Modern Economic Security: Definition and Arguments

"Economic security" has emerged as a key aspect of national strategy to ensure the safety of citizens and preserve the value of the nation. But the complete domestication of strategically important industries is not realistic. Being accepted as an essential part of global supply chains on the technical side is important.

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Economic security is a concept that continues to be a pivotal part of modern economic and industrial policies. It is even reflected in the government's "Growth Strategy" and "Basic Policy on Economic and Fiscal Management and Structural Reform 2021 (the 2021 Basic Policy)," in response to the proposal "Towards 'Formulating Economic Security Strategy" prepared by the Liberal Democratic Party (LDP)'s Strategic Headquarters on the Creation of a New International Order and unveiled in December 2020. In each of these documents, economic security is defined in terms of meaning and image, but that image is not always uniform. Moreover, despite recognition of the importance of economic security, there still hasn't been enough in-depth debate over it. In this article, I hope to summarize the concepts of economic security in modern times, and provide a roadmap that will help direct traffic for future debate.

Looking at the definition of economic security

Let's start by taking a look at the definitions and images of economic security presented in the LDP Proposal and the government's Growth Strategy and 2021 Basic Policy. In the LDP Proposal, economic security is framed as "something that secures the national interest from an economic perspective," and is defined as "ensuring the independence, survival and prosperity of Japan in economic terms. The LDP Proposal recognizes the importance of establishing "strategic autonomy" and "strategic indispensability" as the means to achieving this.

Next, the Growth Strategy focuses on "policies that keep important production infrastructure at home" from an economic security perspective, and examines various ways to achieve this, such as "ensuring technological superiority," "mitigating threats and improving autonomy with regard to critical infrastructure and supply chains," and "mechanisms to secure funding in the medium-to-long term." Specifically, the main goals are to diversify production sites of items such as semiconductors, data centers, batteries and rare-earth elements, and attract them to Japan.

Meanwhile the 2021 Basic Policy describes the direction of economic security as "expanding and deepening cooperation with like-minded countries while ensuring Japan's autonomy and gaining a competitive advantage under an international order based on basic values and rules." This is

envisaged as "identifying key technologies, enhancing efforts to preserve and develop them, and developing the resilience of core industries."

What these definitions all appear to have in common is the idea that economic security, and the independence and prosperity of the country, hinges upon mitigating supply chain risks through the strengthening of core industries. However, the problem is that there are no indications of how far supply chain risks should be mitigated, to what degree industrial infrastructure should be made resilient, and how much should be spent on these measures. In other words, by this definition, the government could continue to provide unlimited subsidies to strengthen domestic production sites or continue to provide unlimited national support of research and development costs to secure the nation's technological advantage, all in the name of "economic security." In the Growth Strategy and 2021 Basic Policy, specific strategic industry sectors and items are specified, but questions remain as to why they were chosen and whether other sectors are not considered important.

Meanwhile the LDP Proposal, which defines economic strategy in comparatively greater detail, discusses strategic autonomy and strategic indispensability as the criteria for establishing economic security. Strategy autonomy is described as "achieving Japan's security purposes of maintaining people's lives and economic operation without overly relying on other countries under any circumstances by strengthening the infrastructure that is essential for maintaining the Japanese people's lives along with social and economic activity." Strategic indispensability is defined as "strategically expanding Japan's presence in fields considered essential to international society within the industrial structure of international society overall, in order to secure Japan's long-term and sustainable prosperity and national security."

However, this definition does not incorporate concepts related to "preserving technology" through the Foreign Exchange and Foreign Trade Act, which are part of the Growth Strategy and 2021 Basic Policy, and this point also reveals a discrepancy in the definitions. In government documents, practices to control the outflow to other countries of technologies Japan already possesses is included as part of economic security. Those practices include reviewing import and export control, reviews of inward direct investment, strengthening the control of technical information at the border, clarifying the targets of deemed export control, ensuring the soundness and fairness of research, and the issue of secret patents.

It appears that these different definitions depend on whether one sees economic security as focusing on "threats emerging from external economic relationships that affect Japan's economic and social activity," or as focusing on "threats to international peace and stability by enhancing the technological and economic capabilities, including military security." Either case is an economic security issue in the sense of mitigating threats to Japan through economic means, but the fundamental thinking behind the two approaches does differ. That is why in this article I will treat economic security as "using economic means to protect the lives and assets of citizens, as well as to preserve the value of the nation," and as the means to achieving this, I will consider three separate forms of economic security: supply chain security, security through the non-proliferation of technology, and security from regulations by other countries.

Supply chain security

In the wake of the Second World War, engaging in free trade was the foundation of the world order. Globalization, which began picking up speed from the 1980s in particular, has revitalized not only the movements of goods but also of capital, resulting in a shift of production facilities from countries with high production costs to cheaper ones, advancing the "hollowing out of industry" in developed countries, and increasing income at many levels in developing countries. As the GATT was dissolved and absorbed into a newly established WTO in 1995 both to link these production sites spread around the globe and promote greater free trade, the networks of global supply chains expanded further as bilateral and multilateral free trade agreements and economic partnership agreements were signed.

Then in 2001 China joined the WTO, was fully integrated into modern-day production systems, and began to play a central role in the international economy both as the "World's Factory" and as a huge market in its own right. Both to Japanese and world manufacturers, China came to represent a production base, a parts supplier, and a consumption region for finished products.

While this was going on, China started to use its economic clout to exert pressure in order to meet its own political goals. There were inklings of this in 2010 when the captain of a fishing boat was arrested after colliding with a Japan Coast Guard (JCG) ship off the Senkaku Islands. China prohibited the export of rare-earth elements to Japan and pressed for the captain's release. In a more recent example, China banned the import of agricultural products and minerals such as iron ore from Australia, which had been insisting on a WHO investigation into the origins of COVID-19. In this way, China has used the size of the Chinese market as leverage to achieve its political or strategic goals through "Economic Statecraft," as it describes its economic actions.

As the countries dependent on China face increased national strategic vulnerability when China employs these tactics, they try to reduce their reliance on China. The Trump administration imposed import tariffs on steel and aluminum for security reasons based on Section 232 of the Trade Expansion Act of 1962, and also increased tariffs on a wide range of items from primary products to industrial goods in what was dubbed the "China-United States trade war." While these were efforts to reduce the reliance on China by increasing the costs of including China in supply chains, the US did not decrease is trade deficit with China and it became clear that a "full decoupling" from the Chinese economy was impossible.

The Biden administration has also continued to recognize the reliance on China as a security risk, but has opted for "partial decoupling" that places a focus on the security of supply chains related to strategically important items instead of a "full decoupling." In a February 2021 executive order, President Biden ordered that a review of supply chains in four areas—semiconductor manufacturing, rare earth elements, high capacity batteries and pharmaceuticals—be reported on within 100 days. In June, the Biden administration took a string of measures including providing subsidies to boost supply chains and coordination on semiconductors agreed to at a US-South Korea Summit Meeting. Only time will tell how much of an effect these measures will have, but they do reveal the current direction of supply chain security in seeking a "partial decoupling" to reduce vulnerabilities among strategically important items.

Considering risks, costs and benefits

There is one question that cannot be avoided when discussing the economic security of supply chains: the criteria for determining what should be done and to what extent, in order to strengthen industrial infrastructure and stop the proliferation of technology in the interests of security.

We tend to see arguments in favor of making all strategic industries into domestic production and achieving as close as possible to a 100% self-sufficiency rate, but that is not realistic. For example, when COVID-19 infections started to spread around March 2020, the supply of masks stagnated and a "mask battle" broke out, not only in Japan but worldwide. At the time, calls recommending the domestic production of masks as "strategic goods" intensified. However, masks are a mass-produced good with low added-value, and are not well suited to being produced in Japan, with its high production costs. As masks go for high prices during an emergency shortage, domestic production would be profitable even with high production costs, but as we have seen, with the subsequent introduction of cloth masks and stabilization in the global mask supply, today masks are sold at prices between one and several yen each. This would mean that products produced in countries with cheaper production costs would have an advantage in the market over those produced in Japan, and Japanese manufacturing would quickly come to a standstill.

In cases such as this, even if items identified by the government as strategic goods suffer inferior price competitiveness in normal times, the industry should be maintained as a strategic industry out of the national budget, and subsidies should be paid to make up for the difference in domestic and foreign prices. Otherwise, the government will need to prepare large stockpiles in anticipation of an emergency (for example the Oil Stockpiling Act requires the stockpiling of items such as crude oil that cannot be produced domestically), or would need to implement measures encouraging businesses to maintain multiple production sites in Japan in order to diversify supply sources. In either case, we need to consider how much it costs out of the national budget just to support these low added-value "strategic goods," and whether there are benefits equal to that outlay of costs.

In this way, economic security in supply chains does not mean producing everything domestically; the situation must be one in which domestic production is encouraged for a good where dependence on foreign countries constitutes a security risk, or one in which the benefits to be gained from domestic production outweigh the costs of maintaining the strategic industry for such goods. Allow me to use the issue of vaccine development in the United States to illustrate this situation.

Based on its experience of terrorism by anthrax in the immediate wake of the September 11 terrorist attacks in 2001, the United States incorporated biotechnology research and development into its security strategy based on the need to prepare for terrorist attacks using biological weapons. The Biomedical Advanced Research and Development Authority (BARDA) was established, and has continued to pursue fundamental research into vaccine development. This was one factor behind the incredible speed at which the development of a COVID-19 vaccine proceeded. That was due to the determination that the security benefits of preparing for emerging infectious diseases that could appear at any time or terrorist attacks using biological weapons were deemed to outweigh the costs

of establishing BARDA and continuing with research and development. It is also because the US assessed the security risks from biological weapon-based terrorism to be high, a recognition that changed the cost-benefit equation.

Security through the non-proliferation of technology

National security through the non-proliferation of technology is an area where economic security is discussed in a different way to supply chain security. While this is already implemented based on the Foreign Exchange and Foreign Trade Act as a traditional security export control framework, in recent years it has become an important issue, not only with regard to weapons of mass destruction and advanced conventional weapons, but also in terms of controlling emerging technologies that could be repurposed for military applications in the future. In particular, China's strengths in unmanned weapon-related technologies and AI-related fields mean that restrictions on exports to China should be imposed, and in 2018 the US adopted the Export Control Reform Act (ECRA), clarifying that emerging technologies would also be subject to export controls in addition to the existing export-controlled items.

Security through the non-proliferation of technology is not a matter of simply controlling the export of technologies. In 2016 China acquired German robotics maker Kuka, in a clear attempt to strengthen China's traditional weakness in robotics technologies through corporate acquisition.

Until then, the US had been controlling technology transfer through foreign capital-backed corporate acquisitions by way of the Committee on Foreign Investment in the United States (CFIUS), but in 2018, the US newly established the Foreign Investment Risk Review Modernization Act (FIRRMA) to further beef up that system and make preparations to deal with technology transfer. In recent years, however, there has been an exponential rise in the number of projects CFIUS has had to handle in response to aggressive investment offensives backed by Chinese capital, particularly targeting start-up companies with advanced technologies, with some saying the committee is overwhelmed.

An even bigger problem is technology leakage through movements of people. Even before, technology leakage through people movements, such as people being re-hired by foreign firms after resigning or engineers familiar with sensitive technologies being headhunted, had been a problem, and there are growing concerns over China's "Thousand Talents Plan" to siphon off researchers or the dispatching of large numbers of Chinese foreign students to the US and elsewhere to master sensitive technologies. Pushing back against the "Thousand Talents Plan" runs up against freedom of occupational choice issues, making it difficult to prevent the movement of individuals. Moreover, in many cases Chinese foreign students are essential to the running of a university and researching funding from China plays an important role, making it hard to exert control even when security risks exist under current circumstances. In the US, Confucius Institutes for learning the Chinese language are handled and managed similar to foreign government organizations, and to ensure "research integrity" rules have been created and implemented to prevent researchers receiving domestic research funds if they have received funding from foreign organizations.

This kind of security through technology non-proliferation, while still being economic security in the sense of protecting the lives and assets of the people through economic means, differs significantly from the nature of supply chain security, which is one of the causes of confusion over the concept when the two approaches are lumped together when discussing economic security. However, the issue of technology non-proliferation is extremely important to the security of Japan amid rising military tensions between the US and China, and thorough control of military and commercial dual-use technologies will likely continue to be a crucial issue for Japan's security.

Security from regulation by other countries

While supply chain security and technology non-proliferation security seem to make intuitive sense as security issues, security from regulation by other countries, or more specifically from the US and China, is somewhat more difficult to grasp as security, despite being an important issue for many countries.

To date, the world has been based on free trade, and using unilateral sanctions and economic pressures, so-called economic statecraft, to change the behavior of other countries has been seen as a violation of free trade rules. But the WTO, whose job is to enforce free trade rules, became dysfunctional during the Trump era in the US, and opportunities to punish parties for not following the rules all but disappeared. There has also been a growing tendency for these economic pressures to be implemented in the name of security in a manner that abuses the "Security Exceptions" based on Article 21 of GATT.

In addition, economic sanctions on the basis of human rights are being actively utilized, as seen with the Global Magnitsky Act in the US. There was even an incident where cargo from a Japanese clothing manufacturer was seized based on an executive order issued in the Trump era that banned the import of cotton and tomatoes believed to have been produced through forced labor in China's Xinjiang Autonomous Region.

In response to these developments, China established a new Anti-Foreign Sanctions Law (AFSL), noting, "If any foreign country violates international law and the basic principles of international relations, contains or suppresses China based on various pretexts or its own laws, takes discriminatory restrictive measures against Chinese citizens or organizations, or interferes with China's internal affairs," China is entitled to take corresponding countermeasures. In other words, if Japan took measures to curb transactions with China in accordance with the US rules, China would in turn take countermeasures against Japan, placing Japan in a conflicting position between the two powers.

If both the US and China try to exert their influence through economic means to advance their values and achieve strategic benefits, the many countries deeply connected to the economies of both countries will be placed in a difficult situation. During the former US-Soviet Cold War era, this was solved by only falling in line with a single camp, such as the Coordinating Committee for Multilateral Export Controls (COCOM), but the economic relationships between the forces of East and West during that time were nothing compared to now. In the era of confrontation between the US and

China, the security challenge is figuring out how to survive in the midst of economic conflict between the two.

Strategic indispensability is Japan's path forward

Given this situation, how should Japan forge a path forward? The key lies in the concept of "strategic indispensability" found in the LDP Proposal. Even if China wanted to impose sanctions on Japan, it would be difficult in practice if China had a high level of reliance on Japan. Having a network of global supply chains under a state of mutual economic dependency would not only put Japan in a position of reliance on China, but also work in reverse. To leverage that situation, Japan needs to possess technologies and products that other countries lack, properly manage them so that they do not simply flow out of Japan, and have Japan command a presence that other countries always regard as essential. Creating this kind of situation represents a deterrence in economic security, and thoroughly ensuring the non-proliferation of technology is an important means to utilizing that deterrence.

Economic security is not about ignoring the costs and restoring strategically important industries domestically in order to secure supply chains. By becoming an essential part of global supply chains and thoroughly ensuring the non-proliferation of technology so that other countries will continue to rely on Japan, we can achieve economic security.

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