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Geopolitical Risk, Strategic Complementarity, and Korea–Japan Cooperation

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I. Background: The Emergence of Techno-Economic Statecraft in Korea

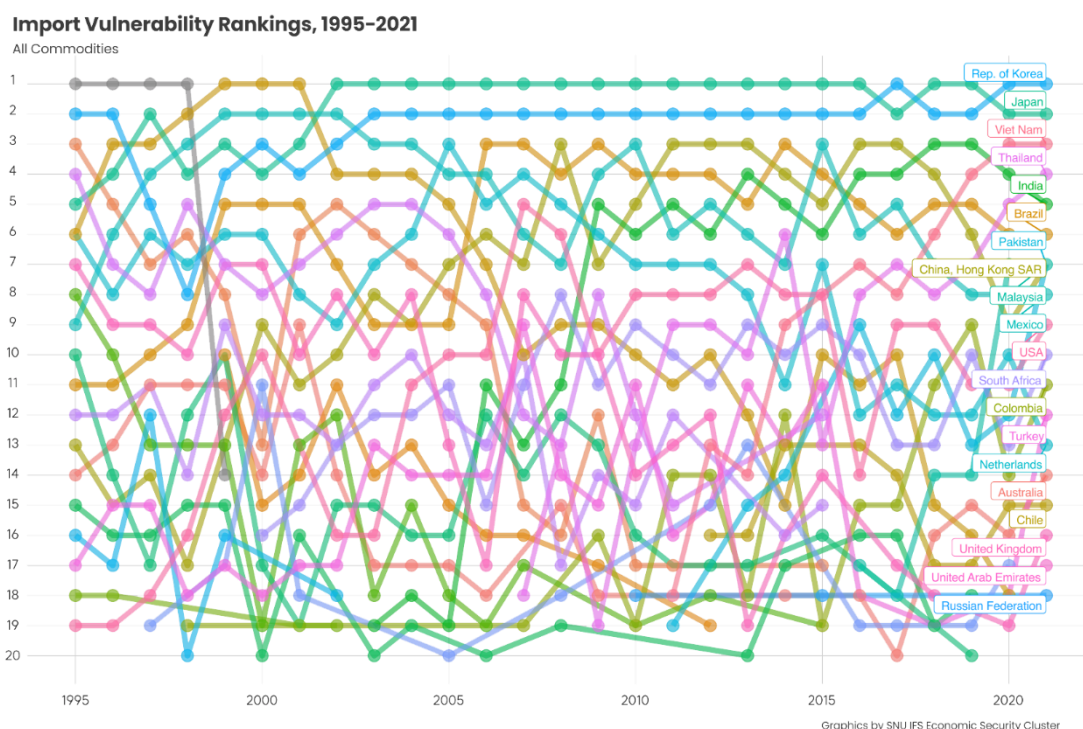
By identifying the emergence of techno-economic statecraft arising from geopolitical risks, this paper aims to explore the possibilities of cooperation between Korea and Japan. Geopolitical risks such as the U.S.-China strategic competition, the Russia-Ukraine war, and the Israeli-Hamas conflict, coupled with other uncertainties such as the increasing frequency of natural disasters due to climate change, the outbreak of pandemics, and the disruption of supply chains on a global scale, have dramatically increased the uncertainty of the world order. Faced with increasing geopolitical risks, Korea has pursued a techno-economic statecraft that utilizes advanced technologies in its economic security strategy. Diversification of high-tech manufacturing, reshoring and friend-shoring, increasing technological independence, combining technological innovation and industrial policy, and high-tech international cooperation are the main components of Korea's techno-economic statecraft.

Based on an examination of Korea's techno-economic statecraft, this study first aims to identify the facilitators and impediments to Korea-Japan cooperation in economic security. Korea and Japan share similar characteristics in terms of the vulnerability of their import structures, the impact of changing U.S.-China trade patterns, and the impact of U.S.-China technological decoupling. Their structural commonalities can serve as a foundation for economic security cooperation. Second, Korea and Japan have a dual nature of competition and cooperation in key industries, noting that cooperation should be prioritized in areas that are conducive to the stability and prosperity of the Indo-Pacific regional order as well as the two countries. Examples include establishing and operating early warning systems necessary to minimize the impact of supply chain disruptions, or leveraging complementary relationships within the value chain of the semiconductor industry.

II. Strategic Complementarity and Korea-Japan Cooperation

Korea and Japan should establish a cooperative strategy founded upon strategic complementarities. First, both Korea and Japan are countries with high levels of competitiveness in export-oriented industries. In 2021, their export competitiveness will rank 11th and 7th in the world, respectively (Seoul National University 2023). However, despite their export competitiveness, Korea and Japan are confronted with a shared challenge in terms of import vulnerability. In 2021, Korea and Japan were respectively in first and second place in the world (see Figure 1). Furthermore, both Korea and Japan are susceptible to import dependence in sectors where their exports are competitive. Korea and Japan should proactively create strategies to capitalize on the robust competitiveness of their export industries, with a view to mitigating the import vulnerability of the other country.

Figure 1. Import Vulnerability Index (1995-2021)

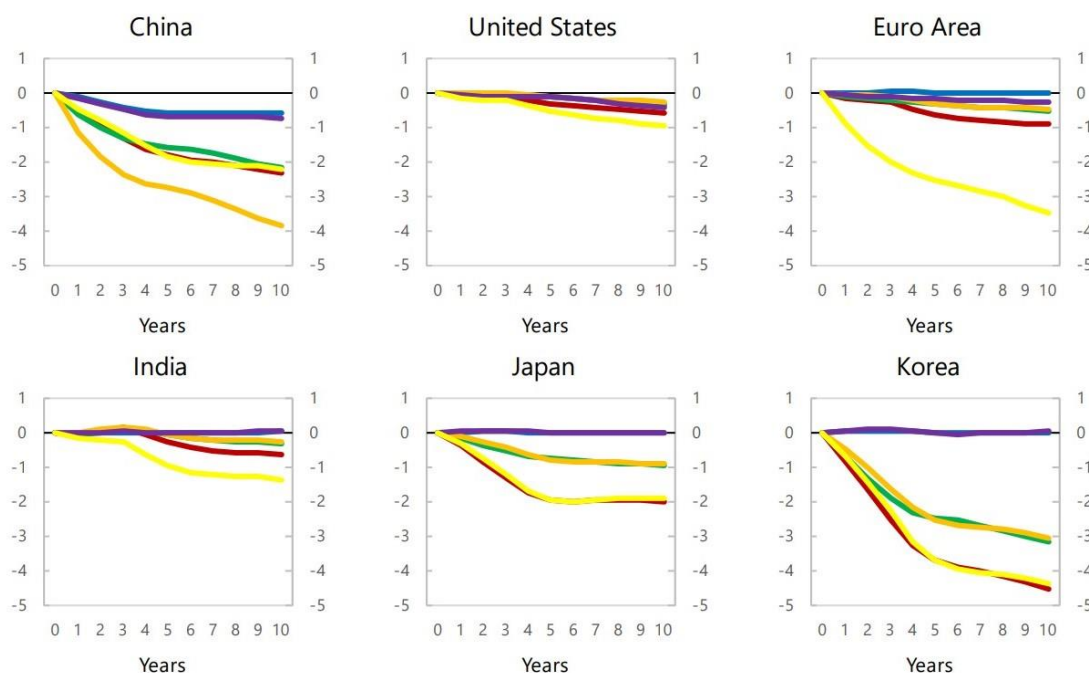


Source: Seoul National University 2023, p. 20.

Second, both Korea and Japan are confronted with a shared challenge, namely the repercussions of technology decoupling between the United States and China. In scenarios 2, 3, 4, and 6, Korea is anticipated to be the most adversely impacted by the decoupling of technology between the United States and China. In scenarios 2 and 6, Korea is even projected to experience a more impact than China. Japan is predicted to experience a lesser degree of impact from technology decoupling than Korea, but a bigger effect than that observed in the United States, Europe, and India (see Figure 2). The vulnerability of Korea and Japan to the repercussions of a technology decoupling between the

United States and China presents an opportunity for strategic collaboration. It would be prudent for Korea and Japan to consider ways to cooperate, including joint research, in order to mitigate the impact of technological decoupling.

Figure 2. The Impact of U.S.-China Technology Decoupling



Source: Cerdeiro et al. 2021.

III. Recommendations

In light of the above analysis, this paper presents policy recommendations for enhanced Korea-Japan cooperation. Firstly, it is recommended that Korea and Japan pursue bilateral cooperation in addition to regional or multilateral cooperation in order to mitigate structural vulnerabilities. Secondly, it is recommended that efforts be made to seek cooperation in order to effectively manage the potential risks associated with the diversification of high-tech industries, particularly those related to China. Thirdly, Korea and Japan should assume a pioneering role in the harmonization of the CPTPP and RCEP, thereby establishing the standards for 21st-century rules.

1. Trump 2.0 and Trade War 2.0

It is anticipated that the advent of Trump 2.0 will precipitate a shift in the dynamics of trilateral cooperation. The inauguration of President Trump in January 2025 will result in a change of leadership in all three countries. The acceleration of trilateral collaboration between Korea, the United

States, and Japan has been largely driven by the establishment of trust and rapport between the leaders of the three countries in addition to a shared understanding of the threats and challenges facing the three nations. It will be of interest to observe the extent to which the leaders of the three countries are able to leverage their personal relationships and mutual trust to sustain the current momentum of trilateral cooperation and advance it further.

In the course of his electoral campaign, President-elect Trump made a commitment to address the issue of trade imbalances. In 2023, Korea and Japan exhibited trade surpluses with the United States of \$51.4 billion and \$71.2 billion, respectively. Indeed, the trade surpluses of both countries are comparatively smaller than those of China (\$279.4 billion), Mexico (\$152.4 billion), and Vietnam (\$104.6 billion) (Bureau of Economic Analysis 2024a). However, the fact that Korea and Japan rank eighth and fifth in terms of trade surplus with the United States is a cause for concern, particularly in light of the stated objective of the Trump administration, which is to correct trade imbalances. This is particularly relevant in light of the Trump administration's repeated assertion that it will impose universal tariffs on all U.S. trading partners.

It is of the utmost importance to conduct a comprehensive examination of the ramifications of the Trump 2.0 tariff policy on Korea and Japan, with a view to formulating a unified response strategy. Immediately after the election, on November 26, 2024, President-elect Trump declared his intention to impose a 25% tariff on all imports from Canada and Mexico on the first day of his tenure. The objective is to restrict Vietnam and Mexico as third countries indirectly exporting to the United States. Furthermore, President-elect Trump has indicated that he will impose an additional 10% tariff on imports from China. It is imperative to conduct a comprehensive analysis of the potential consequences of the proposed changes, including the imposition of tariffs exceeding 60% on Chinese goods and the restriction of bypass exports to Mexico and Canada.

In the near term, the imposition of a 60% tariff on Chinese goods is likely to enhance access to the U.S. market for Korean and Japanese products. It is, however, important to note that this may create a secondary effect of increasing competition from Chinese goods in third-country markets. Moreover, the Trump administration's imposition of tariffs on Chinese goods is likely to culminate in a second US-China trade war. In the event of a resumption of trade tensions between the United States and China, with China imposing retaliatory tariffs in response to those imposed by the United States, it is likely to see the proliferation of protectionism and uncertainty in the global trade order, which is an unfavorable outcome for both countries. It is therefore for Korea and Japan to seek to play a role in managing the situation in order to avoid a second trade war. For this, Korea and Japan should conduct a thorough examination of the implications of the Trump administration's trade policies on their respective economies and the broader Indo-Pacific regional economic order.

2. LNG Cooperation

In light of the Trump administration's approach to trade, Korea and Japan should adopt a strategy to address trade imbalances. European Commission President Ursula von der Leyen made a statement on November 8, 2024, shortly after Trump's victory was confirmed. She indicated that European countries might consider replacing Russian LNG with US LNG. The rationale behind this proposition is twofold. First, U.S. LNG is a more cost-effective alternative to Russian LNG, stabilizing energy prices in Europe. Second, the importation of U.S. LNG would serve to reduce the trade imbalance between the EU and the United States. In 2023, the EU recorded a record high trade surplus with the United States, reaching €156.7 billion. The majority of this surplus was accounted for by Germany (€85.8 billion), Italy (€42.1 billion), and Ireland (€31.1 billion) (Eurostat 2024).

Korea and Japan need to consider utilizing LNG imports not just as a means of mitigating their trade imbalances with the United States but as a potential avenue for bilateral cooperation. Since the Great East Japan Earthquake in 2011, Japan has continued to increase its LNG imports, thereby becoming the world's largest LNG importer. Additionally, Korea is the third-largest importer of LNG in the world, having imported 46.39 million tons in 2022. This indicates that Korea has the potential to employ LNG imports as a means of addressing its trade imbalance with the United States. Furthermore, Korea's long-term contracts for the importation of LNG from Qatar and Oman are scheduled to expire in 2024. Imports from Qatar and Oman account for 19.5% and 11.3%, respectively. There is a concern in Korea that the new long-term contracts will be of a lesser quantity than the existing ones, which could result in import shortages. By expanding its LNG imports from the United States, Korea can achieve two effects simultaneously: reducing the U.S.-Korea trade imbalance and stabilizing LNG imports.

Second, it would be beneficial for Korea and Japan to consider the joint importation of LNG and the establishment of a collaborative effort to construct an LNG trade hub in the Indo-Pacific region. As major importers of LNG, Korea and Japan can collectively leverage their bargaining power to secure favorable import prices through collaboration. Moreover, Korea and Japan can assist in the construction of LNG infrastructure in the Indo-Pacific region, thereby facilitating LNG trade and establishing themselves as regional LNG hubs. In Japan, it is anticipated that domestic consumption will account for 71 million tons of LNG imports in 2022, with a projected decline to 50 million tons by 2030. To address these issues, Japan is working to construct an Asian gas market by providing financial and technical assistance to Southeast Asian countries for the development of LNG terminals. Consequently, Japan's LNG re-exports are projected to reach 31.57 million tons in 2022. With the establishment of a conducive environment for LNG trade in the region, Korea and Japan should collaborate to further enhance the vitality of LNG trade.

3. Supply Chain Cooperation

The Trump administration will undertake a revision of the derisking policies initiated by the Biden administration and pursue a strategy of strategic decoupling. It is important to note that Korea and Japan have the potential to play a significant role in supporting the United States' strategic decoupling efforts. Such a shift will undoubtedly result in a transformation of the United States' supply chain strategy. As the United States continues to diversify its economic relationships, it will speed up reshoring policy, while reducing nearshoring.

The United States has been actively promoting the reshoring of U.S. companies and foreign direct investment (FDI) by foreign companies with the dual goals of expanding manufacturing capacity in key industries and creating quality jobs in the United States. Both Korea and Japan have been observed to be making significant investments in the United States through FDI. In the 2022-2023 period, Japan was the second-largest source of FDI in the United States, ranking behind only the Netherlands (Bureau of Economic Analysis 2024b). Additionally, Korea experienced a 26% surge in U.S. investment from 2020 to 2021.

In 2023, Korea, China, Japan, Germany, and the United Kingdom were the countries that invested heavily in the United States. In terms of the number of investments in the United States, Korea and Japan were in the first and third positions, with 73 and 69 investments, respectively. The number of jobs created in the United States as a result of investments from Korea and Japan was 20,360 and 18,192, respectively, representing 14% and 12% of all jobs created through FDI. Korea and Japan combined to account for approximately one-quarter of the jobs created through FDI (Reshoring Initiative 2023). Both countries' contributions to U.S. supply chain resilience and job creation may continue to be a major driver of the Trump administration's demand for cooperation from Korea and Japan. Nevertheless, Korea and Japan should collaborate to construct a compelling rationale to persuade the Trump administration. While increasing trade imbalances in the short term, both countries' investment in the U.S. not only fortifies the resilience of the supply chains of U.S. manufacturing industries but also significantly contributes to diversification away from China.

IV. Trump 2.0 and Korea-Japan Cooperation

1. Beyond Trilateral

In the Trump 2.0 era, Japan and Korea need to adopt a novel approach to advancing trilateral cooperation. As U.S. involvement in regional leadership is expected to decline, Korea and Japan should adopt a strategic approach that leverages Korea-Japan cooperation as a means of sustaining and enhancing the trilateral cooperation initiative, in contrast to the existing dynamics where cooperation between Korea and Japan has been stepped up by the trilateral cooperation. In the Trump 2.0 era, should the United States adopt a transactional approach even with its allies such as Korea and

Japan, this could have the effect of significantly weakening the momentum of trilateral cooperation. Under the circumstances, it is imperative for Korea and Japan to sustain and upgrade bilateral cooperation, subsequently endeavoring to incorporate the United States into the trilateral cooperation framework through a sequential approach.

2. Regional Cooperation

It is anticipated that the Trump administration will assume a relatively passive role in the exercise of leadership with respect to Indo-Pacific regional cooperation, a policy area that was actively promoted by the Biden administration. It seems probable that the Trump administration will withdraw from the IPEF. Nevertheless, given that the first Trump administration established the Indo-Pacific Strategy, the second Trump administration may revive some elements of the IPEF by rebranding them. The two countries demonstrated the close working relationship as Korea and Japan serve as chair of the Supply Chain Pillar and vice chair of the Crisis Response Network. Based on this, both countries could continue to exercise in rule making in the region.

3. China Strategy

In the context of the Trump 2.0 era, Korea and Japan could consider ways to harmonize their China strategies. The second Trump administration will pursue a more robust containment strategy of China. In the realm of trade, the second Trump administration is anticipated to pursue a comprehensive strategy to contain China, encompassing measures such as tariff wars, the strategic decoupling of supply chains, the tightening of export controls on high technology, and the elimination of national security threats. The second Trump administration will adopt a different approach from that of the Biden administration and the first Trump administration in this regard. In contrast with the approach taken by the Biden administration, which sought to enhance international collaboration in order to contain China, the second Trump administration will pursue a strategy that will focus on burden sharing with allies and partners and pressure on Korea and Japan to align their strategies with the United States. It is advisable for Korea and Japan to initiate discussions on defining the scope of a China strategy in parallel with their cooperation with the U.S. This will require the establishment of enhanced trilateral communication channels. ■

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