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Research Report

The EU-Japan EPA: Freer, fairer and more open trading system: Conference note

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No. 10/2018

Conference note

The EU-Japan EPA

Freer, Fairer and more Open Trading System

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EXECUTIVE SUMMARY

In the context of the EU-Japan Economic Partnership Agreement soon to be concluded by both parties, ECIPE organized a high-level conference to discuss the economic benefits and social dimensions

of this agreement. It is an important agreement for both sides, but also comes at a time when the principles and practice of the open and rules-based trading system are stressed. The conference reflected stakeholders'

positions on what new trade opportunities will this agreement bring and how can it be used as a platform for improving social conditions and the climate of trade policy in the world.

THE CONTEXT OF THE AGREEMENT

On 8th November 2018, the INTA Committee of the European Parliament voted on its draft recommendation to approve the EU-Japan Economic Partnership Agreement (EPA). It will be followed by a vote in plenary scheduled for December, and pending parliamentary ratification, the agreement would enter into force in 2019.

The agreement plays a pivotal role for global economic governance as well as Europe's economy. Japan and Europe lead the multilateral and rule-based order by example: for free and fair trade, and through international cooperation.

The Report of the European Parliament by MEP Pedro Silva Pereira notes: *“The Union and Japan share fundamental values such as respect for human rights, democracy and the rule of law, and a strong commitment to sustainable development and a rules-based WTO system.”*¹

The report also deems the EPA has *“a strategic dimension and is the most important bilateral trade agreement ever concluded by the Union.”* The background report by the European Parliament's Research Service calls the EPA of primary importance to tackle to *“play a leadership role in shaping the future of international trade.”*

At the conclusion of the agreement at the EU-Japan Summit, Prime Minister Shinzo Abe of Japan also demonstrated the intention to tackle protectionism: *“Amid widening protectionist movements worldwide, the signing of this EPA will vividly demonstrate to the international community the firm political will of Japan and the EU to lead the world keeping the flag of free trade waving high”*.²

The EPA covers one-third of global GDP and would be the biggest bilateral trade partnership ever concluded by the EU. The economic gains are expected to be significant as Japan and Europe are complementary: The agreement creates a Euro-Pacific marketplace without tariffs and common technical standards in key sectors, e.g. motor vehicles, life science, food products, clothing, and ICT.³ The EPA also facilitates trade in services and encourage increased activities across a number of services sectors that accounts for 90% of Europe's job creation, while issues relating to investment protection will be dealt with in a separate investment treaty.

ECONOMIC BENEFITS OF THE EU-JAPAN EPA

The EU-Japan EPA holds a high level of ambition in terms of trade liberalisation. At the entry in force of this agreement, 90% of the tariffs on EU exports to Japan are removed. After all the staging phases, 97% of tariffs will be eliminated.⁴ As Trade Commissioner Malmström stated: *“The economic benefits of this agreement are clear. By removing billions of euros of duties, simplifying customs procedures and tackling behind-the-border barriers to trade, it will offer opportunities for companies on both sides to boost their exports and expand their business”*.⁵

¹ P. Silva Pereira, Draft Report containing a motion for a non-legislative resolution on the draft Council decision on the conclusion of the Agreement between the European Union and Japan for an Economic Partnership, 2018/0091(NLE)

² Prime Minister S. Abe, Opening Statement Joint Press Conference Following the Signing of the Japan-European Union Economic Partnership Agreement and Japan-European Union Strategic Partnership Agreement, July 2018, available at https://japan.kantei.go.jp/98_abe/statement/201807/_00003.html

³ H. Lee-Makiyama, At the Nexus of Trade and Investment: The EU-Japan Economic Partnership Agreement, LSE, July 2018, available at <http://www.lse.ac.uk/business-and-consultancy/consulting/assets/documents/at-the-nexus-of-trade-and-investment-white-paper.pdf>

⁴ K. Binder, EU-Japan trade Agreement: a driver for closer cooperation beyond trade, European Parliamentary Research Service, July 2018, available at [http://www.europarl.europa.eu/RegData/etudes/BRIE/2018/625118/EPRS_BRI\(2018\)625118_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/BRIE/2018/625118/EPRS_BRI(2018)625118_EN.pdf)

⁵ European Commission, EU-Japan Summit : a landmark for trade and cooperation, Press Release, July 2018, available at http://europa.eu/rapid/press-release_IP-18-4504_en.htm

The European Commission's analysis and independent scholars agree on the significance of the economic impact of the agreement:

- According to the European Commission, the reduction of tariffs and non-tariff measures foreseen in the agreement (when compared to the situation with no agreement) are expected to add 33 billion euro to the EU GDP when the agreement is fully implemented. This corresponds to around 0.14% of additional GDP with an increase of about 13 billion euro of EU exports to Japan.⁶
- In addition, recent *ex post* assessment of EU agreements in the Far-East show that the EU exports increased by 55% and with significant boost of employment as well.
- Also, estimates by Felbermayr, Kimura, Okubo, Steininger (2018) identify welfare gains of 0.1% of GDP for the EU and 0.3% for Japan with no significant negative impact on third countries.
- However, econometrical models rarely capture all the dynamic effects of trade liberalisation. In the upper end amongst the estimates, Francois (2012) predicts the EPA will increase EU GDP by 0.76% in the case of a comprehensive liberalisation between EU and Japan, while studies by Kawasaki (2017) estimates that Japan real GDP would increase by 0.99% where a quarter of the increase is generated by tariff reduction and three-quarters by non-tariff measures while Brexit reduces the gains by 0.05%.

Moreover, European investments in Japan have also a rate of return that is considerably higher than other EU external investments (average 3.9%) and nearly twice the rate of intra-EU investments.⁷ The agreement will further improve the margins for EU businesses on a highly lucrative market.

But more exports, rate of return and economic output are not the only deliverables of a trade agreement. Factors like legal certainty and non-discrimination often have a bigger impact on the general business environment than nuisance tariffs. Independent surveys show the standards on rule of law is considerably higher in Japan compared to other Asian countries or high-income economies.⁸

Also, the ratification of the EPA sends a clear message promoting free trade and a rule-based international system. On both sides, they pleaded against the protectionist measures taken by the US and therefore, welcomed their intention to further economic cooperation. President Juncker stated at the conclusion of the EPA: *"It is about values, principles and finding win-win solutions for all. As far as we are concerned, there is no protection in protectionism – and there cannot be unity where there is unilateralism."*

⁶ European Commission, DG TRADE, The Economic Impact of the EU-Japan Economic Partnership Agreement (EPA), , June 2018, available at http://trade.ec.europa.eu/doclib/docs/2018/july/tradoc_157115.pdf

⁷ Eurostat, 2017

⁸ World Justice Project, 2017

SOCIAL DIMENSIONS OF THE EU-JAPAN EPA

The agreement provides positive employment effects for both the EU and Japan. As a country with an outward strategy that is primarily investment-led rather than export-led, Japan is a long-term investor in the Single Market, Japan invested in local production sites. Japan's investment-driven strategy is clearly favourable for Europe: 625,000 people were employed by Japanese companies established in the EU,⁹ while subsidiaries and affiliates of EU businesses in Japan employ around 167,000 people.¹⁰

But trade agreements create more than new job opportunities. International trade provides normative influence, and recent FTAs by the EU and Japan contain sustainability chapters with labour provisions, reflecting the principles the signatories promote in a broader sense.

Japan's standards are reflected by its most recent FTA, the Comprehensive and Progressive Trans-Pacific Partnership (CPTPP). Its labour and environmental provisions are enforceable. A panel can be established with possible sanctions towards the CPTPP member in case of non-compliance on these provisions.¹¹

Meanwhile, the EU has to date taken a different route by exempting its trade and sustainable development (TSD) provisions from sanctions. The EU is still discussing the effectiveness of the sanction-based model of agreements, such as CPTPP and in 2017, the Commission released a non-paper evaluating the effect of the current TSD approach, discussing different alternatives.¹² While the EPA lack the sanction element in its enforcement of TSD chapters, this is not due to a negotiation issue with Japan but primarily an internal EU debate. European business confederations have argued that a sanction-based approach would be inefficient.¹³

As the most developed economy in East Asia, the labour standards in Japan are inarguably the highest in its region. Japan has ratified six of the ILO fundamental Conventions, which correspond to the core labour standards (Forced Labour, Freedom of Association, Right to Organise and Collective Bargaining, Equal Remuneration, Abolition of Forced Labour, Non-Discrimination, Minimum Age, and Worst Form of Child Labour). Japan is yet to ratify the convention on non-discrimination (Convention 111) and the abolition of forced labour (Convention 105),¹⁴ or at least while potentially conflicting domestic laws are still being amended.¹⁵ Japan has ratified more core conventions than Korea, with whom the EU conclude an FTA in 2011 and had not ratified the Convention on forced labour, minimum age, and worst forms of child labour.

The number of ILO core conventions signed is not the only policy indicator for labour standards. Reality on the ground can be very different – for instance, Cambodia, Indonesia, and the Philippines are three countries that ratified all ILO core conventions, where the conditions are inarguably not better than in Japan.

⁹ European Commission, DG TRADE, The Economic Impact of the EU-Japan Economic Partnership Agreement (EPA), June 2018, available at http://trade.ec.europa.eu/doclib/docs/2018/july/tradoc_157115.pdf

¹⁰ Id.

¹¹ Comprehensive and Progressive Agreement For Trans-Pacific Partnership, Chapter 28, available at <https://www.mfat.govt.nz/assets/CPTPP/Comprehensive-and-Progressive-Agreement-for-Trans-Pacific-Partnership-CPTPP-English.pdf>

¹² European Commission, Trade and Sustainable Development (TSD) chapters in EU Free Trade Agreements (FTAs), Non-paper of the Commission services, July 2017, available at http://trade.ec.europa.eu/doclib/docs/2017/july/tradoc_155686.pdf

¹³ BusinessEurope, Trade and Sustainable Development chapters in EU FTAs, 2017 available at https://www.besuisseurope.eu/sites/besuisseurope/files/media/position_papers/rex/2017-11-06_sustainability_and_ftas.pdf

¹⁴ European Commission, Trade Sustainability Impact Assessment of the Free Trade Agreement between the European Union and Japan, 2016, available at http://trade.ec.europa.eu/doclib/docs/2016/may/tradoc_154522.pdf

¹⁵ ILO, Country Baseline Under the ILO Declaration Annual Review, 2017 available at https://www.ilo.org/wcmsp5/groups/public/---ed_norm/---declaration/documents/publication/wcms_629641.pdf

Meanwhile, Japanese investments and commercial presence in the wider Asia-Pacific region (with the demands of conscious Japanese consumers and corporate social responsibility of Japanese investors) provide a pressure to improve labour and sustainability standards throughout the regional supply-chain.

The EU and Japan agree to set high labour standards, or as Commissioner Malmström expressed: *“Neither side wants to see those standards decrease because of trade. And they won’t. We both agree to implement fundamental international labour standards, and environmental treaties like the Paris climate change deal.”*¹⁶

CONCLUSIONS

Not ratifying the EPA has an unforeseeable economic cost for the EU. To walk away from a reciprocal and mutually beneficial agreement that opens markets, overcome regulatory divergences and boosts our economies and innovation is simply unthinkable.

However, not ratifying the agreement with a broad political support is enough to call Europe’s commitment to open trade and the rule-based system into question.

The social impact of the agreement is in the long-term positive, and not just for Japan and Europe – but also across the Asia, thanks to the economic influence that Japan exercises despite the emerging competition in the region.

¹⁶ C. Malmström, (2017), The Benefits of an EU-Japan Free Trade Agreement, Speech by EU Trade Commissioner C. Malmström, July 2017, available at http://trade.ec.europa.eu/doclib/docs/2017/july/tradoc_155745.pdf