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## New EU-Japan trade agreement further shapes future international trade trends

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In December 2018, the European Parliament approved the EU-Japan Economic Partnership Agreement and the EU-Japan Strategic Partnership Agreement (EU-Japan EPA) by a vote of 25 to 10. The vote follows approval by the Japanese Diet a week earlier and marks the establishment of the world's largest bilateral trade agreement, encompassing more than 640 million people and close to a third of global gross domestic product. In contrast, the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) includes 11 countries but only 14 percent of global GDP.

The EU-Japan EPA is very forward-looking and includes some of the most comprehensive agreements on environmental protection, labor standards, resolving trade disputes, corporate responsibility and the promotion of environmentally friendly goods. The agreement also wipes away virtually all custom duties between the two parties, includes a clear commitment to fight climate change, and it adopts an adequacy decision under the EU General Data Protection Agreement (2018) that allows for the free movement of personal data. Both European and Japanese leaders have repeatedly characterized the agreement as an alternative to protectionist policies and trade wars.

"Almost five centuries after Europeans established the first trade ties with Japan, the entry into force of the EU-Japan Economic Partnership Agreement will bring our trade, political and strategic relationship to a whole new level," said European Commission President, Jean-Claude Juncker. "Together with close partners and friends like Japan we will continue to defend open, win-win and rules-based trade."

### The basics

The EU-Japan EPA has not received the same attention that other trade deals have—most notably, agreements signed between the United States, Canada and Mexico—but it is perhaps one of the most significant agreements of the 21st century. The agreement removes 99 percent of custom duties on Japanese imports by the European Union and 94 percent of duties on European imports by Japan, totaling more than EUR 1 billion annually. EU agricultural exports will receive unprecedented access to the Japanese market, while Japanese auto manufacturers will see the 10 percent tariff on their automobiles slashed to zero, providing access to the dynamic and lucrative European market. Current protectionist policies regarding rice, wheat, meat, sugar and milk products are still in place, but eventually, Japan will bring the amount of lifted tariffs on European goods to cover 99 percent of all traded goods, as well.

Regarding services and investment, the EU-Japan EPA adopts a "negative list" approach, which guarantees the liberalization of most sectors of the economy in principle, while allowing for a list of specific sectors that will remain protected. Visa restrictions and entry were liberalized for a variety of persons and, critically, both Japan and the EU agreed to open up government procurement. The agreement also provides certain products, such as Kobe beef and Scotch whiskey, with the "geographical indication" special status, which lets consumers know that they come from certain locations, allowing producers to charge a premium for quality.

Under the agreement, Japan's GDP is expected to increase by 1 percent (approximately JPY 5 trillion) and create

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close to 300,000 jobs. The EU expects increases of approximately EUR 8 billion in exports to Japan, including a 50 percent increase in processed foods, a 7 percent increase in chemicals, and a 220 percent increase in textiles, apparel and leather.

## Forging a system for the future

The EU-Japan EPA does not exist in a vacuum. Japan is the largest economy to participate in the CPTPP and is a driving force behind the Regional Comprehensive Economic Partnership (2018), which includes the ten ASEAN nations as well as Australia, China, India, Japan, New Zealand and South Korea. Additionally, the EU recently completed an agreement with Canada, the Comprehensive Economic and Trade Agreement (2018), which eliminated 98 percent of custom duties between the two parties.

These trade agreements give participating countries expanded access to each other's markets and supply chains, establish high standards for labor and environment issues, and most critically, provide platforms for dispute resolution that should prevent trade wars and help harmonize international trade rules.

One of the key elements of the EU-Japan EPA is how it dovetails with the CPTPP in terms of "country of origin" regulations and other supply chain matters. Under the EU-Japan EPA, components and parts sourced from CPTPP members are considered value added, and companies trading with the EU-Japan EPA and the CPTPP receive many reciprocal benefits. In practice, this opens the EU up to the 11 other members of the CPTPP, and vice versa.

The same synergy is possible with the Regional Comprehensive Economic Partnership, which is currently under negotiation. If and when it is finalized, this trade agreement has a considerably larger impact than the CPTPP. The deal covers 24 percent of global GDP and almost 50 percent of the world's population. Although the agreement reduces only 80 percent of custom duties (as of the current draft) due to the very high duties in place with current members, the reduction has a greater effect than either the CPTPP or the EU-Japan EPA. The Brookings Institution estimates the agreement would possibly increase global incomes by as much as USD 300 billion per year by 2030.

## Global response to unilateral action

All of these agreements stand to benefit the signatory members and increase the prevalence of harmonized standards for international trade that span the globe. This is a big deal for the global supply chain. Instead of scrambling to avoid duties and seeking alternatives to existing supply chains in the wake of trade wars and protectionist policies, the agreements between the EU and Asian nations provide safe havens and as much stability and predictability as can be hoped for in a dynamic global economy. The world is responding to trade tensions and emerging powerhouses with agreements that take into account the idea of "win-win" but also peer into a future in which data flows, global value chains, and the increase in environmental, social and governance risks call for concerted and imaginative thought and action.

## Takeaways

- The EU and Japan sign one of the largest bilateral trade agreements in history, encompassing more than a third of global gross domestic product.
- The EU-Japan Economic Partnership Agreement works together with the Comprehensive and Progressive Agreement for Trans-Pacific Partnership, creating a potential super-bloc of trading nations enjoying mutually beneficial policies, such as the complete reduction of tariffs and duties.

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