

A hard Brexit is the last thing Japan wants

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Japan is probably the only non-EU country to have taken a clear stance on Brexit and its consequences for future political, economic and commercial relations with the UK. While the country is close to finalising a Free Trade Agreement (FTA) and Economic Partnership Agreement (EPA) with the EU, the negative vote on the referendum has stirred up debate in Tokyo and prompted changes in the government's views on Europe. The UK reacted by proposing a bilateral FTA, but this of course would be pre-conditioned on the resolution of numerous questions about its future relationship with the EU and the transitional arrangements, amongst others, for the ongoing FTA discussions.

The EU and Japan have a well-developed relationship, dating back to 1984, when both blocs had their first ministerial meeting, leading to the Joint EU-Japan Declaration, issued in The Hague in 1991. Imports and exports of goods between both blocs are quasi-balanced, with about ¾ of Japanese trade being IT, machinery and transport equipment, whereas the EU exports more chemicals, fashion brands and foodstuffs. Over the period 2010-15, the value of EU services supplied to Japan has increased by 46%, allowing the EU to further consolidate its positive balance of payments in this sector. But Japan has a huge investment surplus in the EU. In 2014, Japanese investments in the EU accounted for €166 billion, compared to the €73 billion invested by the EU in Japan. Accordingly, the Japanese net investment position vis-à-vis the EU registered in 2014 a surplus of about €93 billion.¹

In 2013 the EU and Japan decided to launch negotiations for an EPA/FTA, which is close to completion. Some 17 rounds of negotiations have been held, with agreement reached on both sides on the key issues. The EPA/FTA should further open the Japanese market for EU foodstuff, and ease the access for Japanese cars to the EU. Further export gains are expected for both parties in sectors such as chemicals, manufacturing, machinery, transport equipment and business services.

Seen from Europe, Japan was the emerging superpower until 1990, but it disappeared from the international radar screen following its stock market crash and the ensuing problems in its financial system, which took years to overcome. After an extended succession of several governments and prime ministers, it is only with Prime Minister Abe that central bank and fiscal policies started to be aligned, and the situation began to show gradual improvement. The Japanese economy is now

¹ Data from Eurostat and UNCTAD, stock measures.

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expected to grow by around 1% in 2017, which should be its best performance in many years. But the country is not yet back on the agenda in Europe, which is probably why there has been almost no talk about the upcoming EU-Japan FTA, even if others trade deals are attracting so much controversy.

Given this recent experience, the fierce reaction of the Japanese government and the business community to the Brexit vote was surprising. In early September, the public and private sectors jointly published Japan's "Message to the United Kingdom and the European Union", making the country the first to issue a formal reaction to Brexit, spelling out its implications for bilateral relations with Japan. The message is clear: keep us informed and keep the process well managed, which remains a key concern until today. The document notes that "uncertainty is a major concern for an economy" and expresses the hope that "predictability is secured whereby all stakeholders, not just the negotiating parties, have a clear idea of the post-BREXIT landscape".

The Japanese fully endorse the EU in all its achievements: "The presence of a strong and united Europe is essential." The country supports the EU's achievements in promoting in security and economic stability in third countries. The EU has provided a single market with harmonised rules and common external tariffs, which has facilitated operations also for third countries. This open stance has allowed many Japanese firms to concentrate their operations in the UK, as a gateway to Europe, and this was also the way the UK promoted its location. At present, there are more than 1,000 Japanese companies in the UK, which employ about 140,000 people, while about 50% of the total FDI from Japan intended for the EU flowed through the UK from where it was subsequently oriented to other EU countries.²

Against this background, Brexit changes the operating landscape for Japan considerably and creates huge uncertainty. The Message document calls upon the UK to ensure continuity, which it probably cannot provide. Japan wants the UK to maintain its access to the EU single market, to continue to take part in the single passport system, to have no tariffs for intra-EU exports and to apply the same rules as apply in the EU. Japan also wants to maintain access to the UK market for qualified workers from other EU member states.

In short, Japan does not want a hard Brexit at all, but rather wants the UK to minimise any harmful effects from Brexit on (Japanese) business.

The effect of the joint Message has not been without result. So far, Japanese enterprises have been the most outspoken in publicising their plans in response to the UK's withdrawal from the EU. Some banks have openly announced plans to relocate their headquarters, whereas a car manufacturer has requested firm concessions from the UK government in exchange for its decision to staying.

In managing the post-Brexit context, the EU authorities and the UK government will need to be acutely aware of the strategic role that Japan plays on the international scene, especially in maintaining stability in East Asia, an issue that is well managed by Prime Minister Abe and the current government, in difficult circumstances and also with difficult neighbours, such as with China, both Koreas, Russia and the Philippines. The abrasive President Duterte of the Philippines was in Tokyo in early November, there is a Russia-Japan meeting in early December (where the two countries hope to come closer to finally signing a peace treaty) and the trilateral meetings with China and South Korea continue to take place on an annual basis. Prime Minister Abe was also the first foreign leader to meet US President-elect Trump. Japan may seem far away in the day-to-day policy debates, but it is an important anchor in the East. Brexit should not distract the EU from its global responsibilities, however difficult this also may be.

² Data from bilateral FDI statistics published by UNCTAD.