



**Statement before the House Ways and Means
Subcommittee on Trade**

“U.S. – Japan Trade Agreements”

A Testimony by:

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Introduction

Chairman Blumenauer, Ranking Member Buchanan, Members of the Subcommittee, thank you for this chance to offer my thoughts on the trade agreements between the United States and Japan announced by President Donald Trump and Prime Minister Shinzo Abe on September 25, 2019.¹

The U.S.-Japan agreements represent a step forward. The main deal helps redress the imbalance of market access in Japan for many U.S. agricultural exporters that has existed since the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) went into force in December 2018. The digital trade agreement reinforces important principles and disciplines in this critical area of 21st century commerce. The agreements also lift a cloud of uncertainty over the U.S.-Japan relationship created by bilateral trade tensions and allow the two countries to focus on other priorities in their vital alliance.

However, the September agreements fall far short of maximizing the potential of the U.S.-Japan economic relationship.² They leave on the table numerous other market-access commitments made by Japan and the United States in the Trans-Pacific Partnership (TPP), from which President Trump decided to withdraw shortly after he took office in early 2017. The September accords do not fulfill the Trump administration's promise to negotiate a comprehensive free trade agreement (FTA) with Japan; in doing so, they may run afoul of Congressional intentions under the 2015 grant of trade promotion authority (TPA), as well as World Trade Organization (WTO) requirements that such agreements cover "substantially all trade." Perhaps most important, this mini-deal does not do nearly enough to advance the shared U.S. and Japanese interest in updating and upholding the rules of the global economic order, which faces many internal and external stresses.³

Benefits of U.S.-Japan Economic Ties

For decades, the U.S.-Japan economic relationship has brought enormous benefits to both countries. Japan is the world's third-largest economy, with a gross domestic product of about \$5 trillion, and the fourth-largest goods trading partner of the United States. Roughly \$300 billion of total two-way trade flowed between the countries in 2018.⁴ Japan is one of the largest and most profitable markets for U.S. companies in sectors from pharmaceuticals to financial services. In the other direction, Americans are avid consumers of Japanese brands from Toyota to Uniqlo, while Japan is an integral part of U.S. supply chains. In 2018, over 100 of Apple's supplier manufacturing sites were in Japan.⁵ Companies such as Japan Display, which manufactures

¹ Matthew P. Goodman, Dylan Gerstel, Nicholas Szechenyi, and Michael J. Green, "The U.S.-Japan Trade Deal," Center for Strategic & International Studies, September 25, 2019, <https://www.csis.org/analysis/us-japan-trade-deal>

² Matthew P. Goodman, "Scoring the Trump-Abe Trade Deal," Center for Strategic & International Studies, October 1, 2019, <https://www.csis.org/analysis/scoring-trump-abe-trade-deal>

³ John J. Hamre et al., "Home and Abroad: Building U.S. Global Economic Leadership on Strong Domestic Foundations," Center for Strategic & International Studies, July 2019, <https://www.csis.org/analysis/home-and-abroad-building-us-global-economic-leadership-strong-domestic-foundations>

⁴ Japan Factsheet, Office of the United States Trade Representative, <https://ustr.gov/countries-regions/japan-korea-apec/japan>

⁵ Apple Supplier List, Apple Inc, <https://www.apple.com/supplier-responsibility/pdf/Apple-Supplier-List.pdf>

liquid crystal displays for Apple's iPhone screens, have long provided sophisticated technologies for American consumer goods.⁶

Japan is also the third-largest source of foreign direct investment (FDI) in the United States. Through 2018, Japanese companies had invested nearly \$500 billion in the United States, with total investment more than doubling over the last ten years.⁷ Many Congressional districts have Japanese companies operating in them, bringing growth and jobs to your constituents. For example, Toyota recently announced it would invest \$13 billion in the United States from 2017-2021, and Honda has invested \$5.6 billion here over the past five years.⁸ As of 2017, U.S. affiliates of Japanese-owned companies employed over 885,000 Americans.⁹

Yet U.S.-Japan trade and investment ties could be even stronger. Japan remains a difficult market for U.S. companies to penetrate. High tariffs or quotas remain on key U.S. agriculture products. Uneven regulatory enforcement and discriminatory attitudes towards foreign companies pose challenges for U.S. investors. Although Prime Minister Abe pledged to improve the investment climate, Japan continues to have the lowest inward FDI rates relative to total output of any major OECD country.¹⁰

These obstacles point to the need for continued trade and investment negotiations between the United States and Japan. But there is an even more compelling case for greater U.S. economic engagement with Japan. As the world's first- and third-largest economies, with many shared interests and values, the United States and Japan have long been champions of an open, transparent, rules-based global economic order. They have worked together in regional and global institutions, from the Asia-Pacific Economic Cooperation (APEC) forum to the International Monetary Fund (IMF), to support existing rules and norms and to create new ones. At a time when the international economic system is under stress from both an erosion of domestic support and the rise of new challengers like China, it is more important than ever that Washington and Tokyo join forces to update and uphold the existing order.

It is worth noting that international economic collaboration is at the heart of the U.S.-Japan alliance.¹¹ Article II of the security treaty of 1960 reads (in full):

⁶ "Japan Display confirms new plant, source says for Apple," *Reuters*, March 6, 2015, <https://www.reuters.com/article/jdi-plant/update-1-japan-display-confirms-new-plant-source-says-for-apple-idUSL4N0W828T20150306>

⁷ Foreign Direct Investment in the U.S.: Balance of Payments and Direct Investment Position Data, U.S. Bureau of Economic Analysis, <https://www.bea.gov/international/di1fdibal>

⁸ "Toyota Solidifies Its Substantial and Growing Investment in U.S.," Toyota Motor Corporation, March 14, 2019, <https://pressroom.toyota.com/toyota-solidifies-its-substantial-and-growing-investment-in-us/>; Honda in America, Honda Motor Company, Ltd., <https://hondainamerica.com/investment/>

⁹ Foreign Direct Investment in the United States, U.S. Bureau of Economic Analysis, <https://www.bea.gov/international/di1fdiop>

¹⁰ 2019 National Trade Estimate Report on Foreign Trade Barriers, Office of the United States Trade Representative, March 2019, https://ustr.gov/sites/default/files/2019_National_Trade_Estimate_Report.pdf

¹¹ Matthew P. Goodman, Ann Listerud et al. "The Article II Mandate: Forging a Stronger Economic Alliance between the United States and Japan," Center for Strategic & International Studies, November 2018, <https://www.csis.org/analysis/article-ii-mandate-forging-stronger-economic-alliance-between-united-states-and-japan>

“The Parties will contribute toward the further development of peaceful and friendly international relations by strengthening their free institutions, by bringing about a better understanding of the principles upon which these institutions are founded, and by promoting conditions of stability and well-being. *They will seek to eliminate conflict in their international economic policies and will encourage economic collaboration between them.*”¹²

Merits of the September Agreements

The agreements announced in September have a number of useful elements. First, the main agreement levels the playing field for U.S. agriculture products in Japan, especially beef, pork, cheese, and wine.¹³ Following U.S. withdrawal from TPP, agriculture exporters from Australia and Canada gained a leg up against American competitors when Japan began to reduce tariffs under CPTPP. Under the September bilateral deal, Japan will eliminate or reduce tariffs on \$7.2 billion of U.S. products, representing more than half of total U.S. agricultural exports to Japan. In return, Washington agreed to reduce or remove tariffs on certain Japanese agricultural and industrial products, including machine tools and steam turbines.

The digital agreement, meanwhile, addresses barriers and rules governing \$40 billion worth of two-way digital trade. Among other things, the agreement prohibits customs duties on electronic transmissions, ensures the free flow of data across borders, prevents data localization, and protects against forced disclosure of proprietary source code and algorithms.¹⁴ These protections mirror those in the U.S.-Mexico-Canada Agreement (USMCA) and the Japanese-led Osaka Declaration on Digital Economy¹⁵ and are an upgrade of the digital chapters in TPP. This “TPP-plus” agreement is valuable and could provide momentum for plurilateral e-commerce talks at the WTO. More broadly, the U.S.-Japan digital trade agreement demonstrates that the United States is willing and able to set positive rules to govern the 21st century economy. This will be critical in pushing back on Chinese attempts to rewrite global digital governance rules to support its authoritarian model.¹⁶

The September agreements also appear to have lifted the immediate threat of Section 232 tariffs on imported Japanese automobiles. The automotive sector was not explicitly mentioned in the September 25 announcement, nor has there been any public commitment by President Trump not to move ahead with the threatened tariffs. However, the joint statement by President Trump and Prime Minister Abe included the following language: “While faithfully implementing these

¹² Japan-U.S. Security Treaty, Ministry of Foreign Affairs of Japan, <https://www.mofa.go.jp/region/n-america/us/q&a/ref/1.html>

¹³ Fact Sheet on Agriculture-Related Provisions of the U.S.-Japan Trade Agreement, Office of the United States Trade Representative, September 2019, <https://ustr.gov/about-us/policy-offices/press-office/fact-sheets/2019/september/fact-sheet-agriculture%E2%80%90related>

¹⁴ Fact Sheet on U.S.-Japan Digital Trade Agreement, Office of the United States Trade Representative, October 2019, <https://ustr.gov/about-us/policy-offices/press-office/fact-sheets/2019/october/fact-sheet-us-japan-digital-trade-agreement>

¹⁵ Satoshi Sugiyama, “Abe heralds launch of ‘Osaka Track’ framework for free cross-border data flow at G20,” *The Japan Times*, June 28, 2019, <https://www.japantimes.co.jp/news/2019/06/28/national/abe-heralds-launch-osaka-track-framework-free-cross-border-data-flow-g20/#.XdLh8VdKgdU>

¹⁶ Samm Sacks, “Beijing Wants to Rewrite the Rules of the Internet,” *The Atlantic*, June 18, 2018, <https://www.theatlantic.com/international/archive/2018/06/zte-huawei-china-trump-trade-cyber/563033/>

agreements, both nations will refrain from taking measures against the spirit of these agreements and this Joint Statement.”¹⁷ Tokyo has interpreted this to mean that the Section 232 tariffs will not be imposed—and that it has the right to suspend implementation of its market-access commitments if Washington reneges on this understanding.

Finally, the September agreements serve the useful purpose of giving Washington and Tokyo more space to attend to other, pressing issues facing their alliance.¹⁸ Trade is important but not the only priority for the two allies. In particular, they have a shared interest in tackling tensions on the Korean peninsula and managing the challenges of a more assertive China.¹⁹

Missing Pieces

Despite these useful elements, the September agreements fall far short of maximizing the potential of the U.S.-Japan economic relationship. For one thing, the deal does not include several market access commitments agreed to in TPP. Most significantly, Washington did not agree to reduce its 2.5 percent tariff on autos and auto parts made in Japan, which would have been gradually phased out under TPP. For its part, Tokyo did not agree to a tariff-free quota on U.S. rice that it would have granted under TPP, and it offered fewer concessions for U.S. dairy and alcohol products.²⁰

But even if the market-access commitments had matched those in TPP, the September agreements would fall far short of a comprehensive framework for U.S.-Japan economic relations. This shortcoming matters for several reasons.

First, as mentioned, a number of market access and related issues in Japan remain unresolved. These range from agriculture tariffs and quotas not covered under TPP to an array of regulatory impediments to U.S. services companies in Japan. A truly comprehensive agreement would seek to address these perennial points of friction in the bilateral relationship.

Second, concerns have been raised that the Trump Administration’s intended use of Section 103(a) of the 2015 TPA authority to unilaterally implement a tariff-only agreement avoids the need for Congressional approval of the deal and subjects it to fewer notification and consultation requirements under TPA.²¹ At a minimum, Congress is likely to insist that it be fully consulted throughout continued negotiations toward a comprehensive deal and have final right of approval.

¹⁷ Joint Statement of the United States and Japan, The White House, September 25, 2019, <https://www.whitehouse.gov/briefings-statements/joint-statement-united-states-japan-2/>

¹⁸ Matthew P. Goodman, “The right course for a better US-Japan alliance,” *Nikkei Asian Review*, April 9, 2019, <https://asia.nikkei.com/Opinion/The-right-course-for-a-better-US-Japan-alliance>

¹⁹ James Andrew Lewis et al., “Meeting the China Challenge: Responding to China’s Managed Economy,” Center for Strategic & International Studies, January 2018, <https://www.csis.org/analysis/meeting-china-challenge>

²⁰ David Lawder, “U.S.-Japan trade deal versus TPP: where it falls short, where it exceeds,” *Reuters*, October 7, 2019, <https://www.reuters.com/article/us-usa-trade-japan/u-s-japan-trade-deal-versus-tpp-where-it-falls-short-where-it-exceeds-idUSKBN1WM0A3>

²¹ Scott Lincicome and Brian Picone, “United States and Japan Reach ‘Agreement in Principle,’ but Questions and Obstacles Remain,” *White & Case*, September 5, 2019, <https://www.jdsupra.com/legalnews/united-states-and-japan-reach-agreement-48082/>

Another legal question is whether the September agreements are consistent with WTO Article XXIV, which requires that regional trade agreements cover “substantially all the trade” between the parties. This concern could be allayed if, as the Trump Administration has asserted, the September agreements are just the first stage of an agreement that will ultimately be comprehensive, since Article XXIV allows parties to negotiate “interim agreements.” But there is considerable doubt about whether the United States and Japan will ever reach a second-stage deal, given distractions in Washington and resistance in Tokyo. Thus, the WTO risk is real.

A final—and arguably most important—point is that the September agreements do not go nearly far enough to advance U.S.-Japan leadership on economic rulemaking. To be sure, the digital agreement is TPP-plus and puts an important stake in the ground about the kind of disciplines the world’s first- and third-largest economies want to see in this critical area. Frankly, however, the digital agreement also highlights how much was lost when the United States walked away from TPP. That far-broader, 12-party deal included new, high-standard rules on behavior of state-owned enterprises, labor and environment standards, regulatory transparency, and an array of other behind-the border issues that impact 21st century trade. Japan deserves credit for salvaging many of these rules by brokering the CPTPP deal among the remaining 11 members of TPP. However, the United States is not part of CPTPP, and the September agreements with Japan fill only part of the hole left by U.S. withdrawal from regional rulemaking efforts.

The Way Forward

On balance, and with due attention to the concerns raised above, I believe the September agreements with Japan usefully advance U.S. interests and are worthy of support. However, they are insufficient. In my view, the United States should build on the existing agreements to deepen our economic engagement with Japan and reestablish U.S. leadership in rulemaking in the Indo-Pacific region and beyond.

There are various ways to do this, which are not necessarily mutually exclusive. One path would be to continue bilateral negotiations toward completion of a comprehensive FTA. Such a deal could address many of the concerns about the September agreements, resolve a number of outstanding U.S. market-access and regulatory issues in Japan, and advance U.S.-preferred trade rules.

However, comprehensive FTA negotiations would require a substantial commitment of time and political capital by both Washington and Tokyo. I am skeptical that either side will be willing to make these stage-two negotiations a priority in 2020, despite their stated intentions. Moreover, a bilateral FTA would be unlikely to maximize U.S. economic interests, as compared with broader approaches.

Even if it does move ahead with stage-two negotiations toward a broader bilateral deal, the United States could—and in my view should—announce its intention to accede to CPTPP. As I argued in Senate testimony earlier this year,²² this would send a strong signal of commitment to

²² Matthew P. Goodman, Testimony on “ARIA in Action: The Benefits of Economic Diplomacy”, U.S. Senate Foreign Relations Committee Subcommittee on East Asia, the Pacific, and International Cybersecurity Policy, May

the Indo-Pacific region—at a time when partners there are uncertain about our staying power. If ultimately concluded, U.S. accession to CPTPP would restore—and potentially expand—the economic gains lost when we withdrew from TPP. With the United States as a member, CPTPP would again encompass 40 percent of the global economy, making it a magnet for other countries in the region (and beyond) hoping to enjoy the large market and high standards it encompasses.

Beyond trade, there are a number of areas of economic policy in which the United States could—and again should—work with Japan and other partners to advance rules and norms that serve U.S. interests. These include infrastructure, energy, and finance. We discussed these areas for expanded U.S.-Japan cooperation in a CSIS report issued in November 2018.²³

Conclusion

The United States has a compelling interest in working with Japan to update and uphold the rules-based economic order. Deepening engagement with an ally that is aligned with the United States on most areas of trade rulemaking will advance U.S. economic and strategic interests in the vital Indo-Pacific region and beyond. The September 2019 agreements announced by President Trump and Prime Minister Abe are a step in the right direction, but there is so much more to do.

I thank you again for the chance to testify and would be happy to answer your questions.

23, 2019, https://csis-prod.s3.amazonaws.com/s3fs-public/congressional_testimony/190522_MattGoodman_Testimony.pdf

²³ Matthew P. Goodman, Ann Listerud et al. “The Article II Mandate: Forging a Stronger Economic Alliance between the United States and Japan,” Center for Strategic & International Studies, November 2018, <https://www.csis.org/analysis/article-ii-mandate-forging-stronger-economic-alliance-between-united-states-and-japan>