

June 20, 2017

Free Trade between Europe and Japan – hope for global prosperity

Hubertus Bardt

In an environment with growing protectionism and the danger of economic disintegration and shocks for the global trade policy system, a free trade agreement between Japan and Europe could set a positive example. Progress in the negotiations are necessary to foster growth and prosperity and to send a message to other countries, that modern market economies rely on good trade relations.

The economic concept of free world trade is as old as the classical economic theory. The division of labour as well as economic cooperation beyond national borders are crucial sources of economic prosperity. No country can produce its technologies more cheaply or more efficiently without buying components from companies around the world. Despite its positive economic effects, international competition is oftentimes not accepted. Over the last months and years, globalization criticism, protectionist threats and new trade restrictions have become very common. The new US administration is a fundamental challenge for the global trade system. But this challenge also bears opportunities to promote free trade.

Companies around the world have specific strengths, special knowledge and specialization advantages. Nobody creates his product all by himself – from raw material production to final consumer goods. Everyone is dependent on partners. The more complex the products are and the further the technical possibilities advance, the more important becomes the collaboration of companies. Cooperation enables companies to make use of specific knowledge and exploit cost advantages or economies of scale. Without the international division of labour, we would be dramatically poorer. Through the international division of labour, goods are created more efficiently and more innovation opportunities are seized.

Global trade is beneficial for large parts of the economy, not only for the biggest global players. The medium-sized companies in Germany would not be successful if they were bound to national markets. But they are successful in their niche as "hidden champions"

because they can deliver their products to global markets. In general, internationally active companies are typically more successful than those focussing on their home markets. And globalized economies can better secure prosperity. Without global market access, the backbone of the German economy would break. Those who believe that globalization is only something for big conglomerates, ignore the basis of their own prosperity.

But it is also true that not everyone benefits from international trade: international competition is inconvenient and jeopardizes existing market positions. Competition may endanger existing business models. Existing qualifications may no longer be sufficient to get a new employment opportunity at another company. But in a prosperous and globalized world, these people can be supported by globalization – through skills development and government assistance. In addition, international trade reduces prices for consumer goods, which benefits all citizens.

For several years now, free trade has not made huge progress. Significant global initiatives to reduce trade barriers and to open markets have gone missing in recent years. Multilateral negotiations on the Doha Round at the WTO level are stuck. Transatlantic and transpacific initiatives like TTIP, TTP and CETA have been highly controversial for months and years. US president Trump cancelled the TTP process, TTIP negotiations are on hold, probably forever. The member states of the European Union still need to ratify CETA, which is not sure that it will happen. In Germany in particular, globalization critics have dominated the public debate and prevented the opening up of markets. While there seems to be hardly any progress in terms of trade liberalisation, we observe growing trade barriers even among the G20 countries. The WTO regularly reports that new protectionist measures have been erected. Protectionism is rising, not shrinking. Additionally, Brexit and the election of Donald Trump are clear signals of economic disintegration.

The new US administration appears to be highly critical towards free trade, even though open markets are beneficial for all partners. The administration seems to intend to employ trade deals which make the USA benefit disproportionately. However, free trade is not about winning or losing in a deal, it is about win-win exchanges and economic growth. With the United States pulling out of central structures of international cooperation, opposing free trade and threatening to introduce new measures of protectionism, the whole global trade system is at stake.

Against this backdrop, a success of a Free Trade Agreement between Europe and Japan has become more important. The successful negotiations between Japan and the European Union are one of the most prominent examples that bilateral trade agreements are still possible in a climate of mutual respect and goodwill. Both economies account for about a

third of the global gross domestic product. Two of the most developed industry-based economies are about to deepen trade relations and to remove existing barriers. While every agreement has pros and cons for the involved economic actors, the required political agreements will eventually be made. The imminent shift in US trade policy has reinforced the determination of the EU and Japan to conclude a mutually welfare-increasing trade deal.

Agreeing on a trade deal is not an easy thing to do. The EU started to negotiate with India in 2007 and the process stopped without a final result in 2013. The ongoing negotiations between Japan and Europe are not easy either. Access to railway markets, taxation of cars, mechanisms against new trade barriers and other topics are discussed. Becoming more international and more integrated into world markets is beneficial for Europe, but will be beneficial for Japan as well. The Japanese economy has a huge growth potential through increased internationalisation. A joint effort of the two strongest and democratic market economies – Japan and Europe – would help to stabilize global trade and to increase economic prosperity.

Yet, bilateral trade liberalisation can only be a substitute for first-best global initiatives at the WTO level like the recent Trade Facilitation Agreement, which can raise global trade by up to US-\$1 trillion per year. Additionally, more multilateral trade agreements are needed which focus more on non-tariff trade and investment barriers or modern investor-state dispute settlement mechanisms.

The crisis of globalization bears new opportunities. Shaken by the politics of the US administration, support for open markets has grown in other countries. The critique of globalization has become remarkably quiet. Suddenly it has become clear what is at stake. Political decision-makers are increasingly active in promoting open markets. The upcoming G20 summit in Hamburg should send a strong message towards free trade among the industrialized and emerging countries.

However, the new opportunity for globalization can only be seized if we learn from the past. It is not enough to refer to the overall economic benefits of globalization. We also have to name and address the problems of greater international competition. Educational services and other support for those who are among the potential losers of structural change must be part of the national policies. The “forgotten” regions in the US show what happens if negative regional effects of increased competition and global change are not properly addressed.

Globalisation and free trade are economically beneficial, but they are also based on liberal values of the free exchange of goods, services, and ideas. Therefore, discussing the

normative conditions of trade with the international partners should also be part of future trade negotiations in order to find appropriate agreements. A good framework for international competition as well as a sound economic policy which helps to attract investors, to develop innovations and to use entrepreneurial initiatives are the best ways to let society benefit from international trade and cooperation. Japan and Europe should be a good example now.

Dr. Hubertus Bardt is the Managing Director of Cologne Institute for Economic Research. He is also a visiting lecturer at the Bonn-Rhine-Sieg University of Applied Sciences and Heinrich-Heine-University Düsseldorf.

Dr. Bardt received his doctorate in economics from the Philipps University Marburg. He has published numerous papers on energy, climate and resources policies and presented research findings on various international conferences.

Keizai Koho Center (Japan Institute for Social and Economic Affairs, KKC) has served as a bridge for the Japanese business community to interact with its key stakeholders inside and outside Japan. With a wide range of its domestic and international programs, KKC has developed a worldwide network encompassing businesses leaders, lawmakers, government officials, journalists, university scholars, and school teachers.

The **KKC INTERNATIONAL PLATFORM** is a forum to discuss new developments, changes, and challenges of Japan and the international society.

The views expressed in the essays on the **KKC INTERNATIONAL PLATFORM** are solely those of the authors.

Keizai Koho Center

<http://www.kkc.or.jp/english/>

Keidanren Kaikan, 1-3-2 Otemachi, Chiyoda-ku, Tokyo 100-0004 JAPAN

e-mail: platform@kkc.or.jp
