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Political Economy of Free Trade Agreements in China, Japan, and South Korea: Sectoral and National Security Politics of the FTA Wave

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POLITICAL ECONOMY OF FREE TRADE AGREEMENTS IN CHINA, JAPAN, AND SOUTH KOREA:

SECTORAL AND NATIONAL SECURITY POLITICS OF THE FTA WAVE

by

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ABSTRACT

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The University of Wisconsin-Milwaukee, 2013

Under the Supervision of Professor Shale Horowitz

Over the course of three essays, this dissertation examines three important questions regarding free trade agreements (FTAs) in China, Japan, and South Korea (CJK), the three main economies of Northeast Asia: Under what conditions are CJK most likely to establish an FTA? Which factors most significantly influenced U.S. Congressional voting on the Korean-U.S. Free Trade Agreement (KORUS FTA)? Is the establishment of a multilateral FTA among China, Japan, and South Korea (a CJK FTA) possible and, if so, what is the optimal path towards achieving it? In answering these questions, the cumulative findings indicate that an FTA is the result of sectoral and national security politics rather than a calculation based on economic optimality.

The first essay finds that CJK are most likely to establish an FTA when politically potent industry interest groups (IIGs) favor it. This study also finds that the impacts of FTA determinants vary depending on what stage the FTA formation process is in. For

example, political institutions are likely to influence FTA formation in the initial stages but are prone to lose their influence as the process moves forward. In the final stage, support from IIGs is the driving force. Another significant finding is that political leaders are likely to choose their FTA partners in the context of national security politics.

As the first empirical analysis of US Congressional voting on the KORUS FTA, the major findings of the second essay indicate that constituent interest was a highly significant predictor of US legislators' voting. Moreover, constituent interests play a more significant role in the House of Representatives rather than the Senate. National security considerations were also found to greatly influence legislators' voting.

The third study mainly finds that, although the two possible bilateral FTAs (a China-Korea FTA or Japan-Korea FTA) are more feasible than a CJK FTA, neither is likely to serve as a stepping-stone to multilateral FTA formation. Consequently, a multilateral path is optimal, and therefore, CJK should simultaneously participate in a single round of trade negotiations in order to establish a multilateral FTA.

DEDICATION

This dissertation is dedicated to my parents.

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LIST OF ABBREVIATIONS

AC FTA	ASEAN-China Free Trade Agreement
ACU	American Conservative Union
ADA	Americans for Democratic Action
AFL-CIO	American Federation of Labor, Congress of Industrial Organizations
AJ CEPA	ASEAN-Japan Comprehensive Economic Partnership Agreement
ASEAN	Association of Southeast Asian Nations
CCP	Chinese Communist Party
CJK	China, Japan, and South Korea
CJK FTA	China-Japan-Korea Free Trade Agreement
CK FTA	China-Korea FTA
CJ FTA	China-Japan FTA
COC	Chamber of Commerce
CU	Custom Union
DRC	Development Research Center of the State Council
EA FTA	East Asian Free Trade Agreement
ECS	East China Sea
EPA	Economic Partnership Agreement
EU	European Union
FTA	Free Trade Agreement
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GNP	Grand National Party
IIG	Industry Interest Group
JK FTA	Japan-Korea FTA
KIEP	Korea Institute for International Economic Policy
KITA	Korea International Trade Association
KORUS FTA	Korea-US FTA
LCV	League of Conservation Voters
MFN	Most Favored Nation
NAICS	North American Industry Classification System
NGOs	Non-Governmental Organizations
NICs	Newly Industrialized Countries
NIRA	National Institute of Research Advancement
NSI	National Security Index
NTB	Non-Tariff Barriers
PAC	Political Action Committee
PTA	Preferential Trade Agreement
RCA	Revealed Comparative Advantage
SITC	Standard International Trade Classification
TCI	Trade Complementary Index

TPA	Trade Promotion Authority
UAW	United Auto Workers
USITC	United State International Trade Commission
WTO	World Trade Organization

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CHAPTER 1
INTRODUCTION

Over the course of three essays, this dissertation examines three important questions regarding free trade agreements (FTAs) in Northeast Asia: Under what conditions are China, Japan, and South Korea, the three main economies in Northeast Asia, most likely to establish FTAs? Which factors most significantly influenced voting in the United States Congress on the Korean-US Free Trade Agreement (KORUS FTA)? Is it possible to establish a multilateral FTA among China, Japan, and South Korea (a CJK FTA), and what is the optimal path towards achieving it? In answering these questions, this dissertation demonstrates that an FTA is the result of domestic and international political considerations rather than a calculation based on economic optimality. Prior to answering each question, Chapter 1 discusses the determinants of FTA formation developed in existing research and provides an overview of this dissertation.

An FTA is widely defined as an economic agreement between two countries or regional groupings to eliminate tariffs and other trade barriers. In general, there are five types of regional trade agreements (RTAs), listed here in order from lowest to highest level of integration: a) at the lowest level of integration, a preferential trade agreement (PTA) allows member states to grant the other participants preferential access to select segments of their markets; b) in a free trade agreement (FTA), member states eliminate (or reduce) trade barriers on certain (if not all) products; c) in a customs union (CU), barriers are not only eliminated but a common external tariff (CET) is erected vis-à-vis third parties; d) a common market adds more criteria to a CU such as implementing

similar product regulations and permitting the free flow of factors of production between member countries; and e) at the highest level of integration, an economic union requires member states to coordinate fiscal and monetary policies (Mansfield, Milner, and Pevehouse 2008: 67). All RTAs that China, Japan, and Korea (CJK) have established can be considered FTAs.[1]

In recent years, the number of Free Trade Agreements (FTAs) has increased rapidly. As of 2013, the World Trade Organization (WTO) had recorded 218 FTAs in the world and of these, 56 were FTAs wherein one of the signatories was an East Asian country. In the 1990s, Northeast Asian countries were more likely to focus on unilateral, non-discriminatory liberalization, reinforced by the WTO. After experiencing the Asian financial crisis in 1997-98 and realizing disadvantages from other regional blocs, the three countries have become less active in the WTO and more enthusiastic about establishing regional FTAs. Given the growing global trend towards FTA formation, FTAs have become a major interest in various fields of research. Initially, FTAs were mainly paid attention to by economists, who focused on their welfare-enhancing impacts based on the CGE (Computable General Equilibrium) analyses. Since FTAs have distributional consequences, they create economic winners and losers in domestic as well as international markets. It has been easily observed that FTA discussions led to conflicts between those winners and losers in domestic as well as international politics. Therefore, political science has also taken a considerable interest in the causes and consequences of FTA formation.

[1] Indeed, Japan has interchangeably used the terms of an economic partnership agreement (EPA) and an FTA. However, the basic concept of an EPA and an FTA is the same (Ahearn 2005).

FTA formation in CJK has shown quite different patterns from European and North American FTA formation. European and North American countries have pursued extra-regional FTAs after consolidating their own regional blocs. In contrast, CJK have established extra-regional FTAs (e.g., Japan-Mexico FTA, Korea-Chile FTA, China-Costa Rica FTA) soon after they began to launch regional FTA initiatives (Solis and Katada 2007). The three countries have merely discussed the possibility of FTAs with each other and have done so for a relatively long period of time. Discussions about a Japan-Korea FTA (a JK FTA) have been ongoing since 1998 and those of a China-Korea FTA (a CK FTA) since 2005. The three countries have also been considering establishing a multilateral FTA, a China-Japan-Korea FTA (a CJK FTA), since 2003.[2] Accordingly, Northeast Asia is the only major region without a region-level trade agreement, despite the region's economic size and participation in a substantial amount of intra-regional trade. In 2012, the combined GDP (Gross Domestic Product) of CJK accounted for 21% of global GDP, and the combined volume of CJK's trade in 2012 accounted for 18% of the global total.[3] If established, therefore, a trade agreement among CJK would significantly influence the regional as well as the global economy.

Despite these unique features of Northeast Asian FTAs, theories developed from European or American experiences have tended to be inappropriately applied in their understanding and explanation. The primary aim of this dissertation is to construct a distinct and valid theory that can explain the distinctive characteristics of FTA formation in Northeast Asia by answering the three aforementioned questions. To achieve this goal,

[2] The processes of the three FTA discussions are described in Table 4.1 (p. 96).
[3] The economic significance of the three main economies in Northeast Asia is discussed in Chapter 4.

the determinants of FTA formation developed by preceding research need to be discussed first.

Determinants of FTA Formation

Many scholars have contributed to a burgeoning body of literature that sheds light on the determinants of FTA formation. This extensive scholarly interest in FTAs has yet to reach a consensus on which determinants are most significant. Broadly speaking, there are three primary scholarly approaches to explaining FTA formation.

1. Economic analyses of FTAs

1.1 Welfare-enhancing effects of FTAs

Much of the literature on FTAs in the field of economics focuses on the welfare implications of FTAs, both for members and the world as a whole. According to Viner (1950), whether FTAs increase or decrease the national welfare depends upon the relative magnitude of so-called "trade creation" and "trade diversion" effects. Trade creation occurs as low-cost FTA partners displace high-cost domestic producers, while trade diversion happens when the county reorients its trade away from low-cost, non-member countries towards high-cost FTA partners. Viner argues that, "Where the trade-creating force is predominant, one of the members, at least must benefit, both may benefit, and the two combined must have a net benefit, and the world at large benefits…Where the trade-diverting effect is predominant, at least one of the member countries is bound to be injured, both may be injured, the two combined will suffer a net injury, and there will be injury to the outside world and to the world at large" (p. 44). In this connection, a simple conceptual criterion for assessing trade creation and trade diversion is whether the

member countries are "natural trading partners" or not. According to the "natural trading partner hypotheses" mainly endorsed by Wonnacott and Lutz (1989) and Summers (1991), FTAs maximize trade creation and efficiency gains when FTA partners are natural trading partners with a high initial volume of trade and a close distance between them. Opponents to this position argue that the welfare implications of FTAs are not so straightforward, given the reduction of transportation costs and the elasticity of trade (Bhagwati and Panagariya 1996; Krugman 1999).

1.2 Building blocks vs. Stumbling blocks

This ambiguity about the welfare-enhancing effects of an FTA has led to another significant question about whether an FTA will accelerate or inhibit multilateral trade liberalization. This issue is associated with the time-honored question of whether an FTA serves as a "building block" or a "stumbling block." The supporters of the "building block" argument stress that an FTA promotes global free trade. For example, Baldwin (1995) argues that regionalism fosters multilateral trade liberalization by raising the incentives of outside countries to join the existing trading bloc (i.e., domino effect). Ethier (1998), Cadot et al. (2001), Freund (2000), and Ornelas (2005) find that regionalism provides a path to global free trade.

In contrast, several studies support a "stumbling block" argument. Bhagwati and Krueger (1995) and Bhagwati and Panagariya (1996) argue that the rise of FTAs can be a serious threat to global free trade. Levy (1997) argues that an FTA undermines political support for further multilateral trade liberalization. Employing the political economy function and stressing the interaction between political leaders and interest groups, he

finds that if a bilateral trade agreement offers disproportionately large gains to key agents in a country, it can never increase political support for multilateral free trade. Krishna (1998) and McLaren (2002) show that multilateral liberalization that is initially feasible could be rendered infeasible by an FTA. In a similar vein, Aghion, Antras, and Helpman (2007) argue that global free trade is not achieved if political leaders pursue economic self-interest rather than the aggregate welfare of a country.[4] They also insist that multilateral negotiations lead to free trade, while sequential negotiations may lead to an FTA between two countries only.

At present, the trend of CJK FTA formation is more likely to follow the "stumbling block" argument. CJK have tended to pursue bilateral FTA formation rather than multilateral trade liberalization. After establishing FTAs with multilateral groups (e.g., FTAs with ASEAN), CJK have pursued the formation of separate bilateral FTAs with one of the member countries of the groups. Although the ASEAN-Korea FTA came into effect in 2012, for example, the Korean government has officially negotiated bilateral FTA formation with Vietnam and Indonesia by expecting to expand the tariff reduced (or eliminated) items. Moreover, no empirical evidence exists that a bilateral FTA has extended into a multilateral FTA in CJK.

2. National security and FTAs

Economic analyses indicate that an FTA's welfare implications have varied greatly depending on their particular circumstances. Mansfield and Milner (1999) argue that these circumstances involve political conditions that economic studies often neglect.

[4] This issue is more specifically discussed in Chapter 2.

It is widely argued, in particular, that political leaders in Northeast Asia place more focus on national security calculations rather than welfare-enhancing considerations in deciding whether or not to form an FTA. For example, several studies argue that despite huge expected benefits, there is as yet no multilateral FTA in Northeast Asia due to the Sino-Japanese rivalry (Hemmer and Katzenstein 2002; Solis and Katada 2007; Rozman 2007; Bergsten 2007).

Furthermore, a number of studies stress the links between international politics and FTA formation. Emphasizing the effects of hegemony, they argue that eroding hegemony has been associated with the growth of FTAs. As empirical evidence of this, they emphasize that the erosion of US hegemony has stimulated a rise in the number of FTAs and states entering into them. When the power of a hegemon declines, states are more likely to seek insurance against contingency by establishing an FTA (Gilpin 1975; Krasner 1976; Mansfield 1998). In contrast, several studies argue that hegemony has little effect on regionalism, noting the coincidence of the apex of US hegemony and the earlier wave of regionalism during the 1960s (McKeown 1991; Yarbrough and Yarbrough 1997).

The role of multilateral institutions (GATT/WTO) in FTA formation has also been highlighted in the field of international political economics. Mansfield and Milner (1999) indicate that most contemporary FTAs have been established with the support of the GATT/WTO, which has tried to decrease trade diversion by limiting member countries' ability to discriminate against third parties. Mansfield and Reinhardt (2003) argue that developments at the heart of GATT/WTO encourage its members to form FTAs in order to obtain bargaining leverage within the multilateral regime.

However, hegemonic power and multilateral institutions are less likely to be meaningful in the analyses of Northeast Asian regionalism. First, there is no absolute regional hegemon in Northeast Asia; moreover, the extra-regional hegemonic power, namely the US, has been relatively weak in Northeast Asia as compared to Europe and North America. In addition, Northeast Asian countries have become less active in the WTO since the Asian financial crisis.

In contrast, the political-military relationships established during the Cold War era are still important in establishing agreements in this region. Several scholars stress the role of allies in FTA formation, since gains from FTAs can be used to increase states' political-military capability. States can attend to these externalities by trading more freely with political-military allies than with neutral countries or adversaries (Gowa 1995; Gowa and Mansfield 1993; Mansfield and Bronson 1997). In Northeast Asia, the political-military relation is still quite influential on foreign policy decision-making.

3. Domestic politics and FTAs

3.1 Political institutions

This 'outside in' approach to understanding FTA formation is criticized by the 'inside out' framework centering on the domestic political dynamics of policy decision-making (Jayasuriya 2003). The 'inside out' approach mainly argues that an FTA is the result of domestic political games centering on the nature and strength of domestic institutions. One strand of this approach has stressed the effects of regime type, focusing on whether democracies promote trade liberalization. Several studies find that democracies are more likely than autocracies to form FTAs (Milner with Kubota 2005;

Mansfield, Milner, and Rosendorff 2002; Frye and Mansfield 2004; Heniz and Mansfield 2006).[5] In contrast, other studies argue that democracies hinder trade liberalization. Verdier (1998) indicates that democracy empowers various economic groups. If similar regime types empower similar industry groups, this may lead to cross-national competition among them. Kono (2006) points out that political leaders in democracies have an incentive to hold tariffs low for median voters but they also have reason to rely on non-tariff barriers (NTBs) to protect certain industries for their own political incentives. Analyzing 75 countries in the 1990s, Kono (2006) finds that democracies are more likely to have relatively low tariff levels, but relatively high NTBs.

Recognizing that democracies are not homogenous, some recent studies stress the institutional variations among democracies. They place primary focus on the role of veto players and their findings indicate that democracies with a greater number of veto players are less likely to form an FTA (Henisz and Mansfield 2005; Mansfield, Milner and Pevehouse 2008). As existing research on 'two-level games' indicates, it is difficult to forge international agreements when leaders confront an array of domestic groups with diverse preferences and the ability to block policy initiatives (Mo 1994; Milner and Rosendorff 1996). In democracies, an FTA needs to be ratified by legislators to enter into force. Even in non-democratic political systems, one rarely finds an absolute hierarchy with a unitary decision maker and no veto players (Mansfield, Milner and Pevehouse 2008). When veto players reflect the preferences of distributional losers, FTA formation becomes more difficult and unlikely. A higher number of veto players provide more outlets through which the losers can hinder FTA formation.

[5] Chapter 2 discusses why democracies are more likely to promote trade liberalization.

3.2 Preference and power of interest groups

The 'inside out' approach also stresses the influence of interest groups (Rogowski 1989; Viner 1932; Gourevitch 1986; Grossman and Helpman 1995; Maggi and Rodriguez-Clare 1998). These studies generally consider domestic institutions and policy makers as passive actors that supply trade policies as demanded by the most influential interest groups (Ikenberry et al. 1988). However, surprisingly few systematic attempts have been made to address the impacts of interest groups on FTA formation; this is mainly due to difficulty in their measurement. Since the composition and power of interest groups vary greatly across countries, it is very hard to compare different groups' activities in the FTA formation process.

In light of the difficulty of measurement, existing research usually employs qualitative analyses specifically investigating the preferences and activities of important interest groups (in particular, the agriculture industry) related to a single policy (Mulgan 2008; Koo 2008; Lee, Kim, and Wainwright 2010). On the other hand, several quantitative studies examining more general influence of interest groups on trade policies find that interest groups play only a marginal role in a legislator's decision on trade policy (Poole and Rosenthal 2001; Xie 2006). However, the quality of measurement in these quantitative studies is questionable. In light of this need for appropriate measurement, one of the main goals of this study is to develop a new measure of the extent of political pressures from interest groups on FTA formation.

Overview of the Dissertation

1. Chapter 2: Conditions for FTAs in China, Japan, and Korea

The first essay examines the conditions under which the three main economies in Northeast Asia – China, Japan, and South Korea – are most likely to establish bilateral FTAs. A number of studies have investigated the determinants of FTA formation. However, the determinants in existing research have tended to stem from the European and North American experiences. Since CJK FTA formation has arisen in unique circumstances, this element of the study examines whether the determinants in extant research may have similar effects in the analyses of CJK FTAs. Developing a new measure, in particular, this study more correctly investigates the influence of interest groups on FTA formation.

Given the fact that CJK are currently trying to form FTAs with a number of prospective partners and their major trading partners remain in the initial stages of the FTA formation process (FTA under consideration or negotiation), this study assumes that what explains why an FTA is proposed may not as reliably explain why it is subsequently put into place. Therefore, this study also investigates the variations in outcomes across the different stages of the FTA formation process. Such variations have rarely been examined in previous studies. In contrast to existing research employing a dichotomous dependent variable, coded as 1 when an FTA enters into force between two countries, this study divides the FTA formation process into four stages: *FTA under Consideration, FTA under Negotiation, FTA Signed, and FTA in Force.* This serves the goal of this study of investigating the variations in outcomes across the different stages of the FTA formation process.

2. Chapter 3: US Congressional voting on the Korea-US FTA

Following the country-level analyses in the first essay, the second essay examines which factors most significantly influenced sub-national voting in the United States Congress on the Korean-U.S. Free Trade Agreement (KORUS FTA). The KORUS FTA is the only FTA in Northeast Asia in which the US participates. Thus, the KORUS FTA could serve as a model for trade agreements for other countries that desire to establish an FTA with the US. Since the completion of the KORUS FTA was much more dependent on actions in the US than South Korea, this study examines US Congressional voting rather than South Korean National Assembly voting.

Most studies on US legislators' roll-call voting behavior have emphasized the role of political institutions and legislators' ideologies and have found that constituent interests play only a marginal role in a legislator's voting decision. This study argues that these conclusions regarding their marginal role may, in fact, stem from inadequate measurement of constituent interests. Even though constituent interest is usually understood in geographic terms in studies of US Congressional voting, non-geographical constituent interest also exists through campaign contributions. Moreover, preceding studies simply assume that the cleavage of constituent interests on trade policy is formed along the factoral line (capital vs. labor), ignoring possible sectoral interest coalitions (exporting vs. import-competing industries) that have been commonly observed in the US trade policy decision-making process. This assumption may lead to misleading results. This study develops a new measure for constituent interests that considers sectoral as well as factoral constituent coalitions and examines both geographical and non-geographical interests.

3. Chapter 4: The optimal path of a China-Japan-Korea FTA

After quantitatively investigating the determinants of bilateral FTAs, the third essay performs a qualitative analysis of the influences of interest groups and national security relations on FTA formation in order to predict the possibility of a multilateral FTA among China, Japan, and Korea, a CJK FTA, as well as the optimal path towards achieving it. Preceding studies developed from European and North American experiences emphasize the role of leaders in trade liberalization (e.g., the US in the NAFTA formation and Germany and France in the EU formation). Therefore, these studies have tended to focus on the main reasons for the lack of a region-level trade agreement in Northeast Asia, highlighting the absence of leaders given the Sino-Japanese rivalry. Realizing the huge welfare-enhancing effects, a great number of studies emphasize the necessity of the CJK FTA formation. However, studies on precisely how it might be formed and through what paths are extremely scarce.

Given the three players involved, two possible paths to a CJK FTA exist: a multilateral path and a sequential path. In the multilateral path, all three countries simultaneously participate in a single round of trade negotiations. In the sequential path, on the other hand, two countries form a bilateral FTA first and then include the other country in the FTA. While the multilateral path is relatively simple, several key issues exist that should be considered and contrasted with the sequential path. The first issue is whether a bilateral FTA will actually lead to a multilateral FTA. Another significant question is which FTA (a CK FTA vs. a JK FTA) is likely to be established first. Thus, the third study examines the possibilities of all alternative paths to the CJK FTA by

examining the preferences of interest groups and national security considerations in CJK on the agreement.

CHAPTER 2

CONDITIONS FOR FREE TRADE AGREEMENTS IN CHINA, JAPAN, AND KOREA: Sectoral and National Security Politics of the FTA Wave, 1998-2012

<ABSTRACT>

In contrast to the common position that political institutions play the dominant role in forming free trade agreements (FTAs), this study argues that interest groups are substantial players. To explore this proposition, this study examines the conditions under which three main Northeast Asian economies – China, Japan, and South Korea (CJK) – are most likely to establish FTAs. Multinomial logistic regression analyses show that CJK are most likely to establish an FTA when politically potent industry interest groups (IIGs) favor it. Given the fact that CJK's FTA discussions with their major trading partners have often not moved beyond the proposal stage, it is further assumed that FTA determinants may have different impacts depending on what stage the FTA formation process is in. After dividing the FTA formation process into four stages, findings indicate that political institutions are likely to influence FTA formation in the initial stage, but are prone to lose their influence as the process moves forward. In contrast, support from IIGs is the driving force of FTA formation in the last stage where signed FTAs must be ratified (or legalized) to enter into force. Another significant finding is that political leaders are likely to choose their FTA partners in the context of national security politics and their national security consideration is still influential after an FTA is proposed by conducting joint studies. After starting official negotiations, however, political leaders are

more likely to move the FTA discussion to the domestic political arena. The results of this study collectively support the hypothesis that an FTA is the results of sectoral and national security politics.

Given the increased number of FTAs, why particular FTAs are created and what bearing they have on the global economy is of considerable interest in various fields of research. In trying to answer this question, economists center on the welfare-enhancing impacts of FTAs, debating whether an FTA will generate "trade creation" or "trade diversion" effects. However, they generally place little emphasis on the political conditions that form FTAs. Some studies center on international political factors, stressing how power relations and international institutions influence FTA formation (Mansfield 1998; Mansfield and Reinhardt 2003). Others argue that an FTA is the result of domestic political games centering on the nature and strength of domestic institutions. They examine whether particular types of political regimes are more likely to form FTAs and generally find that democracies are more likely to form FTAs than autocracies (Milner with Kubota 2005; Mansfield, Milner, and Rosendorff 2002). Recognizing that democracies are not homogenous, some recent studies stress the institutional variations among democracies (Ahn and Kim 2007; Lohmann and O'Halloran 1994; Milner and Judkins 2005). They place the primary focus on the role of veto players, and their findings indicate that democracies with a greater number of veto players are less likely to form an FTA (Henisz and Mansfield 2006; Mansfield, Milner and Pevehouse 2008).

However, these recent veto player studies disproportionately focus on the 'resistance' side, while the 'support' side of an FTA is left largely unexamined in veto player studies. When there is considerable support for an FTA and less resistance to it, veto players may be less prone to use their veto powers in the FTA formation process (Peterson and Thies 2011). If it is thought that FTAs result from domestic politics, then perhaps the role of veto players on FTA formation should not take sole or primary focus. This study asserts that interest groups play a key role in FTA formation. This argument is supported by much literature on the political economy of trade, which indicates that states are likely to decide whether or not to establish FTAs based on the preferences of policy makers and interest groups (Rogowski 1989; Viner 1932; Gourevitch 1986; Grossman and Helpman 1995; Maggi and Rodriguez-Clare 1998).

Among the variety of interest groups, industry interest groups (IIGs) are one of the most significant groups in FTA formation. Since policy change has distributional consequences, an FTA creates economic winners and losers. In the FTA formation process, sectoral cleavages between exporting industries (potential winners) and import-competing industries (potential losers) have frequently been observed. Surprisingly few systematic attempts have been made to address the impacts of IIGs on FTA formation. This is mainly due to difficulty in their measurement. Since the composition and power of IIGs vary greatly across countries, it is very hard to compare the IIGs' activities in the FTA formation process.

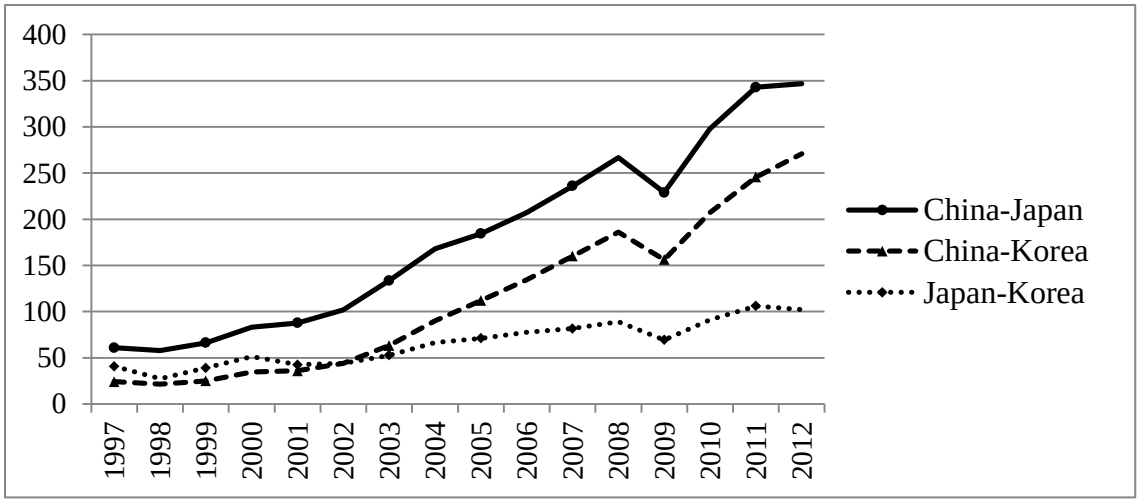
In light of this need for appropriate measurement, this study develops a new measure of the extent of political pressures from IIGs by including four components: a) the trade complementarity of potential FTA country pairs, to predict general reactions of

IIGs toward an FTA given preexisting trade patterns; b) the trade orientation of an industry, to figure out which industries are likely to support or oppose the FTA; c) the share of an industry's GDP, to anticipate how influential the industry's political support or opposition is likely to be; and d) the volume of bilateral trade with an expected partner (% of GDP), to examine how strongly an industry will support (or oppose) the FTA given its expected benefits (or costs).

Setting aside the issue of which factors bear most heavily on FTA formation, the determinants in existing research have tended to stem from the European and North American experiences. Since CJK FTA formation has arisen in unique circumstances, one goal of this study is to examine whether the determinants in extant research may have similar effects in the analyses of CJK FTAs. In the early 1990s, CJK were left behind in the trend of FTA development. They focused on unilateral, non-discriminatory liberalization reinforced by the World Trade Organization (WTO). After the Asian financial crisis in 1997-98, however, they became less active in the WTO and more enthusiastic about establishing bilateral FTAs.[6] In contrast to the pursuit of extra-regional FTAs after the consolidation of regional blocs, as seen in European and North American countries, CJK have established extra-regional FTAs (e.g., the Japan-Mexico FTA, the Korea-Chile FTA, the China-Costa Rica FTA, etc.) soon after they began to launch their regional FTA initiatives (Solis and Katada 2007). More specifically, CJK have not

[6] Ravenhill (2003) points to three factors to explain this trend toward bilateral FTAs: a) an increasing awareness of the weakness of existing regional institutions and initiatives; b) perceptions of positive demonstration effects from regional agreements in other parts of the world; and c) changing domestic economic interests after the economic crisis.

established bilateral FTAs with each other despite their huge amount of bilateral trade,[7] large economic size, and geographical proximity. These three countries have discussed the possibility of FTAs with each other for a relatively long period of time. Discussions about a Japan-Korea FTA (a JK FTA) have been ongoing since 1998, and those of a China-Korea FTA (a CK FTA) since 2005. The three countries have also considered establishing a multilateral FTA, a China-Japan-Korea FTA (a CJK FTA) since 2003. In short, the "natural trading partner" hypothesis developed from the European or North American experiences are limited in their ability to understand or anticipate FTA formation in CJK.



Source: UNCTAD STAT (http://unctadstat.unctad.org) (Unit: US billion$)

Figure 2.1: Bilateral trade between China and Japan, China and Korea, and Japan and Korea, 1997-2012

[7] China is the largest trading partner of both Japan and South Korea, while Japan is the second largest and South Korea the fourth largest trading partner of China. In addition, South Korea is Japan's third largest trading partner, while Japan is South Korea's second largest (Statistics of Economic Trade (reported by Ministry of Foreign Affairs and Trade Republic of Korea), June 2011).

Another distinctive feature of CJK FTA formation is that the three countries are currently trying to form FTAs with a number of prospective partners. In these cases, FTAs have not yet entered into force, but joint studies have been conducted and initial official negotiations have taken place. In particular, discussions with most of CJK's major trading partners have remained in the initial stages of the FTA formation process for a relatively long period of time. These circumstances suggest that what explains why an FTA is proposed may not as reliably explain why it is subsequently put into place. This study also investigates the variations in outcomes across the different stages of the FTA formation process. Such variations have rarely been examined in previous studies. Most statistical studies on FTA formation employ a dichotomous dependent variable, coded as 1 when an FTA enters into force between two countries. This approach limits capacity to examine variation across the different stages of the FTA formation process.

In this study, the FTA formation process is divided into four stages. Stage 1 is *FTA under Consideration*, where countries *i* and *j* conduct joint studies in order to investigate the feasibility of an FTA between them. Stage 2 is *FTA under Negotiation*, where they launch an official negotiation. Stage 3 is *FTA Signed*, where countries *i* and *j* sign a bilateral FTA but the FTA has not entered into force. The final stage (Stage 4) is *FTA in Force*, where an FTA finally enters into force through the domestic ratification (or legalization) process. Using multinomial logistic analyses, this study finds that the determinants that work at the initial stages are quite different from those at the advanced stages. Specifically, political institutions are likely to influence FTA formation in the initial stages but are prone to lose their influence as the process moves forward. In contrast, support from IIGs is the driving force in the final stage of FTA formation.

Moreover, political leaders are likely to choose their FTA partners in the context of national security politics and their national security consideration is still influential after conducting joint studies. After starting official negotiations, however, political leaders are more likely to move the FTA discussion to the domestic political arena.

The remainder of this study proceeds as follows. First, the determinants of FTA formation developed by preceding studies are examined. Their expected influences at different stages of the FTA formation process are also discussed, an element that existing research rarely stresses. A new measure of IIGs' influences on FTA formation is then described. Next, the data and research design are presented. The subsequent statistical analyses confirm that, unlike many other factors, IIGs have a highly significant impact at the final stage of FTA formation. The cumulative results of this study have significant implications for the study of FTA formation – particularly regarding interest groups' impact on FTA formation.

Determinants of FTA Formation at Different Stages

1. Motives to form an FTA: social concerns vs. economic self-interest

Many scholars have contributed to a burgeoning literature that sheds light on the conditions under which states form an FTA. One useful way to organize this literature is to categorize the motivations that would lead political leaders to form an FTA. Broadly, two approaches have been developed: the economic self-interest approach and the social concerns approach.[8] The main idea behind the economic self-interest approach is that the political actors favor (or oppose) a particular trade policy depending on whether the

[8] For an overview of the two approaches, see Baldwin (1989).

policy increases or decreases their political benefits. This approach places primary focus on the preference and power of interest groups that are highly associated with political leaders' incentives (Stolper and Samuelson 1941; Rogowski 1989; Gourevitch 1986; Grossman and Helpman 1995).

In contrast, the social concerns approach demonstrates that trade policies reflect the government's welfare concerns and its desire to promote various national and international goals (Corden 1974; Cheh 1974; Lavergne 1983; Anderson and Baldwin 1987; Mansfield and Mutz 2009). According to the social concerns approach, political leaders search for new and/or expanded market access by forming FTAs in order to increase general welfare for the country they represent. Corden (1974) argues that "any significant absolute reductions in real incomes of any significant sections of the community should be avoided" when trade policy is changed. Cheh (1974) and Lavergne (1983) address the fact that governments often choose the trade policies that minimize adjustment costs, especially to workers. Empirically, Anderson and Baldwin (1987) find that industries with high proportions of unskilled workers or low wages tend to have high levels of protection and low tariff cuts in multilateral trade negotiations. Interpreting the results of two surveys, Mansfield and Mutz (2009) find that "sociotropic" perceptions are more important than self-interests in the explanation of mass attitudes about trade policy.

In reality, however, we have observed that political leaders' decisions on trade policy can significantly reduce net welfare. For example, some industries that have strong political power and will be harmed by an FTA have been excluded from trade liberalization or provided long periods of adjustments even when these compensations reduce net welfare. Given this situation, it is generally argued that the political leaders'

policy decisions are likely to be inseparable from the preference and relative political power of organized special interests. In this sense, the economic self-interest approach demonstrates that political incentives rather than sound economic reasoning determine trade policy. This approach emphasizes the influence of interest groups on trade policy change. Grossman and Helpman (1993) pioneered a set of models where politically organized sectors attempt to influence trade policy change through campaign contributions. They argued that political leaders have clear limits on ignoring them because those contributions are highly significant for their reelection.

H1: Political leaders establish an FTA in order to increase general welfare of the county they present.

H2: Political leaders form an FTA to capture political benefits associated with interest groups' preferences and power.

2. Institutional constraints on political leaders' motives

The extent to which political leaders consider the possibility of an FTA hinges in part on a country's political institutions. A variety of studies address the effects of regime type on FTA formation. It is generally argued that democracies are more likely to form FTAs than autocracies. In democracies, political leaders' general welfare concerns are more salient, since democracies have larger electorates and median voters who benefit from open trade (Bueno de Mesquita et al. 2003; Milner and Kubota 2005). Moreover, foreign economic policy is relatively transparent in democracies. Political leaders in democracies have greater difficulty manipulating the economy for their personal interests, since voters tend to hold politicians responsible for economic downturns (Frye and

Mansfield 2004; Heniz and Mansfield 2006). Publicly violating trade agreements can produce domestic "audience costs" for political leaders, with these costs tending to be higher under democracies (Fearon 1994). Empirically, Milner and Kubota (2005) find that democratization has a positive impact on trade liberalization in developing countries – trade tends to benefit labor and therefore, political leaders who need the support from labor are more likely to liberalize overseas commerce. A related line of research emphasizes that the similarity of states' political institutions affects whether governments will form FTAs and whether, once established, FTAs work well. For example, Katzenstein (2000) argues that the scarcity of RTAs in Asia is partly attributable to the wide variation in the member states' political regimes, which range from democracies like Japan to autocracies like China. Empirically, Mansfield, Milner, and Rosendorff (2000) find that pairs of democracies are more likely to have more open trade relations than mixed pairs (composed of an autocracy and a democracy).

Realizing that all democracies are not homogenous, some recent studies emphasize the institutional variations among democracies. In particular, they center on the number of veto players as an impediment to FTA formation (Henisz and Mansfield 2006; Mansfield, Milner and Pevehouse 2008). A veto player is an independent partisan and institutional actor whose agreement is necessary for policy change, including competing branches of government and coalitions within a given branch. After executives sign an FTA, the governments needs to adjust their trade policies in order to grant FTA partners some types of preferential trade access. In democracies, this adjustment is usually accomplished by domestic legislation. Even in non-democratic systems, politics is rarely an absolute hierarchy with a unitary decision maker and no veto players. For

example, in a dictatorship, the military or local politicians may exercise veto power over the executive's proposal. As existing research on 'two-level games' indicates, it is difficult to forge international agreements when leaders confront an array of domestic groups with diverse preferences and the ability to block policy initiatives (Mo 1994; Milner and Rosendorff 1996). More specifically, when veto players reflect the preferences of distributional losers, FTA formation becomes more difficult and unlikely. A higher number of veto players provide more outlets through which the losers can hinder the FTA formation. Moreover, coordinating a variety of interest group preferences puts big pressures on democratically-elected governments. As the number of veto players rises, so does the number of groups they represent, and the chances of ratifying an FTA are likely to decrease.

H3: Democracies are more likely to form FTAs than autocracies.

H4: As the number of veto players rises, the chances of FTA ratification are likely to decrease.

3. National security consideration

Besides domestic politics, states make the decision to enter an FTA in the context of international politics. Much of the literature stresses the role of interstate power and security relations as well as multilateral institutions in FTA formation. However, hegemonic power and multilateral institutions are less likely to be meaningful in the analyses of Northeast Asian regionalism.[9] First, there is no absolute regional hegemon in

[9] On the role of hegemonic power in FTA formation, see Mansfield 1998; McKeown 1991; Yarbrough and Yarbrough 1997. On the role of multilateral regimes (e.g., GATT/WTO), see Mansfield and Reinhardt 2003.

Northeast Asia; moreover, the extra-regional hegemonic power, namely the U.S., has been relatively weak in Northeast Asia as compared to Europe and North America. In addition, Northeast Asian countries have become less active in the WTO since the Asian financial crisis.

In contrast, the political-military relationships established during the Cold War era are still important in foreign policy decision-making in Northeast Asia. Several scholars stress the role of allies in trade agreements, since gains from the agreements can be used to increase states' political-military capability. States can attend to these externalities by trading more freely with political-military allies than with neutral countries or adversaries (Gowa 1995; Gowa and Mansfield 1993). In Northeast Asia, the political-military relationship is still relatively dominant in foreign policy decision-making processes. There exist a number of studies arguing that national security considerations have caused the absence of regionalism in Northeast Asia (Grimes 2009; Buszynski 2009).[10]

H5: States are more likely to form FTAs with the states holding favorable political-military relations.

4. Determinants at different stages

Unfortunately, the extensive scholarship on FTA formation has yet to reach a consensus on which factors are most likely to be most important in explaining FTA formation. In general, economists argue that economic self-interest almost always dominates one's concerns for the general welfare of other groups or the nation as a whole,

[10] This issue is discussed in Chapter 5 in more detail

when the trade policy is significantly related to an individual's income. They argue that general welfare concerns are more likely to be dominant only when the economic self-interest effects of a trade policy on an individual are small or seem to be unclear. Recently, scholars have agreed that one approach cannot stand alone in the political economy of trade policy. Baldwin (1989) argues that the economic self-interest and social concerns approaches are not contradictory. For example, declining industries are more likely to receive protection not only because of the self-interested lobbying from capitalists and workers who face income losses, but because the typical voter is more willing to provide protection to a declining industry. Though it is agreed here that all approaches are required to comprehend FTA formation, which explanation is more valid under what conditions remains to be seen. I assume that each may be more or less useful at different stages of the FTA formation process. In other words, the factors that lead the governments to propose an FTA may not as strongly determine why the FTA finally enters into force.

Few existing studies try to test the hypothesis that substantial variation may exist at the different stages of FTA formation. In the first stage of the process, governments typically launch a feasibility study jointly made by government, business, and academia in order to calculate future costs and benefits. Krasner and Kim (2007) argue that geopolitical and general welfare concerns are more likely to be significant drivers at this stage, while domestic political constraints (the number of veto players) become more salient at more advanced stages. These studies acknowledge that political leaders have at least some interest in providing public goods (e.g., enhanced social welfare and national security) by proposing an FTA in the initial stage. In domestic politics, an FTA can be a

useful way for governments to signal to domestic audiences that they are pursuing economic policies geared toward the welfare of the median voter rather than toward special interests (Mansfield, Milner, and Rosendorff 2000). In international politics, proposing an FTA can also act as a signal of commitment to a country's friends and allies (Krasner and Kim 2007).

Nevertheless, the general welfare concerns perspective has limited ability to explain why a particular FTA is proposed. In addition to general welfare concerns, this study argues that political leaders' economic self-interests associated with the preferences of interest groups are also salient in the initial stage of FTA formation. Like Grossman and Helpman (1995), this study also assumes that the first movers of the FTA proposal are more likely to be IIGs as opposed to political leaders. More specifically, expected winners may try to lead political leaders to choose a particular FTA partner with which they expect larger benefits.[11] On the other hand, expected losers may attempt to deter political leaders from developing FTA discussions with partners. When political leaders' incentives associated with the expected winners rather than the expected losers are likely to be greater, an FTA is more likely to be proposed.

As the FTA process proceeds, the probability that an FTA finally enters into force is likely to increase because the costs of terminating discussion are higher at more advanced stages. In the initial stages, the costs of terminating are relatively low, because there is not yet a firm commitment to move forward. Thus, the reputational costs associated with not following through are relatively limited. After an FTA is signed,

[11] Following Grossman and Helpman (1995), this study ignores the possibility that the expected winners may offer contributions to a foreign government, because political leaders of foreign governments place a lower value on them in their political objective function.

however, the breakdown of an agreement is likely to generate high costs. In domestic politics, expending resources to negotiate and sign an FTA, only to have it rejected, would significantly undercut politicians' reputations and credibility, especially when it comes to negotiating future accords. Moreover, the breakdown of an agreement (or a long delay in ratification) after it is signed is likely to negatively impact a state's reputation in the international community, generating considerable repercussions in negotiations with other countries for similar trade deals. For this reason, Krasner and Kim (2007) argue that the role of veto players becomes more salient at more advanced stages, because politicians are increasingly likely to anticipate their reactions and preferences in order to avoid unexpected results that can undercut their reputation and credibility. At these advanced stages, executives are beset by considerable conflict over how to distribute the costs and benefits stemming from an FTA and how to compensate distributional losers.

Nonetheless, the veto player perspective places a disproportionate focus on the 'resistance' side, while the 'support' side for trade policy is largely left unexamined. Peterson and Thies (2011) argue that, when there is considerable support for an FTA and less resistance to it, veto players may be less prone to use their veto powers in the FTA formation process. At more advanced stages, political leaders who favor an FTA – whether motivated by general welfare concerns or their own political incentives – may try to increase domestic support for an FTA in several ways. To buffer domestic opposition, for example, they may attempt to exclude politically sensitive sectors (e.g., the agricultural sector) from an agreement or provide several types of compensation (e.g., subsidies, quotas, and longer phase-in periods for reducing trade barriers). Given the higher probability of FTA formation, potential losers represented by veto players are

likely to accept these alternatives if those compensations are expected to bring more benefits to them. In order to determine the conditions of FTA formation, there is a need to give appropriate attention to supporting interest groups.

Mansfield, Milner and Pevehouse (2008) emphasize the impact of veto players that play a key role in the domestic 'ratification' game, even though they do not distinguish the ratification stage from other stages. They argue that executives need to bargain with veto players in order to ratify the proposed FTA and therefore, that the number of veto players is the most significant factor at this stage. In contrast, it is assumed herein that the role of veto players may be salient at the initial stage; in other words, veto players may try to impede the FTA discussion progress as early as possible, especially at lower costs. More specifically, if veto players' main goal in the FTA discussion is to reflect the distributional losers' interest on trade policy and ultimately terminate discussions, they are more likely to succeed in the initial stage. Since the costs of terminating discussions are likely to increase as the FTA formation process moves forward, the resistance to terminating the discussion (i.e., the support for the FTA) is likely to increase as well. Therefore, it becomes harder to break the discussion down in more advanced stages. Consequently, it may be a smarter choice, strategically speaking, for veto players to terminate FTA discussions at the initial stage. In the statistical analyses, the varying impacts of FTA determinants are therefore examined taking into consideration what stage the FTA discussion is in.

H6: The determinants of FTA formation have different impacts depending on the stages of FTA formation.

Research Design

1. Sample and Dependent Variables

The dataset of this study lists all bilateral FTA partners of CJK. As of 2012, 75 countries have established a bilateral FTA with one of CJK, 2 countries have signed but not yet implemented an FTA, 38 countries have been officially negotiating, and 50 countries have considered negotiating an FTA. A complete list of these countries is shown in Table 2.1.

The unit of analysis is the undirected dyad/year, including 160 countries in all dyads worldwide that include at least one of the three countries. The sample covers the years beginning in 1998 when East Asian countries launched their FTA initiatives after the Asian financial crisis. The first FTA joint studies were the Japan-Korea and the Chile-Korea studies established in 1998. The data extends to 2012, when the most recent data is available.[12]

[12] Some studies of FTA formation in East Asia extend their samples over years from 1992. Since they view the Soviet Union collapse in 1991 as the critical juncture of a new era in international politics, they expect that it might cause significant changes in East Asian economic cooperation. In Northeast Asia, however, FTAs have become increasingly pervasive since the member countries in this region pursued regional economic cooperation after experiencing the 1997-98 Asian financial crisis. Therefore, this study considers the year of 1998 as the critical juncture of FTA formation in Northeast Asia.

Table 2.1: List of bilateral FTAs of China, Japan and Korea

	FTAs under Consideration	FTAs under Negotiation	FTAs Signed	FTAs in Force
China	India (2003)	Australia (2005) Korea (2012) Iceland (2007) GCC (2005) Norway (2009) SACU (2004) Switzerland (2011)		ASEAN (2010) Chile (2006) Costa Rica (2011) New Zealand (2008) Pakistan (2009) Peru (2010)
Japan	EU (2011)	Australia (2007) GCC (2006) Canada (2012) Columbia (2012) Korea (2003) Mongolia (2012)		ASEAN (2008) Chile (2007) India (2011) Mexico (2005) Peru (2012) Switzerland (2009)
Korea	China (2004) Central America (2010) Israel (2009) MERCOSUR (2003) Mongolia (2008) Papua New Guinea (2004) Russia (2005) Uruguay (2004) SACU (2008)	Australia (2009) China (2012) Canada (2005) GCC (2008) Japan (2003) Mexico (2006) New Zealand (2009)	Columbia* (2012) Turkey* (2012)	ASEAN (2009) Chile (2004) EFTA (2006) EU (2011) India (2010) Peru (2011) US (2012)

* The Korea-Columbia FTA and the Korea-Turkey FTA entered into force in 2013.
EFTA (the European Free Trade Association): Iceland, Liechtenstein, Norway, and Switzerland.
SACU (the Southern African Customs Union): Botswana, Lesotho, Namibia, South Africa, and Swaziland.
GCC (the Gulf Cooperation Council): Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and United Arab Emirates.
MERCOSUR (Mercado Común del Sur): Argentina, Brazil, Paraguay, Uruguay and Venezuela.
ASEAN (the Association of Southeast Asian Nations): Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, and Vietnam.
EU (the European Union): Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, and United Kingdom.
Central America: Panama, Costa Rica, Guatemala, Honduras, Dominican Republic, and El Salvador.

In this study, the dependent variable is a bilateral FTA established by one of CJK. In order to test Hypothesis 6, the dependent variable is coded on a five-point scale (0 to 4) depending on the status of an agreement. The CJK governments provide specific information about the status of the agreements.[13] In this study, the FTA formation process is examined in the aforementioned four general stages. Stage 1 is *FTA under Consideration* where countries *i* and *j* conduct preparation talks or joint research projects. In Stage 2, *FTA under Negotiation*, countries *i* and *j* launch official negotiations. Stage 3 is *FTA Signed*, where an FTA is signed by the executive but not yet entered into force. Finally, Stage 4 is *FTA in Force* where countries *i* and *j* implement an FTA. The dyads were dropped from the analysis in the years after an FTA enters into force between countries *i* and *j*. For example, South Korea-Chile FTA entered into force in 2004 so I drop out the pair of countries from 2005 and 2012 from the analysis.

2. Measuring the effects of industry interest groups

In order to test Hypothesis 2, first the influence of IIGs on FTA formation needs to be examined. Although interest in the impact of IIGs is longstanding, empirical analyses of these impacts have been scarce. This is mainly caused by difficulties measuring IIGs' preferences and power. Mansfield, Milner and Pevehouse (2007, 406) describe the difficulties in empirically specifying the structure of interest groups in a cross-national context. Since trade policy has distributional consequences, it is expected that certain coalitions support FTAs and others oppose them. Since countries vary with

[13] For Chinese FTAs, China FTA Network (http://fta.mofcom.gov.cn); for Japanese FTAs, Ministry of Foreign Affairs of Japan, http://www.mofa.go.jp/policy/economy/fta; and for Korean FTAs, Ministry of foreign Affairs and Trade, http://www.mofat.go.kr/english/econtrade/fta/issues /index2.Jsp. For some FTAs, the dates of entry into force provided by the WTO are different from those provided by the governments. In that case, this study follows the governments' information.

respect to their comparative advantage, the composition and power of these distributional coalitions differ across countries. In this study, an IIG index is developed to measure the sectoral influences on FTA formation using four components: a) the trade complementarity, to predict general reactions of IIGs toward an FTA given the preexisting trade patterns; b) the trade orientation of the industry, to predict which industries will support or oppose the FTA, c) the share of GDP by industry, to anticipate how influential the industry's support or opposition will be; and d) the volume of bilateral trade with the partner (% of GDP), to examine how strongly the industry will support (or oppose) the FTA, given the expected benefits (or costs) of the FTA.

First, economists emphasize trade complementarity to predict a country's general propensity for FTAs. The trade complementarity index (TCI) measures the degree to which the export pattern of one country matches the import pattern of another. A high degree of complementarity is assumed to indicate more favorable prospects for an agreement. When two economies are complementary, distributional consequences between winners and losers associated with reducing trade barriers are less likely to be greater than when they are competitive. If a huge conflict is expected when an FTA discussion is launched, political leaders are more likely to hesitate in starting the discussion. In this case, IIGs are also less likely to lobby for forming an FTA, because they may need to spend more resources with a lower probability of success. In short, the TCI provides a rough estimate of domestic support for an FTA given pre-existing trade. The TCI is calculated as the sum of the absolute value of the difference between the import shares and the export shares (as 3-digit SITC, Rev.3) of the countries under study,

divided by two. More specifically, the TCI of exporter *i* with importer *j* is calculated in the following:

$$TCI_{ij} = 1- \frac{\sum_k | E_i^k - M_j^k |}{2}$$

where E_i^k is the share of industry (or good) *k* in country *i*'s total exports to the world and M_j^k is the share of industry *k* in country *j*'s total imports to the world. The IIG index includes the average of the TCIs when country *i* is an exporter and an importer in trade with country *j*.[14]

Even though the trade complementarity provides a rough estimate of domestic support for an FTA, the following inter-related questions in order to examine IIGs' impacts on FTA formation still need to be more precisely answered: Which industries will support an FTA and which ones will oppose it? How influential is this support or opposition given the industries' significance in the domestic market? How strongly does the industry support or oppose the FTA given the expected benefits (or costs) of the FTA?

First, the trade orientation of an industry (exporting or import-competing) in bilateral trade sheds important light on the preference of IIGs; if an industry in country *i* exports more than it imports in bilateral trade with country *j*, it is more likely to support the FTA with country *j*, and vice versa. In short, the trade orientation of a given industry tends to answer the first question (regarding which industry will support or oppose an

[14] Data on the TCI are taken from the UNCRTAD Stat http://unctadstat.unctad.org/TableViewer/table View.aspx? ReportId=16420.

FTA). The measure of industry *k*'s trade orientation in country *i* in the trade with county *j*, is constructed as follows[15]:

$$O_i^k = \frac{X_{ij}^k - X_{ji}^k}{X_{ij}^k + X_{ji}^k}$$

**Country i: China, Japan or Korea*

**Country j: 160 countries*

where O_i^k is the trade orientation of industry *k* in the country *i* in the trade with country *j*; X_{ij}^k is the value of industry *k*'s exports from country *i* to country *j*; and X_{ji}^k is the value of industry *k*'s imports of county *i* from *j* (or exports from country *j* to country *i*).[16] This measure takes on values ranging from -1 to 1. A positive value means industry *k* in country *i* is likely to be exporting, and therefore, prone to support an FTA with country *j*. In contrast, a negative value means industry *k* is import-competing, and thus, more likely to oppose the FTA.

However, pre-existing trade patterns are not enough to fully capture the influence of IIGs on FTA formation because of limited ability to determine how influential an IIG's support for (or opposition to) the FTA is. For the auto industry in the U.S., for example, international trade is much less important than domestic sales. Even if the auto industry's volume of trade is relatively small compared to other industries, it is hard for the U.S. government to ignore the auto industry's interests associated with a given FTA. Moreover, some industries enthusiastically support an FTA even though the existing

[15] Data on bilateral trade in the commodity level (based on SITC Rev.3) between country i and country j are taken from UNCTAD STAT.

[16] The basic idea of this measure is taken from Bergstrand (1983).

volume of trade is quite small, because they expect a huge increase in volume of trade after an FTA enters into force (e.g., the pharmaceutical industry in the Korea-U.S. FTA). Moreover, large firms are more likely to mobilize politically since they will disproportionately benefit (or suffer) from trade policy (Olson 1965; Baldwin 1985). The power of the industry in the domestic market can be measured using the domestic production of industry *k* as a % of country *i*'s GDP as follows:[17]

$$P_i^k = \frac{D_i^k}{G_i}$$

where P_i^k is the power of industry *k* in county *i*'s domestic market; G_i is GDP of country *i*; and D_i^k is domestic production of industry *k*.

Given the above two components, political leaders are likely to anticipate which industry will support (or oppose) an FTA and how strongly it will do. In order to create a single value for a given dyad-year, these two industry-level measures are multiplied and all 10 values (from 10 industries) are summed as follows[18]:

$$OP_i^k = \sum_{k=1}^{10} O_i^k * P_i^k$$

[17] The power of industry *k* can be also measured by the employment rates in industry *k*. Since this study focuses more on politically-contingent lobbying from industry interest groups rather than voting power of industries, the domestic production is more appropriate in this study.

[18] China's GDP classified by economic activity is taken from China Statistical Yearbook published by the National Bureau of Statistics of China (http://www.stats.gov.cn/english/statisticaldata/yearlydata/); Japan's GDP is taken from Cabinet office Annual Report on National Accounts published by Cabinet Office (http://www.esri.cao.go.jp/en/sna/data/kakuhou/files/2010/24annual_report_e.html); and Korea's GDP is taken from Statistic Korea (http://kostat.go.kr/portal/english /index.action). At this point, China and Japan's data are only available until 2010 so 2010's data was applied to 2011.

With regard to industry-level measures, the aggregated level of industry should be considered as measures can vary dramatically according to the level of aggregation (Grimwade 2000). Given CJK's industrial characteristics, the 10 aggregated industries most significant in CJK are shown in Table 2.2.[19]

Meanwhile, all FTA partners may not have the same meaning to IIGs. If IIGs in county *i* expect huge benefits (or losses) from an FTA with country *j*, they are likely to provide stronger support for (or opposition to) the FTA. More specifically, IIGs are more likely to take action in the FTA discussion with major trading partners than with minor trading partners given the greater distributional consequences. The significance of an FTA is measured as follows:

$$S_{ij} = \frac{X_{ij} + X_{ji}}{G_i}$$

where S_{ij} is the significance of an FTA between country *i* and *j*; G_i is country i's GDP; X_{ij} is the value of exports from country *i* to country *j* and X_{ji} is the value of imports of country *i* from country *j*. Thus, the numerator represents the volume of bilateral trade between country *i* and country *j*. This is a single measure for a given dyad-year ranging from 0 to 1. Since the preference, the power of IIGs, and the significance of an FTA partner are inter-related issues associated with FTA formation, OP_i^k is multiplied by S_{ij}.

[19] Although there exist several classification systems of industries (e.g., HS, SITC, NACIS etc.), existing research has used, they are less suitable for analysis of CJK FTAs due to data availability. CJK have developed their FTA initiatives in a relatively short time since 1998, as compared to Europe and North America. The industry-level data employing the above classification systems – especially, on shared GDP by industries – are only available until 2006 as of 2012. Rather than employing classification systems, therefore, this study employs industry-level data on 10 main industries in CJK.

Finally, the IIG index is constructed adding the TCI_{ij} to $OP_i^k * S_{ij}$ as follows[20]:

$$IIG_{ij} = TCI_{ij} + (OP_i^k * S_{ij})$$

Table 2.2: List of the main industries in CJK

Industry	SITC Rev.3	Description
Agriculture	0	Food and live animals
	1	Beverages and tobacco
	884	Articles of apparel and clothing accessories
Textile and Leather Products	226	Textile fibers and their wastes
	661	Leather, leather manufactures, n.e.s., and dressed fur skins
	665	Textile yarn, fabrics, made-up articles, n.e.s., and related products
Paper and Wood	224	Cork and wood
	225	Pulp and waste paper
	663	Cork and wood manufactures (excluding furniture)
	664	Paper, paperboard and articles of paper pulp
Chemicals	5	Chemicals and related products, n.e.s.
	223	Crude rubber (including synthetic and reclaimed)
	333	Petroleum, petroleum products and related materials
	662	Rubber manufactures, n.e.s.
Minerals	666	Non-metallic mineral manufactures, n.e.s.
Metals	667	Iron and Steel
	668	Non-ferrous metals
	669	Manufactures of metals, n.e.s.
General Machinery	771	Power-generating machinery and equipment
	772	Machinery specialized for particular industries
	773	Metalworking machinery
	774	General industrial machinery and equipment, n.e.s., and machine parts, n.e.s.
	775	Office machines and automatic data-processing machines
	776	Telecommunications and sound-recording and reproducing apparatus and equipment
Electrical Machinery	777	Electrical machinery, apparatus and appliances, n.e.s.
Transport Equipment	778	Road vehicles (including air-cushion vehicles)
	779	Other transport equipment
Professional Instruments	887	Professional and scientific instruments, n.e.s.

[20] The two values are summed up after rescaling. Since the TCI_{ij} takes on values ranging from 0 to 1, and the real values of the $OP_i^k * S_{ij}$ vary from -0.5 to 0.5, the TCI_{ij} is rescaled from (0 to 1) to (-0.5 to 0.5).

A greater value of the IIG index predicts higher domestic support for an FTA in country *i*. More specifically, as politically strong IIGs are more likely to support an FTA expected to yield more benefits and less conflict, the probability of the FTA formation increases.

3. Institutional variables

To test Hypothesis 3 and 4, two institutional variables are included in the analyses. The political leaders' decision regarding an FTA formation is also affected by the nature of domestic institutions. Past research has found that democracies tend to join FTAs at a higher rate than non-democracies. Consequently, this study includes *Democracy*, measured by the Freedom House annual ratings of political rights ranging from 1 (most democratic) to 7 (least democratic).[21] In order to make high scores reflect the high level of political rights, the scores are transformed by subtracting them from 7; therefore, this variable varies from 0 (least democratic) to 6 (most democratic).

Another domestic institutional variable is the number of veto players , which are expected to work as impediments to FTA formation in the preceding research. Henisz (2000) develops the political constraints index by first identifying the number of independent branches of government outside of the executive's control. Besides party composition and alignment, Henisz goes further, considering the homogeneity of preferences within these branches. For example, the executive should have greater policy discretion if a non-aligned (i.e., opposition) legislature is polarized (heterogeneous) rather than united (homogeneous). The resulting measure is a continuous variable ranging from

[21] Freedom House provides two measures for democracy: political right and civil liberty. In this case, political right measure is more appropriate than civil liberty as this study focuses more on institutional constraints on interest groups' activities.

0 to 1. When the value equals 0, there is a complete absence of veto players in a country. This measure takes on larger values as party control across some or all of the branches diverge from the executive party. *Veto player*, measured by POLCON III scores, is included in the analyses.[22]

4. National security variable

In order to test Hypothesis 5, a national security variable is included in the model. International political-military relationships established during the Cold War are still salient in Northeast Asia. In existing studies, alliance has usually been used to estimate the influence of the political-military relationships on regionalism. However, the number of formal alliances involving CJK is quite small, so such a variable provides little leverage within the sample. Thus, this study turns instead to an alternative measure, *Affinity*, measuring the similarity between two countries' voting patterns in the United Nations General Assembly (Gartzke and Jo 2006; Strezhnev and Voeten 2012). Here I use the s3un variable, which ranges from -1 (least similar) to 1 (most similar), based on category vote data (yes, abstain, no).[23]

[22] This study employs POLCON III, which includes three independent branches of government (executive, lower house, and upper house), rather than POLCON V, which contains five branches (additionally sub-federal units and judiciary). This is because the judiciary is less likely to influence the decision to establish an FTA. 2013 Data release is available in the following (http://mgmt5.wharton.upenn.edu/henisz /_vti_ bin/shtml.dll/POLCON/ContactInfo.html).

[23] Data on Affinity comes from Anton Strezhnev; Erik Voeten, 2012-06, "United Nations General Assembly Voting Data," http://hdl.handle.net/1902.1/12379UNF:5:iiB+pKXYsW9xMMP2wfY 1oQ==V3[Version]. The data for this variable only extend to 2007 as of 2012 so the s3un score in 2007 is identically applied from 2008 to 2011.

5. Welfare concerns variables

To test Hypothesis 1, several welfare concerns variables are included. The core issue of the social concerns approach is that estimating ex ante whether an FTA will generate net positive or negative welfare effects is quite difficult. According to Viner (1950), FTAs have a two-side quality, increasing or decreasing the national welfare depending upon the relative magnitude of the "trade creation" and "trade diversion" effects. A simple criterion for assessing trade creation and trade diversion is whether an FTA partner constitutes a "natural trading partner" or not – given an FTA with a natural trading partner, trade creation is more likely to occur while trade diversion is less likely, and therefore the FTA will increase the national welfare (Wonnacott and Lutz 1989; Krugman 1991). Two criteria have been most commonly used in assessing whether a country is a natural trading partner or not: the volume of trade and the transportation cost (measured by geographical proximity) (Panagariya 1997).[24] If the political leaders' primary goal to form an FTA is driven by an interest in increasing general welfare, they are more likely to pursue an FTA with natural trading partners. This study includes *Trade* as the ratio of bilateral trade between countries *i* and *j* to country *i*'s GDP[25] and *Distance* as the log of bilateral distances between the biggest cities of those two countries.[26]

A number of existing studies have addressed several factors which make an FTA more or less attractive to policy makers based on overall national welfare consideration.

[24] Wonnacott and Lutz (1989), who first coined the term "natural trading partner," along with Schiff (1999), argue that trade complementarity can be a criterion for a natural trading partner. However, this factor has received relatively little attention (Mansfield and Milner 1999) and the TCI is already included in the industry interest group index calculation.
[25] Data on bilateral trade flows and volumes of total trade are obtained from UNCTADSTAT (http://unctad stat .unctad.org /ReportFolders/reportFolders.aspx).
[26] Data on distance are taken from Mayer and Zignago (2011).

Some argue that the state which has a large domestic market is less likely to be open because it tends to depend less on international trade (Katzenstein 1985). Given the lower possibility of FTA formation with larger countries, political leaders may be less likely to propose an FTA with larger countries. To test the impact of domestic market size, *GDP* is included via the log of GDP average between countries *i* and *j* (in current international dollars, expressed in terms of purchasing power parity).

The level of economic development may also affect a country's trade policy. Political leaders in developed economies would easily use an FTA as a tool for increasing general welfare, because developed economies tend to have lower trade barriers (Rodrik 1998; Easterly and Rebelo 1993). *GDP PC* is included via the log of GDP per capita average between countries *i* and *j* (in current international dollars, expressed in terms of purchasing power parity) to measure the level of economic development.

It has been also argued that fluctuations in economic growth may affect whether states enter into an FTA. On the one hand, some research indicates that it becomes easier for political leaders to liberalize trade regimes for general welfare after economic crisis (Mattli 1999; Mansfield and Reinhardt 2003). In contrast, others demonstrate that increased growth is likely to increase a country's demand for imports and supply of exports, creating an incentive to obtain preferential access establishing FTAs (Mansfield, Milner and Pevehouse 2008). To test these arguments, *Growth* is included via the average of the percentage changes in GDP of countries *i* and *j*.[27]

[27] Data on GDP and GDP growth are taken from World Development Indicators (WDI).

In order to mitigate a simultaneity bias, all independent variables are lagged one year. For time dependence control, *Time* is included, which indicates the number of years since 1998 (Carter and Signorino 2010). [28] Descriptive statistics for all of the variables are presented in Table 2.3.

Table 2.3: Descriptive statistics

Variable	N	Mean	S.D.	Minimum	Maximum
FTA	7,007	0.25	0.71	0	4
IIG	6,852	-0.16	0.10	-0.45	0.43
Veto player	6,923	0.30	0.16	0	0.68
Democracy	7,007	3.6	1.74	0	6
Affinity	6,886	0.62	0.22	-0.71	1
Trade	6,852	0.003	0.01	0	0.20
(ln) Distance	6,968	9.08	0.47	6.86	9.88
(ln) GDP	6,781	27.86	0.73	26.47	30.22
(ln) GDP PC	6,780	9.54	0.49	8.29	11.02
Growth	7,007	4.64	3.96	-30.24	57.79
Time	7,007	6.85	4.27	0	14

Empirical Results

Since the dependent variable is nominal, a multinomial logistic analysis (MNL) is employed. Since changing the reference categories (or the baseline) shows how the impacts of the FTA determinants change as the FTA formation process moves forward, different baselines are employed in the analyses. In Table 2.4, the reference category is the absence of an FTA between countries *i* and *j* (the baseline is 0). Therefore, the statistical results in Table 2.4 tell us which determinants are statistically significant at four stages of FTA formation when there is no FTA between countries *i* and *j*. In particular, Stage 1 demonstrates under what conditions CJK propose an FTA by conducting joint studies, while Stage 4 indicates the conditions under which CJK finally

[28] In robustness tests, I also added the square and the cube of the time-count variable and find that they have little impact on the results (Carter and Signorino 2010).

establish an FTA when there is no FTA. Most of the variables show statistical significance at all stages. Interestingly, the coefficient of *IIG* is the largest in Stage 4 while the coefficient of *Veto player* is in Stage 2 and that of *Democracy* is in Stage 1. This finding indicates that IIGs are likely to be most significant in the final stage while the political institutions tend to have stronger impacts at the initial stages.

In order for the substantive significance of these results, this study also estimates the change in predicted probability of FTA formation processes presented in Table 2.4, when the value of each variable changes from ½ standard deviation (SD) below mean to ½ SD above the mean, while holding all other variables constant at their means. Increasing from ½ SD below mean *IIGs* to ½ SD above the mean, while holding all other variables at their means, the probability of FTA formation increases by 0.6 % averaged across all four stages. The probability that an FTA finally enters into force increases by 0.1 %. In Stage 4, other variables show less substantive significance. This result improves the confidence that an FTA is the result of sectoral politics where IIGs rather than the political institutions play a key role.

Table 2.4: Multinomial logistic estimates of the determinants of CJK bilateral FTA formation, with a baseline of No FTA, 1998-2012

	Multinomial Logistic Estimates				Change in Predicted Probabilities			
(B = 0)	**S1**	**S2**	**S3**	**S4**	**S1**	**S2**	**S3**	**S4**
IIG	5.61***	5.54***	5.31***	9.92***	0.012	0.012	0.001	0.0011
	(6.91)	(7.22)	(3.18)	(5.27)				
Veto player	-1.70**	-6.31***	-5.95***	-4.83***	-0.005	-0.023	-0.002	-0.0008
	(-2.03)	(-7.88)	(-3.03)	(-2.67)				
Democracy	0.45***	0.21***	0.39**	0.41**	0.016	0.008	0.002	0.0007
	(5.08)	(2.73)	(2.01)	(2.26)				
Affinity	1.29***	3.49***	2.78***	3.17***	0.005	0.023	0.002	0.0007
	(3.95)	(12.26)	(4.20)	(4.73)				
Trade	36.89***	27.06***	39.30***	8.07	0.008	0.006	0.001	0.0000
	(6.61)	(4.71)	(4.38)	(0.61)				
(ln) Distance	-1.23***	-1.42***	-1.08***	-1.88***	-0.012	-0.015	-0.001	-0.0009
	(-9.11)	(-11.49)	(-3.50)	(-7.13)				
(ln) GDP	-0.96***	-0.70***	-0.48*	-1.06***	-0.014	-0.011	-0.001	-0.0008
	(-7.50)	(-6.24)	(-1.85)	(-4.21)				
(ln) GDP PC	0.17	1.80***	0.93**	0.94**	0.001	0.020	0.001	0.0004
	(0.71)	(11.97)	(2.01)	(2.22)				
Growth	0.08***	0.09***	-0.15***	0.14***	0.006	0.007	-0.001	0.0005
	(4.29)	(5.48)	(-3.80)	(3.27)				
Time	0.30***	0.26***	0.32***	0.58***	0.027	0.025	0.004	0.0033
	(13.01)	(12.61)	(6.17)	(9.34)				
Constant	28.82***	8.98**	6.36	25.78***				
	(7.13)	(2.50)	(0.75)	(3.08)				
Obs.	6525							
Pseudo R2	0.2762							
Prob X^2	<0.0000							

Note: *significant at 90%, **significant at 95%, ***significant at 99% (two-tail test); Z scores are in parentheses

When the reference categories are changed in order to provide further tests of Hypothesis 6, the results provide more convincing evidence in support of the argument that the determinants of FTA formation have different impacts depending on what stage they are in. The statistical results are presented in Table 2.5. In Model 1, the reference category is the FTAs under consideration (baseline is 1), and therefore, it shows under what conditions CJK move to more advanced stages *after* an FTA is proposed. Similarly, Model 2 indicates the conditions under which CJK move their FTA discussion to Stage 3

and Stage 4 *after* launching official negotiations. Finally, Model 3 demonstrates the determinants that lead the CJK governments to ratify an agreement *after* it is signed.

Table 2.5: Multinomial logistic estimates of the determinants of CJK bilateral FTA formation at advanced stages of the FTA formation Process, 1998-2012

	(1) After Consideration (B=1)			(2) After Negotiation (B=2)		(3) After Signed (B=3)
	Stage 2	**Stage 3**	**Stage 4**	**Stage 3**	**Stage 4**	**Stage 4**
IIG	-0.07	-0.31	4.30**	-0.23	4.38**	4.61*
	(-0.08)	(-0.18)	(2.19)	(-0.14)	(2.27)	(1.89)
Veto player	-4.62***	-4.25**	-3.14	0.37	1.48	1.11
	(-4.31)	(-2.04)	(-1.63)	(0.18)	(0.78)	(0.43)
Democracy	-0.24**	-0.06	-0.05	0.18	0.19	0.02
	(-2.20)	(-0.31)	(-0.25)	(0.88)	(1.03)	(0.06)
Affinity	2.20***	1.49**	1.88***	-.71	-.32	.39
	(5.61)	(2.11)	(2.62)	(-1.02)	(-0.46)	(0.42)
Trade	-9.82*	2.42	-28.81**	12.24	-18.99	-31.23**
	(-1.95)	(0.29)	(-2.24)	(1.43)	(-1.48)	(-2.14)
(ln) Distance	-0.19	0.15	-0.64**	0.33	-0.46*	-0.79**
	(-1.17)	(0.47)	(-2.34)	(1.06)	(-1.73)	(-2.04)
(ln) GDP	0.26*	0.47*	-0.11	0.22	-0.36	-0.58
	(1.69)	(1.70)	(-0.39)	(0.79)	(-1.39)	(-1.64)
(ln) GDP PC	1.63***	0.76	0.77*	-0.87	-0.86**	0.01
	(6.38)	(1.52)	(1.66)	(-1.85)	(-2.01)	(0.02)
Growth	0.01	-0.23***	0.06	-0.24***	0.05	0.29***
	(0.26)	(-5.48)	(1.25)	(-5.79)	(1.15)	(5.09)
Time	-0.04	0.02	0.28***	0.06	0.32***	0.26***
	(-1.29)	(0.44)	(4.37)	(1.11)	(4.99)	(3.22)
Constant	-19.83***	-22.45**	-3.04	-2.62	16.80*	19.42*
	(-4.07)	(-2.51)	(-0.34)	(-0.30)	(1.94)	(1.68)

Note: *significant at 90%, **significant at 95%, ***significant at 99% (two-tail test); Z scores are in parentheses

Statistical results still indicate that *IIGs* have a strong influence on FTA formation at the final stage; the coefficients of *IIG* are consistently significant at Stage 4 in all cases, though significance is partially lost. In contrast, the domestic institutional variables (*Democracy* and *Veto players*) have strong impacts at the very first stage where an FTA is proposed but they become statistically insignificant as the FTA formation process moves forward. For example, the coefficients of *Democracy* are not statistically

significant in most cases, are statistically significant at Stage 2 in Model 1, but show the opposite direction than expected. This result implies that CJK are more likely to start the FTA discussion with democracies but the regime type does not really matter after an FTA is proposed. In a similar vein, the influence of *Veto players* is likely to be strong in earlier stages but their impact on an FTA's implementation after it is signed is not likely to be influential. In Model 1, the coefficients of *Veto players* are statistically significant at Stage 2 and Stage 3, but not significant at Stage 4 in any cases. This finding is contrary to existing studies and suggests that veto players are more likely to terminate an FTA discussion as early as possible.

In Model 1, *Affinity* shows statistical significance at all stages. However, it loses its significance in Model 2 and 3. This finding implies that political leaders are likely to choose their FTA partners in the context of national security politics and their national security considerations are still influential after conducting joint studies. After starting official negotiations, however, political leaders are more likely to advance the FTA discussion based on conditions in the domestic political arena.

The welfare concerns variables (*Trade, Distance, GDP, GDP PC,* and *Growth*) are most likely to be significant at the very first stage when political leaders propose an FTA. However, they show inconsistent results as the FTA formation processes move forward. An interesting finding is that the coefficients of *Trade* become negative as the FTA formation process moves forward. This implies that CJK are more likely to start the FTA discussions with major trading partners. However, discussions with these major trading partners often do not advance beyond the proposal stages. For example, Japan and Korea (since 1998) and China and Korea (since 2004) have discussed establishing

bilateral FTAs (a JK FTA and a CK FTA) as well as a multilateral FTA (a CJK FTA), but they have yet to reach an agreement.

The cumulative results strongly support the argument that IIGs have a profound influence on FTA formation. However, it is also important to assess the robustness of these results, particularly with respect to the coding of the dependent variable and the estimation technique.[29]

Consistent with previous research, this study uses the binary dependent variable coded 1 if an FTA enters into force between countries *i* and *j*, and 0 otherwise. In order to test Hypothesis 6, three different models are employed. The first model includes all dyad-years excluding the years after an FTA enters into force between countries *i* and *j*. In order to investigate what factors are determinant at the initial stage where CJK choose their future FTA partners, the sample is limited to proposed FTAs in the second model. In this analysis, the dependent variable is coded 1 if countries *i* and *j* propose an FTA by conducing preparation talks or joining research projects, and 0 if they never discuss it. The South Korea-India FTA, for example, was first proposed in 2005 so the pairs of Korea and India are coded 0 from 1998 to 2004, 1 in 2005, and drop out from the analysis after 2005 in the second model. To figure out the determinants at the advanced stages, the third model includes the dyads where a proposed FTA is already on the negotiating table. Going back to the South Korea-India FTA case, the dyads from 1998 to 2004 drop out; coded 0 in 2005 to 2009; 1 in 2010 (when it finally entered into force); and drop out from the analysis again after 2010.

[29] Whether or not different estimation techniques would lead different findings is also tested. Since the dependent variable is nominal, the ordered logit (or probit) analysis would be also useful. But since the parallel regression assumption (the proportional odds assumption) is violated in the dataset, the statistical results of the ordered logit estimates would be biased.

The statistical results are present in Table 2.6. The logistic analyses show results similar to the MNL estimates. From the results in the second model, the institutional variables (*Democracy, Veto player, and Affinity*) and welfare variables (except *Trade*) are significant, but were not significant in the third model. In contrast, the coefficients of the *IIG* are consistently significant in all three models. These findings imply that institutional constraints and political leaders' welfare concerns are more likely to be influential at the initial stage where an FTA is proposed, but they are less likely to be determinant at the advanced stages after an FTA is proposed. On the other hand, IIGs highly influence FTA formation before and after an FTA is proposed.

Even though it is not the main interest of this study, an interactive effect may exist between *IIG* and *Veto player* variables – political leaders' motives to reflect IIGs' interest on trade policy for their own political incentives might be conditioned by political institutions. The interaction term *IIG*Veto* is included and the statistical results are presented in Table 7 and Table 8. The coefficients of the interaction term, *IIG*Veto*, are not statistically significant in any cases, and the industry interest group index and veto player variables look as they do in models excluding the interaction. The results suggest that neither variable conditions the impact of the other.[30]

[30] An examination of conditional marginal effects remains necessary to determine the potentially varying influence each has over the range of the other. In this study, however, the conditional marginal effects are not examined because the interaction effect between IIGs and veto players is not the primary interest of this study.

Table 2.6: Logistic estimates of the determinants of CJK bilateral FTA formation, 1998-2012

	(1)	(2)	(3)
IIG	5.83***	4.61***	3.32*
	(4.58)	(3.44)	(1.89)
Veto player	-3.71***	-2.91**	-0.28
	(-2.85)	(-2.35)	(-0.15)
Democracy	0.33**	0.38**	0.11
	(2.48)	(2.88)	(0.66)
Affinity	1.75***	2.00***	0.38
	(3.72)	(3.75)	(0.56)
Trade	-7.48	14.50	-25.73*
	(-1.16)	(1.44)	(-1.79)
(ln) Distance	-1.02***	-1.46***	-0.67**
	(-5.20)	(-6.63)	(-2.62)
(ln) GDP	-0.44**	-0.91***	-0.28
	(-2.41)	(-4.96)	(-0.98)
(ln) GDP PC	0.52*	1.36***	-0.51
	(1.68)	(4.69)	(-1.38)
Growth	-0.04	0.07***	0.06
	(-1.44)	(2.70)	(1.22)
Time	0.35***	0.16***	0.38***
	(8.75)	(5.09)	(5.26)
Constant	9.10	17.66***	11.81
	(1.48)	(3.07)	(1.29)

Note: *significant at 90%, **significant at 95%, ***significant at 99% (two-tail test); Z scores are in parentheses

Table 2.7: Multinomial logistic estimates of the determinants of CJK bilateral FTA formation, with a baseline of No FTA, including an interaction between industry interest groups and veto players, 1998-2012

No FTA (Baseline=0)	S1	S2	S3	S4
IIG	5.32***	4.36***	5.90	11.68***
	(2.83)	(3.38)	(1.62)	(3.24)
Veto player	-1.56	-5.76***	-6.13***	-5.45**
	(-1.49)	(-6.13)	(-2.67)	(-2.55)
*IIGs*Veto*	0.98	4.71	-1.83	-6.12
	(0.19)	(1.16)	(-0.17)	(-0.58)
Democracy	0.45***	0.21***	0.39**	0.41**
	(0.19)	(2.67)	(2.02)	(2.32)
Affinity	1.26***	3.37***	2.79***	3.24***
	(3.75)	(11.11)	(4.09)	(4.72)
Trade	36.93***	27.61***	38.78***	6.30
	(6.55)	(4.81)	(4.22)	(0.46)
(ln) Distance	-1.23***	-1.42***	-1.08***	-1.88***
	(-9.11)	(-11.52)	(-3.48)	(-7.12)
(ln) GDP	-0.96***	-0.73***	-0.47*	-1.03***
	(-7.43)	(-6.35)	(-1.74)	(-4.01)
(ln) GDP PC	0.16	1.80***	0.93**	0.96**
	(0.69)	(11.93)	(2.00)	(2.26)
Growth	0.08***	0.09***	-0.15***	0.14***
	(4.29)	(5.48)	(-3.81)	(3.24)
Time	0.30***	0.27***	0.32***	0.58***
	(12.86)	(12.61)	(6.05)	(9.21)
Con	28.98***	9.70***	6.11	25.03***
	(7.11)	(2.66)	(0.71)	(2.96)

Note: *significant at 90%, **significant at 95%, ***significant at 99% (two-tail test); Z scores are in parentheses

Table 2.8: Multinomial logistic estimates of the determinants of CJK bilateral FTA formation at advanced stages of the FTA formation process, including an interaction between industry interest groups and veto players, 1998-2012

	(1) After Consideration (baseline=1)			(2) After Negotiation (baseline=2)		(3) After Signed (baseline=3)
	S2	**S3**	**S4**	**S3**	**S4**	**S4**
IIG	-0.97	0.57	6.35	1.54	7.32**	5.78
	(-0.46)	(0.14)	(1.61)	(0.41)	(2.01)	(1.15)
Veto player	-4.20***	-4.57*	-3.88*	-0.37	0.31	0.68
	(-3.25)	(-1.86)	(-1.69)	(-0.15)	(0.14)	(0.22)
*IIG*Veto*	3.73	-2.81	-7.10	-6.54	-10.82	-4.28
	(0.61)	(-0.25)	(-0.62)	(-0.60)	(-1.00)	(-0.29)
Democracy	-0.24**	-0.06	-0.04	0.18	0.20	0.02
	(-2.22)	(-0.29)	(-0.20)	(0.90)	(1.10)	(0.09)
Affinity	2.11***	1.53**	1.98***	-0.57	-0.12	0.45
	(5.16)	(2.11)	(2.70)	(-0.80)	(-0.17)	(0.48)
Trade	-9.32*	1.85	-30.63**	11.17	-21.31	-32.48**
	(-1.80)	(0.21)	(-2.30)	(1.27)	(-1.61)	(-2.15)
(ln) Distance	-0.19	0.15	-0.65**	0.34	-0.47*	-0.81**
	(-1.18)	(0.47)	(-2.36)	(1.06)	(-1.75)	(-2.06)
(ln) GDP	0.23	0.49*	-0.07	0.26	-0.30	-0.56
	(1.51)	(1.70)	(-0.25)	(0.91)	(-1.14)	(-1.55)
(ln) GDP PC	1.63***	0.76	0.79*	-0.87	-0.84**	0.03
	(6.37)	(1.52)	(1.70)	(-1.85)	(-1.97)	(0.05)
Growth	0.01	-0.23***	0.06	-0.24***	0.05	0.29***
	(0.24)	(-5.48)	(1.25)	(-5.78)	(1.16)	(5.06)
Time	-0.03	0.02	0.28***	0.05	0.31***	0.25***
	(-1.17)	(0.39)	(4.25)	(0.99)	(4.83)	(3.15)
Con	-19.28***	-22.87**	-3.95	-3.59	15.33*	18.92
	(-3.90)	(-2.51)	(-0.44)	(-0.40)	(1.75)	(1.61)

Note: *significant at 90%, **significant at 95%, ***significant at 99% (two-tail test); Z scores are in parentheses

Conclusion

The recent proliferation of FTAs has led scholars in various fields of research to study the effects of these agreements. It has been widely agreed that an FTA is the result of a domestic political game. However, far less effort has been made to examine the specific factors operating in the domestic political arena. Only the role of veto players has been stressed as a surrogate for domestic political activity in FTA formation, because it is quite difficult to compare interest group activities across countries. However, this veto player perspective places too much focus on the 'resistance' side of the domestic actors; the 'support' side for trade policy is left largely unexamined in the veto player study. In order to determine the conditions under which an FTA is established, we need to focus on driving factors as well as on impediments. This study develops an IIG index in order to directly measure the influence of IIGs on FTA formation. The resulting model suggests that political leaders are more likely to establish an FTA as politically powerful IIGs favor the agreement. The IIG index and its estimated impact have important implications for the study of FTAs.

In addition, FTAs in CJK have shown different patterns from those in Europe and North America – CJK's major trading partners have not moved beyond the proposal or negotiation stages. Given this feature of the CJK's FTAs, it is assumed that significant variations may exist depending on the stage of the FTA formation process. However, existing studies employing a binary logistic model have limited capacity to examine such variations. By dividing the FTA formation process into four stages, this study finds that determinants of FTA formation have different impacts depending on what stage an FTA discussion is in. Political institutions (regime type, veto players) and international

political relations are prone to influence FTA formation in the initial stages, but they are likely to lose their influence as the FTA discussion moves forward. In the last stage where an FTA needs to be ratified (or legalized) after being signed, support from IIGs is the primary factor that causes the CJK governments to enter into an FTA. Moreover, political leaders are likely to choose the countries having favorable political-military relations as their FTA partners but they are prone to move the FTA discussion to the domestic political arena. The results of this study collectively support the hypothesis that an FTA is the results of sectoral and national security politics.

Although the focus of this study is on FTA formation in Northeast Asia, the main idea and findings of this study have significant implications for the study of FTAs in other regions. Furthermore, the results bear on other types of RTAs. It is expected that the effect of industry interest groups on RTA formation grows larger as the proposed level of integration in an agreement grows deeper. A higher level of integration will strengthen IIGs' interest in an agreement.

CHAPTER 3
U.S. CONGRESSIONAL VOTING ON THE KOREAN-U.S. FREE TRADE AGREEMENT:
Political Institutions and Ideology versus Constituent Interests

<ABSTRACT>

As the first empirical analysis of United States Congressional voting on the KORUS FTA, the second essay aims to examine which factors likely influenced voting in the US Congress on the Korean-U.S. Free Trade Agreement (the KORUS FTA). Most studies on US legislators' roll-call voting behavior have emphasized the role of political institutions and legislators' ideology, and found that constituent interests are individually insignificant and play only a marginal role in a legislator's voting decision. This study argues that the marginal role of constituent interests may stem from inadequate measurement of constituent interests. To fully capture the effect of constituent interests on congressional voting, this study develops a new measure for constituent interests by considering factoral as well as sectoral coalitions, and by taking into account geographical as well as non-geographical constituent interests. Logistic regressions indicate that constituent interests are highly significant predictors of US legislators' voting for the KORUS FTA. Moreover, exporting and import-competing industry coalitions are slightly more salient than factoral coalitions of business and labor groups. In addition, constituent interests play a more significant role in the House of Representatives than in the Senate. Lastly, national security considerations also greatly influenced US legislators' voting on the agreement.

Since 2006, when the US and the South Korean governments launched official negotiations to establish a bilateral FTA, the FTA has been the central issue in relations between the two countries. After the KORUS FTA was signed on June 30, 2007, under the trade promotion authority (TPA), both governments faced huge domestic opposition. Moreover, when President George Bush's TPA expired, and when the Republican president and the Republican-led Congress were replaced by the Democrat President Obama and a Democrat-controlled Congress, ratification of the agreement stalled. President Obama started additional negotiations in 2010, obtaining South Korean concessions on automobiles, beef and pharmaceuticals. These new conditions brought a four and a half year-long legislative battle to end. The KORUS FTA was ratified by the US congress on October 21, 2011, and by the Korean National Assembly on November 22, 2011. The KORUS FTA entered into force on March 15, 2012.

What factors led legislators to vote for or against the KORUS FTA? What is the relative importance of political incentives related to constituent interests, ideology, political institutions and other factors? Existing research on congressional trade policy voting has emphasized the role of political institutions such as partisanship (Cox and McCubbins 2002; Kiewiet and McCubbins 1991; Rohde 1994; Aldrick 1995; Weller 2009) and committee membership (Fenno 1978; Shepsle and Weingast 1987; Krehbiel 1996; Romer and Snyder 1994). The impact of a legislator's ideology has also been stressed (Jackson and Kingdon 1992). With regard to partisanship, Democrats and Republicans usually have different perspectives on trade liberalization. Since the late 1960s, Republicans have shown strong support for free trade, while Democrats have been

less supportive (Gartzke and Wrighton 1998; Lohmann and O'Halloran 1994). Legislator ideology is a more complex issue, presenting contradictory findings. However, it is usually expected that liberals are prone to support trade interventions in order to increase equity, while conservatives are more likely to oppose trade interventions on efficiency grounds (Nelson and Silbergerg 1987; Levitt 1996). In addition to legislators' beliefs, their power or influence in committee is significant in reflecting their belief on trade policy, and is another factor stressed by previous research. Several studies find members of committees related to trade and labor issues have an important impact on voting for trade policy (Shepsle and Weingast 1984; Gartzke and Wrighton 1998; Romer and Snyder 1994).

In the field of political science, the role played by constituent interests has garnered less attention than alternative theories (Schattschneider 1935; Mayhew 1974; Fiorina 1977; Kalt and Zupan 1984). Even though most scholars have acknowledged the theoretical connection between constituent interests and congressional voting, several studies have found that these interests are individually insignificant and play only a marginal role in a legislator's trade policy vote (Poole and Rosenthal 2001; Xie 2006). However, others argue that the marginal role of constituent interests may be caused by the highly simplified measures of constituent interests used in empirical models (Gartzke and Wrighton 1998; Fordham and McKeown 2003). With a few notable exceptions, appropriate measures of constituent interests are not utilized in most empirical trade policy research.

Constituencies are usually understood in geographic terms in studies of US congressional voting, because the electorate is defined geographically (Anderson and

Baldwin 1987; Lindsay 1990). Geographical interest is usually measured by the ratio of factors (e.g., the ratio of capital or land to labor) or the employment rates of certain industries in a district or a state. However, simply defining constituent interests in geographical terms yields several problems (Fenno 1978; Kingdon 1989; Jackson and Kingdon 1992; Fordham and McKeown 2003). First, the mere presence of an industry or a group of voters in a district or a state does not necessarily mean that its interests are influential. Second, the actual constituency can be much broader than the geographic district, because a legislator's decision on policy can affect interests nationally and even internationally.

In order to include non-geographical constituent interests, a number of studies examine the impacts of campaign contributions from political action committees (PACs) on congressional voting (Chappell 1982; Baldwin and Magee 2000; Beaulieu and Magee 2004; Abetti 2008; Bennett and Loucks 2008). Several existing research studies find that labor contributions are negatively correlated with favorable votes on trade liberalization bills, while business contributions are positively correlated (Kahane 1996; Steagall and Jennings 1996; Holian, Krebs and Walsh 1997; Uslander 1998; Box-Steffensmeier 2005). However, preceding studies about the impacts of PAC contributions assume that the cleavage of constituent interests on trade policy is formed along the factoral line (capital vs. labor) – ignoring possible sectoral interest coalitions (exporting vs. import-competing industries). This assumption may lead to misleading results.

In short, the marginal effect of constituent interests found in existing research may stem from inadequate measurement. This study develops a new measure for constituent interests, which considers sectoral as well as factoral constituent coalitions, and which

examines both geographical and non-geographical interests. Using the new measure, this study finds that constituent interests formed along sectoral line were a highly significant predictor of US legislators' voting on the KORUS FTA. Moreover, national security consideration also greatly influenced US legislators' voting on the agreement. These findings imply that the KORUS FTA was the result of sectoral coalition politics, where exporting industries played a key role by financing political campaigns, as well as national security politics where US political leaders were more likely to support free trade with Korea as a mean of strengthening economic ties with Korea.

In order to examine the determinants of the KORUS FTA formation, the remainder of this study proceeds as follows. First, the KORUS FTA formation process is briefly discussed. The factors influencing congressional voting on trade policy developed by previous studies, and the main problems of constituent interests measurement, are then discussed. In the research design section, a new measure of constituent interests' influence on legislators' voting is described. The following section presents logit regression results. These results show that constituent interests formed along sectoral (rather than factoral) lines were the most significant factor in congressional voting on the KORUS FTA, and that such sectoral interests were more salient in the House of Representatives than the Senate. This study concludes that the new measure of constituent interests developed in this study produces significant contributions to the study of congressional voting on public policies.

The Korea-US FTA Formation Process

The KORUS FTA is the second-largest FTA for both the US (next to NAFTA) and South Korea (next to the EU-Korea FTA). South Korea is the seventh-largest trading partner of the US and the US is South Korea's third-largest trading partner. The KORUS FTA deals with a wide range of trade and investment issues, and thus both countries have expected substantial economic impacts. Under the FTA, nearly 95% of bilateral trade in consumer and industrial products will become duty free within five years and most remaining tariffs will be eliminated within ten years.[31] According to the U.S. International Trade Commission, the KORUS FTA is expected to increase U.S. exports to Korea by an estimated $9.7 billion to $10.9 billion. Moreover, it is also expected to increase US GDP by up to $11.9 billion.[32] On the Korean side, business groups estimate that the FTA can boost Korea's economic output by 5.6% within ten years and create 350,000 new jobs.[33]

The US and Korea agreed to launch a joint feasibility study in November 2004, after the Korean government lifted its controversial import ban on US beef as well as revising its ambiguous emissions regulations in favor of US vehicles. After eight rounds of official negotiations (June 2006 to March 2007), the Bush administration finally signed the KORUS FTA on June 30, 2007, under the trade promotion authority (TPA),

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[31] The USTR (United States Trade Representative) provides more specific information on the economic impacts of the KORUS FTA, at http://www.ustr.gov/trade-agreements/free-trade-agreements/korus-fta.

[32] The United States International Trade Commission (USITC) assesses the economic benefits and costs of specific sectors. See USITC (2007), "U.S.-Korea Free Trade Agreement: Potential Economy wide and Selected Sectoral Effects," Investigation No. TA-2104-24, USITC Publication 3949, at http://www.usitc.gov/publications/332/ pub3949.pdf.

[33] "Focus on Parliament in Free-Trade Deal," October 13, 2011, *Wall Street Journal*, at http://blogs.wsj.com/korearealtime/2011/10/13/focus-on-parliament-in-free-trade-deal/tab/ print/

also called the fast-track authority. Under the TPA, President Bush had the authority to decide when to submit the implementing legislation to Congress. However, President Bush did not submit the legislation to Congress due to differences with the Democratic leadership over the treatment of autos and beef, among other issues, including his lame-duck status.

After the FTA was signed, both governments met huge domestic opposition. The groups which were most disadvantaged by the KORUS FTA were the agricultural sector in Korea and the auto industry in the US. The Korea Rural Economic Institute reported that US agricultural exports to Korea could double after the FTA formation, causing the loss of up to 130,000 jobs.[34] The agricultural industry staged several massive protests against the FTA. These movements were supported by the Korean public, who were concerned that US beef imports could spread 'mad cow disease' in Korea. In the US, the FTA was blocked by legislators who sought additional conditions for the auto and beef sectors as well as organized labor. Much attention has been focused on automobiles given the imbalance in auto trade. During 2005, for example, Korean automakers sold 730,863 vehicles in the United States, while American auto companies sold only 5,795 in Korea, according to Commerce Department figures.[35] These domestic oppositions led the ratification of the agreement to stall.

In 2010, new presidents in both countries, Presidents Barack Obama and Lee Myung-bak, expressed renewed commitment to the treaty. They initiated a series of

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[34] "SOUTH KOREA/US: FTA jumps major hurdles, faces others." April 3, 2007, *New York Times*, at http://www.nytimes.com/2007/04/03/news/03iht-oxan.0403.5124955.html?_r=0.
[35] Olsen, Kelly, "U.S., South Korea Reach Free Trade Deal," April 2, 2007, *Washington Post* , at http://www.washingtonpost.com/wpdyn/content/article/2007/04/02/AR2007040 200273_pf.html

additional negotiations that took place from November 30 to December 3, 2010. During the negotiations, the Obama Administration obtained Korean concessions in the automobile sector – tariff reductions for Korean automobiles were delayed for five years, and U.S. automakers were granted broader access to the Korean market. At the same time, the US made extra concessions in the areas of beef, pharmaceuticals, and visas (Cooper et al. 2013). On October 3, 2011, ten days before President Lee's US visit, President Obama submitted the KORUS FTA to Congress for approval. Finally, the US Congress passed the KORUS FTA (along with two other FTAs, with Columbia and Panama) on October 12, 2011, the day of Lee's arrival. About a month later, on November 22, the South Korean National Assembly also ratified the FTA, despite strong objections from opposition legislators. Figure 1 shows how the two main U.S. parties voted on the KORUS FTA. The KORUS FTA entered into force on March 15, 2012, ending a four and a half year-long legislative battle on both sides.

Without the modifications in 2010, it would have been much more difficult for the KORUS FTA to be ratified by the US Congress. The modifications shifted the politics surrounding the KORUS FTA debate in the United States. After the conditions on the US auto industry were modified, in particular, all three US automakers (Ford, General Motors, and Chrysler) and the United Auto Workers (UAW), which had previously presented strong opposition to the FTA, finally came out in favor of it. Remarking on the UAW's support in particular, an Obama Administration official was quoted as saying, "It

has been a long time since a union supported a trade agreement," and thus the administration hopes for a "big, broad bipartisan vote" in the U.S. Congress in 2011.[36]

Based upon narrative discussions of the KORUS FTA, this study hypothesizes that constituent interests played a key role in congressional voting on the KORUS FTA. At first glance, partisanship seems the main factor in legislators' decisions on the KORUS FTA. In the 2009-2011 111th US Congress, Democrats dominated both chambers. Thus it was not expected that Congress would ratify the bill. As Republicans became the House majority in the 112th Congress, there was a high expectation that the FTA would be passed by the House. As expected, the bill was passed on October 12, 2011. If a legislator's partisanship is the main factor that led the KORUS FTA to be passed, however, why did the Obama Administration need to engage in additional negotiations? Could Congress have ratified the FTA without the 2010 modifications?

The completion of the KORUS FTA was much more dependent on actions in the U.S. than Korea. The Lee Myung-bak Administration and his ruling party, the Grand National Party (GNP), had continuously supported the KORUS FTA and controlled the National Assembly since 2008. In contrast, the Obama Administration and the Democratic Party have been reluctant to support FTAs, particularly given the resistance from their major constituency, organized labor. President Lee and his ruling party awaited the decision of the U.S. Congress and the opposition party, the Democratic Party, agreed

[36] Schneider, Howard, "Obama, Lee outlined U.S.-Korea trade deal in Seoul, official says," Washington Post (12/06/2010), at http://voices.washingtonpost.com/political-economy/2010/12/post_1.html

to handle the FTA at the same pace as the U.S. Congress.[37] Therefore, this study focuses on U.S. Congressional voting on the KORUS FTA rather than Korean National Assembly voting. Table 3.1 provides a timeline of the KORUS FTA process.

Table 3.1: Timeline of the KORUS FTA

Date	Description
Mar. 15, 2012	Korea-U.S. FTA enters into force
Nov.22, 2011	The National Assembly of the Republic of Korea passes the KORUS FTA ratification bill
Oct. 21, 2011	President Obama signs the Korea-U.S. FTA implementing bill
Oct. 12, 2011	U.S. Congress passes the Korea-U.S. FTA implementing bill
Oct. 3, 2011	The Obama Administration submits the Korea-U.S. FTA implementing bill to Congress
Feb. 10, 2011	Signing and exchange of the agreed documents on the December 3, 2010 deal to the KORUS FTA
Nov.30-Dec. 3, 2010	Trade Ministers' meeting (Columbia, Maryland, U.S.)
Jun. 30, 2007	Korea and the U.S. sign the Korea-U.S. FTA (Washington, D.C., U.S.)
May 29-Jun. 6, 2007	Korea-U.S. FTA legal review meeting (Washington, D.C., U.S.)
Apr. 2, 2007	Conclusion of the Korea-U.S. FTA negotiations
Jun. 2006-Mar. 2007	1st to 8th rounds of Korea-U.S. FTA negotiations
Feb.-Apr. 2005	1st to 3rd meetings of the joint feasibility study group
Nov. 2004	Korea and the US agree to launch a joint feasibility study group

Source: Ministry of Foreign Affairs Republic of Korea

Determinants of Congressional Voting Behavior

1. Partisanship

Many scholars have examined the determinants of US congressional voting on public policy. First, partisanship is one of the significant determinants of US congressional voting on trade policy. It is usually argued that Democrats are likely to oppose trade liberalization, while Republicans are prone to support it. There are two explanations for these different perspectives. First, class partisanship explanation argues that the two main parties have appealed to different economic and social classes. For

[37] "Rival parties agree to handle FTA with U.S. in same pace with U.S. Congress," September 1, 2011, Yonhap News, available at http://english.yonhapnews.co.kr/national/2011/09/01/18/0301000000 AEN20110901008600315F.HTML

example, Republicans tend to be more attentive to business interests and therefore more supportive of trade liberalization. In contrast, Democrats are more inclined to support labor unions, hence their protectionist policies (Gartzke and Wrighton 1998; Lohmann and O'Halloran 1994). The second explanation stresses ideological stances (Nelson and Silberberg 1987; Xie 2006). Democrats have supported neo-Keynesian growth strategies, for which trade liberalization is relatively unimportant. By contrast, Republicans have supported the neoclassical growth model, which emphasizes the welfare-enhancing impact of trade liberalization.

2. Ideology

A legislator's political ideology (i.e., liberal vs. conservative) is more complex than partisanship. Politicians may vote for the policy consistent with their ideology of general welfare, rather than focus on their own political and electoral incentives. There exist several types of ideology scores. This study divides all types of ideology scores into three categories: a) pure ideology scores (liberal or conservative), b) interest group scores (pro-labor or pro-business) and c) special issue score (e.g., environmental and national security consideration, etc.)

With regard to the first category, it is usually expected that liberals are prone to support trade interventions in order to increase equity, while conservatives are more likely to oppose trade interventions on efficiency grounds. The Americans for Democratic Action (ADA) annual voting records have served as the standard measure of political liberalism, while the American Conservative Union (ACU) rating measures the conservative leanings of members of Congress. Existing research has shown

contradictory results about the effects of these pure ideology stances on trade policy voting. Some studies find that liberalism is related to protectionism (McArthur and Marks 1988), while others find a positive effect of liberalism on free trade (Goldstein and Lenway 1989). Several studies find that ideology has no impact on trade liberalization (Nollen and Iglarsh 1990).

Second, there are several interest group scores measuring a legislator's attachment to a certain group. For example, the American Federation of Labor, Congress of Industrial Organizations (AFL-CIO) ratings measures how closely each politician is aligned with labor interests. The Chamber of Commerce (COC) ratings tell us how closely a legislator is tied to business interests. Therefore, a legislator having a higher AFL-CIO score should be more likely to oppose trade liberalization, while a legislator's higher COC score indicates support.

Third, special issue scores present how much a legislator is interested in a certain issue. For example, the LCV (League of Conservation Voters) scores show a legislator's support for environmental issue. With regard to the KORUS FTA, one of the most significant issues is US national security consideration. According to several Congressional Research Service (CRS) reports, the US and Korea started to negotiate the KORUS FTA in part as a means to restore the health of a critical foreign policy and national security alliance (Cooper et al. 2013). During the negotiations in 2006 and 2007, both the Korean and US governments had agreed that the KORUS FTA could be a possible counterweight to the friction that developed over several issues, including North Korean nuclear weapons development and the repositioning of US troops in Korea. Based on this background, this study expects that a legislator who places more focus on

national security is more likely to support the KORUS FTA. The American Security Council provides a national security index (NSI) measuring how consistently a legislator votes in favor of strong national defense. In contrast to preceding studies examining whether a legislator's ideological stance is significant in voting patterns on trade policy, this study more specifically investigates which type of ideological stance is more significant.

3. Committee membership

In addition to legislators' beliefs, their power or influence in committee is also an important predictor. Several studies examine the influence of committee members on voting for trade policy (Shepsle and Weingast 1984; Gartzke and Wrighton 1998; Romer and Snyder 1994). Member of the committees on trade matters (e.g., the US Senate Committee on Finance and the House of Representatives Committee on Ways and Means) are often seen as having a national or international orientation to trade policy and to be less responsive to the demands of narrow constituent interests (Whalen and Whalen 1990). In this sense, they are less likely to support classical protectionism. In contrast, members of committees dealing with labor issues are less likely to support an FTA (e.g., the US Senate Committee on Health, Education, Labor and Pension and the House of Representatives Committee on Labor, Health and Human Services, Education, and Related Agencies).

H1: Political institutions (partisanship and committee member status) and ideology influence a legislator's vote on the KORUS FTA.

4. Constituent Interests

These institutional and ideological perspectives have been criticized in terms of placing too little focus on the role of constituent interests. Several scholars argue that policy outcomes are the result of the interactions between elected officials as suppliers and constituents as demanders. There exist two core issues of constituent interests studies: How should constituent interests be defined? And how can the preferences of constituents be determined?

In studies of U.S. trade policies, constituencies are usually understood in geographic terms (Anderson and Baldwin 1987; Lindsay 1990; Fordham 1998). This approach is intuitive because the electorate for members of Congress is defined geographically. In this sense, constituent interests is measured by the ratio of productive factors constituents' districts or states possess, or by the employment rates of certain industries in a district or a state. However, defining constituents in solely geographic terms has several problems. First, the mere presence of an industry or a group of voters in a district or a state does not necessarily mean that its interests are influential. Second, the actual constituency can be much broader than the geographic district, because a legislator's decision on policy can affect interests nationally and even internationally (Fenno 1978; Kingdon1989; Jackson and Kingdon 1992; Fordham and McKeown 2003). For example, lobbying activities from interest groups are rarely limited to geographical regions. In order to measure non-geographical interest, a number of studies examine the impacts of PAC campaign contributions on congressional voting (Chappell 1982; Baldwin and Magee 2000; Beaulieu and Magee 2004; Abetti 2008).

A more complex issue is how to determine the trade policy preferences of constituents. Constituent preferences depend on their comparative advantages and disadvantages. Since policy change has distributional consequences, an FTA creates economic "winner" and "loser" groups. However, the identity of the winners and losers appears to differ significantly across space and time. Two main models provide divergent predictions about which groups will support trade liberalization. First, assuming that factors of production are perfectly mobile, the Heckscher-Ohlin (HO) model expects that relatively scarce factors of production lose economically from trade liberalization, while relatively abundant factors gain. By contrast, the Ricardo-Viner (RV) model assumes the factors of production are immobile and cannot be reallocated swiftly to more efficient sectors of the economy.[38] Therefore, individuals' attitudes toward trade liberalization depend on the industry in which they are employed rather than on their factor status. Consequently, when factor mobility is low, sectoral (that is, industry) division over trade liberalization will form, while factoral divisions will appear when factor mobility is high.

Empirical evidence has supported both models. Several studies have observed sectoral coalitions of exporting versus import-competing industries,[39] while others have found empirical support for the factoral model.[40] One of the main reasons for these inconsistent findings is the difficulty of measurement. With a few notable exceptions, the appropriate measurement of constituent interests is lacking in previous research. For example, some studies (e.g., Fordham and McKeown 2003) measure the factor

[38] See Alt and Gilligan (1994) for the further discussion of the two models.
[39] For the sectoral findings, see Schattschneider 1935; Gourevitch 1986; Deardorff and Stern 1998; Destler and Odell 1987; Hiscox 2002; Busch and Reinhardt 2003; Irwin and Kroszner 1999.
[40] For the factoral supports, see Rogowski 1987; Leamer1984; Midford 1993; Scheve and Slaughter 2001; Mayda and Rodrik 2005.

endowment using the level of education in districts. They find that legislators in the districts with lower (higher) education and lower (higher) income level are more likely to oppose (support) trade liberalization. However, they consider only geographical interests and assume that constituent interests are formed along factoral lines.

Baldwin and Magee (2000) try to test the impacts of factoral as well as sectoral constituent coalitions on congressional voting. To test the factoral model, they divide PACs into labor and business. They find that a legislator who obtains more contributions from business PACs is more likely to vote for trade liberalization, while one who acquires more contributions from labor PACs is more prone to vote against liberalization. In order to test the sectoral model, Baldwin and Magee (2000) examine the employment rate in an industry within each congressional district or state (Fordham and McKeown 2003; Abetti 2008). However, the comparison using different types of evidence make their empirical results less persuasive. Beaulieu and Magee (2004) try to resolve this problem by dividing PACs into labor and business groups and then dividing again each group into export-competing and import-competing industry groups. By classifying PACs by industries as specifically as possible (34 industries), they find that the industry net export position significantly affects labor unions' trade policy preferences, but that industry characteristics have no impact on business group lobbying. However, they give too little attention to geographical constituent interests. In short, most preceding studies have failed to fully capture the influence of constituent interests.

The other explanation for the different empirical results in the literature lies in the time frame and the range of trade policy examined (Hiscox 2002; Beaulieu and Magee 2004; Ladewig 2006). Conclusions from specific trade policy outcomes should not be

automatically generalized to the analysis of other trade policy decisions. Since the sectoral model assumes no factor mobility, it is more appropriate for short run analysis, while the factor model with perfect mobility, is more applicable in the long run. Moreover, the sectoral model is likely to have more explanatory power when the range of trade policy is relatively narrow, affecting specific industries, as with the KORUS FTA.

This theoretical argument is empirically supported by events in the KORUS FTA discussions. After President Obama obtained more concessions in the automobile sector, all three US automakers and the UAW, which had previously presented strong opposition to the FTA, expressed their support for the FTA. Thus, this study expects that sectoral differences are more likely to be salient than factoral differences in constituent interests in US congressional voting on the KORUS FTA. This is because the agreement has a narrow range of tariff reductions with just one country, Korea, rather than broad-based tariff reductions. By considering geographical and non-geographical interests, and including factoral and sectoral models, this study seeks to more fully capture the influence of constituent interests.

H2: Constituent interests across industries (exporting vs. import-competing) rather than across factors (business vs. labor) are more likely to influence the KORUS FTA formation.

The US Congress consists of two chambers, the House of Representatives and the Senate. Several scholars argue that the influence of constituent interests on representatives' votes is likely to be much stronger in the House than the Senate. On the constituents' side, the smaller and more homogenous House district leads its members to

have fewer cross-cutting cleavages on economic issues. Senators represent states in their entirety, where constituents are likely to have competing, heterogeneous interests. Therefore, it may be easier to detect constituent interests in districts on trade policy (Mayhew 1974; Fiorina 1977). Representatives in the House have a short tenure (two years), and therefore they may be more sensitive to the needs and interests of their constituents for their reelection. Senators' six-year tenures allow them to be less sensitive to reelection pressures. Senators tend to be more influential on final chamber outcomes than representatives, therefore partisanship and political ideology are more likely to be salient than constituent interests in the Senate (Nollen and Quinn 1994). Im and Sung (2011) argue that this idea is supported by the fact that the roll-call margin for FTA bills in the Senate is typically wider than in the House and that some bills were passed even without roll-calls.

H3: Constituent interests tend to be more salient in the House than in the Senate.

Research Design

1. Dependent variable

The dependent variable is a US legislator's vote on the KORUS FTA. To test Hypothesis 3, this study examines votes in the House as well as the Senate. Therefore, the unit of analysis is an individual representative or senator in the 112th U.S. Congress. A vote that favors the FTA is coded as 1, and 0 otherwise. Since the dependent variable is binary, this study employs logit regression analyses.

2. Measuring constituent interests

In order to fully capture the effect of constituent interests on congressional voting, this study develops new measures for constituent interests, considering factoral as well as sectoral constituent coalitions in terms of geographical as well as non-geographical interests. Preceding studies have often assumed that constituent interests are formed along factoral lines, ignoring possible sectoral cleavages of exporting versus import-competing industries. This assumption may be due to the more complex pattern of preferences formed along specific industry lines and the lack of detailed industry-level datasets. This study develops a sectoral interest index based on three components: the employment rate in different industries, to measure geographical constituent interests; campaign contributions by different industries to a legislator, to capture non-geographical interests; and the trade orientation of different industries, to figure out whether industries are expected to support or oppose the KORUS FTA.

With regard to industry-level measures, the aggregated level of industry should be discussed first because measures can vary dramatically according to the level of aggregation (Grimwade 2000). Given the aim of this study, determining what factors led the US legislators to ratify the KORUS FTA, rather than more parsimonious examinations of the US congressional voting for all trade policy, this study includes 17 industries that are relatively sensitive with regard to the KORUS FTA. First, this study includes the top ten industries in trade between the US and Korea, as they are more likely to be influenced by the KORUS FTA. However, pre-existing trade patterns have an imperfect ability to explain strong support (or opposition). This is because some sectors have little pre-existing trade, not due to lack of trade complementarity, but as a result of

large pre-existing trade barriers. Such sectors expect large increase of benefits (or costs) after the FTA is established. For example, the U.S. pharmaceutical industry strongly supported the KORUS FTA, because it expected large increases in exports to Korea after the FTA was established, as compared to the pre-FTA period when Korea strongly protected its home market. The United State International Trade Commission (USITC) usually prepares reports assessing the possible sectoral effects of future FTAs before legislators' vote for FTAs. Based on the USITC (2007) report, seven more industries are included. Table 3.2 shows the list of industries based on the North American Industry Classification System (NAICS).

Table 3.2: List of the sensitive industries for the KORUS FTA

NAICS	Description
11	Agriculture, forestry, fishing and hunting
313-6	Textile mills, apparel manufacturing, and leather and allied product manufacturing
32519	Other basic organic chemical manufacturing
3254	Pharmaceutical and medicine manufacturing
326	Plastics and rubber products manufacturing
3311-5	Iron and steel mills and ferroalloy manufacturing, steel product manufacturing from purchased steel, alumina and aluminum production and processing, nonferrous metal (except aluminum) production and processing, and foundries
333	Machinery manufacturing
3341	Computer and peripheral equipment manufacturing
3342	Communications equipment manufacturing
3344	Semiconductor and other electronic component manufacturing
3345	Navigational, measuring, electro-medical, and control instruments manufacturing
3353	Electrical equipment manufacturing (motor and generator manufacturing)
3359	Other electrical equipment and component manufacturing
3361-3	Motor vehicle manufacturing, motor vehicle body and trailer manufacturing, motor vehicle parts manufacturing
3364	Aerospace product and parts manufacturing
51	Information
52	Finance and insurance

2.1 Sectoral coalition

In order to test the impact of sectoral coalitions among constituent interests, a number of studies on congressional voting utilize the employment rate in an industry. They assume that legislators are more likely to support trade liberalization when a greater number of constituents work in export industries relative to import industries. This study also utilizes the ratio of employment rate of an industry to total employment rates of 17 industries (ER_i^k).[41]

The trade orientation of an industry (exporting or import-competing) indicates whether it will support or oppose the FTA. This study uses 2010 industry trade data to identify an industry as either net exporting or import-competing. Data on the real volume of trade at the industry level are not available at the district level, so this study employs state-level trade data. However, using this state-level trade data barely reduces the overall variance in measure of constituent interests in a district because this trade indicator is ultimately multiplied by constituent interests measured at the district-level.[42] The measure of industry *k*'s trade orientation in the US is constructed as follows:

$$O_i^k = \frac{E_i^k - I_i^k}{E_i^k + I_i^k}$$

[41] Data on employment rate in an industry in congressional districts is estimated from data at the county level in the 2010 County Business Patterns. If a county contains more than one congressional district within its borders, the number of workers from an industry who are in each district is estimated by using the fraction of the county's population (in 2010) residing in each district. In this study, all county-level data is transferred in the same way.

[42] Data on the volume of trade is available at http://www.census.gov/foreigntrade/statistics/state/data/ar.html

where O_i^k is the trade orientation of industry *k* in state *i*; E_i^k is industry *k*'s export in state *i* to the rest of the world; and I_i^k is industry *k*'s import in state *i* from the rest of the world.[43] This measure takes on values ranging from -1 to 1. A positive value means industry *k* in state *i* is likely to be export-competing; in contrast, a negative value means industry *k* is import-competing. Consequently, the geographical interests related to industry *k* in district *i* (GI_i^k) is constructed as follows:

$$GI_i^k = ER_i^k * O_i^k$$

As discussed, the geographical interest may be indeterminate by itself, given that the mere presence of an industry's employment does not necessarily mean that it is influential. Thus, to build a more complete model of the influence of economic interests on legislator voting, non-geographical interests are included in this research, and the sectoral interest index includes campaign contributions from an industry to a legislator. The Federal Election Commission (FEC) provides data on all PAC contributions to candidates in each electoral cycle. This study employs PAC contribution data from the 2009-2010 election cycle, taking into account the contributions given during the election before the KORUS FTA votes took place. The Center for Responsive Politics provides the industry breakdown of PACs. However, while it classified business PACs by industry, it treats labor PACs as one group. Using a dataset from the Center for Responsive Politics and the FEC description of each interest group, Beaulieu and Magee (2004) identify the two-, three-, or four-digit SIC industries. In order to capture a more complete delineation of PAC contributions, this study employs their classification coding system of classifying

[43] The basic idea for this measure is taken from Bergstrand (1983).

labor PACs by industry.[44] Instead of employing the real values of campaign contribution of an industry to a legislator, this study calculates the ratio of an industry's campaign contribution to the total amount of campaign contributions given to a legislator. The non-geographical interests are calculated in the following:

$$nGI_m^k = P_m^k * O_i^k$$

where nGI_m^k is non-geographical constituent interests of legislator *m* related to industry *k*; and P_m^k means campaign contributions from industry *k* to legislator *m*.

Political leaders are likely to take account both geographical and non-geographical constituent interests. In order to create a single value for a given legislator, all 17 values (from 17 industries) are summed and finally GI_i^k and nGI_m^k are added as follows;

$$Sectoral\ Coalition = \sum_{k=1}^{17} GI_i^k * nGI_m^k$$

2.2 Factoral coalition

Constituent interests for the KORUS FTA may be formed along factoral lines. According to the HO model, business groups are likely to support an FTA, while labor groups are expected to oppose it. This study also develops a factoral interest index including geographical as well as non-geographical interests. The non-geographical interests are calculated with campaign contributions data in the following;

[44] The coding system is available at http://www.facstaff.bucknell.edu/cmagee/

$$nGI_m = \frac{p_m^b - P_m^l}{P_m^b + P_m^l}$$

where nGI_m is non-geographical constituent interests for legislator *m*; P_m^b means campaign contributions from business PACs to legislator *m*; and P_m^l is those from labor PACs. A positive value means that legislator *m* acquires more contributions from business PACs, while a negative value means that the legislator obtains more contributions from labor PACs. Thus, a greater number of this variable means that legislator *m* is expected to support an FTA.

The level of education provides a rough-and-ready picture of factor endowment in the districts (Fordham and McKeown 2003) on the assumption that the distribution of other types of capital is correlated it. This study measures the geographical interests with the level of education.

Finally, a factoral coalition index is developed adding the geographical and non-geographical interests as follows:

$$Factoral\ Coalition = GI_i + nGI_m$$

3. Political institutions and ideology variables

In order to test Hypothesis 1, this study includes political institutions and ideology variables. First, *Party* equals 1 if a member of Congress is Democrat. Second, all types of ideology scores are also included to test the impact of a legislator's ideology on congressional voting and furthermore, examine which type of ideological stance is more significant: *Pro-defense (NSI), Pro-labor (AFL-CO), Pro-bus (COC), Pro-lib*

(ADA), and Pro-con (ACU). Lastly, two committee member variables are included: *Com-trade* is coded 1 when a legislator is a member of the committees on trade matters (the US Senate Committee on Finance and the House of Representatives Committee on Ways and Means), while *Com-labor* is coded 1 when one is a member of committees related to labor issues (the US senate Committee on Health, Education, Labor and Pension and the House of Representatives Committee on Labor, Health and Human Services, Education, and Related Agencies).

4. Control variables: demographic characteristics

The socio-economic features and conditions of a district (or state) may also affect attitudes of congress members towards the KORUS FTA. This study expects that a lower income level of the median household (*Income*), and a higher unemployment rate (*Unemp*) of a district (or state) will be correlated with a negative stance on the KORUS FTA. Since it is usually expected that the KORUS FTA will increase job opportunities for Koreans in the US, constituent pressure might be expected for members whose districts or states have a large percentage of ethnic Koreans (*Korean*).[45] Constituent membership in unions may impact a representative's likelihood of supporting or opposing the FTA and therefore the level of unionization is expected to be negatively related to a legislator's voting on an FTA (*Union*). Since the data on the level of unionization is available only at the state level, this variable is only included in the Senate voting analysis.

It is expected when working with cross-sectional voting behavior data that potentially influential but unobservable explanatory variables, such as logrolling and vote

[45] Data on the level of income, unemployment rate, the ratio of Korean population are taken from American Community Survey 3-year.

trading, may exist.[46] Nollen and Quinn (1994) suggest that the technique of a lagged endogenous variable (e.g., previous vote for the related issue) can diminish some of the effects of the other explanatory variables, while making it more difficult to obtain statistically significant findings (p. 511). To address this issue, this study includes congressional members' voting for Trade Adjustment Authority (TAA) as a lagged endogenous variable. Before the ratification of the KORUS FTA, Democrats and Republicans were battling each other over passage of TAA. While Democrats argued that TAA should be approved before the agreement's ratification, Republican insisted on the opposite order. Democratic leaders and the Obama Administration considered TAA a quid pro quo for the KORUS FTA (and also for the FTAs with Colombia and Panama). The House of Representatives passed TAA (HR 2832) on September 7, 2011, and about one month later, on October 12, the Senate also passed it. *Pre-vote* is coded 1 if a legislator voted in favor of TAA, and 0 otherwise. Descriptive statistics for all of the variables are presented in Table 3.3.

[46] For a discussion of the errors occurring by failing to control for "unobservable" variables, see Jacobson (1990). For the effects of logrolling on congressional voting, see Stratmann (1992).

Table 3.3: Descriptive statistics

	House of Representatives (N = 433)				Senate (N = 99)			
Variable	Mean	S.D.	Min.	Max.	Mean	S.D.	Min.	Max.
FTA	0.64	0.48	0	1	0.83	0.38	0	1
Sector	0.69	0.68	-1.10	1.91	0.54	0.60	-1.12	1.74
Factor	-2.24e-10	1.35	-3.54	3.57	1.32e-09	1.25	-4.24	2.93
Party	0.45	0.50	0	1	0.54	0.50	0	1
Pro-defense	75.09	24.41	20	100	62.78	32.10	0	100
pro-labor	45.66	44.56	0	100	55.07	43.08	0	100
Pro-bus	58.77	34.34	0	100	58.94	37.04	0	100
Pro-lib	41.78	43.14	0	100	55.66	38.75	5	100
Pro-con	53.55	45.26	0	100	41.91	40.21	0	100
Com-trade	0.09	0.28	0	1	0.24	0.43	0	1
Com-labor	0.09	0.29	0	1	0.22	0.42	0	1
P-vote	0.71	0.45	0	1	0.71	0.46	0	1
(In) Unemp	1.86	0.24	0.92	2.69	2.08	0.24	1.28	2.56
(In) Income	10.85	0.25	10.10	11.58	11.11	0.15	10.84	11.45
Korean	0.58	1.59	0	19.62	0.33	0.35	0.06	1.87
EB con	179.25	181.28	0	1322.74	326.58	344.36	0	1379.17
IB con	2.25	4.61	0	37.5	4.10	7.02	0	43.5
EL con	42.56	57.37	0	650	23.42	39.80	0	203.53
IL con	8.30	12.30	0	68.5	3.56	9.37	0	39

Empirical Results

A logistic analysis presented in Table 3.4 indicates which factors were most significant in the House members' decisions to vote for or against the KORUS FTA. In the House of Representatives' voting analyses, there are 433 observations, and 73-74% of the votes are correctly estimated on the bill through Model 1 to 2. As a full model, Model 1 tests the effects of all variables, while Model 2 excludes several variables that are less likely to be significant in congressional voting in order to reduce noise. In contrast to existing studies, the coefficients of constituent interests (*Sector* and *Factor*) are individually significant in the House analyses.

For substantive interpretations, this study also calculates changes in the predicted probability of a "yes" vote as the independent variable changes from ½ standard deviation (SD) below the mean to ½ SD above the mean holding other variables at their means. This is applied to continuous variables, while for dichotomous variables changes in probabilities are reported as the explanatory variable changes from 0 to 1. In the House models, SD change of *Sector* (from ½ SD below mean *Sector* to ½ SD above the mean) increases the probability of "yes" vote by approximately 9% averaged across Model 1 and 2. Factoral interests also present a significant impact on congressional voting on the agreement –SD change of *Factor* raises the probability of a "yes" vote approximately 8.6% .[47]

Among all types of ideological scores, *Pro-defense* shows the greatest statistical significance. *Pro-bus, Pro-lib, Pro-con* are not significant at all in any cases while *Pro-labor* is significant in the full model but it loses statistical significance in the reduced model.[48] These results may stem from covariation between *Pro-labor* (or *Pro-bus*) and *Factor* because these two variables capture a factoral cleavage between business and labor. SD change of *Pro-defense* raises the probability that a legislator votes for the agreement around 21%. This result implies that US political leaders were more likely to support free trade with Korea as means of strengthening economic ties with Korea.

Another significant variable is whether a representative is a member of certain committees. If a legislator is a member of the Committee on Ways and Means, the

[47] The test whether the effect of sectoral interest on congressional voting is equal to the effect of factoral interest indicates that the effects of *Sector* and *Factor* are not equal (X^2=3.54, p<0.17).

[48] The Likelihood-Ratio test indicates that the effect of having *Pro-labor* is insignificant in the reduced model (LRX^2 = 2.65, P < 0.103).

probability of voting for the agreement increases by 24% averaged across Model 1 through 2. In contrast, whether a legislator is a member of committees expected to oppose the FTA is not a statistically significant variable.

Party is not statistically significant – this is quite contradictory finding from preceding studies.[49] This result may be driven by high correlations between *Party* and other ideology variables. Without any ideological variables, *Party* is highly significant indicating that a Democrat is likely to vote against the KORUS FTA. However, the Likelihood-Ratio test indicates that the effect of having ideological variables (at least one of five) is significant at the 0.01 level ($LRX^2 = 22.30$).

Other demographic variables do not show statistical significance. When compared to previous findings, specifically that the percentage of Hispanics is positive and significant for the NAFTA vote (Baldwin and Magee 2000; Kang and Greene 1999), it is an interesting finding that the ratio of ethnic Koreans in a district is not significant in a representative's decision on the KORUS FTA. This finding implies that the Korean population is not big enough to have a significant influence on policy.

[49] Jackson and Kingdon (1992) emphasize the statistical bias of employing the ideology scores driven from previous votes on relative issues to measure the influence of a legislator's ideology: overestimation of ideology and underestimation of other variables (e.g., constituent interests and party). In this study, the ideology scores may underestimate the influence of party on congressional voting on the KORUS FTA but they barely reduce the impact of constituent interests.

Table 3.4: Logistic estimates of the US Congressional voting on the KORUS FTA

	House				Senate			
	Logistic Estimates		Change in Predicted Probabilities		Logistic Estimates		Change in Predicted Probabilities	
	(1)	(2)	(1)	(2)	(1)	(2)	(1)	(2)
Sector	0.73***	0.71***	0.09	0.09	0.77	1.06*	0.04	0.11
	(3.27)	(3.28)			(1.16)	(2.04)		
Factor	0.30**	0.37***	0.08	0.09	-0.05	0.19	-0.005	0.02
	(2.20)	(3.29)			(-0.13)	(0.88)		
Party	1.59		0.29		5.14		0.58	
	(1.03)				(1.31)			
Pro-defense	0.05**	0.06***	0.23	0.29	-0.01	.02**	-0.00	0.003
	(2.56)	(9.72)			(-0.15)	(2.08)		
Pro-labor	-0.04**		-0.31		-0.02		-0.00	
	(-2.00)				(-0.25)			
Pro-bus	-0.00		-0.01		0.03		0.00	
	(-0.08)				(1.00)			
Pro-lib	-0.02		-016		-0.08		-0.01	
	(-1.03)				(-0.98)			
Pro-con	-0.02		-0.19		-0.02		-0.00	
	(-0.94)				(-0.35)			
Com-trade	1.98**	2.08***	0.24	0.25	0.19		0.01	
	(3.16)	(3.42)			(0.23)			
Com-labor	-0.43		-0.08		-1.46*	-1.42**	-0.16	-0.20
	(-0.86)				(-1.69)	(-2.14)		
Pre-vote	0.60		0.12		0.14		0.01	
	(1.21)				(0.07)			
(In) Unemp	-0.69	-0.92	-0.03	-0.04	1.12	0.84	0.08	0.09
	(-0.97)	(-1.40)			(0.78)	(0.67)		
(In) Income	0.63		0.03		3.06		0.23	
	(0.83)				(0.79)			
Korean	0.11		0.03		2.51		0.19	
	(1.06)				(1.22)			
Union					-0.16	-0.05	-0.01	-0.01
					(-1.39)	(-0.82)		
Cons	-6.22	-2.68*			-31.24	-0.97		
	(-0.64)	(-1.92)			(-0.73)	(-0.36)		
Pseudo R2	0.43	0.40			0.33	0.19		
Prob X^2	<0.01	<0.01			<0.01	<0.01		

Note: *significant at 90%, **significant at 95%, ***significant at 99% (two-tail test); Z scores are in parentheses

In order to test Hypothesis 3, this study also examines US Senate voting on the KORUS FTA. In the Senate models, there are 99 observations and the models predict 88-

92% of the outcomes. The lopsided nature of the Senate vote on the KORUS FTA (83 "yes" votes vs. 15 "No" votes) indicates that party, ideology, and constituent interests had little or no impact. It is usually expected that partisanship is more determinant in Senate votes. In the decision on the KORUS FTA, however, partisanship does not appear to be significant in the Senate. *Factor* is neither statistically significant in Model 1 nor in Model 2 while *Sector* is significant in Model 2. *Pro-defense* is also significant in Model 2, but it loses its significance in Model 1. The impacts of committee member variables in the Senate models present the opposite results of those found in the House models. *Com-labor* is statistically significant, while *Com-trade* does not show statistical significance. In short, the lopsided nature of the Senate vote on the KORUS FTA suggests that the chamber's widespread consensus on free trade with Korea leaves relatively little room for the influence of constituency, ideology or partisanship.

In order to investigate economic influences, especially the significance of campaign contributions (non-geographical interests) on voting probability, four PAC groups' contributions are individually included: exporting business (*EB*), import-competing business (*IB*), exporting labor (*EL*), and import-competing labor (*IL*) contributions. Two geographical interest variables in sectoral coalition and factoral coalition are included. The statistical results are presented in Table 3.5. All types of PAC campaign contributions were statistically significant in the House. However, they are not statistically significant in the Senate. These results confirm again that constituent interests play a key role in representatives' decisions on the KORUS FTA, while it is not likely to be determinant of senators' decisions. Moreover, they prove that industry-level cleavages among business and labor groups exist. A representative, who obtained contributions

from import-competing (export-competing) industry PACs, regardless of whether those industries are labor or business PACs, is likely to vote against (for) the KORUS.

Substantively, in the House model, ½ SD changes of contributions (from ½ SD below mean contributions to ½ SD above the mean) increase the probability of "yes" vote by approximately 11 % averaged across all four types. In order to examine the effects of campaign contributions on voting probabilities in more detail, this study conducts several counterfactual simulations. First, it uses the coefficient estimates from the model and the values for each representative to predict the probability of that representative voting in favor of the KORUS FTA. The sum of all representatives' probabilities of voting for the KORUS FTA yields the predicted number of favorable votes. The model predicts 99.6 percent of the actual vote. Then, each representative's probability of voting for the KORUS FTA under five counterfactuals is predicted. All other variables are held at their actual levels but each of four groups' (*EB*, *IB*, *EL*, and *IL*) contributions are set to zero in each simulation. In the last simulation, all PAC contributions are set to zero.

Table 3.5: The effects of PAC contributions on US Congressional voting on the KORUS FTA

	House		Senate	
	Logit Estimates	Change in Predicted Probabilities	Logit Estimates	Change in Predicted Probabilities
Export/business contribution	0.003***	0.10	-0.002	-0.05
	(2.61)		(-1.00)	
Import/business contribution	-0.14***	-0.12	0.03	0.02
	(-2.83)		(0.52)	
Export/labor contribution	0.01**	0.11	0.02	0.06
	(2.02)		(1.08)	
Import/labor contribution	-0.05**	-0.11	-0.05	-0.03
	(-2.26)		(-0.81)	
*Employ*trade*	0.76***	0.09	-0.28	-0.01
	(3.04)		(-0.70)	
Education	0.05	0.09	-0.05	-0.02
	(2.03)		(-0.33)	
Party	1.43	0.26	7.04*	0.76
	(0.92)		(1.75)	
Pro-defense	0.05**	0.23	-0.002	-0.01
	(2.53)		(-0.07)	
pro-labor	-0.03*	-0.29	-0.009	-0.03
	(-1.81)		(-0.15)	
Pro-bus	-0.01	-0.08	0.03	0.06
	(-0.85)		(0.70)	
Pro-lib	-0.03	-0.27	-0.13	-0.50
	(-1.68)		(-1.57)	
Pro-con	-0.02	-0.18	-0.04	-0.11
	(-0.90)		(-0.60)	
Com-trade	1.47**	0.20	0.20	0.01
	(2.20)		(0.22)	
Com-labor	-0.45	-0.09	-1.60*	-0.16
	(-0.88)		(-1.74)	
Pre-vote	0.47	0.09	0.06	0.00
	(0.95)		(0.03)	
(In) Unemp	-0.62	-0.03	0.37	0.01
	(-0.83)		(0.21)	
(In) Income	-0.36	-0.02	4.25	0.04
	(-0.37)		(0.78)	
Korean	0.07	0.02	3.86	0.09
	(0.60)		(1.64)	
Union			-0.17	-0.00
			(-1.40)	
Cons	3.92		-38.17	
	(0.34)		(-0.69)	
Pseudo R2	0.46		0.35	
Prob X^2	<0.01		<0.05	

Note: *significant at 90%, **significant at 95%, ***significant at 99% (two-tail test); Z scores are in parentheses

The results in Table 3.6, shed light on how important campaign contributions from the PACs are in Congressional voting on the KORUS FTA. As expected, without *IL* contributions, the model predicts that 27.27 more representatives would have voted in favor of the KORUS FTA and 12.65 more representatives would have voted in favor without *IB* contributions. In the absence of *EL* contributions, about 22.77 fewer representatives would have voted for the KORUS FTA and there would have been 25.75 fewer "yes" votes without *EB* contributions. Consequently, without campaign contributions from import-competing industries, there would have been around 39.89 more "yes" votes, while about 48.52 fewer representatives would have voted for the KROUS FTA without contributions from export-competing industries. These results reinforce the belief that export-competing industries play a key role in Congressional voting on the KORUS FTA.

Table 3.6: Counterfactual Predictions of the House Vote on the KORUS FTA

Actual KORUS FTA vote	278
Predicted Votes	
with all PAC contributions	277
with no contributions	262
with no labor/export PAC contributions	254
with no labor/import PAC contributions	304
with no business/export PAC contributions	251
with no business/import PAC contributions	289
Predicted Effect	
EL PAC contributions on number of votes	23
IL PAC contributions on number of votes	-27
EB PAC contributions on number of votes	26
IB PAC contributions on number of votes	-12

For a robustness check on the influence of constituent interests, this study also tests possible interactions. It is argued that a representative's vote on trade policy could be influenced by whether the representative hails from a safe or a marginal district (Fiorina 1989; Uslaner 1998; Wink, Livingston, and Garand 1996). Rather than having a direct impact on Congressional voting on the KORUS FTA, this study expects that electoral marginality mediates the effect of constituent interests – constituent interests are more likely to be salient in marginal districts than in safe districts. Theoretically, the threat of electoral defeat encourages representatives to be as responsive as possible to constituent interests, while in safe districts the lack of electoral threat allows them more room to pursue their own policy agendas. This study measures electoral margin with the margin of victory for a legislator.[50] In a similar vein, constituent interests may be conditioned by the number of years served by a legislator. This study anticipates that, as a legislator has served in Congress for a longer time, that representative is less likely to be sensitive to constituent interests given a lower perceived threat of losing the next election.

Results are presented in Table 3.7. The coefficients of all four interaction terms, *margin*sector*, *margin*factor*, *term*sector*, *term*factor* are not statistically significant. Moreover, the constituent interest variables (*Sector* and *Factor*) look as they do in models excluding the interaction. The results suggest that constituent interests are not conditioned by a legislator's safety in a district (or a state). In other words, legislators

[50] This is calculated by taking the difference in the vote for the incumbent and the second-place competitor in the most recent election.

vote for their constituent interests regardless of how competitive their districts are and how long they serve in Congress.[51]

Table 3.7: Logistic estimates of US Congressional voting on the KORUS FTA with interactions

	House		Senate	
	(1)	(2)	(1)	(2)
Sector	0.90***	0.72**	0.87	0.49
	(2.85)	(2.46)	(1.05)	(0.62)
Factor	.20	0.30	-0.64	-0.81
	(0.93)	(1.49)	(-0.96)	(-1.47)
*Margin*Sector*	-0.01		0.01	
	(-0.85)		(0.42)	
*Margin*Factor*	0.003		0.01	
	(0.62)		(0.86)	
*Term*Sector*		-0.001		0.08
		(-0.08)		(1.39)
*Term*Factor*		-0.001		0.05
		(-0.09)		(1.62)
Party	-0.35	-0.22	0.51	0.82
	(-0.45)	(-0.29)	(0.22)	(0.32)
Pro-defense	0.06***	0.06***	0.04	0.04
	(3.54)	(3.65)	(0.98)	(1.05)
Com-trade	2.03***	2.01***	-0.07	-0.08
	(3.28)	(3.24)	(-0.09)	(-0.10)
Com-labor	-0.51	-0.49	-1.84**	-2.11**
	(-1.03)	(-1.00)	(-2.27)	(-2.54)
(In) Unemp	-0.66	-0.87	0.88	1.73
	(-0.93)	(-1.26)	(0.62)	(1.12)
(In) Income	0.39	0.40	4.44	5.32
	(0.53)	(0.56)	(1.17)	(1.30)
Korean	0.10	0.09	3.00	2.58
	(0.98)	(0.90)	(1.37)	(1.11)
Union			-0.19**	-0.18**
			(-1.96)	(-1.99)
Cons	-6.98	-6.92	-50.38	-62.57
	(-0.79)	(-0.80)	(-1.19)	(-1.99)
Obs.	433	433	99	99
Pseudo R2	<0.01	<0.01	<0.05	<0.01
Prob X^2	0.41	0.41	0.28	0.32

Note: *significant at 90%, **significant at 95%, ***significant at 99% (two-tail test); Z scores are in parentheses

[51] It is still necessary to examine conditional marginal effects in order to determine the potentially varying influence each has over the range of the other. Since the interaction effects are not main interests of this study, the specific examination is not presented in this study.

Conclusion

The KORUS FTA discussions offer significant empirical evidence that support the argument that FTAs are the aggregated results of two-level (domestic and international) political considerations rather than economic calculations. After the US and the Korean governments agreed to form a bilateral FTA and finally signed it in 2007, they had to wait four-and-a-half years for their legislators' ratification. The completion of the KORUS FTA was much more dependent on actions in the US than Korea. What factors led US legislators to vote for or against the agreement?

Developing a new measure for constituent interests by considering factoral as well as sectoral coalitions, and by taking into account geographical as well as non-geographical constituent interests, this study finds that constituent interests played a significant role in US legislators' voting for the KORUS FTA, and that it was more likely to influence the House of Representatives' voting on the agreement rather than the Senators' voting. In particular, both sectoral and factoral coalitions were present in US congressional voting on the KORUS FTA, and sectoral coalitions of exporting and import-competing industries are slightly more salient than factoral coalitions of business and labor groups. This finding implies that the KORUS FTA is the result of domestic political games between expected winners and losers.

Another interesting finding is that a legislator's national security consideration was the most significant among several types of ideology. This finding provides another significant implication – an FTA is also the outcome of international political consideration. The US has been concerned that the development of regionalism in

Northeast Asia since 2000 will exclude the US and has tried to establish FTAs with Northeast Asian countries. Korea was likely to be the best option for establishing the first regional FTA based on economic size and political relations. Since the US is likely to take more economic risks with FTAs with China and/or Japan, owing to the size of their economies. For China, there is also a more problematic security relationship. The KORUS FTA was proposed by the Bush Administration to institutionalize its economic presence in Northeast Asia, and finally entered into force under the Obama Administration after the modification in 2010. In short, the KORUS FTA was the result of domestic as well as international political considerations.

CHAPTER 4

THE OPTIMAL PATH OF A CHINA-JAPAN-KOREA FTA:

Multilateral Path or Sequential Path

<ABSTRACT>

This study aims to analyze the possibility of a multilateral Northeast Asian free trade agreement (FTA), a China-Japan-Korea FTA (CJK FTA), as well as estimate the optimal path towards achieving it. Although there have been a great number of studies examining why a CJK FTA should be formed given its likely welfare-enhancing effects, studies on precisely how and through what paths it might be formed are extremely scarce. The main argument herein is that a multilateral path (rather than sequential path) wherein South Korea plays a key role as a hub (rather than a leader) is the optimal route for establishing a CJK FTA. Investigating the preferences and powers of the main sectors and national security relations among CJK, this study finds that although the two possible bilateral FTAs (a China-Korea FTA and a Japan-Korea FTA) are more feasible in Northeast Asia, they are less likely to serve as a stepping-stone to multilateral FTA formation. In short, this provides evidence supporting the hypothesis that the sequential path to a CJK FTA is less feasible in Northeast Asia and, thus, that the multilateral path is optimal. Therefore, this study argues that the three countries should simultaneously participate in a single round of trade negotiations in order to establish a CJK FTA.

Among major international regions, Northeast Asia is the only major region without a region-level trade agreement. Since the Asian financial crisis, China, Japan, and South Korea (henceforth CJK), the three main economies in Northeast Asia, have realized the need for deeper financial and trade cooperation among them. Under these circumstances, they have started to follow the growing global trend towards FTA formation. One distinctive feature of FTA formation in CJK worth noting is that their FTA partners tend to be extra-regional. CJK have not established bilateral FTAs with each other even though those FTAs would produce huge benefits both economically and politically. The three countries have merely discussed establishing intra-regional FTAs and have done so for a relatively long time; discussions are ongoing regarding two bilateral FTAs – a China-Korea FTA (a CK FTA) and a Japan-Korea FTA (a JK FTA) – and one multilateral FTA (a CJK FTA).

Among these three FTA discussions, a CJK FTA has recently shown the most rapid progress. From 2003 to 2009, CJK conducted trilateral joint research by the representing research institutions in each country[52] and advanced five rounds of the Joint Study Meeting in just one year (2010-2011). Finally, CJK launched the first round of CJK FTA negotiations in Seoul on March 26-28, 2013 with agreements to have two more rounds of negotiations within 2013 to be held in China and Japan. In contrast, the other two bilateral FTAs, a JK and a CK FTA, have not entered into full-fledge negotiations even though they have been under discussion for longer. For example, a JK FTA has been under discussion since 1998 – over 15 years. In this case, Japan and Korea had

[52] The three representing research institutions in each country are the Development Research Center of the State Council (DRC) in China, the National Institute of Research Advancement (NIRA) in Japan, and the Korea Institute for International Economic Policy (KIEP) in Korea.

advanced six rounds of official negotiations from 2003 to 2004, but the negotiations have been suspended since 2004. By establishing "working level consultation," the Japanese and Korean governments have been trying to restart the JK FTA negotiations since 2008. However, the official negotiations do not start yet. Since 2005, China and Korea have discussed establishing a bilateral FTA. After three rounds of the Joint Study Meeting, the Chinese and Korean governments agreed to launch official negotiations in 2012, but the negotiations have not started yet. Table 4.1 presents the processes of the three FTA discussions in Northeast Asia.

Several studies examine the main reasons for the lack of a region-level trade agreement in Northeast Asia, highlighting the absence of leaders that can control the various preferences of member countries. Referring to FTA formation experiences from Europe and North America, existing research emphasizes the role of leaders in trade liberalization (e.g., the US in the NAFTA formation and Germany and France in the EU formation). Aghion, Antras, and Helpman (2007), for example, develop a dynamic bargaining model of coalition formation. In this model, a leading country with "agenda-setting power" endogenously decides whether to sequentially negotiate FTAs with subsets of countries or engage in simultaneous multilateral bargaining with all countries at once. Given the Sino-Japanese rivalry and its hindrance on the emergence of one clear leader in Northeast Asia, this model may be useful in understanding the lack of multilateral trade liberalization in Northeast Asia, but it has a limited ability to discuss how a multilateral FTA might be developed in the region.

Table 4.1: The Processes of Japan-Korea, China-Korea, and China-Japan-Korea FTA discussions

Date	JK FTA	CK FTA	CJK FTA
1998	Joint Study Groups meetings	Not started yet	Not started yet
1999			
2000			
2001			
2002			
2003	1st round of official negotiations		Trilateral joint study research by the representing research institutions.
2004	2nd~6th rounds of official negotiations		
2005		Joint feasibility study	
2006			
2007		1st~3rd round of the Joint Study Meeting	
2008	1st~2nd rounds of working level consultation	4th~5th round of the Joint Study Meeting	
2009	3rd~4th rounds of working level consultation		
2010	1st rounds of director-general-level consultation	1st meeting on the exchange of views concerning sensitivities regarding the Korea-China FTA	1st~3rd rounds of the Joint Study Meeting
2011	2nd round of director-general-level consultation	Korea-China Trade Ministers' Meeting	4th~6th rounds of the Joint Study Meeting
2012		Declare to launch official negotiations	CJK Trade Ministers' meeting in Beijing to discuss FTA
2013			1st round of official negotiations

Source: Ministry of Foreign Affairs, Republic of Korea, at http://www.mofat.go.kr/ENG/policy/fta/status/negotiation/chinajapan/index.jsp?menu=m_20_80_10&tabmenu=t_4&submenu=s_9. China FTA Network http://fta.mofcom.gov.cn/topic/chinarh.shtml.

In the absence of such a leader, the alternative role of a "hub" has been stressed in the discourse on regionalism in Northeast Asia. In terms of economic and military-political power, China, Japan, or both would be the natural hubs in the region. However, these two competitive rivals have played passive roles in developing free trade in the region. It is widely argued that Asian economic regionalism could not be driven by a top-

down, overarching political decision to unify the region (Bergsten 2007). Unlike Germany and France, which cooperated with each other in the process of European Union formation, China and Japan have rarely discussed a bilateral FTA between them (a CJ FTA) while both have discussed establishing bilateral FTAs with Korea and a multilateral FTA including all three countries. Under these circumstances, it is suggested that Korea could act as a "hub" country having FTA discussions with the two "spoke" countries (China and Japan) in the development of Northeast Asian regionalism. Even though it is less likely to be strong enough to control and integrate the various preferences of the two spoke countries, Korea may be able to utilize its strong bargaining position in FTA discussions – it has engaged in separate bilateral FTA discussions with each spoke country while there is simultaneously no FTA discussion between those two spoke countries.[53]

A number of scholars and policy makers expect that all three countries would benefit from a CJK FTA and have therefore emphasized the necessity of CJK FTA formation. However, very little discussion has explored precisely how such an FTA might be formed in light of the international and domestic situations in CJK. Given the three players involved, two possible paths to reaching a CJK FTA exist: a multilateral path and a sequential path. In the multilateral path, all three countries simultaneously participate in a single round of trade negotiations. In the sequential path, on the other hand, two of the three countries form a bilateral FTA first and subsequently include the other country in the FTA.

[53] In the hub-and-spoke system, spoke countries have an incentive to sign a spoke-spoke agreement even if it is undesirable for a hub (Mukunoki and Tachi 2006); consequently, multilateral free trade is achieved. Given the Sino-Japanese rivalry, this is least likely to be feasible in Northeast Asia.

While the multilateral path is relatively simple, several key issues exist that should be considered and contrasted with the sequential path. The first issue regarding the sequential path is whether a bilateral FTA will in fact lead to a multilateral FTA. More specifically in this case, what is the likelihood that if one of the two bilateral FTAs (a CK FTA or a JK FTA) is established first, that both members of the established FTA (China/Korea or Japan/Korea) could agree on the participation of the non-member country (Japan or China) and that the non-member country will accept this suggestion? This issue gets at the time-honored question of whether an FTA is a building block or a stumbling block. Another significant question is which of the two possible bilateral FTAs (a CK FTA vs. a JK FTA) is likely to be established first.

Several studies in economics have developed dynamic bargaining models of coalition formation in order to predict the outcomes of FTA discussions and map the paths to those outcomes (Krishna 1998; Freund 2000; Aghion, Antras, and Helpman 2007; Saggi and Yildiz 2005). Nonetheless, these studies simply assume that each government cares only about social welfare and therefore chooses the FTA path that can maximize the aggregate welfare of its country. However, it is easily observed that political leaders make policy decisions for their own political incentives influenced by interest groups' preferences even though those decisions highly reduce the aggregate welfare (Grossman and Helpman 1995; Levy 1997). Thus, this study examines the optimal path to a CJK FTA employing a political-economy framework that specifically stresses the interaction between industry interest groups (IIGs) and political leaders.

By investigating all alternative paths to a CJK FTA based on the preferences of the main IIGs and national security relations among CJK, this study finds that a

multilateral path (rather than a sequential path) wherein Korea plays a key role as a hub is optimal for establishing the CJK FTA. Taking into account current political and economic considerations, two bilateral FTAs (a CK FTA and a JK FTA) are in fact more feasible than a CJK FTA given the different factor endowments and comparative advantages of the main IIGs and national security considerations. However, it is doubtful that these bilateral FTAs will lead to multilateral FTA formation, making the sequential path is ultimately less likely to lead to a CKJ FTA; therefore the multilateral path is the optimal alternative. This is also empirically supported by the processes of the two bilateral FTA formation of ASEAN (Association of Southeast Asian Nations) with China and Japan. A multilateral FTA, an East Asia FTA (an EA FTA) discussion, was suspended after ASEAN established two separate bilateral FTAs with China and Japan. In order to establish a CJK FTA, therefore, the three countries should simultaneously participate in a single round of trade negotiations. Given the Sino-Japanese rivalry, the role played by Korea as a hub is highly significant for the outcomes of a CJK FTA.

The remainder of this study proceeds as follows: First, the growing benefits of a CJK FTA are discussed given the importance of the Northeast Asian countries in the world economy and the increased economic interdependence among CJK. The main characteristics of Northeast Asian regionalism, where Korea may be required to play the role of a hub given the Sino-Japanese rivalry, are also examined. In order to predict the optimal path to a multilateral FTA, the effects of a CJK FTA on the main sectors in CJK are then investigated. The results of these analyses indicate that the multilateral path is optimal to establishing a CJK FTA. The final section presents policy implications.

Growing Benefits of a CJK FTA

In the 1990s, East Asian countries were left behind in the global trend towards FTA development. Experiencing the disadvantages of operating as independent countries in a global context of increasing regionalism, East Asia started to discuss its own regional development. The first attempt at this came in Southeast Asia in 1977, when ASEAN concluded its preferential trade agreement (PTA), which was subsequently developed into the ASEAN FTA in 1992. However, Northeast Asia has no region-level FTA equivalent to the ASEAN FTA, despite its much greater economic power and greater volume of regional trade. Motivated by a combination of economic and political objectives, CJK have pursued the formation of a multilateral FTA, which would be expected to bring huge welfare-enhancing benefits and increased political stability among CJK via increased economic interdependence.

In 2012, the combined GDP (Gross Domestic Product) of CJK accounted for 21% of global GDP, totaling US$15.2 trillion. CJK are also large trade states; the combined volume of CJK's trade in 2012 reached US$6.6 trillion, accounting for 18% of the global total. Table 4.2 shows the economic importance of CJK in the world and how it has changed during the last 10 years (2002 to 2012).

Table 4.2: Global share of GDP and trade of China, Japan, and Korea (2002 and 2012)

(Unit: %)

	GDP		Trade		Export		Import	
	2002	2012	2002	2012	2002	2012	2002	2012
China	4.3	11.3	4.7	10.5	5.0	11.2	4.4	9.8
Japan	11.9	8.3	5.7	4.5	6.4	4.4	5.1	4.8
Korea	1.7	1.6	2.4	2.9	2.5	3.0	2.3	2.8
Total	17.9	21.2	12.8	18.0	14.0	18.5	11.8	17.5

Source: UNCTAD STAT

The trade intensity index (TII) is usually used to estimate the degree of trade linkages with another country. If the TII is greater than 1, then country *i* and *j* are related more closely as measured against the averaged relations of others. As shown in Table 4.3, all TII scores for CJK are greater than 1, indeed very high in absolute value, indicating that all trading relations among CJK are closely related. More specifically, the TII of Korea with China and that of Japan with Korea are relatively high. In contrast, the TII of Korea with Japan is relatively low.

Table 4.3: The Trade Intensity Index in China, Japan and Korea (1997-2012)

	97	98	99	00	01	02	03	04	05	06	07	08	09	10	11	12
CJ	2.9	3.2	3.1	2.9	3.1	2.9	2.8	2.6	2.3	2.0	1.9	1.8	1.9	1.7	1.7	1.5
CK	2.0	2.1	2.0	1.9	2.1	2.1	2.0	2.0	1.9	1.8	1.8	2.0	1.8	1.6	1.5	1.5
JC	2.1	2.1	2.0	1.9	2.0	2.2	2.3	2.2	2.2	2.2	2.3	2.3	2.4	2.1	2.1	1.8
JK	2.4	2.4	2.7	2.7	2.8	3.0	3.2	3.3	3.2	3.1	3.0	2.9	3.2	2.9	2.8	2.7
KC	4.0	3.3	3.4	3.2	3.2	3.3	3.4	3.3	3.6	3.3	3.3	3.1	3.0	2.8	2.5	2.5
KJ	1.8	1.7	2.1	2.1	2.0	1.8	1.8	1.8	1.8	1.7	1.6	1.4	1.4	1.3	1.5	1.5

*The trade intensity index of country *i* in trade with country *j* is defined as:

$$\text{Trade Intensity Index } (TII_{ij}) = \frac{X_{ij} / X_i}{M_j / M_w}$$

where X_{ij} is export from country *i* to *j*; X_i is total export of country *i*; M_j is total import of country *j*; and M_w is world total import. Therefore, TII_{ij} compares export from country *i* to *j* divided by total export of country *i* to the ratio of country *j*'s import to total world import. If TII_{ij} is greater

than 1 then country i and j are related more closely than others. Data about all volume of trade are taken from UNCTAD STAT.

Table 4.4 shows main regional blocs' intra-regional trade. At first glance, CJK's intra-regional trade seems to be small compared to that of other blocs'. For example, in 2002 the EU's intra-regional trade represented almost 67% of total trade and NAFTA represented 56% while CJK took account for just 13%. Recently, the EU and NAFTA's intra-regional trade decreased slightly due to economic stagnation within the region and, despite the initial appearance of relative smallness, CJK's intra-regional trade has shown the highest increase. This may be caused by China's rapid economic growth as well as CJK's having realized the need for regional economic cooperation and subsequent changes in their trade pattern from extra- to intra-regional.

Table 4.4: Main economic blocs' share of intra-regional trade

(Unit: %)

	EU		NAFTA		ASEAN		MERCOSUR		CJK	
	2002	2012	2002	2012	2002	2012	2002	2012	2002	2012
Intra	67.1	62.8	56.1	48.5	22.7	25.8	11.4	14.5	12.8	18.0
Rest	32.9	37.2	43.9	51.5	77.3	74.2	88.6	85.5	87.2	82

Source: UNCTAD STAT

The development of foreign direct investment (FDI) in CJK, presented in Table 4.5, is also indicative of their increased economic interdependence. The FDI of Japan in China has rapidly increased from US$3,064 million in 2003 to US$12,582 million in 2011. The investment of China in Japan has also increased – it was just US$2.6 million in 2003 but reached almost US$112 million in 2011. Korea's investment in China has also increased from US$1,305 million in 2003 to US$4,967 million in 2011. This represented nearly 25% of Korea's total FDI.

Table 4.5: FDI development in China, Japan, and Korea

(Unit: US million$)

	Inflow		Outflow		Investee		
	2003	2011	2003	2011		2003	2011
China	47,077	228,600	152	43,000	Japan	2.6	111.5
					Korea	184.2	157.5
Japan	2,993	-1,758	28,799	114,300	China	3064.6	12582.2
					Korea	276.9	2434.8
Korea	3,526	4,661	4,135	20,355	China	1305	4976.8
					Japan	49.9	130.5

Source: OECD STAT http://stats.oecd.org/Index.aspx?DatasetCode=FDI_FLOW_PARTNER

Given these increased economic interactions, CJK have been trying to develop regionalism in Northeast Asia in the interest of realizing its benefits, which are potentially substantial. As a result, they have been discussing establishing a CJK FTA for over 10 years. Several joint studies conducted by the three representative institutes (DRC, NIRA, and KIEP) in each country show that all three countries would benefit from a CJK FTA. According to the 2007 joint research summarized in Table 4.6, China's economic welfare would increase by US$4.7 billion and its GDP would increase by 0.3%. Economic welfare gains and GDP growth for Japan would be US$19.1 billion and 0.41%, respectively. The benefits to Korea would be the largest both in terms of welfare and GDP – welfare gains and GDP growth would be US$20.0 billion and 2.8%.

Table 4.6: Macroeconomic effects of the CJK FTA

	Case 1		Case 2		2005 Joint Research	
	EV	GDP	EV	GDP	EV	GDP
China	4.7	0.30	5.0	0.55	3.3	0.30
Japan	19.1	0.41	9.4	0.15	16.8	0.37
Korea	20.0	5.26	10.9	2.61	12.4	3.55

Source: the Korea Institute for International Economic Policy (KIEP).

* Case 1 represents the elimination of bilateral nominal tariffs in all the sectors. Case 2 allows for the exemption in grains.

* Evaluated value is in US billion$ and GDP is in %

Beyond economic advantages, there are additional benefits of the CJK FTA. While many studies present conditions such as the Sino-Japanese rivalry, differences in political systems, current territorial and historical disputes, a lack of community consciousness, and so on as obstacles to regional economic cooperation in Northeast Asia, overcoming these obstacles could actually translate into objectives of a CJK FTA (Corning 2011). A CJK FTA has the potential to promote a community consciousness within the Northeast Asian region and harmonize political differences among CJK. Moreover, a CJK FTA could increase economic interdependence and may therefore alleviate political tensions driven by historical and territorial disputes. In short, all three countries recognize the necessity of developing regionalism, expecting economic as well as political benefits.

Characteristics of Northeast Asian Regionalism: No Leader, but Rather a Hub

1. Competitive rivals: China and Japan

Preceding studies based on the European and North American FTA formation have stressed the importance of the role of leading countries in building economic cooperation. These studies have discussed the negotiation processes of NAFTA with US leadership and those of the EU with the cooperative leadership of Germany and France. With regard to the several potential paths to FTA formation, Aghion, Antras and Helpman (2007) argue that a leader country chooses whether to enter multilateral or sequential bargaining by considering the anticipated payoffs of each. Similarly, this study attempts to identify the potential payoffs to CJK by considering coalition externality, which emerges when the size of a country's payoff depends on whether or not the other

two countries form a coalition. Aghion, Antras and Helpman (2007) find that the leader in FTA formation strictly prefers sequential bargaining when there are negative coalition externalities in at least one of the follower countries and strictly prefers multilateral bargaining when there are positive coalition externalities in both follower countries.[54]

Given the Sino-Japanese rivalry in Northeast Asia, these leadership-based models have limited ability to predict the outcome of FTA discussions and paths to reaching it. In the region, it is expected neither that one of the two strong powers (China or Japan) will be able to act as a single superpower in the near future nor that the two powers will work together in order to establish regional integration as Germany and France did in the establishment of the EU. The Sino-Japanese rivalry is also harmful for another reason: the two rivals still hold contradictory perspectives on a number of issues and would pressure other developing countries in the region to take sides. This could lead to divisiveness in Northeast Asian politics.

The Sino-Japanese rivalry hinders the emergence of a single leader in FTA formation in several ways. China and Japan have confronted each other on several issues expected to be hard to resolve. First of all, China (and also Korea) has severely criticized Japanese nationalist efforts to whitewash the actions of the Empire of Japan during World War II. For example, the Japanese Education Ministry approved academic textbooks revised in such a way as to minimize Japanese aggression during the war. In the textbooks, the term "aggression/invasion" is changed into "advancement" to describe

[54] The authors explain that there are positive coalition externalities in country *j* when $W_f(j) > W(j)$, negative coalition externalities when $Wf(J) < W(j)$. In this notation, $W(j)$ is country *j*'s payoff when there are no free trade agreements; and $W_f(j)$ is country *j*'s payoff when the other two countries form an FTA in which *j* is not included.

Japanese military action in Northeast China in the 1930s.[55] Moreover, Japanese Prime Ministers' recurrent visits to Yasukuni Shrine have aggravated the relations with China (and also with Korea) because the Yasukuni Shrine honors the spirits of Japan's war dead, among which are included 1,068 convicted war criminals and 14 convicted Class A war criminals.[56]

Secondly, the territorial dispute between the two rivals on the East China Sea (ECS) is expected to be a significant factor that could potentially lead to military conflict between China and Japan, as such territorial disputes in rivalry relationships are highly correlated with war (Christensen 1999). Some scholars consider rising energy consumption in China and Japan as a main reason behind a possible territorial dispute over the ECS (Calder 2006). Others regard geopolitics as the main factor rendering this dispute unsolved. There is little doubt that Chinese naval planners intend to extend power from China's territorial sea limits as far as the ECS median line. In response, Japanese naval doctrine has evolved to meet this challenge.[57]

Thirdly, China and Japan have each been developing military capabilities in a way that may exacerbate the contentious relationship between the two countries. China has expressed its concern about Japan's virtual nuclear capability and its shift towards a more assertive strategic posture since the end of the Cold War. Japan has increased its naval capabilities for several reasons. First, the US has requested that Japan have more

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[55] For discussion about the textbook dispute between China and Japan, see Rose (1998) and Schneider (2008).
[56] For more specific information on the domestic politics of Japanese leaders' visit to the Yasukuni Shrine visiting, see Shibuichi (2005) and Takahashi (2006).
[57] Onish, Norimitsu and Howard French, "Japan's Rivalry With China Is Stirring a Crowded Sea," September 11, 2005, *New York Times*.

responsibility for sea-lane defense in regional security. Second, threats from North Korea's missiles have led Japan to increase sea-based ballistic missile defenses (Dreyer 2006). At the same time, Chinese leaders have stressed the development of China's military strength and steadily increased its military spending (Buszynski 2009). The Japanese government has also criticized China's lack of transparency in its defense spending (Manicom and O'Neil 2009). In short, these unresolved issues led to two severe the Anti-Japanese demonstrations 2005 and 2012 in China (and Korea).

Given the competitive rivals, several scholars have discussed the dangers to the rest of the world in either China or Japan's leading of the development of regionalism in Northeast Asia. Ramesh and Yongzheng (2002) point out that the Chinese government has taken the position that developing or underdeveloped countries need to be independent from the rules and controls of Western society. For example, China has explicitly stated that it wants to help protect developing nations' interests in the WTO. A report published by the IMF assesses that China is likely to press for WTO anti-dumping rules in order to guard against attempts to use labor and environmental issues as disguises for protectionism and possibly to push for a reduction of agricultural subsidies. During the October 2002 East Asia economic summit, Long Yongtu, China's vice minister of foreign trade, publicly stated the need for Asia to have a platform to "let our voice sound louder in the decision-making process" now dominated by the West. Given this Chinese attitude, Western countries have expressed concerns about an economic cooperation system established by Chinese leadership (Harvie and Lee 2002).

Japan is usually considered to be a multilateral nation and, therefore, the Northeast Asian regionalism developed by Japan's leading would be more appealing to

the rest of the world. However, Japan has its own problems with multilateral trade liberalization. Its reluctance to open its agricultural market and eliminate various nontariff barriers is more likely to impede free trade. It is unlikely that Japan will allow a CJK FTA to include agriculture and other sensitive sectors.

2. Economic and political hub: South Korea

Though South Korea lacks some key qualifications needed for a leader or an agenda-setter that can control the various preferences of two superpowers and lead economic cooperation among three countries, several conditions make Korea a potential "hub" country in CJK FTA formation. It is widely recognized that the two competitive rivals, China and Japan, are motivated towards FTA formation by political as well as economic interests. In order to take leadership over the East Asian region, China and Japan have been actively promoting economic cooperation with member countries in an attempt to hold back its counter-partner's rapid FTA expansions as well as to avoid falling behind the global FTA trend. Under these circumstances, Korea is one of the most attractive FTA partners to China and Japan in terms of economic as well as political benefits. Consequently, Korea holds the most beneficial position in FTA negotiations with China and Japan as Korea has had independent FTA discussion with both countries, while the two rivals have barely discussed forming a bilateral FTA between them. This situation sets Korea up as a hub and China and Japan as spokes. Considering its geopolitical status in Northeast Asia, the Korean government has since 2003 pursued the "Financial Hub Initiative" (Lee 2004). In the same context, Korea has been planning to become an FTA hub by actively establishing FTAs in Northeast Asia. In February 2013, the Korea International Trade Association (KITA) published "FTA HUB, KOREA"

indicating that Korea's FTA network covers more than 60 percent of the global economic geography and has been developed through its continuous expansion of trade agreements.[58]

Economically speaking, Korea is Japan's third largest trading partner and China's fourth largest. Besides its status as a major trading partner, it is argued that its intermediate level of economic and technological development further leads Korea to be a hub country in the CJK FTA formation (Kim 2005). In East Asia, there have been three huge waves of trade and industrial transformation (Drysdale 2005). The first came with Japan's industrial development after the Pacific War. The second wave was led by the newly industrialized countries (NICs) – specifically the Four Asian Tigers including Korea – in the late 1970s and 1980s. The third wave was driven by China's rapid economic development in the 1990s. These different eras of industrialization led to technological asymmetries amongst CJK. As a country with an intermediate technological relative to China and Japan, Korea may be able to play a role as a hub by alleviating possible disturbances caused by these technological asymmetries when the CJK FTA is established (Kim 2005). However, existing studies have merely focused on the economic qualifications of a hub country such as the intermediate level of economic and technological development.

Besides economic conditions, this study argues that its political status also sets Korea up to play a hub role in CJK FTA formation. Given the complex security and political issues intermingled among CJK, one clear point in Northeast Asian politics is

[58] The full document is available at http://global.kita.net/engapp/FTA_Hub/img_130213/20130213_FTA HUB. pdf

that Korea has maintained a better relationship with both China and Japan than has been seen in Sino-Japanese relations. Korea has expressed its deep grievance towards Japan for its imperialist behavior in the first part of the 20th century. Though these two countries have experienced ongoing confrontation over a number of unresolved issues (e.g., comfort women issues and the Dokdo/Senkaku territorial disputes), free-market economies and democratic politics build stability between them. Since diplomatic relations were established in 1965, Japan and Korea have shown shared perspectives on a number of international issues. Trilateralism among the United States, Japan, and Korea has significantly contributed to peace and security in East Asia over the last 50 years (Cha 1999, 2000; Jo and Mo 2010). At the time when the first North Korean nuclear crisis unfolded, in particular, Korea and Japan shared a threat perception toward North Korea and cooperated with each other in order to remove the threat.

During the Cold War, China and Korea had hostile perspectives towards each other. Holding a pro-North Korea stance, China considered Korea as an enemy supporting the US and Japan's anti-communist strategy. After the Cold War ended however, the relationship between the two countries changed drastically from hostile and aggressive relations to mutually beneficial and interdependent cooperation. After normalizing diplomatic relations in 1992, China has been trying to take advantage of economic and other opportunities with Korea while sustaining its position as North Korea's most significant ally. In particular, China tried to cooperate substantially with Korea as well as the US in order to resolve the North Korean nuclear crisis from 2002 to 2004 (Sutter 2005; Shambaugh 2003).

Besides a need to maintain these favorable relationships with the two spoke countries, Korea may require additional support from other strong extra-regional powers in order to successfully fulfill a role as hub in FTA formation, given its relatively weak military and economic power. In this sense, the US is the country most qualified to influence the Northeast Asian economic cooperation via its political and economic relationships in the region. In the past, the US has tended to consider Japan as the "linchpin" for regional security. This lofty position was first conferred on Korea on the sidelines of the G-20 Summit in Toronto in June 2010. In a meeting with President Lee, Obama declared that the US-Korea alliance "is the linchpin for not only security for the Republic of Korea and the United States but also for the Pacific as a whole."[59] Katz and Cha (2012) argue that the elevated status of the US-Korea partnership and Korea's expanded international presence have been mutually reinforcing. Korea's willingness to contribute to global missions that the US deems important helps to bolster cooperation on longstanding bilateral issues. Since establishing the Korea-US FTA (KORUS FTA), in particular, Korea has been weaving its way towards becoming a hub of trade and investment in Northeast Asia.[60] Lee and Moon (2010) argue that Korea's FTAs with the US and the EU are likely to generate trade diversion (away from China and Japan), and this diversion is more likely to lead China and/or Japan to form an FTA with Korea.

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[59] "Remarks by President Obama and President Lee Myung-bak of the Republic of Korea after Bilateral Meeting," Toronto, June 26, 2010, at http://www.whitehouse.gov/the-press-office/remarks-president-obama-and-president-lee-myung-bak-republic-korea-after-bilateral-.

[60] "Korea as FTA Hub," March 14, 2012, *Korea Herald*, at http://www.koreaherald.com/view.php?ud= 20120314000508

Effects of a CJK FTA on Main Sectors in China, Japan and Korea

In order to predict the outcome of FTA negotiations and the optimal path to reaching an agreement, existing studies develop bargaining models with game-theoretic reasoning. One of the weaknesses of preceding studies is that they simply assume that governments establish an FTA in order to increase the aggregate welfare of their countries. However, it has been observed that some industries with strong political power that will be harmed by an FTA have been excluded from trade liberalization even when these compensations significantly reduce net welfare, thus arguing that politics as well as welfare benefits play a part in establishing an FTA. In this section, this study examines the preferences of the main economic sectors in CJK; considering the aforementioned evidence that such preferences play a part in FTA formation decisions, this examination will aid in making a more a realistic prediction for the optimal path to a CJK FTA.

Despite the overall positive effects of a CJK FTA, its potential impacts on individual industries vary depending on their comparative advantage. Regarding factor endowment, China is a relatively land/unskilled labor abundant country while Korea and Japan are relatively capital/skilled labor abundant countries. According to the Heckscher-Ohlin model (the HO model), China is likely to have comparative advantage over Korea and Japan in the agriculture, natural resources (e.g., paper and wood), and labor-intensive (e.g., textile) sectors while Korea and Japan are prone to show comparative advantage over China in capital-intensive (e.g., automobile) and high technology (e.g., professional instrument) industries. Meanwhile, Japan and Korea are likely to be competitive in most industries given similar factor endowments. In order to thoroughly examine the preferences of IIGs on FTAs, this study performs a qualitative analysis by examining the

revealed comparative advantage (RCA) index, the shared GDP, and tariff rates of individual industries in CJK.

Table 4.7: Revealed comparative advantage index of main industries in China, Japan, and Korea (1995, 2005, and 2012)

Industries	China			Japan			Korea		
	95	05	12	95	05	12	95	05	12
Agriculture	0.91	0.50	0.46	0.06	0.08	0.08	0.27	0.17	0.18
Textile and Leather Products	4.07	3.08	3.30	0.09	0.07	0.09	1.37	0.43	0.27
Paper and Wood	0.72	1.17	1.67	0.20	0.19	0.25	0.36	0.33	0.36
Chemicals	0.61	0.42	0.54	0.69	0.79	0.87	0.72	0.88	1.01
Minerals	1.10	0.90	0.90	0.58	0.57	0.78	0.26	0.24	0.20
Metals	1.06	1.03	1.01	0.86	0.99	1.29	1.09	1.13	1.33
General Machinery	0.45	1.42	1.57	1.75	1.50	1.74	0.64	0.93	0.89
Electrical Machinery	0.96	1.61	1.85	1.93	1.40	1.26	2.48	2.05	1.78
Transport Equipment	0.25	0.35	0.63	2.02	2.26	2.78	1.28	1.89	2.23
Professional Instruments	0.35	1.02	1.38	1.48	1.51	1.92	0.37	1.60	3.28
Expected Losers (in 2010)	Transport Equipment Chemicals			Agriculture Textile			Agriculture Textile		
Expected Winners (in 2010)	Agriculture Textile Paper and Wood			Transport Equipment General Machinery Metals			Chemicals Metals Transport Equipment Professional Inst.		
Highly competitive	Electrical equipment								

*The RCA index is defined by

$$\frac{X_j^k / X_w^k}{X_j / X_w}$$

where X denotes exports, k denotes the industry group classification of exports, j denotes the particular commodity in question, and w refers to the world.

*All export data are taken from UNCTAD STAT

Table 4.7 presents the RCA index of ten main industries in CJK. As can be seen, China has a high comparative advantage in the textile and paper and wood industries. Even though all three countries show weaknesses in their agricultural industries in world trade, China presents a relative advantage as compared to Japan and Korea. However,

China lags in the transport and chemical industries. Japan shows a comparative advantage in transport and general machine industries but its agricultural industry presents the greatest disadvantage among the three countries. Korea sees its highest comparative advantage in the professional instrument industry. It is interesting to consider that Japan had the highest advantage in this industry in 1995 (almost 4 times higher than the other two) but it lost its advantage in 2012. Now, Korea has around 1.7 times greater advantage in professional instruments. Korea also shows comparative advantage in the transport equipment, chemical, and metal industries as compared to China.

However, Japan and Korea are highly competitive in the transport and steel industries. All three countries are highly competitive in electronics. Consequently, the expected losers of a CJK FTA in China are the transport and chemical industries; those in Japan and in Korea are the agriculture and textile industries. The expected winners in China are the agriculture, textile, and paper and wood industries; in Japan this would be the transport equipment, metals and general machinery industries; and the winners in Korea are the chemical, metal, transportation equipment, and professional instrument industries.

Besides the industry preferences for a CJK FTA as measured by the RCA index, its power as measured by shared GDP by industry is another important indicator. If the expected losers account for a large portion of GDP in the country, this will likely make it difficult for political leaders to ignore the industry's preference for a CJK FTA and the FTA will consequently be less likely to form. In contrast, the probability of a CJK FTA formation increases if the expected winners are large industries in the domestic market. Table 4.8 shows the share of GDP by industry in CJK.

Table 4.8: Share of GDP by an Industry in China, Japan, and Korea (2000 and 2010)

(Unit: %)

	China		Japan		Korea	
	00	10	00	10	00	10
Agriculture, Forestry, and Fishing	6.71	4.71	7.82	7.3	7.07	3.89
Textile and Leather products	12.69	8.72	1.23	0.70	7.69	3.83
Paper and Wood	4.14	3.83	3.71	3.08	4.88	3.07
Chemicals	22.99	20.32	16.93	18.01	18.48	15.10
Minerals	5.34	5.73	4.37	3.67	4.27	3.27
Metals	13.66	17.90	15.26	18.61	17.81	12.65
General machine	7.57	10.14	13.17	12.48	8.11	9.11
Electrical machine	17.89	17.58	23.02	18.54	17.19	32.48
Transport equipment	7.75	9.92	12.53	15.58	12.95	14.87
Professional instruments	1.25	1.14	1.97	1.97	1.55	1.82

*For relative significance, these values are calculated as follow:

$$G_k \Big/ \sum_{k=1}^{10} G_k$$

Where G_k is share of GDP by industry *k*.

Source: For China's GDP is taken from Yearbook published by the National Bureau of Statistics of China (http://www.stats.gov.cn/english/statistical data/yearlydata/); Japan's GDP is taken from Cabinet office Annual Report on National Accounts published by Cabinet Office (http://www.esri.cao.go.jp/en/sna/data/kakuhou/files/2010/24 annual_report_e.html); and Korea's GDP is taken from Statistic Korea (http://kostat.go.kr/portal/english /index.action).

Overall, all three countries are large manufacturers in the world market. The expected losers in China are the transport and chemical industries, occupying 10% and 20% of GDP, respectively. In contrast, the expected winners, the agriculture (4.71%), textile (8.72%), and paper and wood (3.83%) industries, occupy around 17% of GDP in total. In Japan, the expected losers, the agricultural and textile industries, account for 8% of Japan's GDP. However, the expected winners, the transport equipment, metals and general machinery industries, occupy around 44% of GDP in total. In Korea, it is expected that the opposition against the FTA is less likely to be strong; the expected losers, the agriculture (3.89%) and textile (3.83%) industries, occupy only 7% of GDP in

total. In contrast, the winners, the chemicals, metals, transport equipment, and professional instrument industries, account for 35% of GDP in total.

The simple average applied most favored nation (MFN) tariff rates for manufacturing products of CJK in 2009 were 8.7%, 2.4%, and 6.6%, respectively, whereas the weighted average applied MFN tariff rates for manufacturing were 3.7%, 1.0%, and 3.2%, respectively as presented in Table 4.9. For all three countries the tariff rates for the agricultural products are the highest. China has higher tariff rates than Japan and Korea in most products, while Japan holds the lower tariff rates in most products.

Table 4.9: Applied MFN tariff rates for main products in CJK (2009)

(Unit: %)

	China		Japan		Korea	
	Simple	Weight	Simple	Weight	Simple	Weight
Agriculture**	29.0	21.9	8.6	4.7	39.7	33.4
Textile and Leather products	13.7	11.2	9.3	9.7	9.9	10.5
Paper and Wood	5.0	1.3	1.3	0.7	3.3	2.8
Chemicals	7.4	6.5	1.8	1.8	5.7	4.7
Minerals	12.1	11.4	1.0	1.0	7.5	7.5
Metals	7.6	5.8	1.1	0.7	4.9	3.7
General machine	5.5	3.2	0.3	0.2	3.9	3.1
Electrical machine	7.4	4.2	0.3	0.6	5.6	3.7
Transport equipment	11.5	10.0	0.0	0.0	6.1	4.6
Professional instruments	9.1	7.2	0.1	0.1	6.6	5.7

Source: Joint Study Report for an FTA among China, Japan and Korea (2011)

*The simple average means the average tariffs, the same weight is given to all products, without taking into account how much the products are traded.

The weighted average means the average tariffs weighted by import flows for traded products, more weight is given to products with larger import flows.

** The applied MFN tariffs of Agriculture could lead to biased predictions in that each government also use a various NTBs to protect its agricultural market.

In short, these statistics indicated that it can be expected that the Chinese government will be most likely to face relatively severe domestic resistance against a CJK FTA while the Korean government will be least likely to meet it. At this point, it should be considered the government's ability to coordinate various preferences of IIGs on trade policy. China is relatively free from domestic societal groups that are not well-organized. More specifically, the Chinese government is more likely to exercise powerful authority over society in designing and implementing FTA policies. As democratic countries, the Japanese and the Korean governments are likely to have greater difficulty in coordinating the preferences of IIGs. For the Japanese government, in particular, it will be quite hard to decide to open its agricultural market in the context of the electoral system, which over-represents rural populations but under-represents urban populations (Cowhey 1993). In Korea, there have been a number of social protests, which were sometimes violent, against the government's FTA policies. For example, since 2008, the Korea-U.S. Free Trade Agreement (the KORUS FTA) has been a serious public issue that has drawn resistance from key interest groups such as farmers, laborers, and non-governmental organizations (NGOs). Given relatively well-organized socio-economic groups, the Korean government does not seem to be well-positioned for pursuing FTAs with China and Japan. However, Lee and Moon (2010) point out that the Korean government was able to overcome domestic obstacles in the FTA negotiations with the US and EU. The lessons from previous experiences may help the Korean government in other FTA negotiations.

Optimal Path of a CJK FTA

Given the three players in the negotiations, two possible paths to establishing a CJK FTA exist: a multilateral path and a sequential path. In the multilateral path, all three countries simultaneously participate in a single round of trade negotiations while, in the sequential path, two countries form a bilateral FTA first and then include the other country in the FTA. While the multilateral path is relatively simple, there are several key issues that should be considered in the sequential path. The first issue is whether a bilateral FTA will subsequently and actually lead to a multilateral FTA. More specifically, if one of the two possible bilateral FTAs (a CK FTA or a JK FTA) is established first, will both members of the established FTA (China/Korea or Japan/Korea) agree on the participation of the non-member country (Japan or China) and will the non-member country then accept the suggestion? This issue is associated with the time-honored question of whether an FTA is a building block or a stumbling block.[61]

The second issue related to the sequential path considers which bilateral FTA (a CK FTA vs. a JK FTA) is likely to be established first. As a hub, Korea is likely to have requisite decision power to choose either a JK FTA or a CK FTA first. Korea has an advantage over China in bilateral trade, maintaining a trade surplus with China. China's trade deficit against Korea jumped from US$5.8 billion in 1997 to US$95.4 billion in 2012, an increase of 15 times over 15 years as a result of mounting China-Korea trade. In contrast, Korea has been disadvantaged through its trade deficit with Japan. Japan's trade surplus with Korea increased from US$11.5 billion in 1997 to US$21 billion in 2012.

[61] For more specific discussion about this question, see Chapter 1 (p.5)

Given these trade balances, it seems that a CK FTA should be given priority over a JK FTA.

Table 4.10 Trade balance between China and Japan, China and Korea, and Japan and Korea

(Unit: US billion $)

	China-Japan	China-Korea	Japan-Korea
1997	2.84	-5.80	11.48
2000	0.14	-11.92	10.25
2003	-14.74	-23.03	16.90
2006	-24.05	-45.20	22.94
2009	-33.03	-48.87	25.29
2012	-43.74	-95.39	20.94

*Trade balance is calculated as follow:

X_{ij} - M_{ij}

where X_{ij} is exports from country *i* to *j*; M_{ij} is imports of country *i* from country *j*.

However, the reactions of IIGs in CJK still need to be specifically examined and considered in order to make this prediction more precise. Investigating the levels of comparative advantages, tariff rates, and shared GDP of IIGs in CJK, this study argues that the sequential path is less likely to lead to CJK FTA formation. Table 4.10 presents the bilateral trade balances between China and Japan, China and Korea, and Japan and Korea.

1. Sequential Path

1.1 A JK FTA first, and then including China

Given the level of comparative advantages, tariff rates, and shared GDP of individual industries in CJK, the sequential path of forming a JK FTA first followed by the inclusion of China in that FTA has the lowest probability of resulting in a CJK FTA.

First of all, most of the main industries in Japan and Korea are highly competitive – in particular, Japan and Korea are most competitive in transport and metal industries. If a JK FTA were established, the Korean transport and metal industries are more likely to be hurt because they have higher tariff rates (4.6% for transport and 3.7% for metal). In contrast, Japan has already removed most tariffs on its transport and metal products (0% for transport and 0.7% for metal). Moreover, these two industries share large portions of GDP in both countries. In Korea, the transport and metal IIGs are more likely to oppose a JK FTA. The counter-partners in Japan are not expected to strongly support the FTA given industry competitiveness. Korea has a high comparative advantage in the professional instrument products, but these account for a relatively small portion of GDP in Korea. Therefore, it is unlikely that this industry will be highly influential in the Korean government's decision on a JK FTA. Consequently, political leaders in Korea are unlikely to support a JK FTA given that stronger opposition from transport and metal industries and relatively weak support from professional instrument industries are expected.

The agricultural sector is one of the most actively organized interest groups in Korea as well as in Japan. Therefore, both governments started FTA negotiations with the partners that are least likely to threaten their agricultural sector. Korea started negotiations with Chile,[62] Singapore, and Japan, while Japan negotiated FTA formation with Mexico, Singapore, and Korea. Among all FTA negotiations of both governments, only those of a JK FTA have yet to be concluded. Korea and Japan's agriculture industries have low competitiveness, place very high tariffs in order to protect domestic

[62] Chile was believed to be a complimentary agricultural country with respect to the Korean agricultural sector.

agriculture, and take large shares of GDP. Therefore, if a JK FTA were established there is a high probability that the agricultural sector would be excluded from the FTA. In this case, China is highly reluctant to participate in that FTA, expecting no benefits from its comparative advantage in agriculture. If a JK FTA is formed, moreover, the agricultural IIGs in Japan and Korea would severely oppose including China in a JK FTA.

In Korea, there have been great concerns about a JK FTA. These concerns include the competitive superiority of Japan and resulting trade deficit, the specialization of the Korean economy in low value-added industries, and the increased unemployment that results from the extended penetration of Japanese products (Kim 2005). In short, a JK FTA is least likely to be feasible among the three FTA discussions in Northeast Asia.

1.2 A CK FTA first, and then including Japan

It can be expected that the sequential path of forming a CK FTA first and then including Japan has a higher probability of success than the previously presented path. Given the different factor endowments, the two countries' industries are quite complementary. Though it is true that the trade complementarity between China and Korea has diminished over time, the trade complementarity is still higher between China and Korea than it is between Japan and Korea. Moreover, Korea has experienced an industrial transition from a heavy chemical to a technology-intensive focus, while China has just entered the intermediate stage of heavy industrialization. Korean manufacturing exceeds China's in terms of technology level and market competitiveness (Jianping 2006). More specifically, China expects benefits in the agriculture, textile, and paper and wood industries while Korea expects production increases in chemicals, auto, and professional

instruments. In particular, the auto industry in Korea has almost 3.5 times higher comparative advantage relative to its counterpart in China. As the auto industry in Korea is large enough to be politically strong, the probability that the Korean government would establish the CK FTA is higher. On the other hand, China expects high production increases in the textile industries; the textile industry in China has a 12 times higher comparative advantage and it accounts for a relatively large portion of Chinese GDP.

Opening the agricultural market also presents an issue of competition in a CK FTA discussion. Korea has concerns that an influx of Chinese agricultural products may destroy the Korean domestic market. Korean farmers' groups have been demanding that the government stop its FTA negotiations with China. The Korea Rural Economic Institute estimates that Korean agricultural production will drop by US$2.1 billion within ten years if tariffs are removed for all Chinese agricultural products except rice. This is nearly three times the amount of reduced production than resulted from the KORUS FTA.[63] In addition, cases of food adulteration in the private sector in China continue to be a major concern to the Chinese government. As a series of food adulteration cases eroded international confidence in Chinese agricultural products, including recently from Korea, the Chinese government has tried to resolve this issue by stepping up its campaign against food adulteration. In order to advance the bilateral FTA discussion, the two governments have agreed to keep out sensitive items such as the opening of agricultural markets.[64]

[63] "Agriculture at risk under FTA with China," May 3, 2012, Hankyoreh.
[64] "Seoul, Beijing to Start FTA Talks in January," June 29, 2013, ChosunIlbo

Given the higher probability of CK FTA formation via this sequential path, the next question is whether China and Korea would agree on the participation of Japan following the establishment of a CK FTA and whether Japan would subsequently accept the suggestion. After an FTA is formed, member countries usually reallocate human and economic resources from the sectors of comparative disadvantage to those with comparative advantage in order to maximize the welfare-enhancing effects of the FTA. A CK FTA would lead the Korean government to reallocate its resources to capital-intensive and high technological industries while China would focus on developing its labor-intensive and heavy industries. Under this situation, Korea's reluctances to the inclusion of Japan can be anticipated since Korea is unlikely to have comparative advantages in capital-intensive and high technology industries over Japan. In particular, the transport and metal industries, which are highly competitive with their counter-partners in Japan, would severely oppose including Japan in a CK FTA.

1.3 The possibility of a CJ FTA

The relationship between China and Japan is economically complementary but politically competitive. Economically, a CJ FTA would bring the greatest benefits to both countries given factor endowments and comparative advantages. In particular, China can expect a reduction in its trade deficit with Japan. Politically, however, several issues have hindered the development of the CJK FTA discussions. Besides unresolved historical and territorial issues discussed above, domestic political considerations have also intensified the hostilities between China and Japan.

It is widely argued that the legitimacy of the Chinese Communist Party (CCP) has always rested on its nationalist credentials, while current Chinese nationalism has been profoundly shaped by China's experience at the hands of Japanese imperialism. As Japan has been the principal foreign threat to China over the last 100 years, Chinese nationalism and anti-Japanese sentiment have become fused (Deans 1998). Zhao (1997) indicates that the rapid decay of Communist ideology has led the CCP to emphasize its role as the patriotic force and guardian of national pride in order to find a new basis of legitimacy. Saunders (1998) argues that, internationally, the collapse of communism in Eastern Europe and the Soviet Union revealed communism's bankruptcy as a political ideology and as a viable economic model. Domestically, moreover, market-oriented economic reforms have increasingly undercut the CCP's claim that China is a socialist country. Therefore, the CCP has been trying to uphold its legitimacy by provoking hostility toward Japan. Under this situation, the CCP would be concerned that establishing a bilateral FTA would increase economic interdependence and mutual exchanges at the individual level, and as a result a CJ FTA might weaken its legitimacy.

Meanwhile, the Japanese Foreign Ministry released "Japan's FTA Strategy" in October 2002 and clearly identified Korea as its primary FTA partner.[65] After Korea, priority was given to ASEAN rather than China. Japanese reluctance to form a bilateral FTA with China would be also driven by domestic political incentives. In particular, there have been conservative movements insisting that Japan should be a "normal country" having a standard military power rather than a self-defense force given China's threat in the region. Japanese conservatives are now aiming to revise the Peace Constitution, and

[65] The summary for this document is available at http://www.mofa.go.jp/policy/economy/fta/strategy 0210.html.

in particular amend Article 9, which forbids the deployment of Japanese forces abroad. China's hostility toward Taiwan, where Japan has substantial financial investments and large numbers of Japanese nationals, is likely to reinforce this stance of Japanese conservatives. Japan's domestic politics have become increasingly conservative and tried to raise (or at least maintain) the tension with China in order to achieve the ultimate goal of returning to being a normal country (Xinbo 2005). Under these circumstances, establishing a bilateral FTA with China is in conflict with the goal of "normalcy." Therefore, no FTA discussion between the two rivals is driven by political considerations rather than by pure economic calculations.

1.4 Empirical evidence: the ASEAN-China FTA and the ASEAN-JAPAN CEPA

The processes of the ASEAN-China FTA (AC FTA) and the ASEAN-Japan Comprehensive Economic Partnership Agreement (AJ CEPA)[66] formation show how difficult multilateralism is to develop in East Asia given the Sino-Japanese rivalry. Since the Asian financial crisis, the main economies in East Asia – the ASEAN countries, China, Japan, and Korea (i.e., the ASEAN-plus-three) – emphasized the necessity of economic cooperation by seeking to establish an East Asian Free Trade Area (EA FTA). Unfortunately, several challenges to consolidating regionalism in the context of the 'ASEAN+1' FTA emerged. China and Japan started to negotiate FTAs with ASEAN respectively rather than pursue a single multilateral FTA. These two regional powers' decision to propose FTAs with ASEAN was a political consideration rather than an

[66] Japan has a multilateral FTA with the ASEAN and several bilateral FTAs with individual ASEAN members. It calls the multilateral FTAs "Comprehensive Economic Partnership Agreements" (CEPA) because they cover several areas of economic cooperation beyond trade in goods and services.

economic calculation (Solis and Katada 2007; Yuzhu and Tong 2010; Sally 2006; Terada 2003).

In 2001, China first proposed an FTA with ASEAN despite the absence of strong complementarities. In the meeting to discuss establishing the ASEAN-China FTA, China emphasized the need for the FTA in order to avoid becoming "victims" of Western trade protectionism and economic trade blocs.[67] The demonstration of benign leadership, in the form of economic cooperation, is an essential element of such a strategy. China's FTA proposal was a means to dispel the growing concern among ASEAN nations of a "China threat." China's rapid rise naturally caused uneasiness among its neighbors who were uncertain about China's intentions. Economically, such sentiment rose from the fear that, as a WTO member, China would become an even stronger competitor for ASEAN's export to third markets as well as for ASEAN's efforts to attract FDI (Yuzhu and Tong 2010). Indeed, most ASEAN countries and China are similar in their development levels and economic structures give similar factor endowments. For Chinese leaders, economic cooperation with ASEAN through establishing an FTA seemed a favorable option to alleviating such anxieties. It is argued that this China-initiated FTA gave China a political advantage to become a more important force in the region. China was encouraged to extend its FTAs in order to occupy a strong position in the process of moving toward an East Asian FTA (Cai 2003).

After China and ASEAN agreed to begin negotiations in November 2001, Japan proposed its own FTA negotiations with ASEAN in January 2002. Japan's AJ CEPA

[67] "Asia Accuses US and Europe of Paying Lip Service to Free Trade," October 8, 2002, *Straits Times*.

proposal can be identified as a defensive response to AC FTA rather than as a sign of Japan having a clear regional strategy or intrinsic interest in an FTA with ASEAN (Sally 2006; Terada 2003). Given the potential danger of an EA FTA led by China and the deterred negotiations for an FTA with Korea, Japan started to negotiate the AJ CEPA and ultimately established a bilateral FTA with ASEAN (Ong 2003).

Some studies counter that China and Japan's decision to establish a bilateral FTA need not be seen as political calculation given their substantial welfare-enhancing effects. It is true that the AC FTA and the AJ CEPA also offer clear economic benefits. A joint study by the ASEAN Experts Group has concluded that by 2020 the AJ CEPA will increase ASEAN's exports to Japan by 44.2% and Japanese exports to Southeast Asia by 27.5% as compared to 1997.[68] A similar joint study by Chinese and ASEAN academics showed that the ACFTA will result in a 48% increase in ASEAN's exports to China and would increase China's GDP by 0.3%.[69] Mochizuki (2008) argues that AC FTA is not necessarily identified as China's intention to deter Japanese influence in the region because AC FTA would give ASEAN improved access to the Chinese market and as such make ASEAN a more attractive location for Japanese FDI. In addition, Pekkanen, Solis, and Katada (2007) show that the Sino-Japanese rivalry alone cannot explain Japan's trade policy choice. Japan has several extra-regional FTAs with Mexico, Chile, and Peru, instead of focusing all its energy on East Asia.

[68] Joint Report of The ASEAN-Japan Closer Economic Partnership Expert Group, September 2002.

[69] "Forging Closer ASEAN-China Economic Relations in the Twenty-First Century," report submitted by the ASEAN-China Expert Group on Economic Cooperation, October 2001.

Although the Sino-Japanese rivalry is not the only determinant for the absence of multilateral economic cooperation in Northeast Asia, it would be hard to discount its importance entirely (Corning 2011). The AC FTA and AJ CEPA established some new areas of cooperation among the signatories but failed to address important issues for regionalism. After establishing two bilateral FTAs (in addition to a third bilateral FTA, the ASEAN-Korea FTA), member countries in East Asia have rarely discussed the possibility of the EAFTA. Given the quite similar situation of the three actors' FTA discussion processes (China, Japan, and ASEAN), it is highly expected that the CJK FTA would produce a similar outcome: the CK FTA and the JK FTA rather than the CJK FTA.

2. Multilateral Path

Ultimately, even if one of the two bilateral FTAs (a CK FTA and a JK FTA) is established, there is a low probability that this will be followed by the subsequent formation of a CJK FTA. Employing computable general equilibrium (CGE) analysis, Lee and Moon (2010) find that "sequence" matters in measuring the economic impacts of FTA scenarios in the region. Moreover, the scenario wherein a CK FTA is established first and followed by a JK FTA would maximize Korea's economic gains. This scenario is quite similar to the ASEAN FTA formations with China and Japan. Given different factor endowments, ASEAN first established an FTA with Japan expecting more economic benefits and then formed an FTA with China. Therefore, it could be hard to establish a CJK FTA via a sequential path. The multilateral path is the optimal one to a CJK FTA formation and thus the three countries should simultaneously participate in a single round of trade negotiations in order to establish a CJK FTA.

In the FTA discussions of ASEAN with China and Japan, establishing two bilateral FTAs rather than a multilateral FTA was a better choice for ASEAN in terms of economic benefits. Generally, a hub prefers a bilateral FTA rather than a multilateral one – since neither spoke imposes a tariff on the hub yet both impose a tariff on each other, the hub country can enjoy privileged access in both spoke countries (Saggi and Yildiz 2005). The result of ASEAN's decisions solely pursuing its economic benefits was two separate bilateral FTAs and no multilateral FTA.

Conclusion

In accordance with the consensus among political leaders, CJK had conducted the Joint Studies for almost 10 years and finally started the first round of official negotiations on March 26-28, 2013. CJK has confirmed that a multilateral FTA among them will serve as an impetus that can increase not only trade and investment, but also political stability among the three countries. Furthermore, it is widely argued that CJK cooperation is one of the prerequisites for regional integration in East Asia.

Investigating the preferences and powers of the main sectors and national security relations among CJK, this study finds that the two possible bilateral FTAs (a CK FTA and a JK FTA) are more feasible in Northeast Asia than a CJK FTA, but they are less likely to serve as a stepping-stone to multilateral FTA formation. In other words, the sequential path to a CJK FTA is less feasible in Northeast Asia and, and thus, the multilateral path is optimal. Therefore, the three countries should simultaneously participate in a single round of trade negotiations in order to establish a CJK FTA.

The economic and political conditions allow Korea to be a hub in CJK FTA discussions. In order to play a role as a hub, and finally establish a CJK FTA, the findings of this study have several policy implications for the Korean government. Even though the scenario wherein a CK FTA is established first and followed by a JK FTA would maximize Korea's economic gains and would be a relatively safe option for political leaders, the Korean government needs to realize that there are other political benefits of the CJK FTA in order to develop regionalism in Northeast Asia. Without cooperation among CJK, the development of regionalism in East Asia is almost impossible given the fact the CJK comprise 90% of East Asia's economy. If the Korea government merely pursues economic gains in FTA discussions with China and Japan, there exists a high probability of a similar result that ASEAN produced in FTA formation with China and Japan, which is the two separate bilateral FTAs.

Moreover, there is still a question whether Korea really can be a hub of this region and take initiatives in cooperation (Lee 2004). The Korean government has been trying to become an FTA hub by concluding many FTAs. The FTAs with the EU and the US are one of the great accomplishments of the Korean government has made. However, a country will not become an FTA hub in the region automatically by establishing many FTAs. Rather, it should increase the quality of FTAs by maximizing market access and harmonizing trade rules (Cheong and Kwon 2006). In this sense, the South Korean government needs to understand the benefits of trade liberalization as well as political benefits of regionalism in Northeast Asia. At the same time, Japan and China are required to understand those benefits in order to establish the first multilateral FTA in Northeast Asia.

CHAPTER 5
CONCLUSION

Over the past decade, there has been growing agreement that the possibility of FTA formation is likely to depend on political considerations rather than aggregate economic welfare calculations. However, far less effort has been made to identify and study the factors operating in the political arena that are most relevant to FTA formation. In particular, the influence of interest groups is left largely unexamined in existing quantitative research. In this dissertation, three distinct essays examine how political considerations influence FTA formation in China, Japan, and Korea (CJK), the three main economies in Northeast Asia. This section discusses the key findings and major contributions arising from this dissertation and several questions that remain unresolved are discussed.

Overview of the Essays

The first essay provides general information about the conditions under which China, Japan, and Korea (CJK) might form free trade agreements (FTAs). The most significant finding of this study is the determinants of FTA formation have different effects depending on what stage the FTA formation process is in. In contrast to the common position that political institutions play the dominant role in forming FTAs, the findings of this study indicate that political institutions (regime type and veto players) are likely to influence FTA formation in the initial stages but are prone to lose their influence as the process moves forward. In contrast, support from industry interest groups is the driving force of FTA formation in the last stage, when signed FTAs must be ratified (or

legalized). Another significant finding is that political leaders are likely to choose their FTA partners in the context of national security politics and their national security consideration is still influential after conducting joint studies. After starting official negotiations, however, political leaders are more likely to advance the FTA discussion based on conditions in the domestic political arena.

Following the country-level analyses in the first essay, the second essay examines which factors influenced sub-national voting in the United States Congress on the Korean-U.S. Free Trade Agreement (KORUS FTA). In contrast to existing studies that find constituent interests play merely a marginal role, the main finding of this study indicates that constituent interests are in fact a significant predictor of US legislators' voting for the KORUS FTA. This result is driven by the development of a new measure of constituent interests' expected influence on congressional voting. Another significant finding is that a legislator's national security ideology was the most significant among several types of ideologies. This result implies that US political leaders were more likely to support free trade with Korea as means of strengthening economic ties with Korea.

After the two quantitative studies in essays one and two, the third essay performs a qualitative analysis of the influences of interest groups and national security relations on FTA formation in order to predict the possibility of a multilateral FTA among China, Japan, and Korea, a CJK FTA, as well as the optimal path towards achieving it. The main findings indicate that although the two possible bilateral FTAs (a China-Korea FTA and a Japan-Korea FTA) are more feasible in Northeast Asia, they are less likely to serve as a stepping-stone to multilateral FTA formation. Therefore, a multilateral path where the three countries simultaneously participate in a single round of trade negotiations is

optimal. The economic and political conditions between CJK situate Korea in a position to act as an FTA hub in the multilateral FTA discussions in order to establish the first region-level FTA in Northeast Asia. At the same time, Japan and China are required to understand those benefits in order to establish the first multilateral FTA in Northeast Asia.

Contributions to Existing Trade Policy Research

One of the major contributions that this dissertation makes to existing trade policy research is the development of a better measure of the influence of interest groups on trade policy decisions. It is widely acknowledged that it is very hard to compare the interest group activities in the FTA formation process, since the composition and power of IIGs vary greatly across countries. For this reason, the role played by interest groups has been neglected.

Due to measurement difficulty, preceding research typically depends on single-case qualitative analyses describing the activities of interest groups in FTA formation. On the other hand, several quantitative studies have tried to more generally examine the influence of interest groups on trade policies, and have found that interest groups play only a marginal role in trade policy decision-making. These results usually stem from inadequate measurement that only partially captures the effects of interest groups on trade policy. For example, some studies (e.g., veto players studies) have disproportionately focused on the 'resistance' side, while the role played by the 'support' side of an FTA has been largely left unexamined. This is discussed in more detail in Chapter 2. Moreover, as discussed in Chapter 3, several US congressional voting analyses only partially measure constituent interests by considering either geographical or non-geographical interests and

either factoral or sectoral coalitions. This dissertation makes meaningful contributions to societal perspective studies, by developing a better measure of the expected effects of interest groups.

Moreover, in contrast to existing research, which typically takes either a societal or an international perspective, this dissertation integrates these two distinctive approaches in the explanation of trade policy decision-making. The findings indicate that an FTA is the result of political considerations at the intra-national as well as at the international level. More specifically, political leaders establish an FTA by calculating how much it will yield both economic and political benefits, given the preferences and powers of domestic actors toward the FTA and international relations with the FTA partner.

In addition to the cumulative contributions of this dissertation, each individual essay makes its own contributions. Given the unique characteristics of CJK FTA formation (i.e., major trading partners have remained at and have not advanced beyond the proposal stage for a relatively long time), the first study proceeds to investigate the specific variations that may exist in the different stages of the FTA formation process. This essay ultimately finds that the determinants of FTA formation have different impacts according to which stage the process is in. Such variations have rarely been examined in previous studies.

As the first empirical analysis of US congressional voting on the KORUS FTA, the second essay constructs an improved measure for constituent interests, fully capturing their impact on US congressional voting. Unlike preceding studies investigating either

factoral or sectoral cleavages related to trade policy, this study tests the two competing economic models (the Heckscher-Ohlin model vs. the Ricardo-Viner model). Another contribution of this study is in the data improvement. Given that district-level data are extremely difficult to obtain, preceding studies employ state-level data for district-level analyses, arguing that such indicators are sufficient to capture the effects of indicators. However, the use of state-level data in the House analyses may reduce the overall variance in state and produce systemic errors. Rather than utilize state-level data, the second study employs county-level data for the indicators when district-level data are not possible to obtain. Moreover, this study disaggregates US industries as specifically as possible (e.g., using the five-digit NACIS code), making it easier to capture sensitivity to the economic impact of the KORUS FTA. As a result, this study examines the preferences and powers of the 17 industries most likely to be highly influenced by the trade agreement with Korea.

The third essay examines not only the possibility of a multilateral FTA (a CJK FTA), but also the optimal path to it, which has rarely been examined in existing research. Preceding studies examine the possibility of a CJK FTA, analyzing either international political relations or the economic effects of the agreement on the main industries in CJK. Considering all relevant factors that would influence political leaders' decisions on the agreement (e.g., the preferences and powers of the main industries, the national security relations, and the regime types), this study provides a more integrated prediction about not only the possibility of a CJK FTA, but also the paths to it.

Broader Implications

There are several questions that should be examined in future research. In the first and the third studies, the level of industry may need to be more precisely disaggregated. Different preferences (support vs. opposition) to a certain FTA in a single industry may exist given their different comparative advantages, particularly when disaggregated into more specific sub-industries. For example, the Chinese auto parts industry has a comparative advantage as compared to the Chinese production of the complete units (passenger cars). Japan and Korea tend to import auto parts from China and then assemble the parts into a complete unit and finally export the unit to China or other countries. In contrast to overall expectations that the Chinese auto industry severely opposes FTAs with Japan and Korea, the Chinese auto parts industry may support them. Future research should employ more disaggregated industry-level data, though such data for Northeast Asia are limited (see footnote 13 in Chapter 2).

In reality, governments (particularly democratic governments) use a number of alternative strategies to achieve their goals in trade policy decision-making. In order to protect the expected losers and their political power, for example, governments usually provide subsidies and non-tariff barriers (NTBs) or exclude the most sensitive sectors (e.g., the agriculture) from agreements. These compensations can potentially lead to different FTA formation results and have implications regarding the paths toward achieving them. For example, if China agrees to exclude the agricultural sector from FTAs with Japan and Korea, an option that would likely be welcome by all three countries, the possibility of the FTAs being established increases greatly. Since the types of compensation allocated to expected losers are too various to be compared across time

and between countries, this study does not thoroughly consider the impacts of these compensations on FTA formation. It would be quite interesting to examine the relation between the amount of subsidies (this is relatively easy to measure quantitatively and therefore to obtain a dataset)[70] and FTA formation. It is expected that these two factors are positively related.

This dissertation also focuses on the role of industry interest groups (IIGs) in FTA formation. Even though IIGs are the most influential groups in FTA formation, they are not the only influencing agent. There are a number of civic groups highly interested in their countries' trade policies, as trade policies are associated with a number of other issues. For example, the Central American FTA was hotly contested by environmental and human right groups (Abetti 2008). Though worthy of further study, the activities of such civic groups on FTA formation are outside the scope and interest of this dissertation.

In addition to these overall questions, each of the three studies also indicates several specific questions that should be considered. The first study focuses more on leaders' political considerations about FTA formation given the preferences of interest groups and national security relations. Therefore, the interactions with FTA partners are largely ignored. For example, there is a possibility that the expected winners of FTA formation may offer contributions to a foreign government. The third study tries to resolve this issue by examining the relevant factors in the country as well as in the FTA partners, but it gives little attention to the interactions themselves.

[70] The World Bank provides the dataset for subsidies at the cross-national level, at http://data.worldbank.org/indicator/GC.XPN.TRFT.CN

In the second study, non-geographical constituent interest is measured via PAC campaign contributions. However, PACs are not the only groups lobbying legislators to secure votes on trade bills (Baldwin and Magee 2000). A variety of interest groups may exist whose interests are highly associated with the KORUS FTA.[71] Baldwin and Magee (2000) examine voting on NAFTA from certain representatives who allegedly obtained special benefits from the Clinton Administration in return for supporting NAFTA. In future research, the influence of various other group types on FTA formation should be examined. However, the data on campaign contributions are largely limited to PACs. Future research may try to overcome the lack of data on campaign contributions by employing data from interviews and various public records.

It would also be interesting to see what factors likely influenced voting in the South Korean National Assembly on the KORUS FTA. In fact, the ratification process in the Korea National Assembly was very dynamic. The ruling party (the Grand National Party) called a snap plenary session. Opposition legislators rushed in, but were too late to prevent their rivals from putting the bill to a vote. In the 299-seat National Assembly, 170 members showed up for the vote, most of them governing party lawmakers.

More possible paths to achieving a multilateral FTA in a more indirect manner also exist. For example, CJK may be able to reach a multilateral FTA among them through ASEAN+3, RCEP (Regional Comprehensive Economic Partnership), [72] or Trans-Pacific Partnership (TPP). In particular, there is growing concern over the TPP in Korea

[71] The following website provide a variety of activities from civil society about the KORUS FTA http://www.citizen.org/Page.aspx?pid=4695

[72] ASEAN+3 is a proposed FTA among ASEAN, China, Japan, and South Korea and RCEP adds three more countries (Australia, India, and New Zealand). Therefore, RCEP is also called as ASEAN+6.

as TPP negotiations have been expanded since 2008. The TPP was originally signed by Brunei, Chile, New Zealand, and Singapore aiming to further liberalize the economies of the Asia-Pacific region. In 2010, the US asked Korea to join the TPP[73] but Korea declined it by stating that the TPP will bring huge benefit because Korea has already established bilateral FTAs with the US, Chile, and Singapore. However, this decision might be also driven by political considerations given the relations with the US, Japan, and China. As Japan is expected to attend the 18th round of TPP negotiations, which will be held from July 15 to 24, 2013, there is much attention towards whether Korea will join the TPP negotiation and towards how the Koreas' decision influence China's attitude. In future research, a wider level of regional integration should also be examined.

[73] "US requests Korea's joining of regional FTA," December 18, 2010, Dong-A Ilbo, retrieved from http://english.donga.com/srv/service.php3?bicode=020000&biid=2010121816208

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