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## A Net Assessment of East Asia

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By [George Friedman](#)

When I began this series a month ago, I pointed out that the most significant feature of the global system currently is the ongoing destabilization of the Eurasian land mass, from the Atlantic to the Pacific, from the Arctic to the Arabian Sea. One important aspect of this is that the destabilization isn't, at this point, a single systemic crisis, but a series of relatively self-contained disorders. Thus the European, Russian and Middle Eastern

systems have different dynamics, and while they touch on each other, they have not yet reached the point of having merged into a single crisis.

It is in this context that I turn to the question of East Asia. Asia is so vast and diverse and geographically fragmented that it is impossible to speak of Asia as a whole. East Asia is that part of Asia east of the Central Asian deserts that extend deep into China, and north of the Himalayas and hilly jungles east of the Himalayas. It consists of two main parts: One is the mainland, the region between the southern barriers and Siberia, which is Han China and its subordinate states, Tibet, Xinjiang, Inner Mongolia and Manchuria. The other is the East Asian archipelago, a string of islands and peninsulas stretching from the Aleutians to the Malay Peninsula-Java interface. Of particular importance to an East Asian net assessment are Taiwan, the Philippines and Japan. One additional feature is noteworthy: the Korean Peninsula, wedged between China and the archipelago. In the simplest terms, at this moment, the critical question is the dynamic in the northeast, involving China, Japan, the Koreans and, of course, the global power, the United States.

East Asia shares one major feature with the rest of Eurasia. It was part of World War II, which both transformed the region and defined it. In East Asia, World War II involved two issues: The first was Japan's ability to access raw materials and manpower from the Asian mainland and the rest of the archipelago. The second was the military balance between the two major Pacific powers, Japan and

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the United States. The two issues became intertwined.

## Economic Development in Japan and Korea

Japan is an island group [almost completely bereft of raw materials](#). When European and American imperialism goaded it into becoming an industrial power, Japan immediately developed dependence on sources of raw materials (and on manpower to support its industrial expansion without immigration). Japan's enormous success at industrializing in the early 20th century made Tokyo insecure about access to these resources and therefore aggressive in trying to secure them. The United States, historically concerned about maritime defense of its coasts, saw Japan's increasing power and insecurity as a threat to U.S. control of the Pacific, which Washington saw as essential to protection of the West Coast.

The United States sought to limit Japan's control and even access to necessary resources in order to control its behavior. The Japanese saw this as an American plan to permanently subordinate Japan to the United States. When the Germans overran France and the Netherlands, the status of Indochina and today's Indonesia became murky, and Japan's ability to secure the resources it historically obtained from these places was uncertain. Japan moved to secure these areas, but doing so required securing the Philippines lest the sea-lanes from the south remain insecure. The Philippines was an American protectorate, so securing it meant war with the United States. This dynamic led to Pearl Harbor, which ultimately [led to the catastrophic defeat of Japan](#).

Two dimensions of this defeat were interesting: The first was that the Japanese industrial plant, and therefore the Japanese economy, was wrecked. The second was that in spite of defeat and disaster, Japanese society maintained its cohesion. In addition, the Americans needed Japan to revive its industry and use its social cohesion and human capital to produce equipment that the United States needed for the Korean War. The destruction of Japan's industrial base, the maintenance of social cohesion, and the American need for Japanese production created a dynamic that has been crucial in shaping East Asia since 1945.

Historically, global capitalism has relied on certain regions providing inexpensive manufacturing. This produced low-wage, high-growth countries like the United States at the end of the 19th century. World War II reset the Japanese and German economies so that they could become low-wage, high-growth engines that were particularly efficient because of the social discipline in these countries.

Japan's postwar recovery depended on the country playing this role, which it did for four decades. Such economies can both build an economic infrastructure and foster rising standards of living. However, a focus on growth rather than on rates of return on capital inevitably undermines profitability. In the end, growth can be maintained only by repressing wages or, when that is no longer viable, by slashing profit margins in order to compete with other low-wage countries. In due course, the country reaches a climax that results in a financial crisis, built around the fact that profitability has been sacrificed for growth. In Japan, this climax occurred between 1989 and 1991, between the last surge of Japanese exports, a crisis with the United States over Japanese export policy, and a banking crisis.

In the wake of its financial crisis, Japan became a much lower-growth country, less dependent on exports and more on domestic consumption. Moreover, to maintain social stability, Japan focused on maintaining full employment, not only by sacrificing profits but also by increasing debt. But another way to put this is that Japan managed the transition from a low-wage, high-growth country to a more stable economic platform without social unrest. Given their imperative, the Japanese did well.

South Korea also went through this process, reaching its climax in the 1997 East Asian financial crisis. Unlike Japan, it did experience social unrest, and unlike Japan it never managed a dramatic reduction of dependence on exports. It has straddled contradictions, but it has managed to maintain a relatively coherent social-economic policy that is still heavily export-oriented but less dependent on low wages.

## China Enters the Next Economic Phase

China is the third wave of this process in East Asia. During World War II, China was both a victim and a battleground. In large part this was because of China's fragmentation before the war. This

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fragmentation was caused by China's forced integration into the international economic system. The vast majority of China's population lives in the interior, where transport is difficult. Western interaction with the Chinese economy tended to focus on relations with coastal Chinese. This created a fundamental schism. The coastal cities were oriented toward the Western powers. Their economic interests aligned more with the Europeans' and the Americans' than with those of the Chinese central government. Thus, when the communists tried to spark an uprising in Shanghai in the 1920s, Mao Zedong failed and took the "Long March" into the interior, where he raised a peasant army. The split between coast and interior was institutionalized, and splits between coastal interests emerged as well. The result was a highly fragmented society at first exploited by Japanese interests, then caught between Japan and the United States.

After the war, Mao defeated the pro-Western factions, closed off China to most international trade, and sought to create national unity by excluding foreign influences. The result was internal repression. China did not come close to fulfilling its potential. When Mao died, the Chinese had to choose between this situation and reopening to the global economy. It chose the latter and assumed its place as the low-wage, high-growth country of its generation. And like Japan before it, when China's customers stopped buying after 2008, Beijing's attempts at maintaining social stability through employment at the cost of profitability led to inflation. This inflation was not massive, but as competition in the class of products China excelled in intensified, and as new players with much lower wage rates entered the game, even limited levels of wage inflation caused China to lose market share. In fact, even Chinese companies began to seek out labor in lower-wage countries. China experienced both the loss of global competitiveness based on low wages and a complex financial problem that was more endemic than a crisis. China is now shifting to [a post-low wage, post-high growth economy to a more sustainable one](#).

It should be remembered that the culmination phase in Japan and South Korea was characterized by massive capital flight, which the West saw as evidence of the Asian countries' economic power rather than as a vote of no confidence in their own economies. Recall the Japanese purchase of American real estate in the late 1980s or Korean purchases of business in the 1990s. These were not particularly successful, nor were they meant to be. They were designed to reduce the Japanese and Koreans' exposure at home. The same can be said with China's current propensity for foreign investment. It is driven, at least in part, by a lack of confidence among those within China who really understand the country's situation. Much of it is state capital flowing out. Some is state capital flowing outward and becoming private capital. Other funds are private capital. The types and patterns vary, but the flow has continued.

## Managing Economic Change

A major difference between China and Japan is social cohesiveness. The economic dysfunction was managed socially in Japan. Given that the majority of the Chinese public participated in this process only marginally, the inability to sustain this model has caused significant fragmentation, as before. The first priority for the Chinese is retaining the power of the Communist Party and the central government in Beijing. Thus, the Chinese are engaging in political repression and purges in order to maintain the political system while the country transitions to a new economic system.

It is important to note the sequential enthusiasm Westerners have had to Japan's and China's economic development. Both were seen not as they were — simply a phase of the Asian countries' history — but as a permanent process that would cause each country to rapidly surpass the rest of the world. Westerners did not recognize that this process had inherent limits that would assert themselves in due course. Therefore, the lingering perception in the West about East Asia — or, in its current phase, of China — is that it is likely to become a singularly powerful international player.

The Chinese have severe limits on their ability to engage in international adventure. The People's Liberation Army is physically blocked from large-scale military operations by terrain. The Chinese navy is similarly limited, blocked as it is in the South China Sea and the East China Sea by the East Asian archipelago. It can exert pressure within these confined spaces until and unless the United States intervenes. Even with its anti-ship missiles, which can be destroyed by air campaigns, China cannot yet risk facing the U.S. Navy. It therefore probes below the threshold of triggering action.

The same can be said about North Korea, a fascinating case of a country whose significance is far less





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than the impression of importance it has created. Its ultimate goal is regime preservation. The position of "not quite ready to use nuclear weapons" aids in this. Passing the threshold to being ready or to actually use them would defeat the North Koreans' primary goal. Nothing would assure regime destruction more certainly than excessive aggression. Its actions have to be carefully calibrated and have been for well over a decade.

What all of this shows is that East Asia is transitioning from a period in which it — or each of its major components in sequence — played a critical role in the global system. Each has now climaxed, and both Japan and China are now playing a much more normal role in the system. This is the result of success and not failure, but it is also the result of the fact that while their previous economic models could exist for decades, [at a certain point a shift is necessary](#).

As they shift, they experience different internal patterns. The Japanese have accepted low and no growth in return for social cohesion. The South Koreans went through spasmodic unrest followed by a shift not in export dependence but in the type of product exported and its position on the value chain. The Chinese are focused on [maintaining centrifugal forces](#).

On the whole, it can be argued that this region is inherently stable. This is true of Japan and, depending on North Korea, true of the South. But China has not yet demonstrated that it can make the transition without internal fragmentation or intense repression. History would seem to argue that either is more likely than a return to the past decades. Mao was minimally aggressive after the lessons of the Korean War, where Chinese losses were extensive, so a strategy of regime preservation would tend to turn China inward. If China fragments and the coastal region draws in foreign powers to protect mutual interests, as happened in the 19th century, that would be another story. But this is not the 19th century, and such action from the coastal region is not highly probable.

## The U.S. Role

In spite of the U.S. rhetoric about a pivot to Asia, East Asia is not the United States' top priority in Asia. Washington's main concerns remain the Middle East and the borderland between Russia and the European Peninsula. Unless East Asia undergoes a fundamental redefinition, the United States has few interests that involve military intervention. South Korea's concern is preventing the collapse of the North Korean regime, but the price West Germany paid to integrate East Germany is not something the South is eager to bear. And China, for all its posturing, is more than content to [not have to face the United States at sea](#).

The country that appears most content is Japan, but it is the wild card. South Korea's power is limited on a broader scale. China can sustain itself, on some level at least, even cut off from the world. Japan is the world's third-largest economy, yet it is the most vulnerable industrial power in the world. It has few industrial resources, and if it loses access to international sources — if only because of chaos among the sources — its industrial ability would wither with extraordinary speed. That the third-largest economy in the world depends completely on imports of raw materials and is incapable of securing those materials by itself is the underlying tension within the region and the global system.

The United States guarantees Japan access to its raw materials. But Tokyo sees the American concern in Russia and the Middle East as potentially dangerous to Japan's ability to access what it needs. A war that closes the Strait of Hormuz would cut Japan off from its supply of oil. Washington, from the Japanese point of view, is prepared to take risks that are minor to the United States but potentially disastrous to Japan. Tokyo's fear is that the United States will act not against Japan, but against a country on the road to a country Japan needs, heedless of the consequences to Japan.

The Japanese are quite aware of the problem, as well as that there is no way to limit this risk apart from staying close to the United States. Tokyo is also aware that the more problems the United States has with China, the more thoughtful Washington will be with Japan. But the United States has a queue of problems, and China, rhetoric aside, is not one of them. Whether it gets there will have less to do with what Beijing intends than with Beijing losing power over parts of China. That would draw the United States in and give Japan the leverage it needs.

But that is, as I have argued, a possibility for the future. The [internal evolution of China](#) is, in fact, the

key to the region. China has moved from limited liberality to increasingly intense authoritarianism. The evolution of this government is at the heart of the East Asian dynamic. North Korean nukes, Chinese aggressiveness at sea and American threats are all secondary.

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