



**Regional Overview:**

**2012 Ends with Echoes of the Past**

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It was déjà vu all over again on the Korean Peninsula as the absence of bad news, highlighted during our last reporting period, came to an end when Pyongyang again defied the international community (and UNSC sanctions) by conducting another missile launch, this time successfully, in December. Nonetheless, Kim Jong Un's New Year's message was seen by some (but not us) as a harbinger of good news in the year ahead. ASEAN leaders at the yearend round of summits in Phnom Penh (including the East Asia Summit attended by President Obama) managed to demonstrate a greater amount of unity than during their July ministerial, but the lingering South China Sea territorial issue showed no signs of being closer to resolution. Meanwhile, hopes for genuine reform in Burma/Myanmar soared as President Obama made an unprecedented visit following his inaugural visit to Cambodia for the EAS, in the context of his administration's continuing rebalance toward the Asia-Pacific.

It was out with the new and in with the old in Japan, as the Liberal Democratic Party returned to power amidst a nationalistic campaign that promised to strain relations with the new leadership coming to power in South Korea and China, and perhaps with the new leadership team in Washington as well. President Obama won a second term and Park Geun-hye returned to the Blue House, this time as president. In China, a new leadership took command of the communist party, and they face myriad challenges, many of which are economic in nature. The year closed with a flurry of trade meetings and initiatives designed to capture the energy of the world's most dynamic economies.

**UNSC resolutions be damned!**

In our last report, we noted that the only good news emanating from the Korean Peninsula was the absence of any real bad news as the much-anticipated North Korean nuclear and follow-on missile tests did not occur. We added the caveat "yet." Hopes that Kim Jong Un would lead his country in a new direction following the mandated (by his father) celebrations honoring his grandfather this past spring were dashed in December, however, when the North for the second time this year fired a three-stage rocket from its west coast missile test facility. Unlike the first attempt in April, which exploded 40 seconds after launch, this one successfully (according to NORAD) put an object into orbit, even if it did not appear to be functioning properly.

Some, ourselves included, had argued that we should not be quick to judge Kim Jong Un and his policies by the failed Feb. 29 "Leap Day Agreement" and subsequent April 2012 rocket launch. Both actions had clearly been mandated by his father, Kim Jong Il, before he died, and these dying wishes had to be honored. That logic no longer applies. While the North still proclaimed

that the December launch was carrying out “the last instructions” of the Dear Leader, this decision rests squarely on Kim Jong Un’s shoulders.

The Boy General wasted little time in bragging about the event (especially after the earlier failure). He made repeated references to this great accomplishment during his New Year’s address: “That we successfully manufactured and launched the scientific and technological satellite by entirely relying on our own efforts, technology, and wisdom was an event of national jubilation that raised the dignity and honor of the Sun’s nation onto the highest level and a great event which inspired all the service personnel and people with confidence in sure victory and courage and clearly showed that Korea does what it is determined to do.”

Not stated, but clearly implied by the last phrase above, was Pyongyang’s rejection of UN Security Council resolutions which ban “all missile activity” by North Korea, including “any launch using ballistic missile technology.” The UNSC was quick to react, issuing a firm (but toothless) press statement on Dec 12, which said, in part: “Members of the Security Council condemned this launch, which is a clear violation of Security Council resolutions 1718 and 1874.” The UNSC statement recalled its April 2012 demand that the DPRK “not proceed with any further launches using ballistic missile technology” and reminded Pyongyang of “the Council’s determination to take action accordingly in the event of a further DPRK launch.” In that regard, it further asserted that “the Security Council will continue consultations on an appropriate response, in accordance with its responsibilities given the urgency of the matter.”

US Ambassador to the UN Susan Rice proclaimed that “The initial statement out of the council is one of the swiftest and strongest – if not the swiftest and strongest – that this council has issued,” quickly adding, however, that “Members of the council must now work in a concerted fashion to send a clear message that its violations of UN Security Council resolutions have consequences.” Alas, this message has yet to be sent; no new consequences have yet been determined. China’s Ambassador to the UN Li Baodong reportedly resisted harder hitting language in the statement – Rice described the debate with the Chinese as “vigorous” while others in the room asserted she told her Chinese counterpart that his government’s stance was “ridiculous” – and the year ended with China blocking any new sanctions or other firm “consequences,” insisting instead that the UNSC response should be “prudent and moderate.” Anyone expecting a firmer response to North Korean provocations from China’s new leadership seems bound to be disappointed.

In Kim Jon Un’s aforementioned New Year address – delivered in person, as his grandfather used to do (but father never did) – the satellite launch was praised as the example and inspiration to be emulated for greater accomplishments in other fields: “In the same manner as we demonstrated the dignity and might of Military-First (Son’gun) Korea through the manufacture and launch of the Juche-based application satellite, the entire Party, the whole country and all the people should wage an all-out struggle this year to effect a turnaround in building an economic giant and improving the people’s standard of living.” Analysts looking for proof that the North, under Kim Jong Un, will leave the “military-first” policy behind will have to search for other evidence. Specifics as to how the North was to become an “economic giant” were also sorely lacking.

## Olive branch to the South?

Much has been made in the international media of Kim's reference in this address to the need "to remove confrontation" between the North and the South." This was widely interpreted as an olive branch being extended to incoming ROK President Park Geun-hye. Perhaps! But a word or two of caution seems appropriate. The reference was in the context of reunification, not North-South cooperation *per se*: "This year the entire Korean nation should turn out in a nationwide patriotic struggle for reunification in unity so as to usher in a new phase in the reunification movement. An important issue in putting an end to the division of the country and achieving its reunification is to remove confrontation between the north and the south."

The path forward was also spelled out rather explicitly: "The past records of inter-Korean relations show that confrontation between fellow countrymen leads to nothing but war. Anti-reunification forces of south Korea [note the lower case "s"] should abandon their hostile policy against their fellow countrymen, but take the road of national reconciliation, unity, and reunification."

The fault, as always, lies with the South, which must first abandon its "hostile policy." This is a familiar refrain to Americans, who repeatedly receive the same advice (but who were not directly referenced in this particular speech). The South must also first live up to all its past promises of assistance: "Respecting and thoroughly implementing the north-south joint declarations is a basic prerequisite to promoting the inter-Korean relations and hastening the country's reunification."

If, by this, he meant the 1992 North-South Basic Agreement and companion Joint Denuclearization Agreement, that would have been big news. But Kim Jong Un's reference was limited to the June 15, 2000 Joint Declaration (with Kim Dae-jung) and the Oct. 4, 2007 Declaration (with Roh Moo-hyun); the latter in particular offered the North billions in unrestricted, no strings attached aid, something that Roh would have never been able to deliver even if he had remained president for many more years (instead of a few more months), and which no ROK president could now honor. While the North may not be good about honoring its own obligations, it is unsurpassed when it comes to holding others to their promises.

Kim's message also noted that "the reunification issue should be solved by the concerted efforts of our nation in an independent manner." In other words, the US (and China) needs to keep out of it. In case this was too subtle, he continued: "The entire nation should vehemently reject any moves for domination, intervention, aggression and war by outside forces, and never tolerate any acts hindering the country's reunification." He later stressed that "the moves of the imperialists to interfere in the internal affairs of other sovereign states and their acts of military aggression pose a serious threat to peace and security of mankind. The Asia-Pacific region, the Korean Peninsula in particular, has become the hottest spot in the world in which constant tension persists." So much for olive branches.

To us, the New Year address had two main messages, both mostly intended for domestic audiences. First, that rumors (and wishful thinking) to the contrary, the "great banner of Military-First (Son'gun)" is not about to be unfurled anytime soon. But Son'gun did not mean

that the military was calling the shots. At the end of the day, it was the Korean Worker's Party to whom both the military and the people owed allegiance.

### **ASEAN (almost) gets it act together**

Recall in our last report how we noted that the Association of Southeast Asian Nations (ASEAN), for the first time in its 45-year history, failed to come up with a joint communiqué at the close of its annual 10-member ASEAN Ministers Meeting (AMM) in Phnom Penh in July, when host Cambodia, a staunch ally of China, reportedly refused to yield to demands by the Philippines and Vietnam to include details of their respective confrontations with China over conflicting South China Sea (SCS) territorial claims in the closing statement. When the leaders assembled in Phnom Penh for the 21<sup>st</sup> ASEAN Summit on Nov. 18, they managed to do slightly better, but not until after one more contentious episode.

At a press conference immediately following the Summit, Cambodian Foreign Ministry official Kao Kim Hourn told reporters that "ASEAN leaders decided that they will not internationalize the South China Sea from now on." This comment drew immediate criticism, first from the Philippines and then by others. An attempt by Phnom Penh (allegedly at Beijing's insistence) to insert the "will not internationalize" comment into the ASEAN Summit Chairman's Statement was reportedly rejected not just by the Philippines, but by Brunei (the incoming ASEAN Chair), Indonesia, Singapore, and Vietnam.

The published statement did not include this clause. Instead, it contained five rather bland paragraphs on the South China Sea (SCS) which "underlined the importance" of the 2002 Declaration on the Conduct of Parties in the South China Sea (DOC) "as a milestone document which signifies the collective commitment of ASEAN Member States and China to promote peace, stability and mutual trust in the South China Sea." It also "underscored the importance of exercising self-restraint by all parties concerned and not to undertake any activities which may complicate and escalate disputes and affect peace and stability, and to handle their differences in a constructive manner." There was no reference in the Chairman's Statement to a more binding SCS code of conduct, although it did highlight the importance of the ASEAN's Six-Point Principles on the South China Sea (negotiated by Indonesian Foreign Minister Marty Natalegawa after the July debacle), which does call for "the early conclusion of a Regional Code of Conduct in the South China Sea."

The most interesting document to come out of the ASEAN Summit was the long-awaited ASEAN Human Rights Declaration (AHRD), which noted, among its nine general principles that "all human rights are universal, indivisible, interdependent, and interrelated." Outgoing ASEAN Secretary General Surin Pitsuwan called the agreement a "major, major development," saying countries in the region have now committed themselves "to the highest standards." Others were not so sure. First of all, the declaration is nonbinding. Second, there are caveats. Article seven, cited above in part, continues: "All human rights and fundamental freedoms in this Declaration must be treated in a fair and equal manner, on the same footing and with the same emphasis. At the same time, the realisation of human rights must be considered in the regional and national context bearing in mind different political, economic, legal, social, cultural, historical, and religious backgrounds." Human rights groups protested that the "cultural loophole" could be

used to deny the very rights the declaration was supposed to be protecting. US State Department spokesperson Victoria Nuland said Washington was “deeply concerned” that the declaration could “weaken and erode” the United Nations Universal Declaration on Human Rights (even though the AHDR twice states that ASEAN member states affirm all the economic, social, and cultural rights in the UN Declaration). A statement by a network of more than 50 human rights groups, including Amnesty International and Human Rights Watch, expressed concern that several basic rights and freedoms – freedom of association and freedom from forced disappearances – were missing. They also lamented the lack of consultation with civil society and grassroots organizations.

## **Obama and the East Asia Summit**

The ASEAN Summit was followed by a number of side meetings, including the fourth US-ASEAN Leaders Meeting (covered elsewhere in this E-journal) and an ASEAN Plus Six gathering (involving Plus Three partners China, Korea, and Japan, along with Australia, New Zealand, and India) which launched negotiations on a Regional Comprehensive Economic Partnership (discussed below), among other summits. These were followed on Nov. 20 by the seventh East Asia Summit (EAS) which for the second time included the United States and Russia, along with the original 16 members.

The White House *Fact Sheet on East Asia Summit Outcomes* described President Obama’s participation as “part of the Administration’s continued focus on rebalancing its engagement in Asia to reflect the economic and strategic importance of this dynamic region.” It identified the EAS as “the region’s premier forum for Asia-Pacific leaders to discuss pressing political and strategic issues,” and highlighted discussion on the following issues: energy cooperation, non-proliferation, humanitarian assistance and disaster relief, health, and maritime security. It identified maritime security as a “priority issue,” and pointed out that President Obama “reaffirmed US national interests in the maintenance of peace and stability, respect for international law, unimpeded lawful commerce, and freedom of navigation.”

The White House *Fact Sheet* also notes that President Obama “encouraged the parties to make progress on a binding code of conduct in the South China Sea to provide a framework to prevent conflict, manage incidents when they occur, and help resolve disputes.” He (among others) no doubt did so. But (initial press reporting to the contrary), the EAS Chairman’s Statement, while noting that the assembled leaders “welcomed the regional efforts to enhance cooperation in promoting maritime cooperation in the region including sea anti-piracy, search and rescue at sea, marine environment, maritime security, maritime connectivity, freedom of navigation, fisheries and other areas of cooperation,” did not include any specific reference to the South China Sea or the DOC or COC.

## **It’s all about Burma (a.k.a. Myanmar)**

While the primary reason for Obama’s Southeast Asia visit was the EAS, he also included stops in Thailand (in case you missed it) and Burma (which you could not possibly have missed). Details are provided in the US-ASEAN chapter. But allow us a few observations.

In the past, we have expressed cautious optimism about the changes underway in Burma and praised both the government there and Washington for its continued measured approach in recognizing both the progress that has occurred and the difficult road ahead. The White House stressed both in explaining the trip: “In becoming the first U.S. President to visit Burma, the President is endorsing and supporting the reforms underway, giving momentum to reformers, and promoting continued progress.”

While the logic appears sound, we still fear the visit may have been a bit premature, for a number of reasons. For starters, it drew attention away from his visit to security ally Thailand and also to Cambodia and the need for reform in that nation. It also tended to overshadow the East Asia Summit, which is fast becoming the premier vehicle for regional and extra-regional cooperation and integration. It also sets the stage for two presidential visits to Burma in two years’ time, since Naypyidaw will assume the chairmanship of ASEAN in 2014 and thus host the EAS the year after next. Had that meeting coincided with Obama’s first visit, it would have put intense pressure on the Burmese government to continue the reform process. If they start backsliding now, it will put not only Burma’s newfound reputation at stake, but Obama’s as well. On the plus side, of course, the opening up of Burma must be seen as one of President Obama and Secretary of State Hillary Clinton’s major successes and Clinton’s return visit with Obama was a fitting swan song for her in Southeast Asia.

### **Rebalance redefined**

Immediately prior to President Obama’s Southeast Asia trip, National Security Advisor Tom Donilon gave an address at our parent organization, the Center for Strategic and International Studies in Washington, to put the visit (and the administration’s overall Asia policy) in broader context. Donilon noted that Obama’s decision to travel to Asia so soon after his reelection “speaks to the importance that he places on the region and its centrality to so many of our national security interests and priorities.” The EAS was also the first major international event that happened to be scheduled after Election Day, but the sentiments were nice, nonetheless.

Donilon pointed out that the “rebalancing” toward Asia was the product of a strategic assessment of America’s global presence and priorities that resulted in a “set of key determinations.” He said it was the president’s judgment that “we were over-weighted in some areas and regions, such as our military commitments in the Middle East. At the same time, we were underweighted in other regions, such as the Asia Pacific. Guided by these determinations, we set out to rebalance our posture in the world.” He said the administration’s approach was “grounded in a simple proposition: the United States is a Pacific power whose interests are inextricably linked with Asia’s economic, security and political order. America’s success in the 21<sup>st</sup> century is tied to the success of Asia.”

[Donilon’s entire speech](#) is available on the CSIS web site and is a must read for those interested in a full explanation of the rebalance strategy. It leaves no doubt that “the region will continue to be a foreign policy priority for the Obama Administration in the years to come.” He states:

Our overarching objective is to sustain a stable security environment and a regional order rooted in economic openness, peaceful resolution of disputes, democratic

governance, and political freedom. This objective stems from our long-term vision of Asia. We aspire to see a region where the rise of new powers occurs peacefully; where the freedom to access the sea, air, space, and cyberspace empowers vibrant commerce; where multinational forums help promote shared interests; and where citizens increasingly have the ability to influence their governments and universal human rights are upheld. This is the future we seek, in partnership with allies and friends.

### **More of the same and then some**

*Obama, round two.* The last four months of 2012 were punctuated by elections and transitions. The US went to the polls in early November and returned President Barack Obama for a second term. His victory over GOP challenger Mitt Romney was sweetened by substantial margins in the popular vote and the Electoral College – before the ballot there were fears that the president might win without a popular majority – as well as an enlarged Democratic presence in the Senate and House. (The Democrats actually won a majority of the popular vote for Representatives, but gerrymandering ensured that the GOP retained its majority, even though it is smaller.) GOP control of the House allows it to lock horns with the president over national priorities and agendas; the Democrat’s failure to win 60 seats in the Senate means that chamber is much more susceptible to a Republican filibuster, although reform of that rule looks increasingly likely.

Those details (some might say minutiae) matter. The balance of power among the executive and legislative branches, and between the two parties, will determine how and whether the US government is able to conduct its business. From our travels around the region, it is the spectacle – and there is no other word for what it looks like – of DC politics that is doing the most damage to US power, influence, and credibility in the region. The prevailing perception that the US is unable to make any decision except under duress, at the last moment, and that is ultimately a temporary fix (and again, only that word will do) contributes to a narrative of US decline. The budget battles at the end of the year suggest that our legislators have learned nothing and this sorry exhibition will continue.

The other important element of continuity is US policy. While the top national security and foreign policy officials in the Obama administration are leaving – the secretaries of State, Defense, Treasury, and the head of the CIA are all to be replaced– the outlines of US policy will not waver. Nor should they: powerful though those people are, the president sets policy and the occupant of the White House has not changed. The US will continue to implement the “rebalance” to Asia and straitened fiscal affairs will oblige all budgets to be tighter. The US will be looking for efficiencies in all its operations and this has the potential to transform relations with allies and partners as together they develop new operating procedures to tackle new challenges within new budget constraints. The trick will be convincing them, and other interested observers, that this is not cover for US disengagement. That is not the case, but again the US must be more aggressive in telling its story, rather than responding to others’ interpretations of what we are doing.

*Abe, again.* To no one’s surprise, the Liberal Democratic Party (LDP) came out on top in the December parliamentary election in Japan. What was a bit of a shocker – but had been foreshadowed by polls right before the ballot – was the size of the win. With its coalition partner,

Komeito, the LDP claimed a supermajority that will allow it to override vetoes by the Upper House. The election results reflected rejection of the former ruling party, the Democratic Party of Japan (DPJ), rather than a vote for the LDP, coupled with an electoral system that can only be described as “rigged” in the LDP’s favor. (It is hard to escape that conclusion when the LDP claimed substantially more seats in this vote than the DPJ did in the last general election, even though the LDP actually had fewer votes in total.)

Abe Shinzo’s return to the Kantei raises all sorts of questions, and most speculation has focused on his agenda. Will he indulge in the same nationalist policies that dominated his first term as prime minister? Will he follow through with suggestions during the campaign – making Takeshima Day a national day of recognition, placing government personnel (Self-Defense Forces) on the Senkakus, reconsidering the Kono statement on sex slaves – that are likely to inflame regional tensions? We think not. Abe has professed to having learned his lesson and will focus on bread and butter issues – getting the economy moving. Moreover, since the election, he has dialed back his rhetoric, dropping all three of those campaign ideas, and dispatched envoys to Seoul and Beijing to smooth relations. Finally, three forces – Komei, Japanese public opinion, and the US government (quietly) – will keep Abe from straying too far from the historic mainstream of Japanese policy.

*Park returns to the Blue House.* In South Korea, conservative party candidate Park Geun-hye won the presidential election and will return to the Blue House, where she once served as First Lady for her father after her mother’s assassination. The election was a squeaker, with most polls showing Park leading, but almost always within the margin of error. She ultimately bested progressive party candidate Moon Jae-in by 3.6 percent of the vote.

Her victory promises more continuity with the policies of predecessor Lee Myung-bak, but there will still be changes, especially when dealing with North Korea (as Aidan Foster Carter notes in this volume’s assessment of North-South relations). She has vowed to resume a dialogue with the North and Seoul and Washington will have to work closely together to ensure that the two governments’ positions remain aligned and don’t present opportunities for Pyongyang to exploit.

*The broom in Beijing.* In addition to the democratic changes in Northeast Asia and the US, China had its own leadership transition as the fifth generation took power in Beijing. At the 18<sup>th</sup> Party Congress, Xi Jinping was confirmed as the new general secretary of the Chinese Communist Party (CCP); he is expected to be named president of China, and Li Keqiang will assume the post of premier, in March 2013 at the National People’s Congress. Those two men assumed the number one and two slots in the Politburo Standing Committee; five others joined them at the supreme post of the CCP bureaucracy. The decision to limit the membership of the Standing Committee to just seven was a surprise. In recent years there have been nine members. While the official word is that the smaller group will be more efficient, there is speculation that the turmoil surrounding Bo Xilai prompted the reduction in size.

There is little reason to expect change in China under the new leadership. After all, Xi has been a member of the Standing Committee for the past five years, and no one rises to top positions in the Chinese leadership – a collective body – by vowing to change course. There have been intense efforts to read significance into every one of Xi’s moves since taking power, from his



December trip to Shenzhen – is he making a statement about his commitment to reform? – to his visits to PLA bases in Guangdong – is this a bow to the PLA and its role in his government?

We expect continuity in the key pillars of Chinese foreign and defense policy. The government will keep calling for a new style of great power relations with the US; it will maintain support for North Korea as Beijing urges Pyongyang to embrace economic reform and calls on all nations to avoid upsetting regional peace and stability; it will keep pushing Chinese claims in territorial disputes. Domestically, however, the rhetoric suggests that the government is going to take a harder line against corruption, which is endemic in China and probably the most dangerous threat to continued CCP rule. Whether the party can genuinely afford to clean house, or whether it will kill a few chickens to scare the monkeys, is still unclear.

### **APEC and Putin's pivot**

We closed our last commentary with the lead-up to the annual Asia Pacific Economic Cooperation (APEC) Leader's Meeting, which Russia was hosting in Vladivostok. President Vladimir Putin, the host, used the meeting to announce Russia's own "pivot" to the Asia Pacific region. Like President Obama, Putin rested his policy on the economic imperative of tapping the energy of the world's most dynamic region. Moreover, he noted in his *Wall Street Journal* op-ed that "Russia has long been an intrinsic part of the Asian-Pacific region." Unlike Obama, however, Putin made the meeting. (Since the US president was in the middle of an election campaign, and made it out to the region for the East Asian Summit weeks later, he is likely to be forgiven. There was no flood of commentary about US "neglect," a sign of some understanding of US political dynamics and their significance.) Besides, East Asian countries really don't consider Russia (even its Far East) as being "Asian" and most rank APEC well below other regional multilateral trade initiatives. Obama is now 3 for 4 when it comes to APEC meetings; George W. Bush was 8 for 8.

As it turns out, however, Obama didn't miss much. Political events in the region – territorial disputes, in particular – and external economic developments – the crisis in Europe – dominated discussion. The joint declaration issued at the end of the meeting highlighted the adverse impact of European problems on growth in the Asia-Pacific region, and leaders pledged to steer clear of competitive currency devaluations. They also reaffirmed "our pledge to refrain through the end of 2015 from raising new barriers to investment or to trade in goods and services, imposing new export restrictions, or implementing WTO-inconsistent measures in all areas, including those that stimulate exports." The document expressed support for the WTO and promised to keep WTO compliant measures to a minimum, while rolling back protectionist measures.

The big deliverable was a list of 54 environmental goods on which tariffs will be capped at 5 percent or less by 2015, a target set at last year's leaders meeting. The size of the list is quite contentious, and the attendees are to be applauded for more than doubling its size during the meeting.

The meeting also provided the venue for the usual sidebar conferences. The most important in retrospect is likely to have been the palaver between Chinese President Hu Jintao and Japanese Prime Minister Noda Yoshihiko. Reportedly, the two men discussed the proposed purchase of

the Senkaku/Daiyutai Islands by the Japanese government, a move intended to head off a similar move by firebrand Tokyo Gov. Ishihara Shintaro. It isn't clear what the outcome of that meeting was; Noda apparently thought he had an understanding with Hu about what Tokyo was doing, but subsequent events indicate that clearly wasn't the case.

### **The “Plus Three” get serious**

At the ASEAN Summit and associated meetings in Cambodia in November, trade and economic leaders from China, Japan, and South Korea agreed to launch talks on a trilateral free trade agreement (FTA). The prospect has been discussed, studied, and debated for several years but it lacked the push from top leaders to take the leap and start negotiations. That hurdle has been surmounted.

The first round of trilateral FTA negotiations is scheduled to begin early in 2013. The three governments have played up the economic benefits of such a deal and for good reason. Together, they account for 20 percent of global gross domestic product and 18.5 percent of global exports in 2010. China is the largest trading partner of Japan and the ROK, Japan is China's fourth largest trading partner, and the ROK is China's sixth. Trilateral trade volume has risen from \$130 billion in 1999 to \$690 billion in 2011. Both Japan and the ROK are big investors in China, with total direct investment reaching \$85 billion and \$50 billion for Japan and South Korea, respectively. Joint research by the three countries shows a trilateral FTA will increase China's GDP by 1.1-2.9 percent, Japan's GDP by 0.1-0.5 percent and the ROK's GDP by 2.5-3.1 percent.

While neither the scope nor the deadline for the talks has yet to be decided, officials anticipate a 2015 conclusion, aiming to tie their agreement to the signing of a comprehensive economic partnership by ASEAN and its six dialogue partners – China, Japan, and the ROK, along with Australia, New Zealand, and India (more on this just below). While the economic benefits of the deal are its primary rationale, there is no missing the political element. All participants hope that a tighter web of economic ties will cushion the relationships and help defuse some of the tensions that have dominated politics in Northeast Asia

### **Dueling trade deals: TPP v RCEP**

The uneasy relationship between politics and economics was evident in another set of trade talks. Also at the East Asia Summit, China, Japan, South Korea, India, and 12 other countries formally launched negotiations on a separate Asia-Pacific free trade agreement known as the Regional Comprehensive Economic Partnership (RCEP). RCEP is an ASEAN-centered trade proposal – not surprising when the 16 members are the 10 ASEAN nations and the six countries with which they have concluded FTAs. Those 16 countries account for nearly half the world's population, about 30 percent of global GDP, and over a quarter of world exports. RCEP aims to achieve a modern, comprehensive, high-quality and mutually beneficial economic partnership agreement that covers trade in goods, services, investment, economic and technical cooperation, intellectual property, competition, dispute settlement, and other issues.

All that seems laudable. What is troubling is the seeming competition between RCEP and the Trans-Pacific Partnership (TPP) that the US is pushing. TPP is starting small, with just 11 members, but it seeks to create a “high standard, broad-based regional pact.” TPP is the economic component of the US rebalance to Asia, proof that Washington takes Asian concerns seriously, both in terms of priority – trade and economics v. the usual military focus – and in terms of presence: a trans-Pacific trade deal is intended to enmesh the US in the region, tying its future more tightly to that of the Asia Pacific and countering fears that the US might disengage.

The US seeks a smaller group to forge a “better quality” agreement; it wants the TPP to be the gold standard for trade deals, in both scope (the range of issues covered) and scale (the degree of openness). Some governments worry that such a deal might be too much for them, imposing US standards on economies that they aren’t ready for. One reason the US hasn’t pushed for more participants is that Washington doesn’t want to dilute the rules.

Other governments see more nefarious designs. They note that China hasn’t been included in the TPP and conclude the deal is intended to forge an alternative economic architecture for the region that puts the US, rather than China, at the center of the network. In discussions in Seoul in December, some Asian analysts went further, asserting that TPP is a device to block Asia’s economic integration. Clearly, the US has a strategic communications problem.

### **The economic outlook**

Driving the increasing attention to the region is recognition that Asia is where the economic action is. With global growth unsteady at best, Asia continues to be a dynamo, with growth rates considerably better than the global average and especially those of the developed world. So, while the UN’s World Economic Situation and Prospects 2013 forecasts global expansion of 2.4 percent in 2013, it anticipates average growth in Developing East Asia of 6.2 percent in 2013, a nearly half-point increase from the 5.8 percent expansion forecast for 2012. For its part, the IMF reckons Asia will post 5.5 percent growth in 2012, a half percentage point below 2011, but still 2 percentage points faster than the global average. It projects about 6 percent growth for the region in 2013.

The biggest issues for many Asian economies are external. The Eurozone crisis remains a source of potential global instability – no real resolution is in sight – and the prospect of US default (at worst) or ongoing paralysis (as seems likely) dampens their prospects for growth. Europe’s embrace of austerity, despite World Bank confessions that its economists didn’t understand the real impact of multipliers, means that policy is likely to continue to exert downward pressure on growth. The failure of Asia’s two largest markets to stabilize and return to solid growth means that regional exporters’ prospects remain equally shaky.

Within the region, China seems to have weathered many of the uncertainties of 2012, and the debate over a soft landing has been quieted. In Japan, the stimulus provided by rebuilding projects after the March 11, 2011 earthquake has worn off. Revised government figures in November showed Japan’s economy shrank 0.9 per cent between July and September. This was the seventh quarterly downturn since the Lehman Brothers collapse in 2008, leading economists

to predict that Japan had entered its fifth technical recession – two consecutive quarters of contraction – in 15 years.

Abe Shinzo, Japan's new prime minister, has vowed to get the country's economy moving again. To achieve that, he had demanded that the Bank of Japan set an inflation target of 2 percent and has lifted the DPJ-imposed limit on the budget. With that cap removed, he intends to resort to the time-tested LDP favorite remedy, public works spending. That may inflate the economy, but the immediate effect has been a fall in the value of the yen against the dollar, a development that delights Japanese exporters – and may well be the real goal.

The other big development to watch in 2013 will be the discussion of the internationalization of the RMB. China sees the US dollar's role as the world's reserve currency as conferring an unfair advantage on the US and affording it undue economic influence. China would like to see that role reduced, and even talks about increasing the role of the RMB as a result. Internationalization of China's currency would cut Chinese trade costs and facilitate more exchange. Consistent with that, there has been a considerable increase in the use of the RMB as a trading currency, reducing pricing in dollars. From 2008-11, the share of global trade that used the RMB rose from 0 to 11 percent. The goal of achieving capital convertibility in the medium run was adopted in the 12th Five-Year Plan for 2011–2015.

But the skeptics counsel caution. Some note that while an increasing number of trades are settled in RMB, they are invoiced in dollars, prompting speculation that there is exchange rate arbitrage at work (i.e., companies are buying and selling RMB offshore to take advantage of exchange rate differentials). Most significant, however, is the Beijing government's desire to maintain control over the economy. Internationalization of the RMB in any meaningful amount means that China must lift its hand. There is no evidence that China is prepared to go that far and thus it will continue to complain about the role of the dollar, but it won't take the steps required to change that reality.

### **And into 2013**

That last prediction is probably good for much of Chinese policy. The region faces a slew of challenges in 2013, and many, if not most, demand that governments respond to internal pressures and problems. Unfortunately, real leadership was in short supply at the end of 2012. The new governments in Asia will have ample opportunities to differentiate themselves from their predecessors. Making hard choices to forge enduring solutions is a good way to start.

## **Regional Chronology September – December 2012**

**Sept. 1-2, 2012:** Cambodian Prime Minister Hun Sen visits Beijing and meets Prime Minister Wen Jiabao who pledges to give Cambodia \$500 million in loans for infrastructure projects. China also approves a \$2 billion industrial park project that would produce 3 million tons of steel per year and employ up to 10,000 Cambodians.

**Sept. 3, 2012:** South Korea announces that it and Japan have temporarily suspended a military exchange program amid the dispute over Dokdo/Takeshima.

**Sept. 3, 2012:** Vietnam and China hold their third Strategic Defense Dialogue in Hanoi with Deputy Defense Minister Nguyen Chi Vinh and Chinese counterpart Ma Xiaotian as co-chairs.

**Sept. 5, 2012:** Secretary of State Hillary Clinton expresses “disappointment” with China and Russia for blocking UN Security Council calls for stronger intervention in Syria.

**Sept. 6, 2012:** Secretary Clinton becomes the first US secretary of state to visit Timor Leste (East Timor) since its independence from Indonesia 10 years ago.

**Sept. 6, 2012:** Chief Cabinet Secretary Fujimura Osamu confirms that Japan’s national government will purchase three of the five Senkaku Islands for about 2.05 billion yen (\$26 million) from the current private owner.

**Sept. 7, 2012:** A Chinese Maritime Safety Administration ship visits Honolulu to conduct a joint search and rescue exercise with the US Coast Guard.

**Sept. 8-9, 2012:** The annual Asia-Pacific Economic Cooperation (APEC) Leader’s Meeting is held in Vladivostok.

**Sept. 9, 2012:** South Korean President Lee Myung-bak and Japanese Prime Minister Noda Yoshihiko hold impromptu talks at the APEC forum and concur on the need to create a future-oriented relationship.

**Sept. 14, 2012:** China sends six patrol boats to the East China Sea near the Diaoyu/Senkaku Islands to carry out “law enforcement over China’s maritime rights.”

**Sept. 16-22, 2012:** US Secretary of Defense Leon Panetta visits Japan, China and New Zealand.

**Sept. 17, 2012:** Myanmar government pardons more than 500 prisoners, at least 80 of whom were prisoners of conscience.

**Sept. 17-Oct. 4, 2012:** Aung San Suu Kyi makes an extended visit to the US.

**Sept. 20, 2012:** Third annual US-Indonesia Joint Commission Meeting chaired by Foreign Minister Marty Natalegawa and Secretary of State Clinton is held in Washington. The US agrees to sell eight *Apache* gunship helicopters to Indonesia.

**Sept. 21, 2012:** The US lifts a 26-year ban on the visit of New Zealand warships to US Coast Guard and Navy bases around the world as Secretary of Defense Leon Panetta visits Wellington.

**Sept. 22, 2012:** US Congress passes legislation supporting lending from international financial institutions to Myanmar, reversing a ban based on concerns that loans would benefit the previous military junta.

**Sept. 27, 2012:** South Korea hosts a Proliferation Security Initiative exercise in waters off Busan. US, Australia, Japan and South Korea participate.

**Sept. 27-28, 2012:** Northeast Asia Cooperation Dialogue (NEACD), an informal dialogue among the participant countries involved in the Six-Party Talks – South Korea, China, Japan, Russia, and the US – is held in Dalian.

**Sept. 27-28, 2012:** China and the US hold annual meeting under the Sino-US Military Maritime Consultative Agreement in Qingdao.

**Oct. 3-5, 2012:** ASEAN Maritime Forum (AMF) is held in Manila. This AMF is the first to include the eight non-ASEAN members of the East Asia Summit.

**Oct. 4, 2012:** The initial rotation of US Marines completes their deployment in Darwin.

**Oct. 7, 2012:** South Korea and the US announce a “missile guideline” agreement that enables South Korea to extend the range of its ballistic missiles from 300 km to 800 km.

**Oct. 8-17, 2012:** US and Philippines conduct their annual amphibious landing exercises (*PHIBLEX*) focused on disaster relief, humanitarian assistance, and maritime security.

**Oct. 14-15, 2012:** Deputy Secretary of State William Burns travels to Japan and meets Foreign Minister Gamba and Defense Minister Morimoto.

**Oct. 15, 2012:** Philippine government and the Moro Islamic Liberation Front (MILF) sign a framework agreement that grants “exclusive powers” to the Bangsamoro Government, with the central government retaining authority over issues such as national security and foreign policy.

**Oct. 16, 2012:** Chinese fisherman is killed by a South Korean Coast Guard officer during a boarding of a fishing vessel charged with illegal fishing. South Korea subsequently impounds two Chinese ships and 24 survivors.

**Oct. 16, 2012:** Deputy Secretary Burns travels to Seoul to meet senior South Korean officials and to participate in the US-ROK Strategic Dialogue.

**Oct. 17, 2012:** Deputy Secretary Burns travels to China to meet senior government officials.

**Oct. 17, 2012:** Japan, South Korea, and the US confirm that they would cooperate in addressing North Korea’s nuclear activities through the Six-Party Talks following a meeting in Tokyo of Shinsuke Sugiyama, director general of Japan’s Foreign Ministry’s Asian and Oceanian Affairs Bureau, Glyn Davies, US special representative for North Korean issues, and Lim Sung Nam, South Korea’s chief negotiator for peace on the Korean Peninsula.

**Oct. 17, 2012:** Former Japanese Prime Minister Abe Shinzo and other senior government official, including two Cabinet ministers visit Yasukuni Shrine. South Korea and China express displeasure over the visits characterizing them as “extremely regrettable.”

**Oct. 18, 2012:** Deputy Secretary Burns travels to Myanmar and meets President Thein Sein, members of his government, and Aung San Suu Kyi.

**Oct. 19, 2012:** Chinese Vice Minister Fu Ying visits Manila and meets Philippine Foreign Affairs Under Secretary Erlinda Basilio to discuss reducing tensions and bolstering trade and economic ties. Fu also meets President Benigno Aquino and other senior officials.

**Oct. 19, 2012:** Deputy Secretary Burns visits New Delhi to meet senior government officials.

**Oct. 19, 2012:** China dispatches naval vessels, aircraft, and helicopters to the East China Sea for a one-day exercise to “strengthen the capacity to safeguard territorial sovereignty and maritime interests.”

**Oct. 22, 2012:** Foreign and defense ministers from India and Japan meet in Tokyo for a second round of their “2+2 dialogue.”

**Oct. 22-23, 2012:** Delegation of former US security officials, led by former National Security Adviser Stephen Hadley visit Tokyo and Beijing to discussion tensions regarding territorial claims in between Japan and China in the East China Sea.

**Oct. 22-26, 2012:** US and Cambodian navies conduct their third annual joint military exercises, called *Combat Afloat Readiness and Training (CARAT)*.

**Oct. 23, 2012:** Fourth US-China Asia-Pacific Consultations are held in San Francisco.

**Oct. 24, 2012:** US and ROK hold the 44<sup>th</sup> Security Consultative Meeting in Seoul.

**Oct. 24, 2012:** Assistant Secretary of State for East Asian and Pacific Affairs Kurt Campbell travels to Tokyo to meet Vice Foreign Minister Chikao Kawai and other senior officials.

**Oct. 26, 2012:** The World Trade Organization (WTO) General Council approves membership for Laos, making it the last member of ASEAN to join the multilateral trading system.

**Oct. 26-27, 2012:** Assistant Secretary Campbell visits Seoul to meet Deputy Foreign Minister Kim Kyou-hyun and others to discuss the DPRK, economic issues, and regional cooperation.

**Oct. 29-Nov. 1, 2012:** Australia, New Zealand, and China conduct *Cooperation Spirit 2012* in Brisbane. It is the first joint exercise to be held by the three nations’ military forces in humanitarian assistance and disaster relief.

**Nov. 4-6, 2012:** Ninth Asia-Europe Meeting (ASEM) is held in Vientiane, Laos.

**Nov. 5-16, 2012:** Japan and US militaries conduct *Keen Sword* naval exercise involving 37,000 Japanese and 10,000 US military personnel.

**Nov. 6, 2012:** Barack Obama is re-elected president of the United States.

**Nov. 7 2012:** Laos starts construction on a \$3.6-billion hydropower dam on the Mekong River that was delayed for 18 months amid opposition from downstream countries and activists.

**Nov. 11-14, 2012:** Chinese Communist Party (CCP) 18<sup>th</sup> Party Congress is held in Beijing. Seven new members are appointed to the Politburo Standing Committee including

**Nov. 12-17, 2012:** Secretary of Defense Panetta visits Asia with stops in Australia to attend the Australia-US Ministerial Consultations, Thailand to sign a Thailand-US Joint Vision Statement, and Cambodia to address the ASEAN defense ministers.

**Nov. 14, 2012:** Australia-United States Ministerial Consultations (AUSMIN) are held in Perth.

**Nov. 15, 2012:** Thailand and the US release a Joint Vision Statement for the Thai-US Defense Alliance that outlines the goals for what is described as a 21<sup>st</sup> century security partnership.

**Nov. 15-16, 2012:** Japan and North Korea meet in Ulan Bator to discuss past abductions of Japanese nationals by North Korea. Japanese negotiator Shinsuke Sugiyama and Song Il Ho, DPRK's ambassador for normalization talks with Japan agree to future discussions on the topic.

**Nov. 15-17, 2012:** ASEAN defense ministers meet in Siem Reap to exchange views on national defense and regional security issues.

**Nov. 17-20, 2012:** President Barack Obama visits Cambodia, Thailand and Myanmar.

**Nov. 18, 2012:** ASEAN heads of government initial the ASEAN Human Rights Declaration – years in negotiation – stipulating the individual to be the focus of human rights, though providing each state with implementation authority based on its national situation.

**Nov. 18-20, 2012:** The 21<sup>st</sup> ASEAN Summit, ASEAN dialogue partner meetings, the 15<sup>th</sup> ASEAN Plus 3 Summit, and the 7<sup>th</sup> East Asia Summit are held in Phnom Penh.

**Nov. 19, 2012:** At the US-ASEAN Summit in Phnom Penh, the “US-ASEAN Expanded Economic Engagement Initiative” (E3) is launched to expand trade and investment ties.

**Nov. 20, 2012:** Official negotiations for the Regional Comprehensive Economic Partnership (RCEP) are initiated by ASEAN leaders and their six regional free-trade partners (Australia, China, India, South Korea, Japan and New Zealand).

**Nov. 20, 2012:** Trade ministers of South Korea, China and Japan meet on the sidelines of the ASEAN Plus 3 Summit to officially open separate talks toward a three-way free trade pact.



**Nov. 26-27, 2012:** The First Vietnam-Japan Defense Strategic Dialogue at the deputy-ministerial level is held in Hanoi, co-chaired by Deputy National Defense Minister Lt. Gen. Nguyen Chi Vinh and Deputy Defense Minister Kanazawa Hironozi.

**Nov. 28, 2012:** US Department of the Treasury releases its *Semi-Annual Report to Congress on International Economic and Exchange Rate Policies*, which does not label China a currency manipulator but instead emphasizes China's actions to appreciate its currency and move to a more market determined exchange rate.

**Dec. 1, 2012:** North Korea announces a Dec. 10-22 launch window for a satellite launch from its launch facility at Sohae.

**Dec. 1, 2012:** Japan announces the postponement of planned talks to normalize relations with North Korea.

**Dec. 3-12, 2012:** Negotiators meet in Auckland for the 15<sup>th</sup> round of Trans-Pacific Partnership (TPP) negotiations.

**Dec. 9, 2012:** Vietnamese police disperse anti-China protests in Hanoi and Ho Chi Minh City that stemmed from tensions over territorial claims in the South China Sea.

**Dec. 11, 2012:** Philippine Energy Secretary Carlos Jericho Petilla announces that Manila will temporarily suspend the process for awarding contracts for three oil and gas blocks in the South China Sea.

**Dec. 11-12, 2012:** Philippines and the US hold their third Bilateral Strategic Dialogue in Manila.

**Dec. 12, 2012:** North Korea launches a satellite into outer space using a three-stage rocket.

**Dec. 14, 2012:** China submits a continental shelf claim to the United Nations that asserts Chinese sovereignty in the East China Sea to the Okinawa trough.

**Dec. 16, 2012:** The Liberal Democratic Party wins 294 seats in the 480-seat lower house of parliament in Japanese general election.

**Dec. 18-19, 2012:** China and the US hold the 23<sup>rd</sup> Joint Commission on Commerce and Trade (JCCT) in Washington.