



COMMENTARY

The EU and Japan: The Revival of a Partnership

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Less than two months before the fulfilment of Brexit and during a wave of global protectionism, one of the biggest trade deals in history, taking place between the European Union and Japan, will enter into practice. While contradicting Brexiters' claims that the EU was preventing their country from achieving advantageous trade agreements, the United Kingdom is left out of it, creating space for a rearrangement of world politics and future economic growth.

A Much Needed Sight of Partnership

From an economic perspective, free trade agreements have proved to be beneficial for participating countries, in overall terms. They boost growth, consequently resulting in the creation of new job opportunities, raise purchasing power and force industries to be more competitive and innovative. The EU-Japan Economic Partnership Agreement (EPA) will be no exception. However, its importance for the EU goes beyond its economic impact.

In a period stained by major international conflicts concerning views on protectionism and an ongoing and increasingly dangerous period of severe nationalism uproar in its domains, the EU is unambiguously re-affirming its pro-globalization stance, as it prepares to engage in a new era of economic and political relations with Japan. Starting on the first day of February of this year, almost five centuries after the Europeans first arrived in the Asian country, a new milestone trade deal enters into action.

More Exports Equal More Growth

EU Member States have high openness levels, with export to GDP ratios well above such as China, Japan and the United States¹. Most of the European international trade takes place within the single market, but with low growth rates.

Despite being the fourth-largest economy in the world, Japan represents only 3.2 per cent of EU's total exports², a percentage that shows a decreasing trend due to the fast growth rate of trade with emerging countries, revealing somewhat of a missed opportunity, having in mind the purchasing power of the Japanese.

During the last few years, the EU had been negotiating a trade agreement with Japan, which received its approval by the European Parliament last December. The deal will have significant

¹ https://data.worldbank.org/indicator/NE.EXP.GNFS.ZS?name_desc=false

² http://bruegel.org/wp-content/uploads/2018/10/EXPO_STU2018603880_EN.pdf

consequences for the Member States, not only through short-term and long-term economic impact, but also through the consolidation of open and global ideologies and the precedent it creates.

Its urgency seriously increased after Japan entered the Trans-Pacific Partnership and later its successor, following the withdrawal of the United States from the deal. Several countries participating in this agreement, such as Vietnam and Australia, are, for example, major competitors of the EU on agricultural goods and raw materials³, a large export of the EU to Japan, creating a relative disadvantage⁴.

This constitutes the biggest bilateral free trade treaty ever signed by the EU in terms of market size⁵, embracing one-third of the world's economy, and covering 635 million consumers, with both figures accounting for the initial presence of the UK.

With the agreement, there will be crucial decreases in the tariffs of key products, such as hard cheese and wine. Their abolishment will create opportunities for additional exports and the increase of competitiveness of European firms in the Japanese market.

However, tariffs are not always, particularly between developed economies, the major barriers to trade. Instead, regulatory obstacles have constituted a big drawback for EU companies, as some Japanese certification procedures can difficult the export of safe European products. But, in this field, a lot has been done. Numerous products will receive a special status and will obtain the same level of protection as they receive in Europe.

At last, it is important to mention the chapter regarding small and medium enterprises, which represent the vast majority of exporters to Japan, with a very high share in agriculture, textiles and leather. However, bureaucracy issues, lack of available information regarding local laws and linguistic communication have posed substantial barriers for them. According to the deal, a special platform will be created for these entities to facilitate their trade, ensuring information available in English and increasing transparency.

As reported by studies commanded by the European Commission, the deal will save European companies around 1 billion euros per year in customs duties and the value of EU's annual exports

³ https://webgate.ec.europa.eu/isdb_results/factsheets/country/overview_japan_en.pdf

⁴ http://bruegel.org/wp-content/uploads/2018/10/EXPO_STU2018603880_EN.pdf

⁵ Data regarding the EPA in this chapter of the paper, unless where noted, is taken from http://bruegel.org/wp-content/uploads/2018/10/EXPO_STU2018603880_EN.pdf

can rise by as much as 20 billion euros⁶. European's processed food exports to Japan is estimated to increase by 50 per cent and exports of textiles and dairy products could more than double. Concerning public budget balances, a positive impact will follow, due to the increase in revenues, while no negative effects are expected.

Quite ironically, nearly two months after this landmark of globalization enters into force, the UK will, after three long years, finally leave the EU. Brexit will undoubtedly constitute a critical moment for British and European relations with Japan. From the moment it leaves the EU onwards, even though they are remaining close allies, the UK will have distinct bilateral relations with Japan. Therefore, dynamics between the three parties will definitely change. But how substantial will Brexit's impact on Europe's relations with Japan be?

Brexit: How a Separation May Allow an Approximation

This Tuesday, the British parliament will decide if the Brexit deal obtained by prime-minister Theresa May with the EU is accepted or if the country will leave abruptly with no deal whatsoever⁷. The outcome of the voting, besides the widely-discussed implications it will have for both sides, will also influence their engagement with Japan.

Aside from being an important market for Japanese industries, the United Kingdom has played a pivotal role in Japan's business strategy in Europe, having long served as the doorway for Japanese products to reach mainland EU⁸. Due to the size of the European domestic market, it constitutes a key and profitable destination for Japanese exports. In fact, as recently remembered by Japanese prime minister Abe Shinzo⁹, having easier access to the EU was the main reason why numerous Japanese companies implemented production in Britain. Therefore, the loss of this privileged access to the Single European Market would imply major problems the said companies.

A no-deal Brexit would mean the transition period would not take place and that, after the 29th of March, the United Kingdom would be out of the Single Market, automatically returning to the framework of the World Trade Organization. That would impose immediate detrimental consequences for Japanese firms. Toyota, for instance, estimates a cost of up to 10 million pounds a day in lost production¹⁰.

⁶ http://europa.eu/rapid/press-release_IP-17-1902_en.htm

⁷ <https://www.cnbc.com/2019/01/11/brexit-vote-parliament-set-to-decide-outcome-of-mays-withdrawal-deal.html>

⁸ <https://www.bloomberg.com/news/articles/2018-10-03/japan-waves-goodbye-to-u-k-as-gateway-to-europe-post-brexit>

⁹ <https://www.gov.uk/government/speeches/pm-statement-at-press-conference-with-japanese-prime-minister-abe-5-may-2016>

¹⁰ <https://www.theguardian.com/politics/2018/dec/04/toyota-no-deal-brexit-warning-uk-factories-10m-a-day>

The above hypothesis, currently widely expected to happen, has agitated Japanese investors since the referendum. Numerous warnings have been made¹¹, both by companies and the government, that preserving the current business approach would be unsustainable and that investment and production in the United Kingdom would suffer a huge blow, with part of it being transferred to mainland Europe, most presumably Germany.

The no-deal line of action is deeply undesired by adepts of a close European cooperation due to the breach it would engender in relations between the UK and the EU. Nonetheless, that, together with a closer economic partnership due to the free trade agreement, would inevitably result in an approximation of Brussels and Tokyo.

In the unlikely scenario in which the deal is accepted, consequences will not be as dramatic as mentioned beforehand. The UK will seize the transition period, lasting until December of 2020, to engage in negotiations for a free trade agreement with the EU. This will give it the chance of trying to develop a framework that minimizes the impact of the separation from the EU on Japanese investors in hope of mitigating its consequences.

However, even if such deal is reached before the end of the transition period, which is everything but certain, Japanese companies will still incur costs arising from trade friction, as the single market conditions cannot be reproduced. Although prime-minister May has confessed her desire of obtaining a frictionless free trade agreement, the president of the European Council, Donald Tusk, has already stated that is simply impossible¹².

Therefore, Brexit, and mainly if it takes place with or without deal, could have shifting repercussions on international diplomacy. While the UK and Japan have experienced very close political ties, the relationship between Japan and mainland EU, even as allies, has been described as rather dispassionate. Nevertheless, the EPA, simultaneously with Brexit, is an auspicious opportunity for the EU to strengthen the indispensable partnership with the Asian giant and improving its presence in the Pacific.

¹¹ <https://www.independent.co.uk/news/uk/home-news/japan-hard-brexit-uk-trade-toyota-panasonic-muji-nissan-tokyo-gateway-to-europe-a8571916.html>

¹² <https://www.bloomberg.com/news/articles/2018-03-01/eu-s-tusk-warns-may-trade-after-brexit-will-come-with-friction>

An Important Solidification of Europe's Values

A nation's trade policy is a very effective and direct way to show its ideas and create certainty towards cooperation. It is undeniable that this agreement represents a critical point in the dynamics of international affairs.

For Brussels, the approval of the deal helps reinstating its trading reputation after there was backlash regarding trade talks with Canada and the United States. Furthermore, it will be the closest reference available for talks with the UK concerning trade¹³.

In a period of large uncertainty regarding trade relations between major international players and the rise of protectionism, the EPA leans against the wind. While China and the United States are engaged in a trade war, one of the most notable trade agreements ever negotiated, both by size and trade policy restructuring, enters into force. The European Union, together with Japan, is embracing globalization and international cooperation as an ultimate path to multilateral economic success.

In a midst of a dark period for international cooperation, with threats to global integration appearing from all fronts, a new opportunity has manifested itself for Europe. In a time where standing up for cooperation as the correct way to achieve political and economic success has become increasingly unpopular, the first day of February of 2019 will reveal itself as a development in the European Union's progressing battle against nationalism, protectionism and further elements threatening a more consolidated process of international integration.

¹³ <https://www.ft.com/content/b25a93ec-fd4e-11e8-ac00-57a2a826423e>

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