The European Union – Japan FTA Negotiations. Access Barriers for European Business to the Japanese Market.

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ABSTRACT

In 2013 the European Union and Japan launched negotiations on a new trade and economic agreement, of which the strategic aim is to create a free trade area between the parties (EU-Japan FTA). The new comprehensive agreement should include a broad spectrum of economic issues not only traditionally relating to tariffs, trade in goods and services, but also more broadly to non-tariff barriers and trade procedures, FDI, IPR, competition policy, public procurement, etc. For the EU the negotiations and agreement are an opportunity to improve openness of the Japanese market for European exporters and investors and to abandon many non-tariff barriers that have a burdensome effects on trade and investments. The general objective of the paper is to identify main barriers/challenges for European enterprises in access to the Japanese market for European goods, services and investments. The conducted analysis brings the following general conclusion: the existing barriers are mostly non-tariff barriers (there are relatively low tariffs for goods imported to Japan from the EU), which are both the biggest challenge for EU negotiators in improving access to the Japanese market and one of the main stumbling blocks slowing down the progress of the whole EU-Japan FTA negotiations.

Keywords: European Union, Japan, FTA negotiations, non-tariff barriers

INTRODUCTION

In 2013 the European Union and Japan launched negotiations on a new trade and economic agreement, of which the strategic aim is to create a free trade area between the parties (EU-Japan FTA). The new agreement which is being negotiated (there have been fifteen negotiating rounds as of 1st April 2016) should include a broad spectrum of economic issues not only traditionally relating to tariffs, trade in goods and services, but also more broadly to non-tariff barriers and trade procedures, foreign direct investments, legal protection of intellectual property, competition policy, public procurement, etc. In this sense the EU-Japan FTA should be a comprehensive agreement enhancing EU-Japan trade and economic co-operation.

The negotiations fit also in a general global process of increasing importance of preferential bilateral and regional agreements within the framework of the international trade system, which has been observed globally from the 1990s. Although the agreement is being negotiated in the shadow of two other important agreements i.e. Trans-Pacific Partnership (TTP) and Transatlantic Trade and

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Investment Partnership (TTIP), the EU-Japan FTA may be classified as a mega-regional trade agreement due to the economic, trade and investment potential of both partners and their position in global value chains. Additionally, the accepted agenda for negotiations foreshadows a deep economic integration once the agreement is achieved, including regulatory compatibility and rules aimed at limitation of differences in investment and business climates, which is characteristic for mega-regional agreements [WEF 2014]. The potential agreement will encompass countries responsible for ca. ⅓ of the global GDP. They are also global scale traders – together they are responsible for ca. 20% of the global trade (excluding EU-intra trade) and are the source of ⅓ of global foreign direct investments [UNCTAD 2015, WTO 2015a]. This makes that EU-Japan FTA will not only affect the parties involved in the negotiations process, but also will influence the global trade and investment architecture.

The economic potential of the European Union and Japan is not reflected in current bilateral trade and investments links between the partners. Trade and investment volume is below the potential and therefore the agreement, which is being negotiated, should create a new comprehensive framework for economic bilateral cooperation and became a long-awaited incentive for revitalizing the EU-Japan relationship. From the EU's perspective Japan remains a relatively closed country in economic terms, thus the agreement will be an opportunity to improve openness of the Japanese market for European exporters and investors and to abandon many non-tariff barriers that have burdensome effects on trade and investments.

The general objective of the paper is to identify main barriers/challenges for European enterprises in access to the Japanese market for European goods, services and investments. Although author is aware of the fact that there are still many barriers on both sides of the relationship, the paper concentrates intentionally only on the barriers faced by EU business in Japan.

The first part of the paper presents a short summary of the EU-Japan relations from a historical perspective. Then some general picture of the EU-Japan economic relations is presented with a focus on trade and investment links, including the most recent statistics within this area. The third part refers directly to the mentioned aim and identifies main barriers/challenges for European enterprises in access to the Japanese market in chosen sectors of trade in goods (food and agricultural products, pharmaceuticals and cosmetics, automobiles and automotive components) and trade in services (financial and insurance sectors, transport services). The chosen sectors are of a great importance for EU exports to Japan and represent a wide spectrum of relevant barriers existing for foreign suppliers. Some general barriers have been also identified for EU companies in allocating foreign direct investments and utilizing the potential of the public procurement market in Japan.

The methodology used for identifying the mentioned barriers/challenges includes: statistical analysis of historical trade and investment co-operation (from Eurostat, JETRO, JMF, OECD, WTO and UNCTAD), the analysis of legal acts regulating trade co-operation between the EU and Japan, including official documents corresponding to the ongoing negotiation process, the analysis of official reports

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presenting surveys on European companies operating in Japan on main barriers faced in export and investments as well as sector reports prepared by EU-Japan business and trade organizations. The identification of main barriers for the European enterprises in access to the Japanese market as well as classification of potential trade and investment expansion sectors have enabled to formulate main challenges for European enterprises that should be addressed by European negotiators during the EU-Japan FTA negotiations.

1. ECC/EU-JAPAN RELATIONS – A HISTORICAL PERSPECTIVE

Officially EEC/EU-Japan relations began in 1959 with the accreditation of Japanese ambassador to Belgium as well as – as a first representative in history - to three European Communities, which was the aftermath of the visit of the Prime Minister of Japan in European capitals, including Brussels [Frattolillo 2013]. However, it took 15 years to establish the delegation of the European Communities in Tokyo (1974), which proves that the relations between the parties in the first years were generally relatively weak. At that time bilateral relations were influenced strongly by trade and economic issues.

In the 1960s and 1970s Euro-Japanese interactions were dominated by economic frictions. Growing Japanese export expansion in sectors and industries considered by Europeans as important in terms of employment and income/growth potential as well as chronic trade deficit for the EEC influenced strongly the agenda of bilateral cooperation [Waldenberg 2013]. Starting from the early 1970s EEC countries experienced also the first boom in foreign direct investments by Japanese companies which was accompanied by hostility towards Japanese trade practices [Yoshida, Leitão & Faustino 2008]. Moreover, it was even more difficult to develop bilateral relations beyond the economic nexus, as both partners were affected by the negative impact of the oil shock.

Although the main axis of bilateral EEC-Japan relations in the 1970s and 1980s were efforts to correct the trade imbalance (a.o. Japan agreed to various voluntary export restrictions), new initiatives in co-operation started to grow. In 1979 the European Commission launched the Executive Training Programme to increase knowledge about Japan, its language, culture and business environment among European businessmen and through this to increase the effectiveness of European industries in their efforts to penetrate into the Japanese market. Additionally, in 1987 the EC-Japan Centre for Industrial Cooperation was opened in Tokyo to stimulate broaden industrial cooperation and support diffuse trade tensions [Schweisgut 2014].

Although the 1980s brought some increasing political activity in bilateral relations (in 1984 the EEC and Japan held the first ministerial meeting), more noticeable turn came with the beginning of the 1990s. The beginning of the decade brought a new geopolitical situation at the European continent, including a.o. the fall of communist system in Central and Eastern Europe and the unification of Germany. Moreover,

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the European Community was heading towards deeper economic and political integration; the Community started to implement two important projects aimed at deeper integration between EC member states, namely a common market and economic and monetary union.

The beginning of the 1990s witnessed also new initiatives in building closer EC/EU relations with Japan, including more political aspects. In 1991 during the first EC-Japan summit held in the Hague, the parties adopted "*The Joint Declaration on Relations between the European Community and its Member States and Japan*", creating an institutional framework for more intensified dialogue and stronger partnership. The new institutional framework included: annual consultations in Europe or in Japan between, on the one hand, the President of the European Council and the President of the Commission and, on the other, the Japanese Prime Minister (EU-Japan summits), an annual meeting at ministerial level as well as the continuation of six-monthly consultations between the Foreign Ministers of the Community and the Member of the Commission responsible for external relations (Troika) and the Japanese Foreign Minister [Declaration 1991].

The Hague Joint Declaration became an institutional landmark for more complex EU-Japan co-operation in new areas. As stated in the declaration: "*The European Community and its member States and Japan will firmly endeavour to inform and consult each other on major international issues, which are of common interest to both Parties, be they political, economic, scientific, cultural or other. They will strive, whenever appropriate, to co-ordinate their positions. They will strengthen their co-operation and exchange of information both between the two Parties and within international organizations*" [Declaration 1991]. Following the declaration the EU-Japan cooperation has expanded beyond original focus on economic issues and triggered a number of sectoral dialogues in a wide variety of policy areas, including a.o. peace and security, global and societal challenges [Frontini 2016]. Regarding trade and investment co-operation the 1990s were characterized by both the normalization of economic dialogues, but also by losing interest in bilateral trade and investment links mostly due to economic processes in the parties' neighborhood (e.g. growing economic co-operation in Asia-Pacific region, political and economic transformation in Central and Easter Europe). Also the announced declaration's objectives of closer political co-operation were far from ambitious implementation and an attempt to substantiate visionary political links largely failed [de Prado 2014].

In 2001 during the 10th EU-Japan summit in Brussels the parties decided to give a new incentive for bilateral activity. The representatives of the EU and Japan adopted "The Action Plan for the EU-Japan co-operation. Shaping our common future", including four major objectives i.e. promoting peace and security; strengthening the economic and trade partnership utilising the dynamism of globalisation for the benefit of all; coping with global and societal challenges; and bringing together people and cultures. The document presented an ambitious outline for closer co-operation between the partners, but many analysts pointed rather modest realization of the plan's goals in following years. Although the EU and Japan developed dialogues in many political, economic, social or environmental issues

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(according to the European Strategic Partnership Observatory maintained by the think-tank FRIDE, there were 34 EU-Japan Dialogues in 2013 [as cited in de Prado 2014]), many of them were not very active and substantial. However, the diagnosis does not reflect the development of EU-Japan dialogues on economic issues (trade, deregulation, industrial policy) and high-level forum on science and technology [de Prado 2014].

Again new ideas for enhancing bilateral EU-Japan co-operation appeared at the end of the decade. Policy-makers on both sides agreed that the agenda and listed issues to be addressed in bilateral cooperation included in the 2001 EU-Japan Action Plan were far too ambitious and contributed to poor implementation of the action plan into effect. As the aftermath in 2010 representatives of both sides agreed to set up the EU-Japan Joint High-Level Group (HLG), the task of which was to discuss and define new format of bilateral EU-Japan framework agreement [Berkofsky 2012].

In March 2011 the European Commission, following the meeting of HLG, published a document "*Options for the Future Framework of EU-Japan Relations*", in which it presented the Commission's ideas on the shape of institutionalized EU-Japan relations and cooperation in future. Following the Commission's proposal, during the 20th EU-Japan summit held in Brussels, the parties agreed to start the process of parallel negotiations on "*(1) a deep and comprehensive Free Trade Agreement (FTA)/Economic Partnership Agreement (EPA), addressing all issues of shared interest to both sides including tariffs, non-tariff measures, services, investment, Intellectual Property Rights, competition and public procurement; (2) and a binding agreement, covering political, global and other sectoral cooperation in a comprehensive manner, and underpinned by their shared commitment to fundamental values and principles*" [Council 2011]. To this end both parties agreed to conduct a joint definition of the scope and level of ambition and the European Commission declared to seek the necessary authorization from the Council to start the negotiations with Japan [Ibidem]. Formally the bilateral negotiations for a Strategic Partnership Agreement and a Free Trade Agreement were launched two years later – during the 21st EU-Japan summit in March 2013.

2. JAPAN AS AN TRADE AND ECONOMIC PARTNER OF THE EUROPEAN UNION

2.1 Trade in goods

Japan's position as one of important trade partners of the European Union is linked to trade and investment potential of its economy. In 2015 Japan was ranked as the 7th biggest trade partner of the European Union with a share in EU total trade volume of 3.3% (respectively 3.5% and 3.2% of total import and export). The importance of the EU among main Japanese trade partners is asymmetrically higher. The European Union corresponds to the 2nd import partner of Japan and the 3rd biggest export market for Japanese goods (table 1).

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The total value of merchandise EU-Japan trade in 2015 amounted to 116.27 billion EUR, of which 59.7 billion EUR was EU import from Japan and 56.5 billion EUR was the European export to the Japanese market. Those numbers reflect quite disappointing performance in bilateral merchandise trade, especially when compared to economic potential of the parties among major advanced economies and major global traders and investors. The total trade volume in 2015 was only 84.4% of the bilateral trade volume recorded in 2000. This is mostly the aftermath of decreasing European import from Japan which fell in 2000-2015 by more than ⅓ from 92.2 billion EUR in 2000 to mentioned 59.7 billion EUR. At the same time European export to Japan was stable (until 2010) and started to increase moderately in recent years. In 2015 it was only ¼ higher than in 2000 (extra-EU export at the same time more than doubled). These trends have resulted in more balanced trade for the EU countries. In 2015 trade deficit for the EU amounted to only 3.2 billion EUR, compared to 46.7 billion EUR in 2000 (graph 1).

Table 1. Main trade partners of the EU and Japan (% of total trade)

European Union (2015)				Japan (2015)			
Import		Export		Import		Export	
China	20.3	USA	20.7	China	24.8	USA	20.1
USA	14.3	China	9.5	**EU-28**	**11.0**	China	17.5
Russia	7.9	Switzerland	8.4	USA	10.3	**EU-28**	**10.6**
Switzerland	5.9	Turkey	4.4	Australia	5.4	South Korea	7.0
Norway	4.3	Russia	4.1	South Korea	4.1	Taiwan	5.9
Turkey	3.6	**Japan**	**3.2**	Saudi Arabia	3.9	Hong Kong	5.6
Japan	**3.5**	Norway	2.7	Taiwan	3.6	Thailand	4.5
South Korea	2.5	UAE	2.7	UAE	3.6	Singapore	3.2
India	2.3	South Korea	2.7	Malaysia	3.3	Australia	2.1
Brazil	1.8	Saudi Arabia	2.2	Thailand	3.2	Vietnam	2.0

Source: own calculations on [EC 2016a; JMF 2016]

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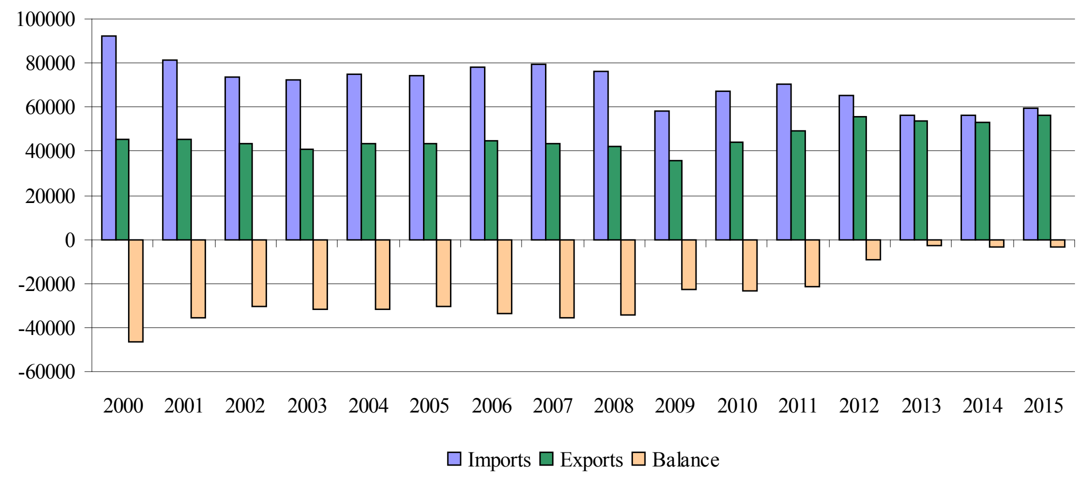
Graph 1. European Union merchandise trade with Japan in 2000-2015 (million EUR)



Source: own calculations on [Eurostat/Comext Database 2016]

The decline in bilateral trade is even more noticeable in relative terms. Starting from the 1960s/70s the share and therefore importance of Japan as a trade partner of the European Economic Community was increasing, which was the embodiment of growing global orientation of both Japanese and European economies. After two decades of spectacular growth of bilateral trade (largely in Japan's favor due to the export-oriented policy of the country which resulted in chronic deficit for the EEC) Japan became in the late 1980s and 1990s the most important trade partner of the EEC countries in Asia, and the second most important one globally after the United States. In 1988 Japan was the Community's second-biggest supplier, accounting for 11% of its imports, and its fifth-largest customer, taking 5% of its total export [MEMO 20/90]. The same applies to Japan for which the EEC countries were among leading trade partners. Referring to the same year 1988, the EEC share in total Japanese export and import amounted to 17.7% and 12.8% respectively, which gave the mentioned European countries the second position among most important trade partners (after the US) [JMF 2016].

Starting from the first half of the 1990s, when Japan was the most important Asian trade partner for EC countries, the share of the country in both total EC import and export has declined substantially. The structural changes in global trade and economy (a.o. shift in EC Asian import from Japan to China and South-East Asian countries) as well as economic situation in both partners (a.o. modest economic growth and consumer demand) have determined that today's EU-Japanese merchandised trade lost its historical dynamic and significance. Japanese share in total EU external import and export is currently only one-third and a half respectively of the values recorded two decades ago (graph 2).

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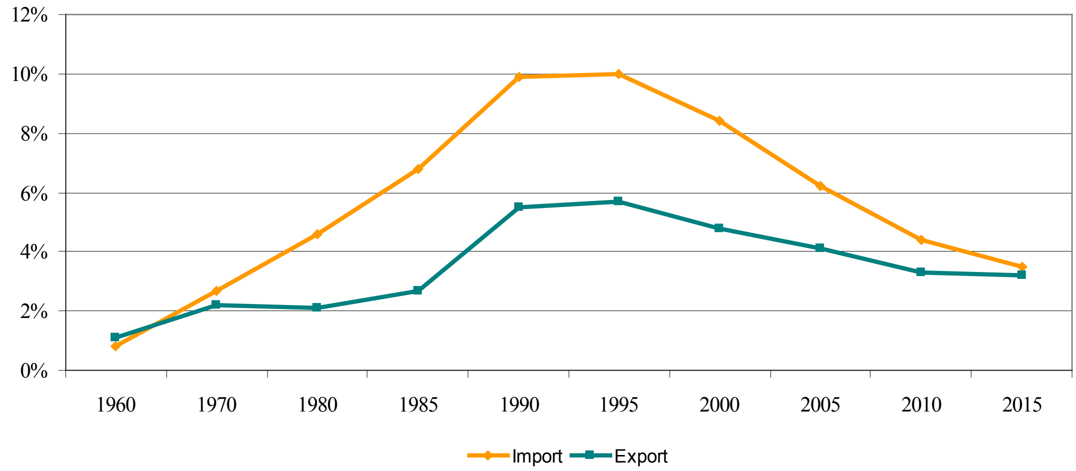
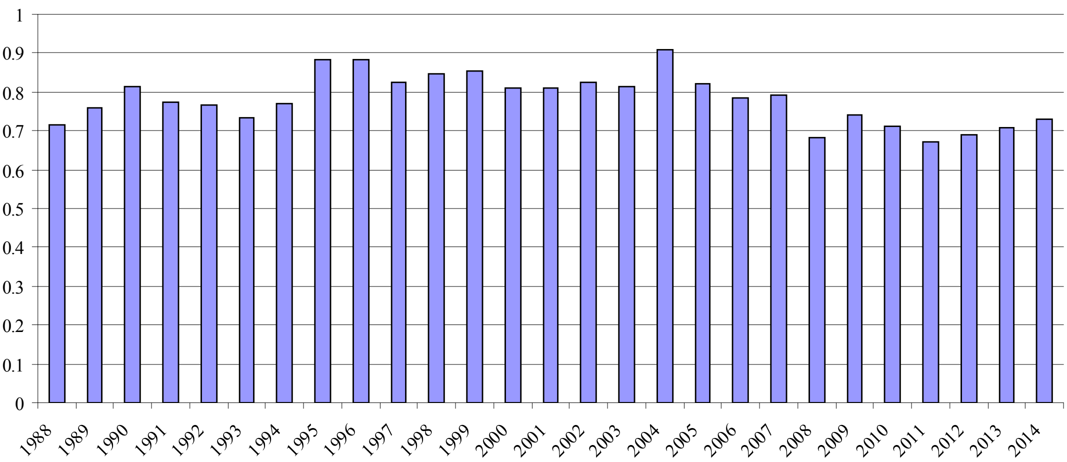
Graph 2. The share of Japan in total extra-EEC/EU trade in 1960-2015 (% of total extra-EEC/EU import and export)



Source: own calculations on [Eurostat/Comext 2016, Eurostat 2011, EC 2015]

The process of declining importance of Japan as a trade partner for the European Union is also perceivable from the trade intensity index, presented at the graph 3. During the whole period 1988-2014 the index value was below 1, which means that the ECC/EU export to Japan was smaller than would be expected on the basis of the importance of both partners in world trade. Last years the trend was slightly downward and at present the index value amounts to only ca. 0.7.

Graph 3. EEC/EU Trade Intensity Index with Japan in 1988-2014



Source: own calculations on [Eurostat/Comext 2016, OECD Database 2016, WTO Database 2016]

The geographical dimension of EU-Japan merchandise trade indicates concentration of trade flows within a relatively narrow group of EU member states (table 2). The

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most important trade partner for Japan within the EU countries is Germany which accounts for more than ¼ of total EU-Japan merchandise trade. In addition to Germany Japan remains an important supplier of goods to the Netherlands (17.32% of total EU import from Japan), the United Kingdom (14.39%), Belgium (12.88%) and France (7.38%). Those five EU member states are responsible for 75.3% of total EU trade import from Japan. In reference to export, Germany with its share in total EU export at the level above 30%, is followed by France (11.20%), the United Kingdom (10.30%), Italy (9.76%) and Ireland (6.73%), which all together amount to 68.63% of total EU merchandise export to the Japanese market.

The structure of EU-Japan bilateral trade in goods by HS (table 3) indicates that EU export to Japan concentrates mostly in products of the chemical or allied industries (25.18% of total), machinery and mechanical appliances (18.70%), transport equipment (16.55%), optical and photographic instruments (9.01%) as well as foodstuffs, beverages and tobacco (4.60%). Those five HS sections are responsible for almost ¾ of total EU trade to the Japanese market. During the last decade the most dynamic increase of export value was recorded in section animal or vegetable fats and oils (by 107% in 2005-2015), products of chemical or allied industries (by 69%) and transport equipment (by 41%). At the same time recent years brought a decrease mostly in European export of articles of stone, glass and ceramic (drop by 17.5%) as well as pearls, precious stones and metals, and articles of thereof (by 10.7%).

Table 2. Import and export of EU members states with Japan in 2015 (millions EUR and % of total EU-28 trade with Japan)

IMPORT			EXPORT		
Germany	13963.94	23.38%	**Germany**	17317.11	30.63%
Netherlands	10346.81	17.32%	**France**	6329.73	11.20%
United Kingdom	8594.30	14.39%	**United Kingdom**	5824.90	10.30%
Belgium	7693.13	12.88%	**Italy**	5517.13	9.76%
France	4408.06	7.38%	**Ireland**	3806.90	6.73%
Italy	3121.71	5.23%	**Netherlands**	3570.30	6.32%
Spain	2465.16	4.13%	**Belgium**	3310.00	5.86%
Sweden	1386.82	2.32%	**Spain**	2469.43	4.37%
Ireland	1311.71	2.20%	**Denmark**	1634.88	2.89%
Hungary	1147.87	1.92%	**Sweden**	1628.04	2.88%
Poland	1126.41	1.89%	**Austria**	1297.93	2.30%
Czech Republic	1007.46	1.69%	**Finland**	1081.07	1.91%
Austria	859.74	1.44%	**Czech Republic**	780.59	1.38%
Denmark	327.44	0.55%	**Poland**	514.37	0.91%

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Romania	292.38	0.49%	**Hungary**	501.58	0.89%
Finland	271.49	0.45%	**Romania**	210.95	0.37%
Portugal	271.27	0.45%	**Portugal**	146.29	0.26%
Slovakia	271.17	0.45%	**Malta**	109.42	0.19%
Greece	248.76	0.42%	**Estonia**	64.22	0.11%
Luxembourg	223.73	0.37%	**Luxembourg**	63.33	0.11%
Bulgaria	84.42	0.14%	**Slovakia**	63.04	0.11%
Slovenia	76.79	0.13%	**Greece**	61.40	0.11%
Malta	69.40	0.12%	**Slovenia**	57.32	0.10%
Cyprus	53.44	0.09%	**Lithuania**	48.74	0.09%
Lithuania	38.46	0.06%	**Croatia**	43.47	0.08%
Estonia	29.06	0.05%	**Bulgaria**	40.34	0.07%
Croatia	26.18	0.04%	**Latvia**	38.96	0.07%
Latvia	20.48	0.03%	**Cyprus**	0.99	0.00%
TOTAL	**59737.61**	**100.00%**	**TOTAL**	**56532.44**	**100.00%**

Source: own calculations on [Eurostat/Comext 2016]

Taking the opposite direction of trade, the EU import from Japan is realized mostly in sections: machinery and mechanical appliances (44.01%), transport equipment (21.79%), products of the chemical or allied industries (9,81%) and optical and photographic instruments (8.90%) and plastics, rubber and articles thereof (4.82%). Listed above HS sections constitute almost 90% of total EU import from Japan. It should be noted that two most relevant import sections have recorded a substantial decrease in value in recent years; import in machinery and mechanical appliances decreased in 2005-2015 by almost 26,9% and in transport equipment by 27.8% (total import from Japan to the EU dropped at the same time by 19.5%). Concurrently, the strongest increase in import has been stated in foodstuffs, beverages and tobacco (by 96%), pearls, precious stones and metals, and articles of thereof (91%), animal or vegetable fats and oils (56%), live animals, animal products and vegetable products (55%). However, trade in mentioned sections remains mostly unsubstantial in nominal value and its relative strong increase has been a result of low value of import in the initial year (2005).

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Table 3. EU-Japan merchandise trade flows by HS section in 2015

SECTION	IMPORT			EXPORT		
	Value Mio EUR	% of Total	change (2005 - 100)	Value Mio EUR	% of Total	change (2005 - 100)
Live animals; animal products	54.51	0.09%	155	1 845.61	3.26%	120
Vegetable products	58.18	0.10%	155	606.67	1.07%	132
Animal or vegetable fats and oils	19.65	0.03%	156	283.12	0.50%	207
Foodstuffs, beverages, tobacco	139.96	0.23%	196	2 601.67	4.60%	138
Mineral products	257.71	0.43%	71	420.04	0.74%	113
Products of the chemical or allied industries	5 861.02	9.81%	103	14 237.22	25.18%	169
Plastics, rubber and articles thereof	2 876.67	4.82%	106	1 352.62	2.39%	110
Raw hides and skins, and saddlery	33.09	0.06%	132	1 204.04	2.13%	102
Wood, charcoal and cork and articles of thereof	5.64	0.01%	75	973.79	1.72%	104
Pulp of wood, paper and paperboard and articles thereof	185.76	0.31%	73	564.24	1.00%	97
Textiles and textile articles	665.18	1.11%	117	1 889.79	3.34%	100
Footwear, hats and other headgear	47.44	0.08%	79	436.48	0.77%	117
Articles of stone, glass and ceramic	669.95	1.12%	133	468.56	0.83%	82
Pearls, precious stones and metals. and articles of thereof	738.15	1.24%	191	885.20	1.57%	89
Base metals and articles of thereof	2 288.14	3.83%	117	1 781.90	3.15%	121
Machinery and mechanical appliances	26 291.74	44.01%	73	10 572.88	18.70%	123
Transport equipment	13 019.17	21.79%	72	9 355.38	16.55%	141
Optical and photographic instruments	5 318.60	8.90%	93	5 096.12	9.01%	114
Arms and ammunition	19.27	0.03%	109	13.68	0.02%	87
Miscellaneous manufactured articles	642.52	1.08%	62	792.74	1.40%	97
Works of art and antiques	427.84	0.72%	56	349.40	0.62%	124
Not classified	117.43	0.20%	174	801.29	1.42%	89
Total	59 737.61	100.00%	80	56 532.44	100.00%	129

Source: own calculations on [Eurostat/Comext 2016]

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Dynamics of trade within the main traded sections have resulted in changes mentioned above in general balance of EU-Japan merchandise trade. Decreasing trade deficit of the EU in recent years has led to relatively balanced flows between the partners. In 2005-2015 trade deficit for the EU in trade with Japan fell from 30.6 billion EUR to only 3.2 billion EUR. This was mostly an aftermath of decreasing value of import in two most important sections – trade deficit in machinery and mechanical appliances decreased in 2005-2015 from 27 billion EUR to 15.7 billion EUR (still the biggest product section deficit for the EU) and in transport equipment from 11.4 billion EUR to 3.6 billion EUR. On the other hand, the most dynamic increase of the EU export was recorded in those sections, in which the EU has traditionally noted trade surplus. Those are products of the chemical or allied industries (trade surplus increased in 2005-2015 from 2.7 billion EUR to 8.4 billion EUR) and foodstuffs, beverages and tobacco (increase from 1.8 billion EUR to 2.5 billion EUR).

2.2 Trade in services

EU-Japan trade in services, although much lower in nominal values compared to merchandise trade, brings more positive tendencies in development of bilateral co-operation. Both parties have increased their exports to each other's markets and the total trade value of services increased in 2004-2014 from 29.2 billion EUR to 40.9 billion EUR. Conversely to merchandise trade the European Union achieves in trade in services with Japan a trade surplus. The total EU export value of services to Japan in 2014 was close to 25.7 billion EUR and was 10.5 billion higher that import of services from Japan (graph 4). Those values make Japan the 5th global consumer of services delivered by the EU (after the US, EFTA, China and Russia) with a share of 3.36% of total services exported and the 4th supplier of services to the EU market (after the US, EFTA, China) with a share at the level of 2.5% [Eurostat 2016].

From EU member states the biggest supplier of services to Japan were (2013) Germany (20.8% of total EU services export to Japan), the United Kingdom (18.0%), Ireland (10.9%), Denmark (8.7%), Italy (6.3%), the Netherlands (5.1%) and Sweden (5.1%). In turn the leading consumer of Japanese services delivered to the EU was the United Kingdom (26.0% of total EU services import from Japan), followed by Germany (23.5%), France (10.7%), Italy (6.6%), Ireland (5.9%) and the Netherlands (5.2%).

The EU services export to Japan concentrates mostly in other business services (21% of total; including a.o.: research and development services (7.9%); professional and management consulting services (5.8%); technical, trade-related, and other business services (7.3%)), financial services (20.7%), transport (17.8%), travel (11.1%) and charges for the use of intellectual property (7.1%). In opposite direction Japan delivers services mostly in the following sections: transport (29.2% of which more than half is realized in sea freight transport), other business services (29.0% of which more than half in technical, trade-related, and other business services), charges for the use of intellectual property (12.9%), financial services (11.9%) and travel (7.3%). In

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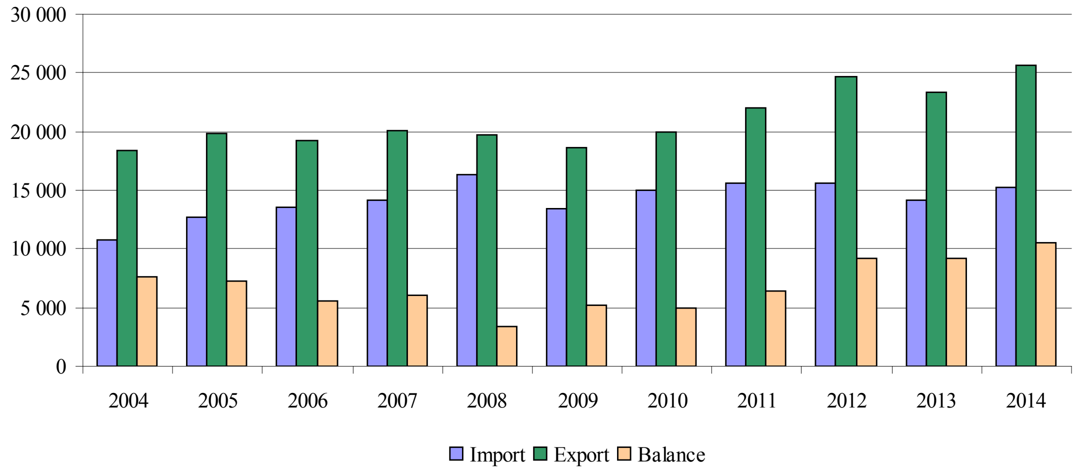
most of the sections mentioned above (except charges for the use of intellectual property and sea freight transport) the EU has a trade surplus in bilateral flows with Japan.

Graph 4. EU-Japan trade in services in 2004-2014 (million EUR)



Source: own calculations on [Eurostat 2016a, Eurostat 2016b]

2.3 Foreign direct investments

The European Union and Japan are beside their trade potential also world-scale investors. In 2015 the EU was globally the second most important source of foreign direct investments with FDI outflows amounting to 280.1 billion USD. At the same time Japan invested in foreign markets 113.6 billion USD, which gave the country the 4th position in the world as an investor. The EU countries are also the most important destination for global FDI, attracting in 2014 investments at the level of 257.6 billion USD. Contrary to this Japan remains very modest place for locating FDI – in 2014 foreign companies invested in Japan only 2.1 billion USD [UNCTAD 2015].

The parties remain important investment partners, although the proportion of relative importance has changed during the last decade. The direct investment stocks between the EU and Japan amounted in 2014 to almost 240 billion EUR, of which 166.3 billion EUR were Japanese investment stocks in EU countries and 73 billion EUR of EU stocks in Japan. Rising regularly during last decade Japanese FDI in the EU, together with rather stable engagement of European investors in Japan, have resulted in current situation in which Japanese FDI stocks in Europe outbalance the European FDI in Japan more than double (graph 5).

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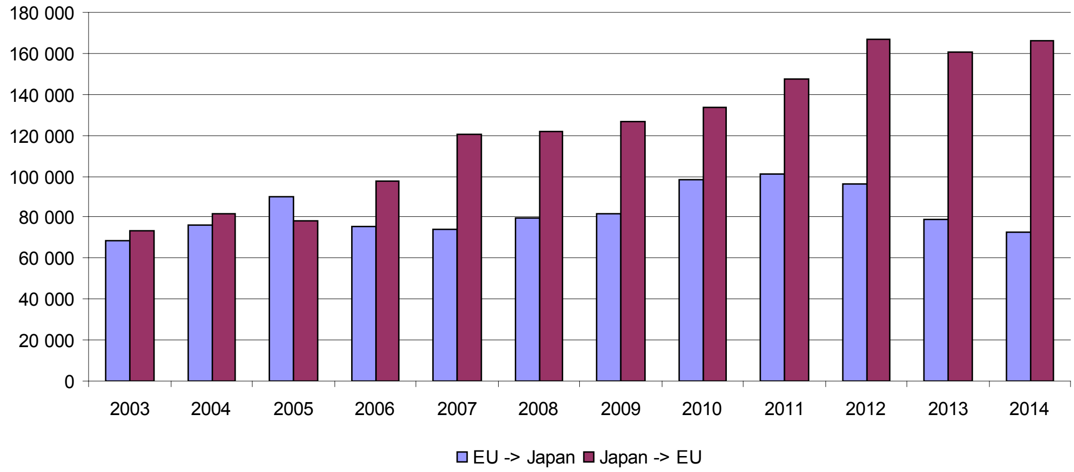
Graph 5. EU-Japan FDI stocks in 2003-2014



Source: [Eurostat 2016b, Eurostat 2016c]

Those numbers also mirror the relative importance of the parties as investors for each other. For the EU investors Japan remains relatively modest place for allocating FDI. The mentioned total FDI stocks in 2014 gave Japan the 10th position in the world (the 3rd in Asia after China/Hong Kong and Singapore) – only 1.27% of total extra EU FDI stocks. On the other hand, Japan is relatively a more important source of investments in the EU countries. With FDI stocks at the level of 166.3 billion EUR (3.63% of total FDI stocks held by the rest of the world in the EU) Japan was the 3rd most important investor in the European Union in 2014 (after the United States and Switzerland).

Conversely to the above mentioned importance of Japan for EU external FDI flows, the European Union is among the most important destinations for Japanese investors. In 2014 the Japanese FDI stocks in the EU constituted 22.8% of total outward Japan FDI stocks (second position after the US with a share of 31.9%). Moreover, European Union members are the most important source of foreign direct investments in Japan. In 2014 the EU' share amounted to 42.0% of the total inward Japan FDI stocks [JETRO 2016].

Among EU countries the biggest investors in Japan are the Netherlands (35.7% of total EU FDI stocks in Japan in 2014), France (31.9%), Germany (10.5%) and the United Kingdom (6.9%), which means that almost 85% of EU FDI stocks in Japan are attributable to only those four countries. In turn, Japanese investments in the European Union are distributed (slightly) more broadly. The most important destinations for Japanese investors in the EU are the United Kingdom (35.0% of total Japanese FDI stocks in the EU in 2014), the Netherlands (27.7%), Germany (11.0%), France (6.9%) Belgium (6.7%) and Denmark (4.1%).

European investments in Japan by economic activity are allocated in manufacturing (45.6% of total EU FDI stocks in Japan in 2013), financial and insurance activities (24.8%), information and communication services (14.8%) as well as wholesale and

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retail trade/repair of motor vehicles and motorcycles (7.1%). The Japanese FDI stocks in European Union countries are concentrated in vast majority in the same economic activities, however with different sequences and share: financial and insurance activities (42.1%), manufacturing (25.9%), wholesale and retail trade/repair of motor vehicles and motorcycles (20.3%) and professional, scientific and technical activities (4.7%).

3. TRADE AND INVESTMENT BARRIERS TO THE JAPANESE MARKET

As the aftermath of the decisions made during the 20th EU-Japan summit in 2011 and the successful completion of the scoping exercise, defining among others a number of non-tariff barriers and other obstacles considered by the EU in accessing the Japanese market, the Council adopted in November 2012 a decision authorizing the European Commission to open negotiations. According to the Council's decision negotiations on the new free trade agreement would be conducted simultaneously to negotiations on a broader bilateral framework agreement with Japan, covering political, global and sectoral cooperation [Council 2012]. The negotiations were officially launched in a teleconference of leaders on 25 March 2013 and the first round of talks was held one month later in Brussels. The first official round of talks was an occasion to discuss the scope and procedures of negotiations [DPA 2013]. There have been fifteen negotiating rounds so far .

Both parties, joining the negotiations on the new comprehensive agreement, had their own interests and priorities to be settled within the new trade framework. Both economies, facing the problem of economic crisis and relatively low level of economic activity in reference to GDP growth, recognized the new agreement as a significant incentive for trade and investment expansion and thereby faster economic growth. Although the level of mutual tariff quotas is relatively low nowadays, there are still many obstacles to utilize mutually full potential of business and economic capability of both parties [Mazur 2013].

3.1 Barriers to merchandise trade

The European Union has a lot of arguments for concluding the new free trade agreement. The European export enters the Japanese market under relatively low tariffs - 68.7% of European products exported to Japan are duty-free and the average customs tariffs amounts to only 1.7%. However European exporters still encounter many non-tariff barriers which are recognized by most of studies and public consultations as a major barrier to EU exports to Japan.

The EU side argues that European exporters and investors cannot fully utilize the potential of Japanese market due to trade impediments preventing a higher degree of economic cooperation. Among the main obstacles for European business when entering and operating the Japanese market are: "(…) *unfair competition rules, strict licensing system and restrictive issuing of permits, poor quality standards for food products, punitive tariffs and quotas on liquors and leather footwear or complex procedures for outlet opening*" [FTA 2013]. All of them account for the fact that the

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country still remains closed, especially for agricultural products, some transport equipment and aeronautical products. The mentioned non-tariff barriers affect mostly those business sectors which cover the lion's share of EU export, i.e. processed foods, chemicals (including pharmaceuticals), medical devices, automotive and transport equipment, telecommunication and financial services [EC 2012].

According to a survey conducted in 2009 among 120 European firms exporting to and operating in Japan within the above mentioned sectors, ¾ of the companies perceive the Japanese market as more difficult than the other ones. Language barrier, differences in consumer preferences as well as mentioned technical standards and regulatory issues were identified among main difficulties. Additional costs resulting from the indicated barriers increase the cost of exporting to Japan by 10-30%, depending on the sector, and 2/3 of surveyed companies reduce the variety of exported goods due to existing barriers in access to Japanese market (60% of EU exporters stated that they have a smaller or much smaller product range in Japan than other markets in Asia; 39% declared that their firm offers substantially fewer products on the Japanese market than other Asian markets) [Sunesen et al. 2009].

3.1.1 Food and agricultural products

In the context of the above mentioned obstacles difficult negotiations may be expected in liberalization of trade in agricultural products which is among priorities of EU negotiators. Japan remains one of the most important export markets for the EU producers. The country with a share in total EU agricultural and processed agricultural products export at 4.1% ranks as the 5th export destination for the EU (5 354.0 million EUR in 2015). The main products exported by the EU to Japan include pork (18.8%), wine, cider and vinegar (14.5%), cheese (5.0%), spirits, liqueurs and vermouth (4.6%), preparations of vegetables, fruit or nuts (4.4%), casein, other albuminoidal substances and modified starches (4.4%), olive oil (4.2%), pet food (3.5%), chocolate, confectionery and ice cream (3.1%), pasta, pastry, biscuits and bread (3.1%). The EU has a significant trade surplus in trade of agricultural and processed agricultural products with Japan – the EU import in 2015 amounted to only 238 million EUR (55th as a supplier to the EU market). The EU imports mainly soups and sauces (17.2%), spirits, liqueurs and vermouth (11.8%), vegetable products (vegetable seeds) (8.0%), as well as food and cereal preparations (7.1%) [EC 2016b].

The Japanese food and agricultural products market has been strongly protected. The agricultural policy and resulting form this the organization of agricultural markets together with highly restrictions on import of agricultural and food products – similarly to the EU system – make the Japanese internal system one of the most protected in the world. In 2015 the simple average final bound tariff was at the level of 18.2% (simple average MFN applied – 14.3%) and only ⅓ of agricultural products import (by % of tariff lines) was duty-free. Similarly to the EU, tariff rates for food and agricultural products reach peak levels in this group of goods. The most protected products group is dairy products with an average applied tariff at 76.3% and only 9.1% of duty-free lines (tariff peak rate in this group – 586.0%). Among strongly protected products are also cereals and preparations (average tariff – 34.7%) with

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tariff peaks at 783.0%, sugars and confectionery, beverages and tobacco, animal products as well as coffee and tea (table 4) [WTO 2015b].

Table 4. Japan's tariffs and imports by product groups (2015)

Product groups	Final bound duties				MFN applied duties			Imports	
	AVG	Duty-free in %	Max	Binding in %	AVG	Duty-free in %	Max	Share in %	Duty-free in %
Animal products	14.2	45.7	*360*	100	11.3	46.6	*360*	1.5	2.6
Dairy products	102.7	0	*587*	100	76.3	9.1	*586*	0.2	26.2
Fruit, vegetables, plants	9.3	19.6	*268*	100	10.1	19.4	*268*	1.2	15.3
Coffee, tea	13.5	22.2	*138*	100	14.1	22.7	*138*	0.4	59.5
Cereals & preparations	61.0	8.2	*783*	100	34.7	21.8	*783*	1.5	69.4
Oilseeds, fats & oils	7.5	46.2	*381*	100	8.0	46.0	*381*	0.8	80.0
Sugars and confectionery	27.1	7.3	*131*	100	19.7	12.0	*50*	0.1	64.6
Beverages & tobacco	16.1	19.1	*48*	100	14.5	30.8	*48*	1.1	63.7
Cotton	0.0	100.0	0	100	0.0	100.0	0	0.0	100.0
Other agric. products	3.7	66.5	*261*	100	3.4	68.2	*215*	0.7	70.5
Fish & fish products	4.9	4.9	12	91.3	5.7	3.2	15	1.9	4.9
Minerals & metals	1.0	69.9	10	99.9	1.0	70.4	10	23.4	94.0
Petroleum	13.4	54.2	*285*	80.0	0.6	64.6	8	21.0	94.5
Chemicals	2.3	37.4	7	100	2.2	38.8	7	8.4	59.0
Wood, paper, etc.	1.0	78.8	10	97.6	0.8	80.8	10	3.0	66.5
Textiles	5.5	7.6	25	100	5.4	8.1	25	1.9	7.1
Clothing	9.2	0	13	100	9.0	2.0	13	3.9	3.1
Leather, footwear, etc.	9.6	50.3	*434*	100	9.4	54.1	*432*	1.7	38.7
Non-electrical machinery	0.0	100.0	0	100	0.0	100.0	0	7.7	100.0
Electrical machinery	0.2	95.5	5	100	0.1	97.8	5	11.3	99.8
Transport equipment	0.0	100.0	0	100	0.0	100.0	0	3.5	100.0
Manufactures, n.e.s.	1.1	77.0	8	100	1.2	75.7	8	5.1	90.5

Source: [WTO 2015b]

The Japanese market of imported food and agricultural products remains inaccessible not only due to high tariffs imposed on many products, but also many existing non-tariff barriers which are recalled by EU exporters as relevant impediment for trade expansion. Among the main protectionists barriers to import of agriculture products and food are listed for mostly license regimes as well as import surcharges and import permits. Those restrictions, applied a.o. to liquors, dairy (frozen) products, rice (e.g. rice imports are limited by quotas) and soft drinks make import very difficult [FTA 2013].

Regarding the import of alcoholic beverages special restrictions refer to both import and sale of those products at the Japanese market. For example malt and quota

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management system, based on tariff quota system for brewing-malt, allows that a company must manufacture beer or import malt exclusively for the use of a particular brewery. Additionally, application for the quota are only twice a year, which means that any imports using the quota must be based on forecasts and not on actual short-term demand. The system, aimed at protecting Japanese barley farmers and malt manufactures, brings impediments for imported products of this category [EBC 2015].

Japan applies also a strict liquor wholesale licensing system, in which quotas are reallocated only once per year [FTA 2013]. The licensing system is complex and applications are not processed in a clear, transparent and consistent manner. Moreover, prices of liquor are controlled by the National Tax Agency and the categorization of alcoholic beverages for tax purposes is different form that one used in the EU countries or the United States. It is often declared by European exporters that product definitions for alcoholic beverages in Japan are broad and do not comply with internationally accepted product specifications that are based on production methods and geographical indications. Moreover, the geographical indication terminology in Japan is not compatible with the EU-origin concept and rules and threatens to undermine European products in the Japanese market [EBC 2008, EBC 2015]. Although the Japanese liquor market belongs to one of the largest in the world, it still remains mostly controlled by domestic consumers with a very limited access for imported products, including those from the EU. In 2014 imported products constituted only 4% of the total Japanese liquor market [EBC 2015].

Other relevant obstacles indicated by European exporters derive from the fact that Japanese domestic regulations in many aspects are not harmonized with internationally recognized standards for food safety and quality. This also applies to animal and plant trade. High costs of additional conformity tests because of denial of acceptance by Japanese authorities of evaluations made by the EU/international bodies, constitute an additional burdensome barrier for export to Japan. Many food additives of worldwide common use and recognized as being safe by international food safety bodies such as the Joint FAO/WHO Expert Committee on Food Additives (JECFA) remain prohibited by Japan [EC 2008]. This eliminates completely from the sale and import many products containing the additives and therefore creates serious trade barrier for EU export of food products. Substantial increasing of the list of recognized by the Japanese authorities food additives together with shorten and revised approval process as well as progress in mutual recognition of conformity assessment procedures would eliminate the duplicate costs of evaluations and enhance the access for European exporters to the Japanese market of food products [EU-Japan BRT 2013].

The problem of denial of international standards refers also to other aspects of trade in food and agricultural products, including animals and plants, e.g.: different regulations on organic food , standards on non-quarantine pests are not in line with international standards, legislation on trade in beef and other BSE products is not in line with the World Organisation for Animal Health, plant quarantine regulations are not in line with GATTs Sanitary and Phytosanitary chapter. There is also no regulatory compliance with CODEX standards for organic crop imports, safe food additives and testing regimes for pre- and post-harvest pesticides. Moreover, exporters

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to the Japanese market accentuate many other technical and administrative barriers for trade in food and agricultural products, which next to high tariffs and incompatibility impede effectively import to Japan, such as e.g.: slow process of examination of the data submitted and the questions to what is necessary for risk assessment for meat/beef import, different standards for labelling, high fumigation costs, or low tolerance regime for insects or the requirement for an individual organic certificate to accompany every shipment [EBC 2008, EBC 2014, EBC 2015, Sunesen et al. 2009].

3.1.2 Pharmaceuticals and cosmetics

The Japanese market, due to its size, ageing population and level of spending on healthcare (in 2014/2015 - 10.3% of GDP compared to the OECD average of 9.3%) is perceived also as an attractive market for European producers of pharmaceuticals. Although during recent years in many barriers such as incompatibly of Japanese regulations with international standards, insufficient reward of products' innovation or burdensome import processes [Sunesen et al. 2009] some progress has been achieved, making import and the pharmaceuticals market in Japan more transparent and accessible, there are still non-tariff barrier with a destructive effect for import.

In 2010 the Japanese authorities introduced on a trial basis (extended in 2012 and 2014) an innovation premium known as the "premium to promote the development of new drugs and eliminate off-label use". The initiative has resulted in a sharp increase in the number of new drug development projects in Japan, which was the main target of the initiative. However, there are still regulations, which are perceived as burdensome for introducing innovative products into the market. For example a regulation on max. 14 days prescription of a drug during the first 12 months after it is launched, results in situation in which new drugs are not commonly prescribed. It is described by many producers as an unnecessary rule and as such acts as a barrier for innovative new products [EBC 2014].

Even more complex problem for European exporters of pharmaceuticals are limitations in clinical trials. Although the Japanese Good Clinical Practice (GCP) in clinical trials has been conformed to international standards in recent years, there is still a need to reduce differences between Japanese medical institutions in the efficiency of the clinical trials they conduct. European producers and exporters also complain about the insufficient scope of the Mutual Recognition Agreement (MRA entered into force in 2002) for EU and Japanese Good Manufacturing Practice (GMP), which results in duplication of inspections and tests leading to increase in delays and costs [EBC 2015]. Also national tests for vaccines should be eliminated or reduced to an absolute minimum [EU-Japan BRT 2015a].

Some controversies still also arise around the IPR related to pharmaceuticals. As in many other FTAs negotiated by the EU, European producers and exporters aim not only at better access to foreign domestic markets, but also on improving patent protection of their products. In this connection the European business is in a position that the Japan Patent Office (JPO) should consider supplementary experimental evidence to support generic drug patent claims, as the current practice is that for many

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types of applications the JPO grants only protection for embodiments disclosed in the application as filed [EU-Japan BRT 2013].

Other group of products which is important to European exporters and which still faces burdensome barriers in import to the Japanese market constitutes cosmetics and quasi-drug products. Although the EU is an important supplier of those products, due to their value recognized by Japanese consumers, there are still non-tariff obstacles to trade.

Similarly to food and agricultural products, trade in cosmetics and quasi-drug products is negatively affected by the low harmonization of products standards, regulations on ingredients, permitted efficacy claims as well as standards for alternatives to animal testing [Sunesen et al. 2009]. Additionally a slow validation process of testing on cosmetics makes that the launch of European products in Japan is often severely delayed, even though the same products are in global use and have clinically proven efficacy. European exporters also claim that there is a lack of sufficient access to information on the approval of different ingredients in Japan. The process is even more complicated as the approval of products meeting existing approval standards is delegated to the prefectural authorities, which sometime leads to differences in interpretation by different prefectural offices [EBC 2015].

3.1.3 Automobiles and automotive components

One of the most important issues to be addressed in the agenda of ongoing negotiations for the EU-Japan FTA is trade in automobiles and automotive components. Both parties are world-scale car producers with worldly recognized brands. The European Union is the 2nd biggest producer of motor vehicles in the world and Japan ranks at the 4th position (3rd as a national economy after China and the United states) [OICA 2016]. Regarding trade in automobiles between the EU and Japan, there is a noticeable imbalance in trade. The EU market is more attractive for Japanese car manufacturers than the other way round. According to an analysis prepared by Deloitte Consulting the Japanese market is not a strategic market for EU car producers and its shrinking tendency and traditional 'inward looking' character do not bring promising future prospects for EU exporters [Deloitte 2012].

The European automobile manufacturers are skeptical about the benefits of EU-Japan free trade agreement which is being negotiated. The skepticism derives from forecasted effects of FTA on trade in cars as well as existing import barriers in the Japanese market and its organization. According to the analysis it is estimated that FTA would result (by 2020) in 443 000 additional units exported from Japan to the EU and only in 7 800 additional units exported from the EU to Japan. In contrast to the EU market, which is predicted to grow in size in forthcoming years, the Japanese market is forecasted to shrink due to demographic trends. Moreover, it is strongly inaccessible due to non-tariff barriers posing significant obstacles for more effective market penetration. Additionally, the Japanese market is quite specific – preferential treatment (in terms of tax, insurance, motorway tolls and parking registration) is given to the mini car segment (*Kei*), which currently constitute more than 40% of all sold cars (in 2014 – 2 272 789 units and a record market share of 40.9%). Moreover, the

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segment is predicted to grow to ½ of the total market by 2020. The production and sale in this segment is dominated by the Japanese producers, which naturally eliminates European manufacturers and exporters form the significant share of the market [Deloitte 2012].

As the FTA does not address the issue of trends and structure of the Japanese car market and consumers' behaviour, the agreement is expected to improve access especially in reference to current regulatory non-tariff barriers. The low level of harmonization of Japanese standards with internationally recognized ones, which has been already evoked several times in other product groups, applies also to trade in automobiles and automotive components. In this context European exporters perceive the harmonization of technical standards and certification procedures as the most important step to improve their export possibilities that should be addressed in EU-Japan negotiations agenda. The EU representatives accentuate that Japan, although being a signatory of the UN-ECE (United Nations Economic Committee for Europe) 1958 Agreement on the harmonisation of technical requirements and certification procedures, still do not approve some standards covered by the UN regulations (e.g. emission of pollutants, CO2 emissions and fuel consumption and noise) and do not accept a UN certificate as demonstrating compliance with Japan's national requirements [EBC 2015]. Steps towards harmonization and full adoption of UN standards would allow to sell in Japan vehicles certificated in the EU without modifications or further testing.

Similar efforts of adopting international standards should be also undertaken in reference to requirements for commercial vehicles [EC-Japan BRT 2015a], where national Japan's regulations on a.o. the maximum width, length and axle load for buses, the method of calculating gross vehicle weight and the endurance testing requirements for emission control devices for heavy-duty vehicles create additional restrictions for European exporters. However, it should be underlined as some progress in this issue has been made last time and 2016 witnesses further progress in harmonization (adoption of International Whole Vehicle Type Approval (IWVTA) system) [EBC 2015].

Low harmonization with UNECE standards as well as lack of recognition of foreign tests hampers also trade in automotive components. Those barriers together with still existing reliance of Japanese producers to co-operate with affiliated companies as well as legal system distorting free and open competition in the procurement of component make the Japanese market difficult place for trade in automotive components. In this context Japan, as one of the greatest car manufacturers in the world, presents itself for European exporters as a very attractive market due to its size and production structure, however with many still existing technical and administrative barriers [EBC 2015].

European producers perceive also as a significant barrier in access to the Japanese market regulatory and fiscal privileges applied to Kei cars segment [Sunesen et al. 2009]. This system of classification as well as privileges given to those specific vehicles make that European producers are out of the lion's share of the passenger car market in Japan (it applies even to European compact cars). In this context European exporters demand from Japan authorities to put Kei cars to the same regulatory and

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fiscal footing as for other motor vehicles [EBC 2014], which should enable to penetrate more effectively this segment for foreign exporters and also stimulate development of other market's sectors which are currently under discriminatory provisions. Moreover, the European exporters also recommend reforming the automobile tax system in Japan (a.o. on the purchase and ownership of motor vehicles) based on international best practices. Additionally, the EU also encourages to adopt together by the EU and Japan internationally harmonized standards to measure fuel efficiency and exhaust emissions, which would be a base for tax system promoting environmentally friendly vehicles [EBC 2015].

3.2 Barriers to trade in services

The European Union of 28 countries is the most important exporter of commercial services in the world. In 2014 the total share of extra-EU export of commercial services amounted to ¼ of total world's export and was higher that the combined share of the next two most important suppliers of commercial service i.e. the United States and China (the Japan's share in global export of commercial services amounted to 3.2%) [WTO 2015a]. The potential, high competitiveness and importance of trade in commercial services for many EU countries make this issue as one of the most important during the negotiations on the EU-Japan FTA.

In terms of trade in services, the Japanese market is perceived by European companies as highly inaccessible due to numerous non-tariff measures faced by external service suppliers. According to the assessment of barriers to trade and investment between the EU and Japan prepared in 2009, ⅓ of all non-tariff measures identified at the Japanese market by European companies applied to trade in services (62 of 194 NTM). The identified barriers affect different dimensions of delivering services: the establishment (regulations on the ability to establish physical presence in an economy and supply services thorough those outlets/branches), operational issues related to delivering services after entering the market, special discriminatory regulations applied to only foreign services suppliers as well as barriers affecting costs/prices of service providers/services [Sunesen et al. 2009].

In this context barriers to trade in services are strongly correlated with identified barriers for general foreign direct investments as well as with competition policy of the importing country. The European Commission in its position paper on EU-Japan FTA [EC 2012] underlined that negotiations and potential future regulations to be included in the new agreement should be aimed at "*effective opening of key services sectors to European providers, including through addressing all kinds of non-tariff barriers, ensuring more open competition and establishing a level playing field for EU industry in the services sector, especially with regard to existing regulatory barriers and ensuring effective national treatment and non-discrimination*". Moreover, an additional challenge to be tackled is inconsistency of treatment of foreign investors and service providers on regional a level. Japanese local authorities often impose their own individual procedures and/or interpretation of regulations, contributing additionally to discriminatory treatment of external/foreign companies.

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Among the most affected by non-tariff barriers service sectors, and through this remaining relatively closed to the EU investors, are financial services sector (almost ⅓ of all barriers identified), communication services, transport services (all types, of which the mostly affected is air transport) and insurance [Sunesen et al. 2009]. All mentioned sectors are of crucial importance to EU economy and constitute the lion's share of export of services from the European Union to Japan.

3.2.1 Financial and insurance sectors

Referring to conditions of delivering services by EU suppliers in financial sector, the EU objections address mostly assets management, banking sector and insurance. Regarding the first one, external partners expect a.o. introducing on a larger scale operational platforms for the asset management industry which still are relatively isolated from the global environment and systems (e.g. usage of SWIFT messages in Japan for domestic assets is still limited to a few trustee banks). Additionally, foreign investors underline that Japan's authorities should also address the challenge of high fragmentation of the Japanese asset management industry which consists of a high number of funds. In this context higher elasticity and possibility of mergers should be provided, as current legal situation brings a burdensome administrative and information costs. In addition, the European side also expects greater flexibility (e.g. capital ratio requirements) depending on type of activity for asset management companies when entering the market [EBC 2015].

Also banking sector faces in Japan barriers influencing negatively the scope of their activity and supplied services/products. Among main existing barriers are duplicated inspections made by many Japan's financial control institutions (e.g. Financial Services Agency, Securities Exchange and Surveillance Commission, Tokyo Stock Exchange, Japan Securities Dealers Association, Japan's Ministry of Finance or the Bank of Japan). In this context a greater transparency and regulatory efficiency would be expected e.g. through the adoption by the FSA universal rules and regulations, which could support tackling the unnecessary administrative burden. Another example of barriers affecting the EU suppliers of financial services is a requirement from the branches of EU banks operating in Japan to apply for a special business license each time when introducing any new banking services provided by another banking entity (also within the same financial group located outside Japan). In this context the application process for banking agency licenses should be clarified by the FSA. Additional improvement should be also made in relation to ban on information sharing between financial institutions, even within the same financial group [EBC 2015].

Some controversies arise also in insurance services, and within this sector especially to the position of the Japan Post and conditions of competition between this institution and other private delivery companies, banks, and insurance companies. The controversies here extend into two dimensions: to the Post's traditional services, but also to its insurance products offered within the Japanese financial market. Regarding the first one, the EU delivery service providers require that the JP should be covered with the same requirements as other private postal delivery operators (a.o. in customs procedures and formalities, quarantine and security clearance or the issuance of

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parking tickets for delivery vehicle parking infringements) [EU-Japan BRT 2015a]. Concurrently the Japan Post became also an important player at the insurance market in Japan. In this context controversies arise around the further reform and privatization of the JP as well as clear division between different JP group companies and transparent selection of their business partners to provide financial services [EBC 2015].

Among other barriers and challenges in delivering insurance services in Japan by foreign companies are also: privileged position of the insurance business of cooperative societies (*Kyosai*) which are not under supervision of FSA and are exempted from Insurance Business Law [FSA 2016], convergence between Japanese and global solvency standards as well as other regulatory standards, the FSA product approval process which is overly lengthy and has burdensome effect for the product development strategy and effective business strategy planning, regulations preventing insurance sales by loan managers and the use of information from the banking system in identifying potential customers for insurance products [EBC 2014, EBC 2015].

3.2.2 Transport services

Transport is one of the most important sections of trade in services between the EU and Japan. In 2014 transport services accounted to 17.8% of all EU services exported to Japan and even 29.2% for the EU services import. Contrary to total trade in services, bilateral EU-Japan supply of services in this section is rather balanced in terms of value (respectively 4.56 and 4.44 billion EUR). Undistorted co-operation in this sector is also of crucial importance for a proper trade in manufactured goods as well as other types of services.

However, the European carriers providing transport services to Japan complain about many barriers they face when operating within the Japanese market. As regards the air transport, the carriers raise the issue of high airport service fees (landing, navigation) which are inadequate to the quality of provided services and infrastructure (a.o. criticism refers to capital airports NRT and HND and their insufficient catering and cargo facilities or insufficient immigration and customs staff) as well as not transparent cost structure used by some airports. Some concerns result also from the privileged treatment as well as the bail-out and recapitalisation of Japan Airlines (JAL) by the Japanese government. In this context European airlines underline a need of fair competition, including also broader access to slots at HND, which now is not fully available to international flights. Another more general issue, which is combined with FDI regulations refers to discrimination and non-transparency in foreign ownership of airports [Sunesen et al. 2009, EBC 2014, EBC 2015].

The European producers and exporters would like to utilize also more open access to highly developed Japanese market of railways. The market is highly dominated by the Japanese companies delivering most of services and rolling stock within the sector. The limited access for foreign suppliers results largely from the general public procurement regulations applied in Japan and also from specific regulations of the railway sector. In this respect the European producers underline a need of enhanced access to the market through the avoidance of duplicate extensive testing that is

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required for the Japanese market as well as common approval of test results and certification by all operators functioning at the Japanese market (standards and requirements imposed by Japanese operators should be available openly to European companies to ensure better understanding and preparation of offered goods and services) [EU-Japan BRT 2015a]. Moreover, the European side expects from Japanese authorities to take efforts in defining precisely the so called Operational Safety Clause, which was negotiated within the WTO's Plurilateral Agreement on Government Procurement (GPA) and gives the right to exclude the procurement related to the operational safety of transportation [EBC 2015]. According to EU producers, due to the vague character of the clause definition, it is often used as an unjustifiable barrier for broader calls for tenders in this sector.

Some other limitations are also met by freight and logistics operators delivering services to Japan. High operating costs, already mentioned in the case of airports, apply also to Japanese sea ports, which undermine their competitiveness against other East Asian ports and reduce a.o. trans-shipping services. Furthermore, foreign shipping lines are still not allowed to trans-ship their own overseas cargo onto their own vessels in Japan. Additional restrictions come also from fixed operating hours of Japanese ports. The EU carriers expect also further liberalization of stevedore services that should be provided through open tenders as well as higher flexibility for shipping companies in changing their operations, which now requires prior approval from the Japan Harbour Transportation Association (JHTA) and thus limits alternative and competitive services [EBC 2015].

Beside the sectoral barriers exampled above, EU service providers face also some general barriers in access to the market. One of the issues is the customs jurisdiction and in particular customs clearance and declaration. Japan with its nine separate customs areas and the requirement of logging customs declarations at clearance operation physically located within the jurisdiction of the responsible customs office make the system difficult to work, especially for foreign companies. In this connection international companies, including the European ones, would expect some deregulation and through this greater flexibility in filing clearances independently of the territory of the responsible customs office and the physical presence of the company. Although some progress has been made in this area a more standardized interpretation and application of customs rules and reporting requirements should be developed [EBC 2015].

Some relaxation and simplification of requirements was also expected with the implementation of the Authorised Economic Operator (AEO) concept in Japan (for logistics and customs operators since 2008) that should provide more favorable consideration in customs enforcement proceedings and better relations with customs according to its type of AEO . However the system, which was aimed at simplification of many of the transport and customs processes, has resulted in converse results bringing more administrative load. In connection to this the system should be revised to focus more on offering simplifications if the operator meets the agreed criteria for traceability and to introduce real trade facilitations such as a.o. deregulated customs clearance beyond the local customs jurisdiction territories (according to Japan Customs' announcements this should be introduced by 2017),

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reduction of the physical examination of shipments or alternative documentation for showing "direct shipment" under free trade arrangements [EU-Japan BRT 2015a].

3.3 Barriers to foreign direct investments

Although Japan is a world-scale investor the country is not a popular place for allocating foreign direct investment. FDI flows to Japan in 2014 amounted to only 2.1 billion USD (in a sharp contrast to FDI outflow at the level of 113.6 billion USD) [UNCTAD 2015]. This modest number results in a fact that Japan's stock of inward FDI has stayed below 4% of GDP since 2008, putting the country in this aspect at the last position among all OECD countries. The Japan Revitalisation Strategy announced in 2013 as a component of '*Abenomics*' (so called '*the third arrow*') includes among other priorities enhancing Japan's integration in the world economy. One of the elements that should enable this process is to double the stock of inward FDI from 18 trillion JPY in 2012 to 35 trillion JPY in 2020. However, the adopted goal will not be easy to achieve as there are many factors which hinder foreign investors to locate FDI in Japan [Fukukawa 2013, OECD 2015].

Among the key factors affecting negatively FDI inflows to Japan are: the low level of corporate mergers and acquisitions, which is an important channel for FDI flows; the high corporate income tax rate (the rate in Japan - along with that in the United States - remains the highest among the world's advanced economies); vague regulatory environment; low flexibility in employment and termination rules for labour and the lack of mid-career mobility as well as restrictions for the entry into Japan of foreign workers [OECD 2015].

Similar barriers for locating FDI in Japan were defined and listed in 2012 by the European Commission in a report preceding the launch of EU-Japan FTA negotiations. In the document the Commission presented issues which need to be addressed in tackling against the non-tariff barriers for FDI in Japan. These are: restrictions on the entry of foreign workers; requirement for prior approval of FDI in sectors where there is (a risk of) a significant adverse effect on smooth management of the national economy, and in other sectors on grounds of public order, public safety, and national security; numerous of regulatory barriers to entry in network industries (including gas, electricity, rail, airlines, and post) as well as the ineffectiveness of so called Japan's "triangular merger" scheme [EC 2012].

Following the defined problematic areas the Commission also identified operational objectives in the area of FDI that must be addressed during the negotiations and finally in the regulations of the new EU-Japan agreement. Under the Treaty of Lisbon that entered into force in 2009, the European Union is empowered to negotiate on the investments issue on behalf of all member states, as it became one of the integral components of the Common Commercial Policy of the EU. In this respect negotiations on investments became an indispensable point during FTA negotiations, including the EU talks with Japan.

Operational objectives as regards investments, which stay behind the EU's position during ongoing negotiations, address the identified by the EC problematic areas. In

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this connection the EU side stresses the importance of abolishing all discriminatory regulations both before and after establishment of economic activity in Japan. Moreover, special attention should be dedicated to eliminating investment controls based on unclear and excessively wide definition of the national interest, and ensure as transparent as possible an application of controls such as those based on national security considerations [EC 2012].

The EU business expects also further facilitations in cross-border mergers and acquisitions, especially trough providing more flexible and extended utilization of tax deferral on capital gains referring to the M&A processes [EC 2008]. There is an expectation that the Japanese authorities should consider allowing tax deferrals also for capital gains originating from direct cross-border mergers and re-organisations. Moreover, other tax regulations should be reformed e.g. more advantageous rules for Net Operation Loss (NOL), which will allow (since 2017) companies in Japan to carry forward 50% of their losses for ten years (in neighbouring countries those regulations are more advantageous) or disadvantageous rules on inheritance tax which in many countries has already been removed [EU-Japan BRT 2015a]. The bilateral FDI flows between the EU and Japan should also be supported by modernizing the tax treaties between the partners. Special attention should be placed to measures to avoid double taxation which should became an important instrument to reward taking risks associated with cross-border investment. Additionally, also stronger convergence of policies on transfer pricing taxation should be addressed during negotiations, which could lead to limitation of compliance costs associated with the transfer pricing taxation requirements [EU-Japan BRT 2015b]. In the survey by Sunesen et al. [2009] taxes and high business costs have been identified as the second most important obstacle by surveyed companies (24% of participating companies) for investing in Japan.

Conditions for making investments in Japan are also strongly co-related with another important factor creating general business environment in the country, namely the regulations of competition policy. Nontransparent and unfair competition rules applied within the Japanese market have already been mentioned in many examples (e.g. trade in services (p. 3.2), where competition in Japan is relatively weaker than in many other developed economies; it also makes that Japan's trade in services is underdeveloped). However, also general approach to the policy has to been reformed. The vague competition policy limits market access for foreign businesses and raises new barriers to substitute for tariffs or traditional non-tariff barriers. In this connection the EU-Japan FTA should address strengthening and enforcements of the Japan's antitrust rules together with harmonization of the law with international standards [FTA 2013, EC 2012]. Moreover, the EU underlines that the surcharge rate and criminal penalties in Japan for breaking the competition law are relatively low and do not bring the deterrent effect. Also further limitations should be accepted in reference to exemptions from the anti-monopoly act (the exemptions cover a wide range of areas, e.g. in insurance sector) as well as the role of trade associations of which activities may influence competition within specific sectors [Sunesen et al. 2009]. The competition policy and its further transparent development is also an issue of a great importance to Japan. This is a crucial element of enhancing the competitiveness of

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Japanese economy (especially in some service sectors) which is now hindered by domestic regulations and limited foreign competition pressure [Solis 2010].

3.4 Access to public procurement

The non-discriminatory treatment of foreign companies refers also to another issue of great importance for EU companies, which is access to public procurement in Japan. The total value of government procurement by Japan's central government entities, prefectures and designated cities under the WTO Agreement on Government Procurement regime was estimated in 2013 by the government at the level of ca. 33 billion EUR. However, EU estimations on the actual size of the government procurement market in Japan, including local entities, is much higher and amounts to 550-565 billion EUR [Griek 2014]. The numbers illustrate that non-discriminatory access to Japanese public procurement market is crucial for succeeding in more effective access for EU exporters of goods and services to Japan in general.

In 2002-2012 the EU companies delivered only 0.6-1.4% of the total value of public government procurement in Japan, which means that the penetration of the Japanese market by EU suppliers was low [Griek 2014]. The difficulties faced by European companies may be divided into two groups: problems of market access and problems of rules within the sectors that are formally accessible, but require specific rules hampering the EU companies and placing them at a disadvantageous position [Mazur 2015]. There are still some strategic sectors which are not under the coverage of WTO Government Procurement Agreement and therefore have a restricted access. In sectors which are formally accessible some barriers arise due to restrictiveness of Japan authorities in interpretation of the GPA commitments. Additionally, EU producers complain about difficult access to information (notices on calls for tenders) as well as procurement practices giving advantageous position to domestic suppliers [EC 2012]. The main sectors affected by access barriers are the construction sector (e.g. building materials), transport equipment sector (e.g. railway equipment, trains and other urban transport equipment) as well as public service sectors (e.g. water treatment).

At the operational level European companies indicated numerous barriers which hinder them from effective participation in calls for tenders. One of the barriers is language as most of subsequent inquiries and administrative procedures are in Japanese [Griek 2014]. Although some progress has been made in this area the complete information in English is rarely available. Some progress would be made if the use of English for tender proposals (or at least e.g. for technical specifications) was allowed [EU-Japan BRT 2015]. Another problem is also access to information, as mentioned above. This should be eliminated by ensuring access to procurement information relating to all Japanese procuring entities via a central portal. Additionally, compatibility between the EU's and Japan's e-procurement systems would support better access to information in a comparable way [EC 2012]. Even more complex obstacle for EU companies submitting tender proposals are standards and qualifications that must be met by a bidder. As a basis for this in most cases are exclusively used the Japanese Industrial Standards, which are only partially compatible with international standards [Griek 2014].

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Serious limitations result also from different regulations in reference to thresholds applied for public procurement in Japan. For example for construction works (at sub-central government entities) in Japan only contracts on works above 15 million SDR are open to foreign bidders, while the same threshold in the European Union amounts to only 5 million SDR [Sunesen et al. 2009]. This makes that many contracts with lower value in Japan are not covered by the WTO regulations on public procurement and as such are inaccessible for foreign suppliers. The issue could be resolved by lowering the threshold for public tenders to levels used in other countries, including the EU.

Many concerns arise also around the already mentioned “operational safety clause" used frequently in the procurement of railway equipment for Japan Railways and other urban transport operators. The clause gives the right to limit access to contracts due to the legitimate objective of safety, which is often used to hinder access for external/foreign suppliers. Although the right of using the clause was granted to Japan under the WTO Government Procurement Agreement, European business states that the clause has never been clearly defined by the Japanese side and is applied to contracts that could be realized by foreign companies with complementing necessary security standards [ESF 2010].

CONCLUSIONS

The existing barriers for European exporters are mostly of non-tariff character (there are relatively low tariffs for goods imported to Japan from the EU). This creates situation in which the issue of non-tariff barriers should be addressed as the biggest challenge for European negotiators in improving access to the Japanese market for European exporters. The non-tariff barriers are especially burdensome in sectors of a great importance to the EU exports (processed food and agricultural products, pharmaceuticals and transport equipment) and in sectors, where currently applied tariffs remain relatively low.

Although there are still some tariff peaks in different product groups (e.g. processed food and agricultural products, leather, footwear), the non-tariff barriers remain one of the main stumbling blocks slowing down the progress of the whole EU-Japan FTA negotiations [Nelson 2012]. The low harmonization of standards with those recognized commonly in the world (also by international organizations such as e.g. UNECA) and the lack of transparency of existing national regulations and processes (e.g. licensing) are listed among the most burdensome barriers to trade and investments.

Not only manufacturers, but also many European service companies (mostly in finance, banking, telecommunication, postal services and transport) face discriminatory treatment at the Japanese market through domestic national regulations for specific sectors, restrictions introduced by local authorities as well as non-transparent (and sometimes unique compared to global environment) regulations relating to foreign direct investments and competition policy. European

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exporters/investors face also many barriers in access to Japanese public procurement sector. Main problematic issues in this area include the lack of single public procurement offers database, unclear qualification conditions, restricted tenders list, high value thresholds for contracts open to foreign providers and required experience in providing goods and services in Japan.

The economic potential of the EU and Japan make the future free trade agreement one of the most important trade frameworks between developed countries. The successful conclusion of the ambitious and comprehensive EU-Japan FTA, and through this tackling the differences between economic and business systems of the European Union and Japan, is of crucial importance to both partners not only to stimulate bilateral economic and trade links, but also to give a new impetus for economic growth on both sides. As stated in many analysis and comments, Japanese FTAs, including that being negotiated with the EU, might be used by politicians as an argument for reforms and restructuring of some Japanese economy sectors (as a next step of '*Abenomics*'), which should be implemented whether the comprehensive agreement will be finally achieved or not.

Stronger presence of European business (especially in services) in Japan, also through foreign direct investments, should increase competition at this relatively restricted market and stimulate increase in competitiveness of many sectors of Japan's economy. The forecasted impact of the comprehensive EU-Japan free trade agreement indicates that the GDP of partners - the EU and Japan - would increase by 0.8% and 0.7% respectively. Moreover, the EU export could increase by 32.7%, while Japan's export to the EU would expand by 23.5% [EC 2012]. As the economic relations during the last decade have been considered to be below economic potential of both partners, the new agreement should support revitalization and actuation of bilateral trade and investment links.

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