"EU-Japan Economic Relations: Present and Future"

Summary of the Japan–Europe Conference
held in Paris on July 12, 2013

40 participants attended the Japan–Europe conference co-hosted by Japan Economic Foundation and Institut Aspen France, which was organized in Paris on July 12, 2013, at the Paris Chamber of Commerce and Industry, with the support of the Comité d'échanges franco-japonais.

At the top of the agenda lay discussions on the various strategies hammered out in Japan and in Europe to restore confidence and foster economic growth.

The political response to the economic crisis appears to diverge to a large extent in Japan and in Europe. In the European Union, the responsibility for tackling sluggish growth rests first and foremost in the hands of national governments who must embrace structural reforms and show determination to regain control over public finances. In the European policy mix, the European Central Bank (ECB) played a central role in consistently easing refinancing conditions since the aftermath of the collapse of Lehman Brothers. This contributed to restore calm on financial markets thereby providing Eurozone member states with extra time for undertaking reforms. After stating to do "whatever it takes", the latest of the unconventional moves by the ECB has been to give forward guidance on the evolution of interest rates. While the European reaction to the crisis focused primarily on fiscal consolidation and a somewhat accommodating monetary policy, the Japanese government under Prime Minister Shinzo Abe crafted a much bolder unconventional policy mix labelled as "Abenomics".

Abenomics managed to secure first quick wins. The three arrows of Abenomics aim at exiting the deflation trap to jump towards a "normal" economic equilibrium. The first arrow of this three-pronged policy mix consists in a renewed monetary policy based on inflation targeting (2%) backed by drastic quantitative and qualitative easing (QQE). Secondly, the Japanese fiscal policy aims at a short-run stimulus followed by medium-run consolidation. The third arrow deals with structural reforms designed to restore the competitiveness of Japanese industry. The main components of this growth strategy rely on deregulating and strengthening the industry base (attraction of foreign capital and skilled workers…), reforming the labour market (mobility, women's work, child care centres, and foreign languages) and facilitating new industries (medical industry, tourism, infrastructure…). The launch of Abenomics was followed by a significant increase in stock market prices (50%) and its economic impact should be further bolstered by a JPY depreciation which has reached 25% to date. However, the most difficult parts of this economic strategy (fiscal consolidation and structural reforms) remain to be implemented as doubts are already emerging.

Doubts and scepticisms over the efficiency of Abenomics have already surfaced. As far as QQE is concerned, some might regard the swift JPY devaluation as the start of currency wars. On the other hand, the Japanese government argues that the Bank of Japan (BoJ) policy is not different than the sharp increase of central bank balance sheets in the United States, in Europe, and in England. In addition, JPY depreciation may also be interpreted as a correction of over evaluation. Likewise, the fiscal arrow is not uncontroversial, as the short run stimulus could appear merely as a quick fix to boost the growth rate to win the upper house election in July, while it may hasten an eventual fiscal burst given the situation of the Japanese public finances. Therefore, medium-term consolidation is deeply needed and the rise in the consumption tax rate could contribute to curbing public deficit. Eventually, while a consensus on structural reforms priorities may be taken for granted, the real challenge is now to implement them. In this respect, successes in free trade agreements will be a test for the Japanese government, as well as for the European Union which launched a new generation of trade talks.

New trade negotiations burgeoned around the world. As chances of multilateral trade liberalisation fade out in with the "comatose" Doha round, Japan and Europe revived FTAs and triggered new ones. The EU secured an FTA with Korea and started talks with Japan (JEU) and the United States (Transatlantic Trade and Investment Partnership – TTIP) in 2013. Japan concluded bilateral FTAs with twelve countries and one region (ASEAN) over the last six years and launched negotiations with five countries and four regions. This new wave of FTA negotiations has several motives: moving towards trade liberalisation at a faster pace than through the WTO, completing the dismantling of tariffs and tackling non-tariff barriers to trade, as well as providing momentum for domestic reforms agenda. As a result, this new generation of FTAs that are particularly ambitious and comprehensive can be described as "mega-FTAs".

In the aftermath of Doha's impasse, a new era of mega-FTAs is coming. The ascent of mega-FTAs is directly linked to the stalemate in the WTO and the slowness and narrowness of the Doha Round. Some regard the decision making system in multilateral talks as flawed as it based upon consensus and single undertaking. As a consequence, "mammoth" economies accounting for a large share of the global wealth such as the EU27 (27% of the world GDP), the USA (24%), China (10%) and Japan (9%) embarked on mega-FTA negotiations such as JEU, TTIP, TPP, RCEP and CJK. Other industrial, emerging and developing G20 members are also involved in comprehensive FTA talks, such as India (RCEP), Indonesia (RCEP), Australia (RCEP/TTP) and Mexico (TPP). However, there is likelihood that these mega-trade negotiations may put the global trade governance at risk.

Huge economic opportunities for trade liberalisation, mega-FTAs may also jeopardise global trade rules. Whilst major world economies negotiate bilaterally with each other at the same time, diverging agreements are likely to emerge, hence resulting in a fragmentation of trade rules. This has been sometimes called the "spaghetti bowl" scenario. In order to avoid harming world trade rules harmonisation, negotiators should stick to a clear vision on the future of the global trade system based on the importance of the WTO framework and the avoidance of "hegemonic" trade games. Moreover, collaboration towards a global solution is central through FTAs that are as inclusive as possible. Issue-based rulemaking should also be targeted in order to use issue-based plurilateral agreements to complement the WTO. The integration of China in the global trade regime is also a major challenge.

China's growing assertiveness in Asia and in the world needs to be coped with. China's rapid rise has been recently hampered by economic changes such as the deceleration of growth and a cost overhang. Internal challenges are also surfacing: China's ageing population and environmental issues question the sustainability of China's growth model. In order to encourage China to become a stakeholder in the global system, there is a necessity for collaboration among major players such as the EU, Japan, and the US. Possible collaborations in trade areas include enforcing WTO compatibility, securing an investment regime as well as intellectual property. In this respect, RCEP and CJK FTA are paving the way for the integration of China as a real stakeholder in the global trade system. However, tensions with neighboring countries are still present, continuing to impede flourishing trade talks. The latest major feud occurred with Japan over the Senkaku Islands (Sept. 2012) but similar issues may arise as China further strives to become an oceanic power safeguarding what it considers as its maritime rights and interests.

Soaring unconventional oil and gas production in the US is likely to have economic and geopolitical consequences. The so-called "Shale Gas Revolution" witnessed in North America means that the US is poised to become the largest oil producer in mid-2020s and a net oil exporter in 2030. The major shift has global implications – most notably on American industries which will be granted a decisive competitive edge thanks to lower energy costs. Heavy industries in Europe and Japan will have to find new ways to survive to this massive global reshuffling in production costs. Another predictable consequence of the rapid, steady rise of unconventional oil and gas in the American energy mix is the subsequent decrease in the US's dependency on Middle Eastern oil. Hence, America's pivot toward the Pacific Ocean will be reinforced by the US dwindling geo-economic interest in the Middle East. Other advanced and emerging countries appear to possess technically recoverable shale gas resources. However, the global shale gas production depends on social acceptability in these countries. In Europe, for example, environmental concerns regarding fracking still remain a major impediment to shale gas exploration.

With economic and environmental concerns in mind, energy policies need to be redefined in Europe and Japan. In Japan, the main challenge will be to overcome energy constraints with cost reduction. This applies to energy production, through power and fuel supply diversification, as well as to energy distribution, through a full market liberalisation that will impact the electricity market and a strict tariff assessment. In both Europe and Japan, another frontier is to promote energy efficiency in industries and for households in order to reduce the energy bill. These energy challenges are likely to create new business and market opportunities. They are also a thriving field for Euro-Japanese cooperation.

Ageing societies is another field of common concern, challenge, and opportunities for Japan and Europe. Ageing is a matter of concern for advanced economies, first and foremost Japan, where the downward demographic trend results in a negative contribution to the breakdown of growth factors. Off-balance sheet public debt relates mostly to pensions, hence the need to increase the number of contributors and decrease the number of recipients, by fine-tuning the set of actuarial incentives and penalties, whatever the vested interests - especially by raising the retirement age. Labour force participation for the population aged between 55 and 64 is much higher in Japan than in France. In both countries however, the issue of social cohesion is at stake, outlining the need for income transfers between generations.

Mature markets can provide economic opportunities. Clients pay a growing attention to the service offered, which should be personalized. Customer expectations go further than mere consumption: it is about living an experience, for instance by travelling off the tourist track. Moreover, customers' greater sense of responsibility and awareness of environmental and health issues refine their wishes, which now typically include sustainable development. Lastly, ageing-related industries, like care and pharmaceuticals, are a field of business opportunities. The aim is to turn this silver market into gold.

Innovation and education are key growth drivers in mature economies. Technology can provide a decisive contribution to total factor productivity, including in the services and retail industry with an appropriate use of information technology (IT). Among the right segments for Japan and Europe to pick, stand life sciences, innovative medicine, IT, nanotechnologies, sustainable products, environment and energy efficiency as well as the monitoring thereof, and infrastructure. The underlying innovation can be scientific and technological, but also service-oriented. To create the conditions for such innovation to happen, governments should focus on stimulating investment and promoting a fertile business environment. In addition, education and life-long learning should remain a top priority in Europe and Japan to continue to invest in the future and expand human capital.