

# **Japan's FTA Politics and the Problem of Agricultural Trade Liberalisation**

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### **Introduction**

In 1999, Japan adopted a dual trade policy of seeking trade liberalisation through both multilateral and bilateral trade negotiations.<sup>1</sup> Since 2002 and the Japan-Singapore Economic Partnership Agreement (JSEPA), FTAs have superseded the WTO as the main vehicle for Japanese trade liberalisation. Japan has signed FTAs with eight countries, chiefly in Southeast Asia. It is in the midst of FTA negotiations with a number of others, including Australia and Vietnam, and is nearing an agreement with ASEAN.

Various explanations have been offered for the diversification in Japan's trade strategy.<sup>2</sup> The most

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<sup>1</sup> The 1999 White Paper on Trade was the first in which the Japanese government discussed its new FTA strategy.

<sup>2</sup> See, for example, Mireya Solis, 'The Political Economy of the Japan-Mexico EPA: How Does a Cross-Regional Initiative Affect the Future of Japan's Regional Integration Efforts?', <http://www.rieti.go.jp/en/events/bbl/05070401.html>; Naoko Munakata, 'Evolution of Japan's Policy Toward Economic Integration' RIETI Discussion Paper Series 02-E-006, December 2001, <http://www.rieti.go.jp/jp/publications/dp/02e006.pdf>; Saadia M. Pekkanen, 'Bilateralism, Multilateralism, or Regionalism? Japan's Trade

convincing is that the switch was defensively motivated. While initially slow to jump on the FTA bandwagon, expansion of FTAs in the world market forced Japan to change its approach to one of promoting FTAs in order not to be left behind in the trend towards regional and bilateral trade agreements.

Japan's burst of FTA activity should not be interpreted as a sign that it is ready to liberalise its agricultural trade sector. It is well known that agriculture has interfered with the implementation of Japan's FTA strategy, just as it has with its WTO trade strategy. Agriculture has consistently been the major sticking point in Japan's negotiations with partner countries, not only delaying their completion but in some cases bringing them to an abrupt halt.

Difficulties over agriculture have meant that the degree of trade liberalisation for Japan is lower than for partner countries.<sup>3</sup> Developing countries such as Mexico, Thailand, the Philippines and Malaysia have accepted the uneven terms in the expectation of benefits in areas such as aid, investment and technical cooperation.<sup>4</sup> Japan has used a variety of mechanisms to limit the extent of agricultural concessions 'including outright exclusions, renegotiations, and tariff rate quotas'.<sup>5</sup> On balance, FTAs have had a limited although positive effect on agricultural trade liberalisation.<sup>6</sup>

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Forum Choices', *Journal of East Asian Studies*, Vol. 5, No. 1, 2005, pp. 77-103.

<sup>3</sup> Itō Takatoshi, 'FTA Teiketsu no tame Seiji Ketsudan o Isoge' ['Hurry the Political Decisionmaking Process for Concluding FTAs'], *Shūkan Tōyō Keizai*, 9 June 2007, p. 9.

<sup>4</sup> Kimura Fukunari has also commented that 'Japan's FTA partners have so far accepted the uneven terms because of Tokyo's strong bargaining power and the expectation that agreements could lead to increased economic cooperation and investments from Japan'. Quoted in *The Japan Times*, 13 October 2007.

<sup>5</sup> Solis, 'The Political Economy of the Japan-Mexico EPA', <http://www.rieti.go.jp/en/events/bbl/05070401.html>.

<sup>6</sup> As Ando and Fukunari observe, FTA agreements have been shown to have 'a certain degree of liberalizing effects...on the Japanese agricultural

Many interpret the start of Japan's FTA negotiations with Australia as a significant turning point in its FTA strategy. A bilateral agreement with Australia would be Japan's first with an industrialised country and major agricultural exporter. Not only do agricultural products account for more than 20 per cent of total Japanese imports from Australia, but most of the trade is composed of so-called 'important items' (*jūyō hinmoku*) protected by high tariffs such as beef, dairy products, wheat and sugar.<sup>7</sup> The most important farm exports for Australia are, therefore, amongst the most highly protected by Japan. Along with rice, these products are state-traded (except for beef), and so are shielded by the institutionally vested interests of the Ministry of Agriculture, Forestry and Fisheries (MAFF) and the Agriculture and Livestock Industry Corporation (ALIC), which channel profits from international purchasing into subsidies for the local industries.

These features of Australia-Japan agricultural trade make negotiations with Australia significantly different from those with Mexico or with Southeast Asian countries. As Suzuki has warned:

If highly-tariffed agricultural products such as beef, dairy products and wheat, which account for a significant part of the total amount in imports to Japan from Australia, are excluded [from liberalisation], the EPA could not meet the requirements of GATT Article 24. In addition, in contrast to negotiations with developing countries, in the negotiations with Australia, aid cannot be an option to avoid tariff reduction on important items. That is, Japan's conventional strategy is not available. This means that the options left for Japan are to give up beef,

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sector.' Mitsuyo Ando and Fukunari Kimura, 'Japanese FTA/EPA Strategies and Agricultural Protection', Paper prepared for presentation to the Tenth Convention of the East Asian Economic Association, Beijing, 18-19 November, 2006, p. 2.

<sup>7</sup> 'Nichi-Gō EPA de Nōgyō wa Kaimetsu? "Gote ni Mawatta" Nōsuishō no Ukatsu' ['Is the Japan-Australia EPA Devastating Agriculture? Mistake of the "Careless" MAFF'] *Shūkan Tōyō Keizai*, 12 January 2007, p. 34.

sugar or wheat – in any case, the negotiations will force Japan to sacrifice an important agricultural product.<sup>8</sup>

The following section examines the domestic politics of FTAs in Japan. It argues that FTAs are theoretically a more effective instrument of Japanese agricultural trade liberalisation than the WTO because FTAs reshape the domestic politics of Japanese trade in ways that are conducive to further market opening. FTAs do this by altering the domestic politics of trade policymaking on the demand side. I use a public choice framework to illuminate the changes in demand-side dynamics.

The paper then analyses the obstacles FTAs face in the policymaking process, which prevent the altered demand-side dynamics from necessarily delivering market-opening outcomes. This section explains why FTAs end up being only moderately effective in liberalising Japanese agricultural trade.

### **A Public Choice Explanation of Japanese Agricultural Protection**

Public choice theory provides a textbook explanation of Japanese agricultural protection as a typical case of concentrated benefits versus diffused costs. A very small number of farmers receive enormous benefits in terms of increased income from agricultural production, which represents a relatively large proportion of their total agricultural income. On the other hand, the costs of protection in terms of higher food prices are spread across the broad mass of consumers and represent a relatively small proportion of total household expenditure. So, for producers, the benefits of agricultural protection are visible, concentrated and immediate, while the costs to consumers are diffused, delayed and hidden. Consequently, farmers have a strong incentive to engage

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<sup>8</sup> Professor Nobuhiro Suzuki of the Graduate School of Agricultural and Life Sciences, University of Tokyo, quoted in 'Nichi-Gō EPA de Nōgyō wa Kaimetsu?', p. 35.

in rent-seeking behaviour - to invest time, money and resources in lobbying and influencing politicians to maintain agricultural protection. Consumers, on the other hand, are not sufficiently motivated to lobby for the removal of trade distortions.

On the supply side, Japanese politicians seeking to gain and retain power have an incentive to supply agricultural protection in exchange for votes, monetary donations, campaign support and other forms of political backing from farmers and their organisations. In comparison, politicians have very little to lose by not supporting the interests of consumers who do not organise on issues of food prices. Thus, for politicians, the marginal political benefit (MPB) exceeds the marginal political cost (MPC) of maintaining agricultural protection. Opposition from other potential losers such as business has traditionally muted because the costs of agricultural protection to individual firms have not been sufficiently concentrated, direct and immediate for them to mobilise strongly against it.<sup>9</sup> Certainly the degree of business opposition has not disturbed the prevailing political calculus of politicians.

FTAs alter these domestic demand and supply-side dynamics in ways that are theoretically unfavourable to the maintenance of Japanese agricultural protection. The prospect of FTAs (including amongst Japan's trading partners) creates a wider web of domestic interests committed to agricultural trade liberalisation. On the demand side, this wider web consists of special business interests that run directly counter to special agricultural interests. FTAs thus add business as an important countervailing element on the demand side and produce a much more balanced domestic political equation of 'business versus agriculture'. The following section

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<sup>9</sup> When these costs have been immediate and concentrated on Japanese manufacturers (as in China's imposition of 100 per cent tariffs on imports of Japanese cars, mobile phones and air conditioners in 2001 in retaliation against Japan for invoking WTO safeguards against Chinese vegetable and *tatami* rush imports), business has strongly and successfully pressured the government for a change in policy.

analyses why FTAs generate such heightened opposition to agricultural protection from business.

### **The Significance of FTAs to Japanese Business**

The existing literature on agricultural market opening in Japan identifies the WTO as an effective instrument of agricultural trade liberalisation because of trade-offs between agriculture and business in the sense that the gains to business offset the losses to agriculture.<sup>10</sup> I argue, however, that while the WTO may have a much broader agricultural trade reform agenda and may be a source of *gaiatsu* (external pressure) to open Japanese agricultural markets, FTAs are a much more potent source of leverage to open agricultural markets because they generate strong *naiatsu* (domestic pressure) against agricultural protection. This *naiatsu* comes from special business interests that demand an end to agricultural protection for several reasons.

First, FTAs are increasingly seen as a preferable option to the WTO's multilateral scheme for expanding Japanese business opportunities abroad because of speed and feasibility. The WTO can deliver many of the benefits of FTAs, but FTAs promise many of the same benefits in a shorter time frame. The gains to business from FTAs are, therefore, more immediate than under the WTO, where negotiations are characterised by considerable delays in reaching final settlements.

Second, FTAs bring more concentrated and direct benefits to firms operating in specific business fields whereas the benefits from the WTO tend to be more diffused across the wider business community.<sup>11</sup> In the frontline of

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<sup>10</sup> Christina Davis, *Food Fights Over Free Trade: How International Institutions Promote Agricultural Trade Liberalization*, Princeton, Princeton University Press, 2003.

<sup>11</sup> Pekkanen comments that 'it is not particularly surprising to note that organized special business interests benefit from preferential arrangements. What is of greater interest is that such forums deliver immediate, direct, and concentrated benefits to the sectors concerned.

potential beneficiaries from FTAs are firms that manufacture goods for export and general trading companies, which have a relatively high dependence on foreign trade, and which act as major importers of energy goods, minerals and raw materials into Japan as well as exporters of finished goods. The general trading companies are also prime movers of commodities within Japan's intra-regional networks of production and distribution.

Amongst Japanese manufacturers, firms in the steel, transport machinery and electronics sectors are likely beneficiaries of FTAs.<sup>12</sup> As Pekkanen observes, perhaps the most important factor behind Japan's choice to pursue FTAs...[is]

specificity of market benefits – virtues seen to be lacking in a multilateral forum, especially by businesses interested in the speedy protection of market access and investment. It is not a surprise that Japanese automobile and steel makers, which constitute some of Japan's most formidable global competitors, are behind the turn to FTAs....Indeed officials acknowledge that the Japanese-Mexican FTA agreement was pushed and applauded by the Japanese automobile as well as electronics industry.<sup>13</sup>

Among the exports from Japan to Mexico, for example, machinery products accounted for 75 per cent (in 2002), with tariff abolition expected to contribute to a significant

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Key economic sectors need market access and they need their investments protected in foreign settings. FTAs, it appears, are the speediest means of achieving these twin goals...Clearly at this point in time, business and government bodies both perceive that Japanese interests are far too diffused, and the results slow, in painstaking multilateral negotiations involving the economic cross-linkages that are a hallmark of GATT/WTO rounds.' 'Bilateralism', p. ?

<sup>12</sup> Kawasaki points out that for Japan, the greatest growth from an East Asian Free Trade Area would be in the production of transport machinery. Kawasaki Kenichi, 'Ajia Shokoku to no FTA ni yoru Keizai Kōka' ['The Economic Impact of FTAs with Asian Countries'], *Nōgyō to Keizai*, Vol. 70, No. 10, August 2004, p. 60.

<sup>13</sup> 'Bilateralism', p. ?

expansion of Japanese exports to the country.<sup>14</sup> The First Report of the Working Group on Economic Partnership Agreements and Agriculture of the Expert Committee on Reforms Addressing Globalization of the government's Council on Economic and Fiscal Policy (CEFP) pointed out that an EPA with the United States would yield obvious benefits in terms of lower tariffs on Japanese exports of products such as commercial vehicles, passenger cars, thin-screen TVs and other items of concern to Japanese firms.<sup>15</sup> In contrast, former Administrative Vice-Minister of Foreign Affairs until August 2005, Tanaka Hitoshi, pointed out that domestic industries such as car exporters 'would suffer disadvantage as a result of trade liberalisation under the WTO'.<sup>16</sup>

Other special industry interests motivated to pursue FTAs are those operating in the resources sector. Increasingly Japanese high natural resource-use industries are concerned about guaranteed and stable access to mineral and energy resources in light of increasing competition with China. The Australia-Japan FTA, for example, is of vital interest to firms that tap into and rely on Australian natural resources for manufacturing and energy generation purposes. As Hiroyuki Kanehara, Manager of the International Section, Nippon Keidanren, has pointed out, 'the EPA [with Australia] is important for the stable supply of natural resources and energy'.<sup>17</sup>

Third, the business agenda encompasses more than just trade. As the First Report of the CEFP observes: 'An EPA makes it possible to form closer trade and investment ties

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<sup>14</sup> Honma Masayoshi, 'Nihon Nōsei no Taigai Seisaku – WTO to FTA – ' ['External Policies of Japanese Agriculture – WTO and FTA –'], in *Nōsei Kaikaku to Kore Kara no Nihon Nōgyō* [Agricultural Policy Reform and Japanese Agriculture After This], Nihon Keizai Kenkyū Sentaa, March 2005, p. 21.

<sup>15</sup> 'Acceleration of Economic Partnership Agreements and Strengthening Agricultural Reform', First Report of the Working Group on Economic Partnership Agreements and Agriculture, 8 May 2007, p. 6.

<sup>16</sup> Quoted in *Nihon Keizai Shinbun*, 25 July 2007.

<sup>17</sup> 'Nichi-Gō EPA de Nōgyō wa Kaimetsu?', p. 34.

with the partner country which would be difficult to achieve through multilateral negotiations.<sup>18</sup> Firms want better conditions for Japanese business in partner countries in terms of investment, government contracts, procurement and so on.<sup>19</sup> Nippon Keidanren's Kanehara has volunteered that 'the EPA [with Australia] will provide Japanese firms with business opportunities in government-related projects in Australia'.<sup>20</sup> Moreover, because Japan's bilateral agreements are Economic Partnership Agreements (EPAs) not FTAs, they extend to more comprehensive agreements that deal with the free movement of labour, capital and services as well as goods.<sup>21</sup>

Fourth, FTAs can be seen as the building blocks of regionally integrated business networks. As Kimura notes, 'FTAs are expected to contribute to the development of international networks of production and distribution with Japanese firms as their core'.<sup>22</sup>

Fifth, procedures for developing rules in so-called 'new areas' such as labour standards, competition policies and the environment are more feasible in FTA negotiations partly due to the increasing number of WTO member countries. The WTO finds it difficult to deal with these new areas because of growing divisions between developed and developing countries. The JSEPA, for example,

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<sup>18</sup> 'Acceleration of Economic Partnership Agreements', p. 3.

<sup>19</sup> Fukui Seiichi, 'Nikokukan Keizai Rentai Kyōtei (EPA) Kōsō no Keii to Saikin no Jōsei' ['Progress and the Current Situation with Bilateral Economic Partnership Agreements (EPAs)'], *Nōgyō to Keizai*, Vol. 70, No. 10, August 2004, p. 16.

<sup>20</sup> 'Nichi-Gō EPA de Nōgyō wa Kaimetsu?', p. 34.

<sup>21</sup> Fukui, 'Nikokukan Keizai Rentai Kyōtei', p. 15.

<sup>22</sup> Kimura Fukunari, 'Tsuyoi Seijiteki Ishi o Motte Susumeyo - Jiyū Bōeki Kyōtei Teiketsu no Jūyōsei to Nihon no Nōgyō Mondai' ['Work On it With Strong Political Will - The Importance of Concluding FTAs and Problems of Japanese Agriculture'], *Nouvelle Époque*, No. 21, 20 November 2003, <http://www.kiser.or.jp/press/data/021.pdf>.

'addressed the framework of competitiveness policies, which had not been agreed in WTO negotiations.'<sup>23</sup>

Last but not least, the opportunity cost of being excluded from FTA networks is potentially huge for many Japanese firms. This is due to the principle of discrimination: as IPE analysts so often remind us, FTAs are preferential trading agreements that discriminate against non-signatories. They provide a direct contrast with the WTO that works on the principle of non-discrimination embodied in unconditional MFN treatment.

Being left out of FTA networks can impose concentrated costs on specific industry sectors. These costs are direct, immediate and identifiable. Inaction as other countries negotiate FTAs can result in an erosion of Japan's competitive position in particular markets.<sup>24</sup> Japanese firms were in an increasingly unfavourable situation as a result of the growth of FTAs in the international market, particularly since the mid-1990s.<sup>25</sup> The First Report of the CEFPP devotes a whole section to analysing the 'Prevention of disadvantages from lagging behind FTA and EPA negotiations', pointing out that when Japan lags behind, 'it often ends up disadvantaged in competition with third countries that have gone ahead and concluded an FTA.

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<sup>23</sup> Urata Shūjirō, 'Gurōbarizeeshyon to Zōka suru FTA' ['Globalisation and Expansion of FTAs'], *Ajia Kenkyū*, December 2001, pp. 10-11. In fact, the JSEPA 'included areas such as mutual approval of standards, the conversion of trade procedures into electronic modes, electronic commerce, property rights, competition policies, environmental policies, mobility of people and human resource development, as well conventional areas such as abolition of trade and non-trade barriers for goods and services. Under such a comprehensive liberalisation agenda, companies in Japan and Singapore stood to gain business opportunities without borders.' Ozaki Haruo, 'Joron: Sekkyokuteki "Kaihō" o Nihon no FTA Seisaku no Hashira ni' ['Introduction: Positive Market Opening as the Core of Japan's FTA Policies'], *Ajia Kenkyū*, December 2001, p. 2.

<sup>24</sup> See Australian Government, Department of Foreign Affairs and Trade, 'Advancing the National Interest: Australia's Foreign and Trade Policy White paper, [http://www.dfat.gov.au/ani/chapter\\_4.html](http://www.dfat.gov.au/ani/chapter_4.html).

<sup>25</sup> Fujiwara Jun, 'Ajia ni Okeru Jiyū Bōeki Kyōtei no Kadai' ['Issues of Free Trade Agreements in Asia'] *Zenei*, Vol. 761, March 2003, p. 160.

This is the trade diversion effect.<sup>26</sup>

Mexico was the first object lesson in the trade diversion effect. As Honma explains, 'the Japan-Mexico EPA was motivated by the need to avoid the demerits of being excluded from trade networks. In addition to the 1994 NAFTA, Mexico had concluded FTAs with other 32 countries including the EU – the countries with which Mexico had concluded FTAs accounted together for 60% of the world's GDP.<sup>27</sup> The market situation for Japanese firms became tougher and tougher without a Japan-Mexico FTA, not only for Japanese exporters but also for Japanese corporations operating in Mexico.<sup>28</sup> Japan's share of total Mexican imports declined from 6.1 per cent in 1996 to 4.8 per cent in 2001.<sup>29</sup> Car manufacturers were particularly affected. With the tariff rate for automobiles exported to Mexico at 20-30 per cent, which was exempted for Mexico's FTA partners, Japan could not produce cars in Mexico profitably because it had to import parts under tariffs.<sup>30</sup> In addition, 'Japan could not bid for government projects in Mexico as eligibility was limited to countries that had concluded FTAs with the country.'<sup>31</sup>

Mexico was not the only case. The First Report cites 'the case of Chile, where the Republic of Korea was ahead of Japan in forming an FTA. As a result, Chile's imports from Japan went flat while its imports from the Republic of Korea grew rapidly. In early April 2007, the United States and Republic of Korea concluded their FTA negotiations,'<sup>32</sup>

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<sup>26</sup> 'Acceleration of Economic Partnership Agreements', p. 4.

<sup>27</sup> Honma, 'Nihon Nōsei no Taigai Seisaku', pp. 19-20. As Urata points out, 'the opportunity cost of being excluded from regional integration increases as the number of member countries increases.' Gurōbarizeeshyon, p. 10.

<sup>28</sup> 'Acceleration of Economic Partnership Agreements', p. 4.

<sup>29</sup> Yamashita Kazuhito, *Kokumin to Shōhisha Jūshi no Nōsei Kaikaku: WTO, FTA Jidai o Ikinuku Nōgyō Senryaku [Agricultural Policy Reform that Seriously Considers the People and Consumers: An Agricultural Strategy That Survives the WTO, FTA Era]*, Tokyo, Tōyō Keizai Shinpōsha, 2004, p. p. ?

<sup>30</sup> Honma, 'Nihon Nōsei no Taigai Seisaku', p. 20.

<sup>31</sup> Honma, 'Nihon Nōsei no Taigai Seisaku', p. 20.

<sup>32</sup> 'Acceleration of Economic Partnership Agreements', p. 4.

a deal that has 'shocking' implications for Japan.<sup>33</sup> South Korean exports into the US domestic markets will now have preferential access to the US market ahead of their main competitors, principally Japan and China. Japanese firms producing commercial vehicles, passenger cars and thin-screen TVs, on which the United States imposes tariffs, will be the most affected.<sup>34</sup>

The concentrated benefits of FTAs to special business interests and the concentrated costs of not signing them motivate the Japanese business community to press for FTAs with particular countries and to demand an end to agricultural protection as the chief obstacle to the successful conclusion of these agreements. Japanese business is demanding reform of agricultural structure to lay the groundwork for agricultural trade liberalisation. Kitashiro Kakutarō, head of the Japan Association of Corporate Executives, or JACE (Keizai Dōyūkai) argues, 'FTAs are supposed to "prime the promotion of structural reforms in fields such as agriculture".'<sup>35</sup> A 2001 'Survey of Individual Firms' done by the Nihon Keizai Shinbunsha found that more than 30 per cent of firms expected FTAs to 'facilitate structural reforms in economic sectors with less competitiveness'.<sup>36</sup> Honma has also observed that 'while consumers in Japan may be relatively tolerant of agricultural protection because of their high incomes, industries now are not because the opportunity for growth through globalisation is being blocked by such a small sector sharing just 1 per cent of GDP. Thus, the problem of agricultural protection is not high domestic food prices but the loss of growth opportunities. Such frustrations shall be bound into a power to reduce agricultural protection.'<sup>37</sup>

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<sup>33</sup> Itō, 'FTA Teiketsu no tame Seiji Ketsudan o Isoge' p. 9.

<sup>34</sup> 'Acceleration of Economic Partnership Agreements', p. 6.

<sup>35</sup> Quoted in *Nikkei Weekly*, 15 December 2003.

<sup>36</sup> Ozaki, 'Joron', p. 2.

<sup>37</sup> Personal communication, 14 October 2007.

### **Intervening Policymaking Structures: An Institutional Approach**

The changed dynamics on the demand side theoretically alter the supply-side dynamics, namely the predisposition of politicians to continue to supply agricultural protection. Increased opposition to agricultural protection from special business interests theoretically raises the MPC of supplying protection. Pekkanen has predicted that the 'quick, fast and narrow' benefits to specific sectors of FTAs 'may force changes in usually highly protectionist sectors like agriculture.'<sup>38</sup>

In reality, however, structural obstacles in the Japanese policymaking process prevent altered demand-side dynamics from necessarily delivering market-opening outcomes. In public choice explanations of economic policy, the policymaking system is treated simply as a 'black box'. Special interests demand particular policies and politicians supply them based on their own rational, self-interested calculations of MPC and MPB.

Understanding why changes in the Japanese political equation on the demand side do not necessarily translate into policy changes on the supply side requires that we open this black box. We need to look into these intervening policymaking structures, thus exposing some of the over-simplifications of the public choice explanation of Japanese agricultural protection.

I argue, as institutionalists do, that state institutions influence how political demands are processed and therefore shape policy outcomes. The most relevant structural feature of the Japanese policymaking system that determines the delivery of public policy outcomes on FTAs is vertical segmentation along sectoral (special interest) lines. This means that for industry and agriculture, demand and supply-side actors in each sector operate together within traditionally closed policy networks or subgovernments (the agricultural policy subgovernment and the industrial policy subgovernment).

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<sup>38</sup> 'Bilateralism', p. ?

In the case of agriculture, farm politicians in the ruling Liberal Democratic Party (LDP), MAFF bureaucrats, and key industry representatives (the executives of the main peak agricultural organisations), who share a strong common interest in the promotion of domestic agriculture, have the primary role in *making policy for that sector including agricultural trade policy*. The industrial policy subgovernment, on the other hand, consists of bureaucrats from the Ministry of Economy, Trade and Industry (METI), LDP politicians with close ties to industry and executives of peak business organisations. They seek to promote the interests of Japanese industry, not only in the domestic market but also in markets abroad. Significantly, the bureaucrats within these policy subgovernments exercise policymaking authority and in this sense also act as supply-side actors although not according to the same politically self-interested calculus of politicians.<sup>39</sup>

The industry and agricultural policy subgovernments are structurally equal within the Japanese policymaking system; they exercise no rights of veto over each other's policies and legislation. Within these subgovernments, decisions are made by adjusting the interests of the actors through consensus decision-making. It is a bottom-up process: all major policies and legislation are subject to prior scrutiny and approval by the LDP's Policy Affairs Research Council (PARC) committees and Executive Council before being passed on to the Cabinet for ratification. Once ratified, bills are submitted to the Diet. The PARC committees, in particular, are the primary locus of policymaking by special interest politicians. The LDP's larger Diet membership is obligated to agree with bills and policies approved by the PARC committees and Executive Council because this approval is subject to unanimous

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<sup>39</sup> I argue in *Japan's Interventionist State*, for example, that they operate according to an intervention-maximising calculus. See Aurelia George Mulgan, *Japan's Interventionist State: The Role of the MAFF*, London and New York, Routledge, 2005.

agreement. As a result, METI has no choice but to comply with the intentions of agriculture-related Diet members even on matters concerning WTO and FTA negotiations. Otherwise, they would face strong opposition from farm politicians in areas relating to industry.<sup>40</sup>

The prime minister and his administration made up of key LDP and coalition party executives, the Prime Minister's Official Residence (Kantei), Cabinet Secretariat, Cabinet Office and Cabinet Office councils including the CFP lack strong top-down authority and inter-sectoral coordination ability. Certainly it is insufficient to override the independent policymaking authority of the subgovernments, the vertical alliances that they form and the policy stalemates they engender, particularly if the subgovernments firmly oppose the prime minister's policy. This lack of strong top-down authority and inter-sectoral coordination ability means that FTAs make slow progress because of the clash of interests between agriculture and industry. The lack of coordination power of the prime ministerial executive also limits the possibilities for trade offs between industry and agriculture.

International trade negotiators have observed that when they negotiate with Japan, they find themselves dealing with an internally divided set of policymakers. The current United States Trade Representative (USTR), Wendy Cutler, for example, in expressing her reluctance to engage with Japan in FTA negotiations, commented that 'Japanese government ministries are often not unified over policy'.<sup>41</sup> Each ministry, including the Ministry of Foreign Affairs (MOFA), which is concerned with the wider political, diplomatic and strategic implications of Japan's involvement in bilateral and regional FTAs, has its own taskforces and sections dealing with FTAs. Bureaucrats from each of the ministries are directly involved in trade

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<sup>40</sup> Yamashita Kazuhito, 'Nōsei no Seiji Hikeizaigaku – Nōgyō Biggu Ban no Kanōsei' ['Political Non-Economics of Agricultural Policies - Possibilities for an Agricultural Big Bang'], in *Nōsei Kaikaku*, p. 52.

<sup>41</sup> Associated Press, 19 October 2007.

negotiations, which makes them key players in reaching final agreements.

In consequence, Japan does not have one FTA strategy or policy; it has several. There is no single body producing trade policy for Japan. Nor is there an independent body capable of coordinating and unifying conflicting domestic interests on trade issues.

Prime Minister Koizumi took initial steps in this direction in order to make progress on FTAs. In 2002, he set up a special party committee on FTAs (FTA Tokumei Iinkai) chaired by his appointee as PARC Chairman, Nukaga Fukushirō, a veteran commerce and industry politician. The committee's task was to work with METI to formulate basic party policy on FTAs,<sup>42</sup> but its capacities were inadequate to override the vertical divisions within Koizumi's own government. In late 2003, the Kantei announced a plan to inaugurate a joint conference of related government ministries to promote FTA talks with other countries. The aim was to facilitate greater coordination amongst the relevant ministries on FTAs as well as to resolve inter-ministry differences that were delaying a positive outcome from negotiations with Mexico. In March 2004, a new Council of Ministers Concerned With the Promotion of Economic Partnerships (Keizai Renkei Sokushin Kankei Kakuryō Kaigi) was charged with promoting the formation of FTAs. Chaired by Prime Minister Koizumi, the council included all the relevant cabinet ministers. A subsequent plan to appoint a new minister in charge of FTAs was rejected by the prime minister who declared that he would take the lead in making relevant ministries cooperate, playing the role of FTA minister himself.<sup>43</sup> In December 2004, his administration adopted its first set of basic guidelines for

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<sup>42</sup> Several comments critical of the government's handling of this issue were made at a December 2003 meeting of the panel, such as "the government lacks an FTA strategy" and "its response is haphazard". *Asahi Shinbun*, 4 December 2003.

<sup>43</sup> *Nihon Keizai Shinbun*, 21 December 2004.

signing FTAs, which called on “all ministries and agencies to make all-out joint efforts” to realize the early conclusion of...EPA and FTA talks with Thailand, Malaysia and South Korea’.<sup>44</sup>

However, the problem of a divided Japanese government on FTA issues has not been fully overcome. Nippon Keidanren has proposed creating ‘a council on external economic strategy, stressing the need for a unified body going beyond the wall of government agencies.’<sup>45</sup>

Professor Urata Shūjirō of the Graduate School of Asia-Pacific Research at Waseda University has called for the Kantei ‘to take the lead in determining the nation’s external economic strategy while removing the conventional vertically segmented system of government administration.’<sup>46</sup> Former MOFA Administrative Vice-Minister Tanaka has proposed that ‘the ruling and opposition camps should cooperate to create a mechanism, under which an industry-government-academia body composed of private citizens from the agricultural and manufacturing sectors propose an EPA strategy with a view to the future of Japan.’<sup>47</sup>

### **Diffused Gains and State Interests**

Both the Koizumi and Abe administrations, seeking to advance state interests, were highly responsive to the prospect of diffused gains from FTAs across wider areas of the economy and polity. They represent the wider web of domestic interests committed to agricultural trade liberalisation on the supply side. FTAs, for example, offer the prospect of major benefits in areas such as resource security,<sup>48</sup> consolidation of Japan’s broader political and

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<sup>44</sup> *Nikkei Weekly*, 27 December 2004-3 January 2005.

<sup>45</sup> *Yomiuri Shinbun*, 19 April 2007.

<sup>46</sup> *Yomiuri Shinbun*, 19 April 2007.

<sup>47</sup> Quoted in *Nihon Keizai Shinbun*, 25 July 2007.

<sup>48</sup> As the First Report points out: ‘A Japan-Australia EPA could be expected to contribute to the stable supply of natural resources, energy, and food, and to the promotion of industrial product exports. Such benefits to the Japanese economy as a whole should be clarified in order to obtain public

security relationships with particular countries including Australia and the United States, and considerations relating to competition with China for regional economic and political leadership, including over the regional integration process in East Asia.<sup>49</sup>

These diffused gains arise because FTAs are about a lot more than trade. FTAs have political and diplomatic effects, as well as economic effects.<sup>50</sup> They are about the totality of relationships between countries and also within regions. The First Report, for example, pointed out that an EPA with the United States would invigorate trade and investment in both countries, as well as further strengthening close relations between the two countries.<sup>51</sup> Former Prime Minister Abe provided a lot of personal impetus behind the initiation of FTA talks with Australia because of his own private policy agenda that included encouraging expansion and diversification of relations with Australia. The prime minister was also highly apprised of the fact that FTAs with East Asian countries could be used as an engine of growth for the Japanese economy, including as one element of a strategy for dealing with the aging Japanese population and declining birthrate.

These aspects of FTAs are an additional factor helping to change the supply-side dynamics of agricultural protection, because although unconnected to a specific special-interest calculus, prime ministers and others recognise the value of FTAs for broader state interests. Indeed, these interests become important to the public debate about trade policy and can be used to gain public understanding of the need to sacrifice special interests, such as agriculture, and to counter national interest

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understanding of the matter.' 'Acceleration of Economic Partnership Agreements', p. 6.

<sup>49</sup> See Aurelia George Mulgan, 'Where Foreign Policy Meets Agricultural Trade Policy: The Australia-Japan FTA', forthcoming in *Japanese Studies*, May 2008.

<sup>50</sup> Honma, 'Nihon Nōsei no Taigai Seisaku', p. 20.

<sup>51</sup> 'Acceleration of Economic Partnership Agreements', p. 6.

arguments coming from the protectionist side, which stress food security and multifunctionality.

Recent changes in policymaking processes are also conducive to greater trade policy reform: the electoral system is no longer one that encourages politicians to appeal to a narrow constituency and hence it is much more difficult for politicians to operate exclusively as farmers' representatives; selection of LDP election candidates is much more centralised within the party executive, which helps to standardise the policy orientation of the party's Diet membership; the prime minister's right to initiate basic national in the cabinet policy has been recognised in law; cabinet functions have been strengthened; and the institutional structures supporting prime ministerial policy direction have been buttressed. Prime Minister Koizumi actively pursued structural reform of the policymaking system focussing on weakening the role of the LDP as representatives of special interests. Since Koizumi's administration, the agricultural policy subgovernment has found it harder to dominate the agricultural policymaking process and its previously pervasive influence over sectoral policy, including trade policy, is slowly being eroded.

Furthermore, on policy issues where industry and agriculture are in direct conflict, penetration of the top levels of government by business leaders and the generalised influence of industry over the ruling LDP through financial donations to the party are significant factors in their favour as is the disproportionate representation of industry on Cabinet Office councils. The creation of the CEFPP has provided an important additional channel of institutional access for the captains of industry and peak business associations, particularly as the CEFPP sets broad directions for government policy on the economy and the budget, and was pro-actively used by both Koizumi and Abe. Under Prime Minister Abe, for example, the CEFPP set up expert panels on EPAs and agricultural reform and these panels discussed what

measures should be taken. The First Report was the product of one of these panels.

However, despite all these developments, many of the institutional obstacles to FTAs remain. Even when the CEFP receives submissions from the MAFF, METI and MOFA on EPAs, these materials are always crafted from a ministry perspective. At the 7<sup>th</sup> February meeting this year, for example, the MAFF argued (with respect to the EPA with Australia) that: ‘The government should make very effort to obtain “exclusion” or “renegotiation” of “important items (rice, wheat, beef, dairy products and sugar)”’.<sup>52</sup>

To date, the political decisionmaking system has undergone insufficient structural reform in key areas such as the policy convention of prior scrutiny and approval by LDP policy committees over policy and legislation, and therefore remains insufficiently responsive to the shift in demand-side dynamics on FTA policy. On balance, agricultural trade policy reform in Japan is inhibited by path dependent outcomes generated by traditional institutional policymaking arrangements.

Even if the prime minister can now set broad policy directions, he cannot deliver desired outcomes simply through the exercise of executive power. This would inevitably produce a policy stalemate and considerable conflict between elements of the ruling LDP and the administration (as it did on postal reform). Nor can a strong push from business compensate for the weakness of the prime ministerial executive in exerting top-down authority and inter-sectoral coordination power. The requirement for moving forward on particular policy issues is still to achieve a workable consensus between the special-interest subgovernments and the administration.

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<sup>52</sup> ‘On EPAs in the field of agriculture, forestry and fisheries’, Ministry of Agriculture, Forestry and Fisheries, 7<sup>th</sup> February 2007, material presented to the Council on Economic and Fiscal Policy (CEFP), p. 3.

Because of business demands, the adjustment of domestic interests has become much more important on FTAs than in the WTO negotiations. FTAs have also seen much greater involvement of the prime ministerial executive on trade issues. This has meant that adjustment of opinions between the subgovernments and the prime ministerial executive is a more substantial element of the Japanese policymaking process than it has been in previous years. On agricultural trade policy, however, this inevitably produces some kind of compromise well short of free trade.