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Changing International Politics on the Korean Peninsula: from Geo-politics to Geo-economics

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Abstract

Traditionally, international politics on the Korean peninsula has been strategically oriented. Nevertheless, the axis of international politics on the Korean peninsula has shifted from geo-politics to geo-economics, due largely to the emergence of Chinese leader Xi Jinping. In this paper, the author explores reasons behind this policy change and its implications for the two Koreas, Japan, Taiwan, and Northeast Asia as a whole.

With his goal of making the Sino-U.S. condominium into reality through a new type of big powers relationship, Xi Jinping has decided to make a strategic move by shifting the axis of international politics on the Korean peninsula from geo-politics to geo-economics, exemplified by Xi's trip to Seoul and his agreement with Park Geun-hye to sign a mainland China-South Korea FTA by the end of this year. This strategic change is intended to enhance the era of the G2 in the coming APEC (Asia-Pacific Economic Cooperation) summit slated for November 10-11 this year through their joint promotion of the FTAAP (Free Trade Area of the Asia Pacific).

Keywords: Mainland China, South Korea, FTA, North Korea, Japan, Taiwan

I. Introduction

With the advent of the 21st century, we have witnessed mainland China and the United States taking two different approaches to deal with the changing international environment. While targeting realist goals, mainland China favors a liberalist approach, given the economization of international relations and regionalization of the world economy. In contrast, the U.S. emphasizes a realist approach dominated by security maneuvers. These include strengthening the U.S.-Japan security cooperation, the proposal of deploying the Terminal High-Altitude Area Defense (THAAD) system in South Korea,¹ and selling South Korea advanced F-35A jet fighters.² These have been realized in view of the rise in terrorist attacks since September 11, 2011, North Korea's provocations, and military threats, as well as the rise of mainland China and its strategic challenges to the existing regional security architecture while embracing economic goals from time to time.

Traditionally, international politics on the Korean peninsula has been strategically oriented. Nevertheless, the axis of international politics on the Korean peninsula has shifted from geo-politics to geo-economics, due largely to the emergence of Chinese leader Xi Jinping. In this paper, the author explores reasons behind this policy change and its implications for the two Koreas, Taiwan, and Northeast Asia

1. Jun Ji-hye, "Seoul won't oppose US missile interceptors," *The Korea Times*, September 2, 2014, <http://www.koreatimes.co.kr/www/news/nation/2014/09/116_164038.html>.

2. "S. Korea to pay US\$7 billion for 40 F-35A fighter jets," *The China Post*, September 25, 2014, <<http://www.chinapost.com.tw/asia/korea/2014/09/25/418000/S-Korea.htm>>.

as a whole.

II. Background behind Xi's *Démarche*

In order to shape a new type of major powers relationship with the U.S., mainland China's President Xi Jinping has decided to re-prioritize mainland China's policy toward Northeast Asia and to put geo-economics ahead of geo-politics in the formation of its Korean peninsula policy. This policy shift is not abrupt but rather is a result of the evolution of mainland China's grand strategy. It originated from Beijing's response to the changing international environment since the second half of the 1990s with an attempt to create an image of Sino-U.S. condominium in East Asia through big powers diplomacy and proactive economic diplomacy. So, this *démarche* can be regarded as part of the second phase of mainland China's grand strategy for the 21st century.

Given the 1995-1996 cross-Strait crisis and the 1997 Asian financial crisis, mainland China has inaugurated a series of diplomatic initiatives, including major powers diplomacy and a new security concept featuring multilateral cooperation in non-traditional security issues in addition to economic diplomacy revolving around the World Trade Organization (WTO) and free trade agreements (FTAs). The goals of those diplomatic initiatives were successfully achieved before 2010. Mainland China has replaced Japan's leadership in Asian economic integration through its proactive FTA with ASEAN, exemplified by mainland China's emergence as Taiwan (2003), South Korea (2004), Japan, and ASEAN's biggest trading partner since 2009.³ In

3. S. Pushpanathan, "The importance of private sector," *The Jakarta Post*, September 2, 2010, <<http://www.thejakartapost.com/news/2010/09/02/the-importance-private-sector.html>>.

2012, mainland China's contribution to Asia's economic growth was more than 50%.⁴ This regional leadership has given mainland China leverage to negotiate with the other two leading economic blocs in the world, NAFTA (led by the U.S.) and the European Union, on equal footing, given the regionalization of world economy. Additionally, the 2008 global financial *tsunami* has solidified mainland China's rise as an economic powerhouse and the growth engine of the world economy, and it has paved way for the formation of an era of the Group of Two (G2), led by Beijing and Washington. This period, between 1996 and 2012, can be regarded as the first phase of mainland China's grand strategy for the 21st century.

Against this background, when Xi Jinping ascended to the top leader position in March 2013, he believed that it was about time to launch the second phase of mainland China's grand strategy for this century. Unlike the first phase, which was designed to create an image of Sino-U.S. condominium in Northeast Asia, the primary goal of this new phase is to turn image of Sino-U.S. condominium into reality through a new type of major powers relationship featuring division of their sphere of influence and respect for each other's choice of development paths. Since he assumed the presidency, Xi Jinping more than once has mentioned that the Pacific Ocean is big enough to accommodate both mainland China and the U.S., the two biggest powers in the region, for joint development. On the other hand, in the opening ceremony of the sixth round of the Sino-U.S. Strategic and Economic Dialogue in July this year (2014), he warned that it would be a disaster for both countries and the whole world, should mainland China and the U.S. engage in confrontation.⁵

4. Liu Zhenmin, "Insisting on Win-Win Cooperation and Forging the Asian Community of Common Destiny Together," *China International Studies*, June 17, 2014, <http://www.ciis.org.cn/english/2014-06/17/content_6987936.htm>.

In addition, in order to build mainland China's global leadership in the capacity of the leading nation of the Global South, Xi Jinping is also keen to shape a new global financial order favorable to mainland China and developing economies through the creation of the New Development Bank, sponsored by the so-called BRICS countries that include Russia, India, Brazil and South Africa,⁶ and the Asian Infrastructure Investment Bank (AIIB), as well as the internationalization of *Renminbi*.⁷ Mainland China is actively promoting the use of its currency as an alternative to the dollar in global trade and finance. The British pound became the fifth major currency to be exchangeable directly for yuan in Shanghai in June 2014, joining the Australian and New Zealand dollars, the Japanese yen, and the U.S. dollar.⁸ The third component of this new grand strategy is to extend mainland China's clout through its vision for the New Silk Road, consisting of a "new Silk Road economic belt" and a "maritime Silk Road".⁹ The former is to be built on networks of high-speed

5. 〈習近平：中美對抗必成災難 大國關係首重互信〉，《亞太日報》(*Asia Pacific Daily*), July 9, 2014, <<http://www.apdnews.com/world/zhongmeiguanxi/2014/0709/58017.shtml>>.

6. "China, Asian nations sign on for \$57bn global bank," *The Australian*, October 25, 2014, <<http://www.theaustralian.com.au/news/world/china-asian-nations-sign-on-for-57bn-global-bank/story-e6frg6so-1227101449434>>.

7. 〈日本央行推動係統改革 為日圓全球化鋪路〉，《華爾街日報中文版》(*The Wall Street Journal*), August 26, 2014, <<http://cn.wsj.com/gb/20140826/ecb165833.asp>>; 〈中國銀行在法蘭克福正式啟動人民幣清算銀行服務〉，《亞太日報》(*Asia Pacific Daily*), August 27, 2014, <<http://www.apdnews.com/business/finance/2014/0827/78425.shtml>>.

8. "South Korea Agrees Won-Yuan Trading Link, RQFII Quota With China," *Bloomberg*, July 3, 2014, <<http://www.bloomberg.com/news/2014-07-03/won-yuan-trading-on-agenda-as-china-south-korean-leaders-meet.html>>.

9. Shannon Tiezzi, "China's 'New Silk Road' Vision Revealed," *The Diplomat*, May 9, 2014, <<http://thediplomat.com/2014/05/chinas-new-silk-road-vision-revealed/>>.

railways all the way to Europe through Central Asia and Russia plus a pan-Asia high-speed railway down to Southeast Asia, while the latter is perceived to be a strategic attempt to ameliorate relations with South and Southeast Asia. In the end, the New Silk Roads will make mainland China the hub of the global economy.¹⁰

III. Relations between Mainland China and North Korea in the Xi Era

When it comes to Northeast Asia, the salient example of this policy implementation was President Xi's July trip this year to Seoul. He became the first Chinese leader to visit South Korea ahead of visiting North Korea. Apparently, this has sent a strong signal to the Kim Jong-un regime that it can no longer hijack Beijing's policy toward the Korean peninsula. Mainland China's Korea policy is now defined by its own national interest. Kim Jong-un must behave well (no more provocations and be serious about abandoning its nuclear weapons) and play according to Beijing's rules, otherwise it is going to face a tough mainland China. Xi Jinping is more serious than previous Chinese leaders about the realization of the denuclearization of the Korean Peninsula, stressing that the long-stalled six-party talks are the best means to denuclearize the Korean Peninsula.¹¹ While attending his June 2013 summit in the Sunnylands with U.S. President Obama, Xi Jinping publicly joined in calls for North Korea to pursue denuclearization.¹²

10. Justyna Szczudlik-Tatar, "China's New Silk Road Diplomacy," *Policy Paper*, No. 34 (82), December 2013, <https://www.pism.pl/files/?id_plik=15818>.

11. "Xi emphasizes resumption of six-party talks," *The Korea Times*, October 14, 2014, <http://www.koreatimes.co.kr/www/news/nation/2014/10/116_166285.html>.

12. "The China-North Korea Relationship," *Council on Foreign Relations*, August 22, 2014, <<http://www.cfr.org/china/china-north-korea-relationship/p11097>>.

In fact, following North Korea's third nuclear test in February 2013, Beijing implemented new trade sanctions, reducing energy supplies to the Kim Jong-un regime, and calling for denuclearization talks with an attempt to press Pyongyang to return the six-party talks, which broke down in 2009 through a coalition of Beijing-Seoul-Washington. Rising labor costs in mainland China have hit low-end manufacturing hard recent years. Therefore, Chinese business owners have started to attract migrant labor from North Korea to slash their labor costs by one-third. It is estimated that as many as 120,000 North Korean workers were working in mainland China's hotels, construction, factories, and restaurants in 2012, most working in Dandong. This provides a major source of hard currency for the cash-hungry Kim Jong-un regime.¹³ Since February of this year, Beijing has put a limit on giving visas to North Korean workers.¹⁴ Nevertheless, North Korea has tried its best to woo mainland Chinese firms to hire more of its citizens by boasting of a well-educated pool of labor at a five-day trade fair that was held in the Chinese border city of Dandong recently. According to a North Korean booklet, North Korea's total population stood at 24.34 million last year. About 12.17 million people constituted a "prepared labor force that can adapt to randomly-chosen professions."¹⁵ Additionally, according to mainland China's customs statistics, the country ceased to provide North Korea with crude oil in the first six months of this year. In the past, mainland China regularly had provided 500,000 tons of crude oil to Pyongyang.¹⁶

13. "North Koreans Meet Chinese Demand For Cheap Labor," *Forbes*, April 27, 2012, <<http://www.forbes.com/sites/simonmontlake/2012/04/27/north-koreans-meet-chinese-demand-for-cheap-labor-report/>>.

14. "North Korean Workers in China Face Stepped-up Restrictions," *Radio Free Asia*, March 15, 2013, <<http://www.rfa.org/english/news/korea/workers-03152013155124.html>>.

15. "N. Korea hails labor force to woo Chinese firms," *The Korea Herald*, October 20, 2014, <<http://www.koreaherald.com/view.php?ud=20141020000940>>.

Mainland China also deliberately has frozen their economic activities in the *Weihua* and *Huangjinpings* islands special economic zones since last December. Sino-North Korea trade volume in 2013 totaled US\$ 6.5 billion,¹⁷ an increase of more than ten percent from 2012 and accounting for 89.1 percent of the North's overall trade in 2013. Nevertheless, North Korea's bilateral trade with mainland China stood at US\$ 4.05 billion in the first eight months of this year, down 1.1 percent from the same period last year, according to Mainland Chinese customs data. North Korea's exports to mainland China declined 0.8 percent year-on-year to US \$1.84 billion during the eight-month period, while imports fell 1.2 percent to US\$ 2.21 billion.¹⁸ Clearly, the December 2013 execution of Jang Song-taek, Kim Jong-un's uncle and adviser with close ties to Beijing, has poured cold water on their bilateral economic interactions.

IV. Mainland China-South Korea FTA — Based Northeast Asian Economic Integration

In contrast, mainland China has been working hard on its charm offensive toward South Korea,¹⁹ given their common interest on the de-nuclearization of North Korea; opposition to Japan's collective self-defense rights and history-related issues, such as comfort women;

16. 〈中国、北朝鮮への原油輸出ゼロ…4か月連続〉, 《読売新聞》(*Yomiuri Online*), June 4, 2014, <<http://www.yomiuri.co.jp/feature/TO000301/20140604-OYT1T50033.html>>.

17. "The China-North Korea Relationship," *Council on Foreign Relations*, August 22, 2014, <<http://www.cfr.org/china/china-north-korea-relationship/p11097>>.

18. "N. Korea, China kick off annual trade fair," *The Korea Herald*, October 16, 2014, <<http://www.koreaherald.com/view.php?ud=20141016001126>>.

19. Jin Kai, "China's Two-Front Diplomacy: 'Go West' and 'Leap East'," *The Diplomat*, September 12, 2014, <<http://thediplomat.com/2014/09/chinas-two-front-diplomacy-go-west-and-leap-east/>>.

Japan's rising rightist movements of the Abe regime; and the strengthening Japan-U.S. alliance. Xi Jinping's Seoul trip was engineered by Beijing to have the function of enhancing mainland China's political and economic influence in South Korea, driving a wedge between Park Geun-hye and Shinzo Abe, as well as between South Korea and the U.S. In addition, during his trip, Xi said specifically that mainland China wants to accelerate free trade talks with South Korea and deepen cooperation in finance and macroeconomic policies. So, he reached an agreement with his counterpart Park Geun-hye to sign a bilateral FTA by the end of this year. This represents a tactical shift in mainland China's approach to Northeast Asian economic integration from focusing on a mainland China-Korea-Japan trilateral FTA to a mainland China-Korea FTA, aiming at killing four birds (Japan, Taiwan, the U.S., and North Korea) with one stone. Of course, this is also related to Japan's decision to join TPP negotiations (this means that Japan made choice between TPP and the mainland China-Korea-Japan trilateral FTA). With checking and balancing mainland China in mind, Japan under Abe has attempted to influence and control the Asia-Pacific integration process by supporting the U.S. strategies so as to form a TPP jointly led by the U.S. and Japan, given that the two countries together account for 80% of total GDP of TPP member states.²⁰

While on his Seoul trip in July of this year, Xi Jinping indicated that mainland China's strategy for the 21st century is to establish a new order in Northeast Asia and he regards this as a core component of his China Dream. He expects South Korea to join this framework and to create Northeast Asian economic integration based on a Sino-

20. Jiang Yuechun, "Asia-Pacific Regional Economic Cooperation and CJK Cooperation," *China International Studies*, No.39, March/April, 2013, <http://www.ciis.org.cn/english/2013-04/26/content_5908704.htm>.

South Korea FTA.²¹ Against this backdrop, Xi and Park agreed to sign an FTA by the end of this year. Currently, mainland China is South Korea's largest trading partner and largest export market. Total Sino-South Korea Trade volume was over US\$ 270 billion in 2013,²² which is two times larger than South Korea-Japan total trade volume,²³ with a substantial trade balance in favor of Seoul. In 2013, South Korea's global exports totaled US\$ 5.59 billion, 26.1% went to mainland China, namely US\$183.1 billion, which is more than South Korea's exports to Japan (US\$ 162.3 billion).²⁴

What is worth particularly mentioning in Xi's Seoul trip is the expansion of their bilateral financial cooperation, with the People's Bank of China and the Bank of Korea signing a memorandum on the establishment of *Renminbi* clearing arrangements and mainland Chinese agreeing to give South Korea an 80 billion yuan QFII (Qualified Foreign Institutional Investors) quota (US\$ 12.9 billion) for Korean investors to buy securities in mainland China under the *Renminbi* Qualified Foreign Institutional Investor program.²⁵ This will

21. 朴普均,〈習近平的新朝鮮策略〉,《韓國中央日報中文網》(*JoongAng Ilbo*), July 10, 2014, <http://chinese.joins.com/big5/article.do?method=detail&art_id=121949>.

22. Mel Gurtov, "China-South Korea Relations: "Xi Jinping Visits Seoul: The Bigger Picture"," *The Asia-Pacific Journal*, Vol. 12, Issue 30, July 28, 2014, *Global Research*, <<http://www.globalresearch.ca/china-south-korea-relations-xi-jinping-visits-seoul-the-bigger-picture/5393765>>.

23. 〈習近平年內訪韓 中韓拋開日本關係更加緊密〉,《朝日新聞中文網》(*The Asahi Shimbun*), January 2, 2014, <<http://asahichinese.com/article/world/AJ201401020040>>.

24. 〈社論：中貿易額世界第一，韓該做何準備〉,《80視點網》, January 15, 2014, <<http://www.80sd.org/pl/2014/01/15/35558.html>>.

25. 〈中韓簽署自貿協定對日本影響最大〉,《日本經濟新聞中文網》(*Nikkei*), July 4, 2014, <<http://cn.nikkei.com/politicaeconomy/investtrade/10007-20140704.html>>.

help South Korea become an offshore yuan center and bring visible economic benefits. The establishment of the RMB clearing arrangements will not only help improve South Korea's position in world trade, but will also promote the internationalization of the *Renminbi*. The won-yuan direct trading will cut currency risks, and RQFII will encourage South Korean investors to trade the yuan. In turn, this collaboration will have a synergistic effect in boosting financial transactions between the two nations and lessen South Korea's dependence on the U.S. currency.²⁶

Furthermore, the two countries are likely to jointly promote Asian economic integration through financial cooperation. In Xi's Seoul trip, he invited South Korea to attend the Asian Infrastructure Investment Bank (AIIB), which was first proposed by Xi Jinping in October of 2013, when he met former Indonesian President Susilo Bambang Yudhoyono, in an aim to support the construction of infrastructure in Asian countries and sustainable development. Park Geun-hye welcomed the proposal during her summit with Xi. Some South Korean experts view this as an opportunity for their country to benefit from the future AIIB infrastructure projects and to emerge as a financial hub in Asia if mainland China allows *Songdo* to serve as the bank's headquarters,²⁷ while opponents take a cautious stance for the negative impact on Korea's relations with Washington. Other proponents suggest that the Park Administration should consider

26. "South Korea Agrees Won-Yuan Trading Link, RQFII Quota With China," *Bloomberg*, July 3, 2014, <<http://www.bloomberg.com/news/2014-07-03/won-yuan-trading-on-agenda-as-china-south-korean-leaders-meet.html>>.

27. 〈사설：AIIB 참여문제, 경제실익 기준으로 접근하라, 매일경제〉,《每日經濟》(*MK News*), July 15, 2014, <<http://news.mk.co.kr/column/view.php?sc=30500003&cm=사설&year=2014&no=991676&relatedcode=&won-No=995765&siID=>>>.

seriously mainland China's proposal, in order to maximize South Korea's national interest by taking advantage of the dual track competition under the Sino-U.S. strategic tit-for-tat in Asia, namely ADB versus AIIB as well as TPP versus RCEP.²⁸ Nevertheless, the U.S. expressed concerns about Beijing's AIIB initiative, which is designed to expand its security and financial structural clout in Asia *vis-à-vis* the U.S. Washington openly opposes South Korea's participation in the mainland China-led AIIB. This is exemplified by remarks of both White House National Security Council (NSC) member Sydney Seiler and Department of State spokesperson Jen Psaki in July this year.²⁹

Additionally, South Korea's immediate economic gains include a flood of mainland China investment and tourists. The amount of foreign direct investment (FDI) that flowed into South Korea in the January-September period hit an all-time high. In particular, FDI from mainland China, the largest contributor, increased more than threefold, year-on-year. In the first nine months of this year, the amount of new FDI pledges to Korea reached US\$ 14.82 billion, up 37.9 percent year-on-year, according to South Korea's Ministry of Trade, Industry and Energy. This is the highest-ever figure for the nine-month period, exceeding last year's entire amount of US\$ 14.55 billion. In contrast, FDI from Japan dwindled by nearly 17 percent year-on-year due to a weakening yen and tense relations between Seoul and Tokyo.³⁰ Meanwhile, the disputes with mainland China

28. <아시아인프라투자은행 참여 놓고 정부 '딜레마' 미국 반대 속 국내 경제 전문가들 찬반 양론 나뉘어>, 《비즈니스한국》, July 18, 2014, <<http://biz.hankooki.com/lpage/economy/201407/d20140718171025135870.htm>>.

29. <한국에 중추도 아시아인프라투자은행 불참 요구>, 《연합뉴스》, June 28, 2014, <<http://www.yonhapnews.co.kr/international/2014/06/28/0601010100AKR20140628053000073.HTML>>.

30. "Most New Foreign Investment in Korea Comes from China," *The Chosunilbo*, October 6, 2014, <http://english.chosun.com/site/data/html_dir/2014/10/06/2014

have contributed to a sizable drop in Japan's direct investment in mainland China starting last year – a 4.3 percent decline – followed by a nearly 49 percent decline in the first half of this year.³¹ On the bilateral trade in services, South Korea saw the highest rise in the world in credit card transactions by Chinese tourists during this year's Chinese national holiday week in early October, as the figure soared 111 percent year-on-year. Some 160,000 Chinese tourists visited South Korea over the holiday week, a fourfold increase from the same period last year.³² According to South Korea's Education Ministry, around 53,000 Mainland Chinese people studied in Korea as of April this year, accounting for a whopping 59 percent of all foreign students in the country. This marks around a fourfold increase from nine years ago.³³

Apart from enhancing economic interactions with mainland China, another significant segment of Park Geun-hye government's mainland China policy is to make sure that South Korea is in the driver's seat in international politics on the Korean peninsula through building an axis of Sino-U.S.-ROK special relationship taking advantage of the emergence of the G2 era and mainland China's grand strategy, such as the high-speed railways network (Silk Road) as well as promoting reconciliation of the two Koreas through nurturing trust politics with the Kim Jong-un regime. This explains why inter-Korea

100601797.html>.

31. Mel Gurtov, "China-South Korea Relations: "Xi Jinping Visits Seoul: The Bigger Picture".

32. "Chinese Holidaymakers Spend Big in Korea," *The Chosun Ilbo*, October 10, 2014, <http://english.chosun.com/site/data/html_dir/2014/10/10/2014101000982.html>.

33. "More Than 50,000 Chinese Study in Korea," *The Chosun Ilbo*, October 18, 2014, <http://english.chosun.com/site/data/html_dir/2014/10/18/2014101800412.html>.

talks on reopening the Kaesong Industrial Complex were successful in August 2013. Even though President Park and her predecessor Lee Myung-bak come from the same conservative party, Park Geun-hye, during her presidential campaign, promised to act different from the Lee Government in dealing with North Korea so as to bring the tense inter-Korea relations under Lee back into the orbit of political peace and economic prosperity found during the liberal governments of Kim Dae-jung and Roh Moo-hyun. As a result, compared to President Lee's Grand Bargain, under which he proposed the irreversible denuclearization of North Korea in a single agreement in exchange for security assurance, normalization of relations, and economic assistance to North Korea, President Park instead has stressed the importance of North Korean denuclearization for Korean unification while de-linking her three proposals from denuclearization itself. In her landmark speech in the former East German city of Dresden, South Korean President Park Geun-hye made a three-point proposal to North Korea for the "humanity, co-prosperity, and integration" of the two Koreas. Under her humanitarian agenda, she proposed the regularization of the family reunions between the two Koreas and provision of a "1,000-day package project" to support North Korean mothers and infants. To promote the co-prosperity of the two Koreas, President Park offered major inter-Korean projects, such as South Korea's infrastructure-building investments and building of multi-farming complexes in North Korea, collaborative projects with mainland China and Russia, and joint development projects on natural resources.³⁴

On the other hand, according to the Satoshi Okuda and Yuichi Watanabe report in 2011, Japan would become the biggest victim of a Sino-South Korea FTA, if implemented. In terms of trade

³⁴ "President Park Geun-hye's Dresden Declaration," *CSIS Asia Policy Blog*, April 10, 2014, <<http://cogitasia.com/president-park-geun-hyes-dresden-declaration/>>.

diversion in both the Chinese market and the Korean market, Japan is estimated to lose almost US\$7 billion, followed by Taiwan (US \$ 3.5 billion).³⁵ As a result, an agreement to conclude a mainland China-Korea FTA by the end of this year will force Japan to respond positively to either mainland China-Korea-Japan FTA negotiations or RCEP negotiations.³⁶

V. Mainland China-South Korea FTA: Implications for Taiwan

In fact, Taiwan's case could be worse than Japan if one considers investment diversion and the disconnection of Taiwan investors and the domestic exporting operational mode. A Sino-Korea pact threatens to divert trade and investment away from Taiwan. Sectors where South Korea and Taiwan compete fiercely in both in mainland China and world markets, such as semiconductors, mobile phones, and digital TVs, are already not included on the ECFA's early harvest list. Now, if the Sino-South Korea FTA takes effect, all of the benefits Taiwan has earned from the early harvest program will be neutralized. Given that Taiwan and South Korean exports have a 63% overlap, the Sino-South Korea FTA will cost Taiwan dearly. For example, the value of foreign products in the South Korean market to be replaced by Chinese products due to the implementation of Sino-Korea FTA would amount to up to US\$ 6.7 billion. The EU would suffer the most (US\$ 1.7 billion), followed by Japan (US\$ 1.6 billion), the U.S.

³⁵ 奥田聡、渡辺雄一、〈韓中・日中FTAの影響—締約国および第三国への影響〉、《ジェトロ・アジア経済研究所》(IDE-JETRO), March, 2011, p. 2, <http://www.ide.go.jp/Japanese/Publish/Download/Seisaku/1010_01.html>.

³⁶ 〈16 國自貿區談判或先排除印度〉、《日本經濟新聞中文網》(Nikkei), September 24, 2014, <<http://cn.nikkei.com/politicaeconomy/investtrade/11100-20140924.html>>.

(US\$ 820 million), and Taiwan (US\$ 190 million). Alternatively, in the mainland China market, the foreign products that would suffer the most are those from Japan (US\$ 5.3 billion, in particular electrical engineering products, US\$ 1.1 billion), followed by Taiwan (US\$ 3.3 billion, in particular optical and precision machinery, more than US\$ 1.5 billion), the E.U. (US\$ 2.8 billion), and the U.S. (US\$ 860 million). Altogether, Taiwan is expected to lose almost US\$ 3.5 billion in both mainland Chinese and South Korean markets. According to Chung-Hua Institution for Economic Research in 2011, a Sino-Korea FTA will bring about a huge impact on Taiwan's exports, amounting to more than US\$ 1.7 billion. Chemical, plastic, and rubber products would suffer the most (US\$ 767 million), followed by textiles (US\$ 554 million) and machinery (US\$ 452 million).

What is more, the arterial blood vessel of cross-strait economic ties would be cut off because, if tariffs on those items produced in South Korea were exempted due to the Sino-Korea FTA, Taiwanese manufacturers would lose their price competitiveness. This would force Taiwanese investors in the mainland to stop importing key components from their home island and instead purchase them from local mainland producers or from firms in ASEAN countries or even South Korea. This would cause Taiwan's trade surplus with mainland China to decline significantly and disconnect the traditional modes of international operation by Taiwan enterprises. According to the 2014 Report on Foreign Investment in mainland China by the University of International Business and Economics in Beijing, investment on the Chinese mainland by Taiwan dropped by 27 percent year-on-year in 2013. This indicates that companies in Taiwan are adjusting their industrial development structures.³⁷ Inbound FDI in Taiwan would

³⁷ "Major FDI boost on the way for services," *China Daily*, October 11, 2014, <http://www.chinadailyasia.com/business/2014-10/11/content_15176481.html>.

be affected as well. Since the signing of the ECFA, Japanese companies have used Taiwan as a gateway into the Chinese market, but this phenomenon could come to an untimely end, as Japan is likely to shift its investment to South Korea, due to zero tariffs on products produced there.

VI. North Korea's Response to Xi's *Démarche*

Sino-North Korea relations have been sour since Pyongyang conducted its third nuclear test in February 2013 and have further deteriorated since the execution of Jang Song Thaek for treason in December 2013.³⁸ Since Xi Jinping became mainland China's top leader, he has refused to allow mainland China's Korea policy to be hijacked by North Korea. He has turned a cold shoulder to the Kim Jong-un regime, meanwhile attempting to form a coalition with Seoul and Washington to push North Korea to become denuclearized.

Against this background, the Kim Jong-un regime has launched aggressive diplomatic moves since the first half of this year with the hope of defying mainland China and breaking from its international isolation and economic woes. After consolidating his power at home, Kim Jong-un appointed his right-hand man, Ri Su-yong, as foreign minister in April this year. Since then, Ri Su-yong has launched a diplomatic offensive, with his visit to the Middle East, including Iran, Africa, and ASEAN.³⁹ The climax of its diplomatic offensive was in September of this year (2014), with the seasoned North Korean

³⁸ "Kim's aunt appears OK after husband's execution," December 15, 2013, *Mainichi, Japan*, <<http://mainichi.jp/english/english/newsselect/news/20131215p2g00m0im070000c.html>>.

³⁹ 〈北朝鮮外相・15年ぶり訪米 27日、国連総会で演説へ〉, 《朝日新聞》 (*The Asahi Shimbun*), September 23, 2014, <<http://www.asahi.com/articles/ASG9Q7R2XG9QUHB102F.html>>.

diplomat Kang Sok-ju's rare trip to Europe and Mongolia,⁴⁰ which coincided with Ri Su-yong's trip to New York to attend the U.N. General Assembly and to present a letter from Kim Jong-un inviting Ban Ki-man, Secretary-General of the United Nations, to visit Pyongyang. Ri became the first top North Korean diplomat in more than a decade to attend the UN general assembly in New York. In his speech at the UN forum, Ri indicated that, "Despite unprecedented persistent economic blockade, military threat and political obstruction, we have firmly safeguarded national dignity, effectively deterred war and put the stagnant economy onto an upward track." The move was a reflection of the North's attempts to break away from its international isolation, as Pyongyang is under a set of sanctions imposed by the global community. Speculation is growing that North Korea and the U.S. may revive their contact channels amid reports that high-ranking officials from the U.S. made a secret visit to Pyongyang on an aircraft on August 16 to discuss the issue of three detained American citizens.

Subsequently, Ri Su-yong also paid a visit to Iran and Moscow. He met his Russian counterpart, Sergei Lavrov, in an attempt to boost their bilateral economic cooperation between the two countries in Russia's far-eastern regions. Since relations with the west have become ever more strained over events in Ukraine this year, Russia has increasingly looked eastwards. In May 2014, Russia formally announced it would write off US\$ 10.9 billion of North Korean debt owed to the former Soviet Union, with the remaining US\$ 1.09 billion

40. Kang was involved in crafting the 1994 Agreed Framework between the U.S. and North Korea, under which Pyongyang promised to freeze its nuclear activities in return for light water reactors and oil, as well as a gradual normalization of diplomatic ties. Please refer to "NK diplomatic moves show urgency to escape isolation," *The Korea Times*, September 3, 2014, <http://www.koreatimes.co.kr/www/news/nation/2014/09/485_164072.html>.

to be paid in installments over the next 20 years. Russia hopes to ramp up its trade turnover with North Korea to US\$ 1 billion by 2020, up from the current US\$ 112 million.⁴¹ Russia exported US\$ 21.16 million's worth of jib cranes, machinery used mostly for cargo handling at ports, to North Korea last year, accounting for nearly 22 percent of its total exports to the North, according to the report by the Korea Trade-Investment Promotion Agency (KOTRA). North Korea and Russia maintain economic relations that include a project that would make North Korea's northeastern port city of Rajin a logistics hub by connecting it to Russia's Trans-Siberian Railway. North Korea is said to have agreed to a long-term lease of the No. 3 dock at Rajin port to Russia and that it is modernizing facilities there.

Ri's trip to Russia could herald closer cooperation with North Korea. According to Russian agencies, the visit is the first by a North Korean minister since Kim Jong-un assumed power in Pyongyang more than two years ago. Russia is the only major world power other than mainland China to maintain a close relationship with North Korea, with ties going back to the Communist period. After visiting Moscow, Ri traveled to Russia's far east, including Sakhalin island and the Primorsky region, which has a small land border with North Korea.⁴²

What is worth noting is that Xi's July trip to Seoul coincided

41. "Russia to forgive DPRK debt (2006-present)," *North Korean Economy Watch*, June 5, 2014, <<http://www.nkeconwatch.com/2014/03/20/russia-to-forgive-dprk-debt/>>.

42. "North Korean foreign minister begins 10-day Russia visit Ri Su-yong will meet counterpart Sergei Lavrov and tour far-east Russia in attempt to boost cooperation between countries, NK diplomatic moves show urgency to escape isolation," *The Guardian*, September 30, 2014, <<http://www.theguardian.com/world/2014/sep/30/north-korean-minister-visits-russia>>.

with Japan's unilateral decision to scrap sanctions against North Korea. The political landscape in Northeast Asia is in upheaval amid a power struggle between the U.S., mainland China, Japan, and Russia. In May of this year, reversing its original stance that investigation into the abducted Japanese had closed (no need for re-investigation), North Korea agreed to re-investigate the fate of Japanese people believed to have been abducted by the North's agents in the 1970s and 1980s. Then, in July, Pyongyang launched a special committee to investigate the case and, in return, Japan lifted some of its unilateral sanctions imposed on North Korea. Japan's move has raised concerns of a negative impact on trilateral cooperation among Seoul, Washington, and Tokyo on curbing the North's nuclear weapons programs. A Japanese government official reaffirmed Tokyo's push for talks with Pyongyang, saying that North Korea's continued missile and rocket launches will not affect the ongoing discussions on the abduction issue. The six-party talks aimed at curbing the North's nuclear ambitions have been dormant since late 2008, when Pyongyang walked away from the negotiating table. The talks involve the two Koreas, the U.S., mainland China, Russia, and Japan. North Korea has called for an "unconditional" resumption of the talks, but Seoul and Washington insist that Pyongyang should first take concrete steps toward denuclearization.⁴³

With the support of Washington's "pivot to Asia" policy, Tokyo has approved a reinterpretation of Japan's pacifist constitution, allowing it to wage war even if it is not under direct attack. Japan has also agreed with North Korea to lift sanctions imposed in 2006 if Pyongyang re-investigates what became of the Japanese victims of a bizarre abduction campaign from the 1970s and 1980s. There

⁴³ "Veteran N.K. diplomat likely to visit Europe," September 2, 2014, <<http://www.koreaherald.com/view.php?ud=20140902000898>>.

are even forecasts that Japan's far-right Prime Minister Shinzo Abe could visit North Korea this year to meet with leader Kim Jong-un.⁴⁴ Obviously, North Korea is eager to establish formal diplomatic relations with Japan so as to get huge economic assistance from the Abe government, which shares Kim Jong-un's desire to defy Xi Jinping. This scheme will not easily materialize, mainly because of the U.S. opposition to Japan's independent action, which could have negative impact on the coalition sanctions against Pyongyang. It is reported that Abe has delayed his desired Pyongyang trip.

With regard to relations between the two Koreas, the Kim Jong-un regime has also shown some unusual conciliatory gestures mixed with some unexpected military exchanges of fire and threats plus harsh rhetoric toward Seoul and Park Geun-hye. In addition to driving a wedge between the U.S. and South Korea, the unexpected flexible gesture is believed to be an attempt to make a breakthrough in its relations with South Korea for economic assistance, exemplified by a group of three top North Korean officials' surprise visit to Seoul to attend the closing ceremony of the Asian Games in Incheon, where North Korean athletes competed. The three officials close to Kim Jong-un are Hwang Pyong-so, the top political officer in the Korean People's Army and considered by analysts to be the country's second most important official after Kim, and Choe Ryong-hae and Kim Yang-gon, who are secretaries to the ruling Workers Party. It was unprecedented for such high-level North Korean officials to travel together to South Korea. The North Korean officials held meetings with South Korean officials, including Prime Minister Chung Hong-won, Unification Minister Ryoo Kihl-jae, and National Security Adviser Kim, and agreed to hold a new round of high-level inter-

⁴⁴ "Park, Xi Face Multiple Regional Challenges," *The Chosun Daily*, July 3, 2014, <http://english.chosun.com/site/data/html_dir/2014/07/03/2014070301744.html>.

Korean talks between late October and early November. North Korea is eager to bring the stalled Mount Kumgang tourism project back on track.⁴⁵ For the first time since 2011, the two Koreas held senior-level military talks, led by North Korean General Kim Yong Chol and South Korean Retired Lt. Gen. Ryu Je-seung, in a border village in late October of this year (2014), but they failed to narrow differences after two exchanges of fire in the previous week.

Kim Jong-un has made both building strong nuclear capacities and economic reforms his two domestic policy priorities ever since ascending to power. North Korea's goal in its new initiatives is to weaken global sanctions, which are designed to pressure the country into giving up its nuclear arms program, and to seek an inbound capital flow for North Korea's economic reform. Nevertheless, this is against an international environment characterized by a strong request to remove its nuclear weapons and by escalating economic sanctions on Pyongyang in the wake of its testing missiles and its third nuclear bomb test in the past more than two years. This contradiction between domestic priorities and the international environment has made his domestic economic reforms realize few achievements and his foreign policy goals unattainable. While North Korea under Kim Jong-un is aiming to boost its economy by attracting foreign investors and tourists, most of its own people still suffer from a lack of food and other necessities, as well as any large scale foreign economic assistance.

According to the World Food Programme, the average daily ration distributed to the North Korean people was 250 g in August.⁴⁶ Alter-

45. "NK trip to South no surprise to Washington," *The Korea Times*, October 7, 2014, <http://www.koreatimes.co.kr/www/news/nation/2014/10/120_165864.html>.

46. "N. Korean Rations Dwindle to Measliest in 3 Years," *The Chosun Daily*, Sep-

natively, chances for Kim Jong-un to get huge economic aid from neighboring states through major diplomatic breakthroughs are slim due to the emergence of Sino-U.S. condominium to get rid of North Korean nuclear weapons under Xi Jinping's changing approach to the Korean peninsula from focusing on geo-politics to geo-economics, as discussed above.

VII. Conclusion

With the goal of turning the image of the Sino-U.S. condominium into reality through new types of big powers relationship, mainland China under Xi Jinping has decided to make a strategic move by shifting the axis of international politics on the Korean peninsula from geo-politics to geo-economics, exemplified by Xi's trip to Seoul and his agreement with Park Geun-hye to sign a mainland China-South Korea FTA by the end of this year. This strategic change is intended to enhance the era of the G2 in the coming APEC summit, slated for November 10-11 this year, through their joint promotion of the FTAAP. This is actually an application of the Chinese traditional approach of "using the enemy's spear to attack his shield" (以子之矛攻子之盾), because the FTAAP was first proposed by former U.S. President George Bush in 2006 and the Obama Administration has mentioned that the final goal of its TPP is FTAAP. Given the deteriorating U.S.-Russia relations due to the Ukraine issue, along with the U.S. being mired in the Islamic State (IS) war in the Middle East and Ebola threats,⁴⁷ there is a possibility that Washington will seek

tember 25, 2014, <http://english.chosun.com/site/data/html_dir/2014/09/25/2014092501213.html>.

47. 〈美國又將陷入一場長期戰〉,《日本經濟新聞中文網》(*Nikkei*), September 24, 2014, <<http://cn.nikkei.com/politicsaeconomy/politicsasociety/11179-20140924.html>>.

a compromise with mainland China on free trade by accepting Beijing's suggestion to endorse the FTAAP in the coming APEC summit in exchange for Beijing's support for other issues that concern the U.S.⁴⁸ In addition, history proves that Sino-U.S. economic co-operation is the best way to bring peace and prosperity in the region.

With the Clinton administration's support, mainland China's admittance to the WTO in 2001 has brought about Sino-U.S. economic interdependence.⁴⁹ Both the U.S. and mainland China have benefited hugely from their cooperation, and so has our region. In their recent meeting, mainland Chinese Foreign Minister Wang Yi and U.S. Secretary of State John Kerry agreed that the two sides should be especially well-prepared for the summit in an effort to further enrich the idea of the new model of major country relations between mainland China and the U.S.⁵⁰ Their ongoing bilateral investment treaty (BIT) negotiations are another front in their common interest.⁵¹

In sum, mainland China's liberalist approach has brought about some initial positive results for Beijing, including Abe reemphasizing the importance of maintaining Sino-Japanese rapprochement (given the imminent APEC summit in the forthcoming November) and North Korea downgrading its level of threats and resorting to diplomatic

48. 〈賴斯訪華或為中美密約〉,《日本經濟新聞中文網》(Nikkei), September 24, 2014, <<http://cn.nikkei.com/columnviewpoint/column/11137-20140924.html>>.

49. John Frisbie, "Ten Years of WTO Membership: Gains for China and the US, but More Must Be Done," *China Business Review*, October 1, 2011, <<http://www.chinabusinessreview.com/ten-years-of-wto-membership/>>.

50. "China, US to jointly prepare for Obama's trip," *China Daily*, October 13, 2014, <http://www.chinadailyasia.com/nation/2014-10/13/content_15177104.html>.

51. Stephanie Henry, "Bilateral Investment Treaties: What They Are and Why They Matter," *China Business Review*, July 29, 2014, <<http://www.chinabusinessreview.com/bilateral-investment-treaties-what-they-are-and-why-they-matter/>>.

initiatives (as the Kim Jong-un regime is the biggest loser in mainland China's strategic shift). For the first time in years, Japan and mainland China have held high-level talks on maritime issues aimed at easing tensions over disputes in the East China Sea. Both sides have agreed, in principle, to resume maritime liaisons between defense agencies of the two countries. A day later, Japanese Prime Minister Shinzo Abe renewed his call to hold a summit with mainland China, urging both Beijing and Tokyo to make "quiet efforts" to ease strains between the two Asian giants. Rising tensions have overshadowed Sino-Japanese ties in recent years with the Asian neighbors fighting over the territorial dispute over the *Diaoyutai* Islands and over Abe's visit to the *Yasukuni* Shrine.⁵² The Abe Administration is worried about the possibility of emerging Sino-U.S. leadership in Asian economic integration. If that is the case, Japan's effort to create a joint leadership of TPP will vanish.

In stark contrast to South Korea, who is the biggest beneficiary of mainland China's strategic shift, Taiwan could be the biggest potential loser if we do not act quickly and strategically. At this critical moment, we need actively to seek agreement on trade in goods with mainland China as soon as possible and at the same time to give support to FTAAP, given our membership in APEC. In this way, we will be free from the negative impact of the mainland China-South Korea FTA, not including the TPP and RCEP negotiations.

52. "Are China-Japan relations thawing?" *Deutsche Welle*, September 26, 2014, <<http://www.dw.de/are-china-japan-relations-thawing/a-17957317>>.

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