



# The Future of a World Divided into Economic Blocs: Multilateral trade contributes to economic security



The author points out the trend of decoupling in terms of trade and investment, which is occurring mainly between the United States and China, is making headway through the recent friendshoring movement like IPEF, the U.S.-EU Trade and Technology Council (TTC) and APEP). And he emphasized that “Japan should pursue a trade strategy based on the concept of the maintenance of the multilateral trading system in order to avoid the adverse effects of excessive decoupling and reconcile economic security with economic growth.”

Photo: President Biden launched IPEF in Tokyo on May 23 2022, Cabinet Public Affairs Office

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The fragmentation of the international trade and investment system is proceeding in the name of national security. In particular, since the years of the Trump administration, the United States has implemented many trade measures for national security reasons. Specific examples include: (1) aggressive application of the Export Administration Regulations (EAR); (2) the imposition of other restrictions on trade in goods and services; (3) the imposition of restrictions on foreign direct investment; and (4) the application of trade regulations from the viewpoint of human rights as a national security matter (see table).

## Major national security-related trade measures introduced by the United States

### (1) Aggressive application of the Export Administration Regulations (EAR)

Aggressive imposition of export restrictions against Chinese high-tech and communications companies (e.g., Huawei and ZTE)

Strengthening of export restrictions on advanced semiconductors, semiconductor-making equipment, and supercomputers

### (2) Restrictions on trade in other goods and services

Imposition of additional tariffs on steel and aluminum imports (Section 232 of the Trade Expansion Act of 1962 )

Increase in tariffs on 370 billion dollars' worth of imported Chinese products (Section 301 of the Trade Act of 1974)

Restrictions on the use of TikTok

### (3) Restrictions on foreign direct investment

Tightening of the review of foreign direct investment in the U.S. by the Committee on Foreign Investment in the United States (CFIUS)

Imposition of restrictions on U.S. direct investment in China under an executive order based on the National Defense Authorization Act of 1999

### (4) Application of trade regulations from the viewpoint of human rights as a national security matter

The imposition of export bans for reasons of forced labor, and the enactment of the Uyghur Forced Labor Prevention Act

Application of the EAR to Hikvision and Dahua Technology for using technology for the purpose of human rights repression

Ban on the use of the “Made in Hong Kong” label (Hong Kong Policy Act)

On the other hand, the trend of decoupling in terms of trade and investment, which is occurring mainly between the United States and China, is making headway through the recent friendshoring movement, which refers to the building and strengthening of supply chains among like-minded countries. Following the conclusion of agreements on the Indo-Pacific Economic Framework (IPEF) and the U.S.-EU Trade and Technology Council (TTC), negotiations on the Americas Partnership for Economic Prosperity (APEP) started in January 2023.

Those partnership frameworks place emphasis on ensuring national security and sharing of values and aim to conclude agreements on cooperation for: the strengthening of supply chains particularly for strategic goods and technologies such as semiconductors, critical minerals, and post-quantum technologies; decarbonization; the reliability of artificial intelligence (AI); and export controls and investment screening.

Those developments indicate the expansion of the concept of national security, which has traditionally centered on military and defense matters.

When the United States applied the EAR to Chinese companies due to China's acts of repression in the Xinjiang Uyghur Autonomous Region and Hong Kong, it treated the human rights issues in China as a matter of national security for itself. The Biden administration has also clearly recognized climate change as a top national security challenge. The framework of friendshoring, which is rooted in national security concerns, covers not only human rights and climate change but various other challenges, such as pandemics, cybersecurity, energy transition, and advanced technology.



However, the series of measures taken as a result of the expansion of the concept of national security has created divisions even among allied countries, thereby undermining national security. For example, the EU and other Western economies filed complaints with the WTO against the United States in relation to the additional U.S. tariffs imposed on steel and aluminum imports in 2018. The enactment of the Inflation Reduction Act and CHIPS Act of the United States has also brought about trade disputes with Japan and South Korea, whose products have been put at a disadvantage under those laws.

On the other hand, the EU has enacted its own version of the CHIPS Act in order to promote the semiconductor industry and also launched the Green Deal initiative, which facilitates support for the decarbonization industry. As a result, there is a cause for a future trans-Atlantic trade war over subsidies.

There are also concerns over acts of protectionism disguised as national security measures. A WTO dispute settlement panel did not recognize the U.S. tariffs on steel and aluminum imports and the U.S. requirements concerning country-of-origin labeling of products from Hong Kong as measures taken for national security reasons. With regard to the supply of strategic goods and the development of strategic industries, the U.S. tax credit program for electric vehicles (EVs) under the Inflation Reduction Act imposes conditions that are neither consistent with the WTO agreements nor sufficiently reasonable from the perspective of national security, such as mandating the use of critical minerals manufactured or processed in the United States or in the regions covered by FTAs, and assembly in the United States.

The provision of subsidies under the CHIPS Act also has a strong element of industrial policy, as it requires compliance with conditions that are unrelated to national security, such as the use of U.S.-made materials in the construction of semiconductor plants and the disclosure of advanced technology to the government.

Meanwhile, ensuring free trade helps to diminish economic coercion. Australia was confronted with China's restrictions on imports of wine and barley but succeeded in defending itself against the Chinese

economic coercion by finding alternative export markets under the open, multilateral trading system.

Sometimes, countries resort to economic measures, such as trade restrictions and financial embargoes, in order to achieve their own geopolitical objectives (such practices are known as economic statecraft). Ensuring free trade prevents the “weaponization of interdependence,” which refers to the practice of taking advantage of the choke points in international supply chains for critical goods and technologies to engage in economic statecraft.

Typical examples include the Chinese export ban on rare earths introduced in the early 2010s due to the dispute over the Senkaku Islands and the export restrictions on rare earth magnets that China is preparing to introduce in retaliation against the Western export bans on semiconductors and related equipment and materials. The presence of the WTO rules eventually led to the removal of the Chinese export ban on rare earths.



The importance of economic security for Japan cannot be denied, but caution must be exercised in relation to promoting economic security. According to Yoichi Funabashi, chairman of the Global Council of the International House of Japan, Japan is a country with a “national security deficit” because of the regional geopolitical environment—it is surrounded by countries that are considered to be potential national security threats, namely China, Russia and North Korea—and also because of its dependence on foreign supply sources of resources and food. For Japan, maintaining the open multilateral trading system as a basic policy contributes to its own economic security by securing a diverse range of alternative procurement sources and foreign markets.

For example, a survey conducted in 2022 by the Economist Group of the United Kingdom ranked Japan sixth in the global food security rankings of countries, despite the country’s low food self-sufficiency rate and the impact of the Ukraine crisis, because Japan ensures stable supply through trade. On the other hand, the current situation of Germany, which increased its energy dependence on Russia, with which an intimate relationship was cultivated at the top-leader level in the recent past, is an indication of the risk that depending excessively on partner countries through friendshoring presents to economic security.

In that sense, over-reliance on friendshoring or reshoring (bringing home manufacturing and other business operations from abroad) will not be in Japan’s best interests. They are merely measures for reducing excessive dependence on China by diversifying supply chains and dispersing risk, and, therefore, the emphasis should remain in maintaining the multilateral, free trade system. The nature of Japan’s national interests is critically different from the nature of the national interests of the United States, which is a country with a “national security surplus” in terms of domestic natural resources, technologies and markets, and which can create supply chains with its friendly neighboring countries, Canada and Mexico.

Given the abovementioned circumstances, Japan should pursue a trade strategy based on the concept of the maintenance of the multilateral trading system in order to avoid the adverse effects of excessive decoupling and reconcile economic security with economic growth.

Therefore, first of all, Japan should exercise caution in taking trade measures for national security reasons. Measures permitted under the WTO rules and FTAs are limited to those that are essential for protecting critical national interests. As a WTO panel pointed out in the past, national security is not a magic word that can justify everything. The recent export control of semiconductor-manufacturing equipment must be a measure that contributes not to the U.S. industrial policy but to the national interests of Japan itself.

The joint efforts to counteract economic coercion that were proposed at the G7 trade ministers' meeting represent a trade version of “collective defense,” so to speak. When considering whether or not to engage in such collaboration, it is necessary to keep in mind the possibility that doing so could cause fundamental changes to the relationship between the multilateral trading system and national security.

Exercising leadership in maintaining and further developing the traditional multilateral trading system should be the basis of Japan's future geopolitical policy. In the negotiations over China's accession to the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), Japan should cooperate with like-minded countries, such as the United Kingdom and Canada, and should not compromise over the principle of ensuring compliance with the rules and commitment to a high level of market openness. At the WTO, it is essential to restart the Appellate Body, which remains dysfunctional, before the target year of 2024, and to continue exercising leadership in the negotiations over digital trade rules in order to deliver concrete results at the WTO ministerial conference scheduled for 2024.

Japan has joined the Multi-Party Interim Appeal Arbitration Arrangement (MPIA), which reviews appeals against panel decisions in the absence of an operational Appellate Body. The EU and Australia have filed complaints against the series of acts of economic coercion by China on the premise of using the MPIA. For Japan, too, using the MPIA to maintain the trade order based on the WTO rules will contribute to its economic security.

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