit (EAS) group (additionally including India, Australia and New Zealand), the region’s leaders signed the Cebu Declaration on Energy Security in January 2007, committing EAS states to similar sets of objectives previously agreed with ASEAN and APT. In 2001, China formed the Shanghai Cooperation Organisation (SCO) with Russia, Kazakhstan, Kyrgyzstan, Tajikistan and Uzbekistan where managing cross-border energy security related issues have particular prominence. In 2005, China also entered into a trilateral agreement with the Philippines and Vietnam (with their respective NOCs also as signatories) for joint oil and gas prospecting in the South China Sea. A number of ambitious sub-regional ventures have too been proposed, such as Gobitec, a South Korean initiative that conceives a huge solar panel array in the Gobi desert feeding electricity to the industrial centres of Northeast Asia.

In the wider Asia-Pacific context, APEC’s Energy Security Initiative (ESI) introduced in 2001 consists of various short-term measures to respond to temporary energy supply disruptions (e.g. oil price volatility, occasional security threats to sea-lanes supply routes), as well as longer-term policy measures aiming to address challenges concerning the region’s security of energy supply, such as technology and infrastructure cooperation. Under a Japan led proposal, the APEC Peer Review of Energy Efficiency Mechanism (PREEM) was created in 2008 whereby member economies demonstrated their plans to achieve energy efficiency objectives, these then being reviewed by specialists from other member economies. Meanwhile, the Asian Development Bank (ADB), a largely Japanese dominated institution, has for many decades facilitated energy sector development assistance for the region’s lesser developed countries, and its recently introduced Clean Energy Programme promotes the adoption of low-carbon energy practices in Asia through investment projects, shared best practice dialogues, and other means.

Two new potentially very important regional level government-business dialogue initiatives have recently emerged within the Asia-Pacific. The Asia-Pacific Partnership on Clean Development and Climate (APP) was established in 2006 where seven member governments (Australia, Canada, China, India, Japan, South Korea, US) work in partnership with private sector actors on a range of energy-environment nexus themes. The inaugural Pacific Energy Summit was held in November 2009 at Tokyo, convened by the US’s National Bureau of Asian Research and sponsored by
various organisations including the ADB, Japan Foundation Centre for Global Partnership, and ExxonMobil. Amongst its key recommendations were to incorporate stronger energy security provisions in FTAs, especially on green energy technology trade and intellectual property rights, and on fostering stronger cooperation on transnational energy issues generally. Pacific Energy Summits are held biennially: the second was convened in February 2011 at Jakarta and the third at Auckland in March 2013.

Wider afield, since 2005 Asian and Middle East governments have been discussing energy security issues in Asian Ministerial Energy Roundtable meetings. There has also been growing East Asian participation in Europe’s Energy Charter Treaty (ECT), which was established in the early 1990s as a framework for international cooperation and trade rules on the land-based transit of energy supplies across third countries (WTO rules mainly cover maritime based energy trade, i.e. oil and coal), thus with particular focus on pipelined natural gas. Japan was an original signatory, a substantial ECT budget contributor, and has advocated strong Asian participation from the start. China, Indonesia and South Korea have all seconded officials to work at the ECT Secretariat in Brussels, and APEC is currently looking to adopt some ECT principles in an Asia-Pacific context.

**Summary**

No other region in the world will affect future global energy security more than East Asia. As its own energy resource supplies fast deplete and energy demands continue to expand at high rates, increasing pressure will be applied on existing sources of energy elsewhere on the planet. This will compel East Asian states to strengthen its energy diplomacy on all fronts, and we may expect Britain and the EU to sign a growing number of energy agreements with them over forthcoming years. East Asia is also now the world’s biggest investor in and generator of renewable energy power and producer of renewable energy products, and is arguably Europe’s most important global partner in green energy industries. Despite the Fukushima disaster of March 2011, many East Asian states have ambitious plans as part of their long-term energy security strategies. There has also been a number of interesting developments in East Asia centred multilateral energy diplomacy, especially at the regional level, that have emerged since the early 2000s in particularly. However, most are yet to progress beyond the level of structured dialogue about how to achieve substantive international energy cooperation rather than actually realise it. The energy diplomacy objectives of East Asian states are still predominantly subordinated to national interests rather than those of the regional or other multilateral collective, despite deepening interdependencies in East Asia’s international energy relations.

**Further Reading**


*Christopher M. Dent is Professor of East Asia’s International Political Economy in the White Rose East Asia Centre and Department of East Asian Studies at the University of Leeds. He may be contacted at c.m.dent@leeds.ac.uk*
The Loch Erne Summit of the Group of Eight (G8) took place in County Fermanagh, Northern Ireland from 17 to 18 June 2013. Under the UK’s presidency this was the thirty-ninth summit in a process that dates back to November 1975. Reflecting changing priorities in its agenda and shifts in the global order through its membership, the G8 has served as a microcosm of the broader picture of world politics across this period of time.

As an original member of this informal grouping, Japan has cherished the associated great power status and has actively sought to contribute to the success and continuation of the group. However, as the G8 places the emphasis on the role of individual leaders, Japanese efforts have been dependent on the ability of the leader of the day. Abe Shinzo represented Japan at the Loch Erne Summit having been returned to the prime ministership as a result of the Liberal Democratic Party’s (LDP) landslide victory in the House of Representatives election of 16 December 2012. This briefing paper outlines the background to Abe’s attendance at the Loch Erne Summit and explores his participation in order to highlight the direction of his evolving foreign policy.

The G8 and Japan

In November 1975, faced with considerable macroeconomic challenges, French President Valéry Giscard d’Estaing and German Chancellor Helmut Schmidt invited the leading powers of the day to what was envisioned as a ‘fireside chat’ to build consensus and foster cooperation. This summit was intended to be a one-off gathering of leaders with no bureaucrats present or notes taken. However, for a number of reasons, the leaders of France, West Germany, the UK, the US, Japan and Italy found the format to be useful enough to invite the Canadian prime minister and convene a second summit of the Group of Seven the following year in San Juan.

Thereafter, the summit process evolved in a number of ways. First, its membership continued to expand with the President of the European Commission joining the 1977 London Summit. Russia became an official member of the G8 that met in Birmingham in 1998. From the 2003 Evian Summit, the G8 began a process of inviting important stakeholders (such as African or Middle Eastern leaders) and rising powers (such as China) to its annual meetings. Second, in the same way that the G8’s membership reflected changes in the global order, the focus of its agenda went through a similar metamorphosis moving from macroeconomic issues to political and security issues surrounding East-West tensions in the 1980s to the end of the Cold War, global poverty and climate change. Finally, the G8 has also demonstrated institutional depth by supplementing its annual meeting of leaders with regular meetings of finance and foreign ministers and irregular meetings of other ministerial portfolios including crime, energy and the environment.

Throughout its history, the G8 has been accused of lacking legitimacy, effectiveness and relevance. These accusations have become more voluble since the creation of the Group of Twenty (G20) at the leaders’ level in November 2008. The received wisdom today is that this more inclusive summit process has superseded the G8. However, rumours of the G8’s death have been greatly exaggerated and in fact a settlement appears to have emerged between the two whereby the G8 meets ahead of the G20 each year and the treatment of particular issues can be mutually reinforcing.

Within this process, the G8 has mattered to Japan. Historically excluded from, or still constrained within, the official and legal mechanisms of global governance, inclusion in the first of these informal summits of contemporary great powers accorded status and recognition to Japan. In response, Japan sought to demonstrate its credentials as a responsible great power and ensure the
success of the process, especially on the five occasions Japan hosted the summit (1979, 1986, 1993, 2000 and 2008). As the only non-North American/European member, Japan has also played the role of Asia’s representative, including issues of regional concern in the summit’s discussion, such as the Cambodian conflict, the East Asian Economic Crisis of the late-1990s and North Korea’s nuclear development. Finally, the G8 has provided opportunities for the Japanese leader of the day to manage a number of bilateral relationships on the edges of the summit meetings, particularly with the US, and promote issues more closely related to Japan’s immediate national interests than global governance (e.g. North Korea’s abductions of Japanese citizens).

However, participation in the summit has been challenging for Japan. Informal groups place a great emphasis on the role of individual leaders and the interpersonal relationships they construct between and amongst each other. In the case of the Japanese prime minister, he has often been regarded as a reactive and transitory figure both domestically and internationally. Exceptions such as Nakasone Yasuhiro and Koizumi Junichiro certainly exist but the Japanese prime minister has on average only attended two summits. Between 1975 and 2013, twenty Japanese attended thirty-nine summits; this contrasts with seven US presidents and seven UK prime ministers. This prompted former Brazilian President Lula da Silva to comment that ‘it’s like that in Japan - you say “good morning” to one Prime Minister and “good afternoon” to a different one!’ Although this revolving door of Japanese prime ministers has often been spoken about as a recent feature of Japanese politics, it has a longer history as demonstrated in G8 summitry.

Equally, the rise of the G20 has questioned not only the G8 but also Japan’s position in global summitry. Not only does the expanded membership of the G20 dilute the status of belonging to an exclusive elite grouping, the inclusion of a number of Asian countries (China, India, Indonesia, South Korea and, by extension, Australia) creates rivals to Japan’s traditional and self-appointed role as Asia’s representative. In reaction, Japanese prime ministers have sought to ensure the continued existence of the G8 by stressing the advantages of the G8 over the G20; namely, the utility of a smaller, more exclusive forum, in reaching decisions as well as the shared values that exist between G8 leaders based on the first summit’s declared shared belief in ‘open, democratic society, dedicated to individual liberty and social advancement’.

The Loch Erne Summit

The general narrative surrounding Abe represents A Tale of Two Abes. On the one hand, Abe the nationalist seeks to continue a number of revisionist policies from his first short-lived administration (September 2006 to September 2007) that settle postwar accounts and make Japan less reactive and more assertive. On the other hand, we have Abe the pragmatist who has learned from a misplaced emphasis on nationalism during his failed first administration, has conducted a listening exercise with the Japanese public and as a result has placed the emphasis on economics. So, which Abe came to Loch Erne?

In line with UK Prime Minister David Cameron’s efforts to return the G8 to its roots as an economic summit by placing the emphasis on tax, transparency and trade, Abe came to Loch Erne with the goal of promoting and getting support for his programme of ‘Abenomics’. ‘Abenomics’ consists of monetary easing to target inflation, fiscal stimulus including a ¥10 trillion package and the promotion of growth strategies through structural reform. The unpredictable and negative effects of quantitative easing and the weakening of the yen on the global economy were reported to have caused concerns amongst some G8 leaders. Thus, Abe’s strategy at Loch Erne was a tried and tested one that has characterized Japan’s participation in global summitry over the years and looks to the international as well as the domestic – preempt open criticism of Japan at the summit by pitching ‘Abenomics’ and claiming endorsement so that the policy can be presented at home as an international commitment in order to secure leverage (this was the same approach adopted by Abe’s predecessor Noda Yoshihiko at the 2011 G20 Cannes Summit as regards the consumption tax). Abe was successful insofar as he was
presented with the opportunity at Loch Erne to explain ‘Abenomics’ and thereafter claimed G8 endorsement. However, there is a difference between endorsement and not hearing opposition and Abe was pushed in the summit’s communiqué for details on what his ‘credible medium-term fiscal plan’ will be.

Beyond ‘Abenomics’, the fifth Tokyo International Conference on African Development (TICAD) met before the G8 from 1 to 2 June and celebrated its twentieth anniversary. As was the case in 2008 when the Japanese sought to create synergy between the fourth TICAD and the G8 summit in Toyako, Abe came to Loch Erne and trumpeted Japan’s pledge to support African growth through public and private funds totaling ¥3.2 trillion over the next five years.

Although the G8’s focus was on economic issues, political and security issues continued to feature, particularly North Korea. In line with his predecessors, Abe succeeded in including mention in the final communiqué of human rights issues and specifically the abductions of Japanese citizens by North Korean agents.

Finally, summitry concerns the bilateral as well as the multilateral and Abe conducted several meetings with his G8 counterparts, including Cameron. Since the beginning of the year, the G8 summit had been the target for the creation of a comprehensive agreement promoting UK-Japan intelligence sharing and the joint development of defence equipment. The agreement endorsed at Loch Erne allows Japan to provide the UK with defence technology despite fears that this contradicts the principles that have historically banned the export of weapons and related technology.

Abe’s Evolving Foreign Policy

Although we may be some way short of a fully-fledged, eponymous foreign policy doctrine, Abe’s participation in the Loch Erne Summit brings both sides of his personality and policy platform into relief and reflects the wider picture of his evolving foreign policy.

On the one hand, the pragmatic approach that dominated at Loch Erne is reflected elsewhere. ‘Abenomics’ continues to dominate debate surrounding the administration and has resulted in some successes so far (the yen falling to below ¥100 to the dollar, the surge in the Nikkei and annualized growth figures of 4 per cent in the first quarter of 2013). However, there are considerable challenges ahead and ultimately, consumption tax increases and cutbacks to welfare and government will also be necessary to reduce Japan’s debt. There will also be considerable resistance to structural reform of the Japanese economy, chiefly from within the LDP and the sections of Japanese society that have traditionally supported it.

On the other hand, and although these challenges require the full attention of the Abe administration and are the ones that the Japanese electorate prioritized in recent elections, the nationalist approach that emerged during this year’s G8 discussions is also in evidence in a number of areas. For example, the LDP’s plans for constitutional revision have received a great deal of attention, especially since the release of a draft constitution in April 2013 that seeks to make the Emperor the head of state, rename the Self-
Defence Forces, recognize the right of collective self-defence, and prioritize ‘order’ and ‘the public good’ over ‘fundamental human rights’.

In addition, there has already been discussion of Japan exercising a preemptive strike capability under the medium to long-term New Defence Programme Outline that is currently being prepared for the end of 2013 to replace that of the previous Democratic Party of Japan government. This ‘would allow Japan’s Self-Defense Forces to launch a pre-emptive missile strike at an enemy’s military target when an imminent attack on Japan from that specific site is confirmed’.

Similarly, Abe appears to be taking a more robust approach towards China by resurrecting the containment strategy known as ‘values-oriented diplomacy’ and the ‘arc of freedom and prosperity’ from his first administration. Already, Abe has called for a similar Democratic Security Diamond that bring together the democracies surrounding China of Japan, the US, Australia and India with their shared values of democracy, the rule of law, and respect for human rights (similar to the shared values Japan has stressed lie at the heart of the G8 and provide the ideological glue that can keep it together). In addition, the Abe administration has made approaches into Southeast Asia, particularly Vietnam and the Philippines, who also have territorial disputes with China in the South China Sea, which Abe has provocatively described as ‘Lake Beijing’ and connected to the East China Sea and Senkaku Island dispute.

Summary
So, we return to the same question of which Abe – pragmatist or nationalist – will prevail?

To summarize the main points of this paper:

- The G8 as a forum of global governance has mattered and will continue to matter to Japan for a number of reasons outlined above. It will also continue to provide clues as to Japan’s broader foreign policy goals and behavior.

- Abe’s evolving foreign policy displays both these pragmatic and nationalist tendencies but they are not mutually exclusive; rather, they are mutually reinforcing.

To embellish the final point, as was seen at Loch Erne, both sides of Abe’s personality and policy platform can co-exist. In fact, they inform each other. Japan cannot provide a strong regional and global presence unless it emerges from its long-running economic malaise. For the time being and foreseeable future, it will be these challenges that the Abe administration should focus its energies and political capital on at the expense of settling postwar accounts as this commands little approval or acceptance within Japanese society, the Asian region or international society.

Further Reading


Hugo Dobson is Professor of Japan’s International Relations in the National Institute of Japanese Studies and School of East Asian Studies at the University of Sheffield. He may be contacted at h.dobson@sheffield.ac.uk