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## About the Author

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## **Abstract**

The turn of the European Union (EU) towards the conclusion of mega-regional free trade agreements (FTAs) in the past decade signified the beginning of an ambitious trade policy. Although initially marked by limited success and civil society opposition in certain cases, some of the EU's mega-regional projects have borne fruits. A recent example of such a comprehensive agreement is the EU-Japan Economic Partnership Agreement (EPA). Drawing on historical institutionalism, this paper aims to explain why the EU negotiates mega-regional FTAs, to illustrate these motivations through a case study of the EU-Japan EPA, and to examine likely implications of EU mega-regionals for the partners to the agreements, third countries and the multilateral trading system.

The paper argues that the stalemate of the World Trade Organisation (WTO), which triggered the 2006 Global Europe Strategy, constitutes a critical juncture that opened the path towards mega-regional agreements. Furthermore, the EU's long-standing practice of promoting rules and values in its trade relations, as well as the more recent path created by the 'template' of the Comprehensive Economic and Trade Agreement between the EU and Canada (CETA), contribute to the motivations of the EU to conclude mega-regionals.

In the case of the EU-Japan EPA, agreements such as the Transatlantic Trade and Investment Partnership (TTIP), the Trans-Pacific Partnership (TPP) and CETA acted as critical junctures. Power asymmetries and bargaining help explain how the EU and Japan succeeded in negotiating a comprehensive EPA, including some pioneering elements such as climate change and corporate governance. Among the likely implications of EU mega-regionals are positive feedback effects, such as economic growth for the partners to the mega-regionals, domino effects inducing non-members of mega-regionals to join the bloc, as well as the (unintended) consequences of mega-regionals for the multilateral trading system.

## Introduction: from multilateral trade negotiations to mega-regionals

Bilateral and regional trade agreements have existed alongside the multilateral trading system of the World Trade Organisation (WTO) for quite some time.<sup>1</sup> In recent years, despite the WTO Doha Round, the number of such regional agreements has been on the rise. For some of the more encompassing, complex and politically significant agreements, the term ‘mega-regional’ has been coined.<sup>2</sup> The EU has negotiated several mega-regionals, such as the Transatlantic Trade and Investment Partnership (TTIP) or the EU-Canada Comprehensive Economic Trade Agreement (CETA). The TTIP negotiations were launched in 2013, faced significant hurdles and ended without conclusion at the end of 2016.<sup>3</sup> Despite the uncertainty surrounding the policy of the Trump administration and the global slowdown of trade, the EU has remained on the path of free trade agreements (FTAs).<sup>4</sup> While widely debated in policy circles and by the wider public, CETA provisionally entered into force in September 2017 and still awaits ratification by some national – and some regional – parliaments in EU countries, before it can take full effect.<sup>5</sup> Despite the complex and long negotiation processes, at times accompanied by civil society opposition, that characterise mega-regional agreements, the recent example of the EU-Japan Economic Partnership Agreement (EPA) stands out as a successful negotiation of a comprehensive agreement between like-minded partners. The EPA is to date the biggest trade deal of the EU having fully entered in force.

This paper aims to explore why the EU negotiates such mega-regional agreements, to check these motivations in a case study of the EU-Japan EPA, and to discuss how these agreements may impact the parties involved, other global actors and the multilateral trading system as a whole. It draws on historical institutionalism to explain the turn of the EU towards mega-regionals. This theory allows for the study of

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<sup>1</sup> P.T. Stoll, “Mega-Regionals: Challenges, Opportunities and Research Questions”, in T. Rensmann (ed.), *Mega-Regional Trade Agreements*, Augsburg, Springer, 2017, p. 3.

<sup>2</sup> *Ibid.*, pp. 3-4.

<sup>3</sup> European Commission, *The Transatlantic Trade and Investment Partnership (TTIP)*, DG Trade, updated 15 April 2019, retrieved 20 June 2020, <http://ec.europa.eu/trade/policy/in-focus/ttip>.

<sup>4</sup> “Increase in policy uncertainty may account for up to 75 percent of the worsening of the trade slowdown in 2016”: C. Constantinescu *et al.*, “Trade Developments in 2016: Policy uncertainty weighs on world trade”, World Bank Group, Washington D.C., 21 February 2017, p. 7.

<sup>5</sup> European Commission, *EU-Canada Comprehensive Economic Trade Agreement (CETA)*, DG Trade, updated 12 April 2019, retrieved 16 July 2020, <http://ec.europa.eu/trade/policy/in-focus/ceta>.

institutional changes from a chronological perspective, taking into account the sequence of events. It thus offers a dynamic view of institutional changes over time. The different explanatory factors reveal “patterns of institutional reproduction and change”.<sup>6</sup> The combination of a chronological and institutional approach is also particularly useful for the case study of the EU-Japan EPA, as it can provide an explanation for the shift in EU-Japan relations, from indifference to a comprehensive like-minded partnership.<sup>7</sup> At the same time, discussing the origins and likely impacts of mega-regionals, and elaborating on the identified motivations through the case study of the EU-Japan EPA, may provide possible insights for the path the EU policymakers could pursue regarding trade policy in the future.

The paper follows an hourglass structure, as it will move from a general section on the motivations behind the negotiation of mega-regionals, to the specific case study of the EU-Japan EPA, and then return to a more general section on the likely implications of mega-regional FTAs on the bilateral, global and multilateral level.

## Framework of analysis

This section briefly introduces the main analytical tools to be used throughout the paper. It first provides a definition for the term ‘mega-regional trade agreement’ and discuss whether the EU-Japan EPA can be considered as one. It then introduces the key concepts of historical institutionalism that will serve as factors to explain the EU’s turn towards such comprehensive regional agreements.

### *What are ‘mega-regionals’?*

There are multiple voices in the literature regarding what the first part of the term (‘mega-’) entails. According to some definitions, ‘mega’ implies more than two partners and would thus mean a plurilateral agreement, such as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP).<sup>8</sup> However, an agreement between only two partners can also be considered as a mega-regional

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<sup>6</sup> O. Fioretos, “Historical Institutionalism in International Relations”, *International Organisation*, vol. 65, no. 2, 2011, p. 374 [hereafter, “Fioretos (2011)”].

<sup>7</sup> F. Waldenberger, “EU-Japan Relations – Past, Present and Future”, *Fondation France-Japon de l’EHESS Paris*, 2019, retrieved 20 June 2020, <http://ffj.ehess.fr/index/article/303/eu-japan-relations-past-present-and-future.html>.

<sup>8</sup> Bilaterals, “Mega-regional FTAs”, *bilaterals.org*, October 2016, retrieved 20 June 2020, <https://www.bilaterals.org/mega-regional-ftas>.

if the partners are very large trading entities, given the economic magnitude of such an agreement.<sup>9</sup> Riffel argues that “the term ‘mega-regionals’ describes a trend in international trade law to negotiate FTAs among countries encompassing a considerable share of world trade”.<sup>10</sup> Indeed, mega-regional trade agreements have also been defined as “partnerships between countries or regions with a major share of world trade and foreign direct investment”, which “beyond simply increasing trade links ... aim to improve regulatory compatibility and provide a rules-based framework for ironing out differences in investment and business climates”.<sup>11</sup> According to this definition, the term ‘mega’ refers to the size of the economies of the negotiating parties, as well as to the high level of ambition.<sup>12</sup> Finally, while a study for the European Parliament requires that an agreement needs to comprise three or more countries or regional groupings in order to be considered a mega-regional, it goes on to argue that the EU, comprising 27 countries, meets this criterion in all of its bilateral agreements.<sup>13</sup>

Therefore, the term ‘mega’ does not necessarily imply a plurilateral agreement. For the purpose of this paper, a mega-regional trade agreement is a deep integration partnership among large economies that is meant to “transform and shape the international economic order and ... promote more far-reaching geopolitical goals”.<sup>14</sup> As argued for example by Solis and Urata or by Frey, the EU-Japan agreement is considered a mega-regional FTA.<sup>15</sup> Furthermore, already the Commission’s impact assessment indicated that the “EU-Japan FTA can be seen against the broad background of developments in FTAs and in particular the ‘mega-

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<sup>9</sup> Interview with P. Lamprecht, Senior Economist at ECIPE Brussels, 12 February 2019.

<sup>10</sup> C. Riffel, “Encyclopedia Entry: Mega-regionals”, *Max Planck Encyclopedia of Public International Law*, December 2016, ), updated December 2016, retrieved 2 July 2020, <http://opil.ouplaw.com/view/10.1093/law:epil/9780199231690/law-9780199231690-e2177>.

<sup>11</sup> T. Hirst, “What are mega-regional trade agreements?”, *World Economic Forum*, 9 July 2014, retrieved 18 June 2020, <https://www.weforum.org/agenda/2014/07/trade-what-are-megaregionals>.

<sup>12</sup> P. Lamy, “Is trade multilateralism being threatened by regionalism?”, *Adelphi Papers*, vol. 54, no. 450, October 2014, p. 67.

<sup>13</sup> European Parliament, *Impacts of the CETA agreement on developing countries*, Study - EP/EXPO/B/FWC/DEVE/2013-08/Lot5/13, Brussels, February 2017, p. 12.

<sup>14</sup> S. Griller et al., *Mega-Regional Trade Agreements New Orientations for EU External Relations*, Oxford, Oxford University Press, 2017, p. 3.

<sup>15</sup> M. Solis & S. Urata, “Abenomics and Japan’s Trade Policy in a New Era”, *Asian Economic Policy Review*, January 2018, vol. 13, no. 1, p. 107; C. Frey, “Mega-Regional Trade Agreements and Post-2015 Climate Protection: Bridging the Gap”, *Journal for European Environmental and Planning Law*, vol. 12, no. 3-4, 2015, p. 268.

regional' agreements".<sup>16</sup> As Ponjaert argues, "the sheer size of the economies involved makes any trade agreement between Japan and the EU of systemic importance".<sup>17</sup> The EU and Japan together cover one third of the global gross domestic product (GDP) and one fifth of global trade, and the EPA is thus so far the EU's biggest FTA to have fully entered into force.<sup>18</sup> The EPA covers more than 600 million people, around 30% of the world GDP and 37% of world trade.<sup>19</sup> Next to the "traditional" provisions on trade in goods or services, the EPA includes some of the "strongest commitments to environmental protection, labour and sustainable development ever contained in a trade deal"; what is more, the EPA is the first and only international trade agreement to include a clear commitment to fight climate change and support the implementation of the Paris Agreement.<sup>20</sup>

In view of its economic importance and comprehensiveness, the EU-Japan EPA qualifies as a mega-regional trade agreement. The following subsection defines components of historical institutionalist theory that will then be used to explain why the EU negotiates such agreements.

#### *A historical institutionalist approach*

According to Fioretos, historical institutionalism redefines its object "from one directed at the study of stationary outcomes to one focused on explaining diverse and dynamic processes of institutional development".<sup>21</sup> First of all, institutions, according to North, are "the rules of the game in a society or, more formally, ... the humanly devised constraints that shape human interaction".<sup>22</sup> Applying this definition to a trade agreement, whose role it is to shape the rules governing trade relations between two partners, allows one to consider such an agreement as a type of institution. Thus, the way mega-regional agreements are negotiated, as well as their

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<sup>16</sup> European Commission, *Trade Sustainability Impact Assessment of the Free Trade Agreement between the European Union and Japan*, Final Report, DG Trade, Brussels, 2016, p. 52 [hereafter, "Impact Assessment"].

<sup>17</sup> F. Ponjaert, "The Political and Institutional Significance of an EU-Japan Trade and Partnership Agreement", in P. Bacon *et al.* (eds.), *The European Union and Japan: A New Chapter in Civilian Power Cooperation?*, Surrey, Ashgate Publishing, 2015, p. 86.

<sup>18</sup> Interview with representatives of the Japan Business Council Europe (JBCE), 8 April 2019.

<sup>19</sup> Interview with members of the Delegation of the European Union to Japan in Tokyo (EEAS), 29 March 2019.

<sup>20</sup> *Ibid.*

<sup>21</sup> *Ibid.*, p. 371.

<sup>22</sup> D.C. North, *Institutions, Institutional Change and Economic Performance*, Cambridge, Cambridge University Press, 1990, p. 3.



development over time, can be examined through the lens of historical institutionalism. The paper will use some of the key elements of this theory, including critical junctures, path dependences, the role of power asymmetry, unintended consequences, sequence and positive feedback effects.

*Critical junctures* are “moments where substantial institutional change takes place thereby creating a ‘branching point’ from which historical development moves onto a new path”.<sup>23</sup> If these paths manage to shape “the subsequent trajectory in ways that make alternative institutional designs substantially less likely to triumph”, a new *path dependence* is created.<sup>24</sup> Path dependences may render a reversal of the initial choice difficult.<sup>25</sup> When a path towards a certain direction is created, this may induce further steps in the same direction, and this “is even more likely when over time the relative benefits compared to other options and the costs of exit and policy change increase”.<sup>26</sup> Regarding institutions as “carriers of history” allows to examine how different policies, strategies and patterns of behaviour existing within institutions, through time, led towards the mega-regional path.<sup>27</sup>

Another important concept in historical institutionalism is the role of *power asymmetry*, which occurs when the “power relations present in existing institutions give some actors or interests more power than others over the creation of new institutions”.<sup>28</sup> As Bayne and Woolcock argue, relative economic power is one of the factors shaping economic diplomacy and a major determinant of the outcome of economic negotiations.<sup>29</sup> As one of the biggest markets and trading entities in the world, the EU can exert more bargaining power and benefit from the fact that its partners may have a stronger desire to conclude an agreement.<sup>30</sup> Furthermore, in

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<sup>23</sup> P.A. Hall & R.C. Taylor, “Political Science and the Three New Institutionalisms”, *Political Studies*, XLIV, 1996, p. 942.

<sup>24</sup> Fioretos (2011), *op. cit.*, p. 376.

<sup>25</sup> M. Levi, “A Model, a Method, and a Map: Rational Choice in Comparative and Historical Analysis”, in M. Lichbach & A. Zuckerman (eds.), *Comparative Politics: Rationality, Culture and Structure*, Cambridge, Cambridge University Press, 1997, p. 28.

<sup>26</sup> S. Gstöhl, “Theoretical Approaches to the European Neighbourhood Policy”, in S. Gstöhl & S. Schunz (eds.), *Theorizing the European Neighbourhood Policy*, London, Routledge, 2017, p. 8.

<sup>27</sup> P.A. David, “Why Are Institutions the ‘Carriers of History’? Path Dependence and the Evolution of Conventions, Organizations and Institutions”, *Structural Change and Economic Dynamics*, vol. 5, no. 2, 1994, p. 205.

<sup>28</sup> Hall & Taylor, *op. cit.*, p. 954.

<sup>29</sup> N. Bayne & S. Woolcock, *The New Economic Diplomacy: Decision-making and Negotiation in International Economic Relations*, Surrey, Ashgate, 3<sup>rd</sup> edn, 2011, p. 6.

<sup>30</sup> Interview with P. Lamprecht, *op. cit.*

the international arena, attention is paid to the *sequence* in which trade agreements are concluded and this 'sequencing game' is another important aspect of the negotiation process.<sup>31</sup> According to historical institutionalist theory, "the sequence of political events can have a causal effect for later developments" and therefore should be examined, especially because "the order in which things happen can affect the interests of political actors, their ability to shape outcomes, and thus also the direction of history".<sup>32</sup>

Finally, when it comes to the likely implications of mega-regionals, a focus will be placed on *positive feedback effects*, which "exist when the choice of multiple individuals generates positive externalities", leading to a self-reinforcing behaviour and the wish to remain on the path that created these effects.<sup>33</sup> Moreover, likely implications in the form of *unintended consequences* will also be examined. According to Pierson, these occur in situations, where actors that "may be in a strong initial position, seek to maximize their interests, and nevertheless carry out institutional and policy reforms that fundamentally transform their own positions (or those of their successors) in ways that are unanticipated and/or undesired".<sup>34</sup>

The following section addresses the question why the EU negotiates mega-regional agreements. While the motivation behind a given mega-regional agreement is case-specific and depends on the countries involved and the point in time, some general motivations of the EU can be identified in light of historical institutionalism.<sup>35</sup>

### **Motivations of the EU to negotiate mega-regionals**

This section first argues that the stalemate in the WTO triggering the EU's 2006 Global Europe Strategy was a critical juncture leading to the creation of the mega-regional path. Second, the EU's traditional dependence on its values-based, standard-setting path, as well as a new path dependence since CETA will be discussed. Third, the

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<sup>31</sup> *Ibid.*

<sup>32</sup> Fioretos (2011), *op. cit.*, pp. 381, 382.

<sup>33</sup> *Ibid.*, p. 377.

<sup>34</sup> P. Pierson, "The Path to European Integration: A Historical Institutional Analysis", *Comparative Political Studies*, vol. 29, no. 2, 1996, p. 126.

<sup>35</sup> S. Schwab & K. Bhatia, "The Rationale behind Mega-regionals – Two Views", in *Mega-regional Trade Agreements: Game-Changers or Costly Distractions for the World Trading System?*, Report, World Economic Forum, July 2014, p. 18.

paper elaborates on the role of power asymmetries and bargaining, shedding light on deeper integration ambitions and economic motivations.

*Critical juncture: from Doha 2001 to 'Global Europe' 2006*

The concept of critical juncture can be understood as a “turning point”, a moment of “structural indeterminacy and fluidity” allowing for options of institutional innovation.<sup>36</sup> The motivation of the EU to shift towards mega-regional agreements will be elaborated as a consequence of a critical juncture leading to the mega-regional path: the stagnation of the Doha Development Round, which triggered the European Commission’s 2006 Global Europe Strategy.

One of the main motivations for the EU and other actors to pursue the mega-regional path is the fact that, since the Doha Development Round failed to produce significant results in liberalising trade, alternative ways towards liberalisation needed to be found.<sup>37</sup> This negotiation deadlock in the WTO led to a major shift towards bilateral FTAs. Interestingly, since the Mongolia-Japan agreement of February 2015, there is not a single member of the WTO that is not party to a preferential trade agreement.<sup>38</sup> This situation left the world trade landscape with a dense web of agreements and a complex interplay among multiple trade regimes.<sup>39</sup> In order to increase clarity and consistency, but also to help in transforming the international economic order despite the paralysis in the WTO, the mega-regional path was opened to “plurilateralise” this complex web of bilateral agreements.<sup>40</sup> Thus, the Doha stalemate marked a “branching point” at a critical juncture.<sup>41</sup>

Since 1999 the EU was following the so-called ‘Lamy doctrine’ – named after the EU Trade Commissioner at that time –, which introduced a moratorium on the conclusion of bilateral FTAs in order to demonstrate the EU’s commitment to the multilateral trading system and the new WTO round.<sup>42</sup> However, by 2005, it became clear that an

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<sup>36</sup> G. Capoccia, “Critical Junctures”, in O. Fioretos *et al.* (eds.), *The Oxford Handbook of Historical Institutionalism*, Oxford, Oxford University Press, 2016, pp. 89, 101.

<sup>37</sup> M.S. Akman, “Global Trade Governance and G20: A Response to Mega-Regional Trade Agreements”, *Rising Powers Quarterly*, vol. 1, no. 1, 2016, p. 85.

<sup>38</sup> Frey, *op. cit.*, p. 267.

<sup>39</sup> Lamy, *op. cit.*, p. 61; Griller, *op. cit.*, p. 5.

<sup>40</sup> Griller, *op. cit.*, pp. 5, 7.

<sup>41</sup> Hall & Taylor, *op. cit.*, p. 942.

<sup>42</sup> S. Gstöhl & D. De Bièvre, *The Trade Policy of the European Union*, London, Palgrave, 2018, p. 129.

agreement would not be in sight, despite EU efforts to satisfy the demands of developing countries.<sup>43</sup> Thus, in 2006, the EU stated in its "Global Europe - Competing in the World" strategy that, while remaining committed to multilateralism and the WTO, it would implement a more strategic bilateral approach.<sup>44</sup> This Communication produced a shift in the EU's broader trade policy orientation and many of the regulatory issues that the EU tried to address through the Doha Round became instead the subject of bilateral or regional agreements.<sup>45</sup> At the core of these ambitious agreements is the aim to increase the market potential of the EU, while exporting regulatory standards and promoting "a model of development based on sustainability standards and human rights".<sup>46</sup>

The EU's commitment to remain on this path was recently reaffirmed by Trade Commissioner Hogan who underlined the importance of reinforcing even "stronger alliances with like-minded partners", especially in light of current challenges which include the Covid-19 response.<sup>47</sup> The model of "open strategic autonomy" that the EU wishes to follow includes getting the maximum from the network of EU trade deals.<sup>48</sup> This demonstrates what will be elaborated in the following subsection, namely a path dependence of the EU in pursuing a strategy of concluding comprehensive mega-regional FTAs, in order to set innovative standards.

#### *Path dependence: standard-setting and the 'CETA template'*

Further motivations of the EU to conclude mega-regionals can be found in certain path dependences, also taking into account the importance of sequence.

Besides economic gains, the wish to set global standards is a core motivation for the conclusion of mega-regionals. EU trade policy falls under Art. 21 TEU, which lays down

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<sup>43</sup> A. Poletti & D. Sicurelli, *The Political Economy of Normative Trade Power Europe*, Cham, Palgrave Macmillan, 2018, p. 24.

<sup>44</sup> European Commission, *Global Europe Competing in the World: A contribution to the EU's growth and jobs strategy*, COM(2006) 567 final, Brussels, 4 October 2006, pp. 8-10 [hereafter, "Global Europe"].

<sup>45</sup> Poletti & Sicurelli, *op. cit.*, p. 24.

<sup>46</sup> *Ibid.*, p. 16.

<sup>47</sup> P. Hogan, Speech at Launch of Public Consultation for EU Trade Policy Review, *EUI Florence*, 16 June 2020, retrieved 20 June 2020, [https://ec.europa.eu/commission/commissioners/2019-2024/hogan/announcements/speech-commissioner-phil-hogan-launch-public-consultation-eu-trade-policy-review-hosted-eui-florence\\_en](https://ec.europa.eu/commission/commissioners/2019-2024/hogan/announcements/speech-commissioner-phil-hogan-launch-public-consultation-eu-trade-policy-review-hosted-eui-florence_en).

<sup>48</sup> *Ibid.*

the principles upon which EU external action is based: democracy, the rule of law, human rights, solidarity and the promotion of multilateral solutions.<sup>49</sup> “Trade negotiations represent a preferential arena for the EU to emerge as a normative leader internationally” also for the EU’s ambitions to conclude mega-regional agreements.<sup>50</sup> A trade agenda promoting sustainable development, human rights and good governance, and, in that sense, consistency of trade policy with other areas of the EU’s external action, is at the core of the EU ‘Trade for all’ strategy of 2015.<sup>51</sup> Two years later, the European Commission highlights the importance of “safeguarding high European standards of environmental, consumer, social and labour protection as well as fundamental rights without compromise”.<sup>52</sup> In the 2017 Communication, the EU remains on the mega-regional, bilateral path by expanding its partnerships to Australia and New Zealand.<sup>53</sup> Mega-regional agreements do not simply seek to increase trade between the partners at the bilateral or regional level. They also have the potential to (at least partly) fill the gap that was created with the stalemate at the WTO. An inherent value of two large trading entities coming together in a bilateral mega-regional agreement is to define among themselves standards, which could be exported to third parties.<sup>54</sup> Thus, standard setting is an important motivation behind negotiating mega-regional agreements.

The sequence of events is a very useful factor to explain trade negotiations and in particular the efforts to set standards. In the international arena, attention is paid to the order in which agreements are negotiated and deals are made. For instance, post-Brexit the UK will find itself at the back end of the sequence of trade agreements, and, given its smaller size, its bargaining power vis-à-vis other countries will be weaker compared to the EU’s.<sup>55</sup> On the flipside of this coin is the need to be among the first in the sequence, in order to define the rules of the game before others do so. “It is easier to help write rules now than to accede to them later”, where there is much less room for the promotion of one’s interests.<sup>56</sup>

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<sup>49</sup> European Union, Consolidated version of the Treaty on European Union, *Official Journal of the European Union*, C 326, 26 October 2012, Art. 21 TEU.

<sup>50</sup> Poletti & Sicurelli, *op. cit.*, p. 15.

<sup>51</sup> European Commission, *Trade for All: Towards a more Responsible Trade and Investment Policy*, COM(2015) 497 final, 19 October 2015, p. 15.

<sup>52</sup> European Commission, *A Balanced and Progressive Trade Policy to Harness Globalisation*, COM(2017) 492 final, Brussels, 13 September 2017, p. 4 [hereafter, “Communication 2017”].

<sup>53</sup> *Ibid.*, p. 2.

<sup>54</sup> Interview with P. Lamprecht, *op. cit.*

<sup>55</sup> *Ibid.*

<sup>56</sup> Schwab & Bhatia, *op. cit.*, p. 19.

Furthermore, CETA has created a new path dependence for the EU in the negotiations of mega-regionals by serving as a 'template' for future agreements.<sup>57</sup> In 2016 EU Trade Commissioner Malmström considered CETA to constitute a model of EU agreements.<sup>58</sup> When CETA was created, it was "in all probability the most lengthy and complex FTA ever drafted", including provisions on sustainable development, environmental and labour standards, and the regulation of e-commerce.<sup>59</sup> The French Minister of State for Foreign Trade in 2016, Matthias Fekl, argued that the provisions of CETA should serve as a template for other ambitious EU agreements, such as TTIP, which was still under negotiation in April 2016, when CETA was concluded.<sup>60</sup> In essence, CETA was the first in a line of EU agreements, for which the term "new generation FTAs" has been coined, as they contain, "in addition to the classical provisions on the reduction of customs duties and of non-tariff barriers ..., provisions on ... intellectual property protection, investment, public procurement, competition and sustainable development".<sup>61</sup> CETA created a path the EU has followed for the negotiation of its subsequent ambitious agreements.<sup>62</sup> Therefore, CETA also acted as a critical juncture, creating a new path for the EU's pursuit of the ambitious, mega-regional path.

### *The role of power asymmetries and economic motivations*

Power asymmetry plays a significant role in bilateral FTAs, where the EU, given its economic significance, can exert more bargaining power vis-à-vis smaller partners. Even though mega-regionals are negotiated among relatively equal partners, there

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<sup>57</sup> Example for the 'template' characterisation: F. Simon, "France sees the EU-Canada agreement as a 'template' for TTIP", *euractiv*, 8 March 2016, retrieved 15 June 2020, <https://www.euractiv.com/section/trade-society/news/france-sees-the-eu-canada-agreement-as-a-template-for-ttip>.

<sup>58</sup> C. Malmström, "Signing our trade agreement with Canada", *Blog post – European Commission*, 30 October 2016, retrieved 16 July 2020, [https://www.europa-nu.nl/id/vk8rc7cj14zz/nieuws/signing\\_our\\_trade\\_agreement\\_with\\_canada?ctx=vhyzn0ozwmz1&tab=0](https://www.europa-nu.nl/id/vk8rc7cj14zz/nieuws/signing_our_trade_agreement_with_canada?ctx=vhyzn0ozwmz1&tab=0).

<sup>59</sup> A. De Mestral, "When Does the Exception Become the Rule? Conserving Regulatory Space under CETA", *Journal of International Economic Law*, vol. 18, no. 3, September 2015, pp. 641, 642.

<sup>60</sup> cited in Simon, *op. cit.*

<sup>61</sup> Court of Justice of the European Union, *The free trade agreement with Singapore cannot, in its current form, be concluded by the EU alone*, Press Release no. 52/17, Luxembourg, 16 May 2017.

<sup>62</sup> S. Chowdry *et al.*, "The EU-Japan Economic Partnership Agreement", *Bruegel Special Report*, Brussels, 28 September 2018, retrieved 14 July 2020, [http://bruegel.org/wp-content/uploads/2018/10/EXPO\\_STU2018603880\\_EN.pdf](http://bruegel.org/wp-content/uploads/2018/10/EXPO_STU2018603880_EN.pdf), p. 8.

are still certain asymmetries depending on specific aspects or policy areas. While the bargaining power asymmetries may be smaller between equal partners, reaching an agreement can be all the more invaluable, as the EU cannot “dictate terms”, but has to accept “the prospect of meaningful concessions” to gain improved access to another large market; this “raises the stakes” for the parties and can offer a motivation to engage in mega-regional talks.<sup>63</sup> Space is therefore provided to negotiate and reach an agreement that goes deeper and touches upon various issues that exceed the traditional tariff-only agreements.

The bilateral approach constitutes a further motivation to negotiate mega-regionals for two reasons: first, because it allows the EU to adopt a more ambitious attitude and open up the scope of the agreement together with its like-minded partner, and, second, because this ambitious approach allows for substantial economic and commercial gains.

The power play and negotiation tactics when only two players are involved allow for a broadening of the areas covered by an agreement. This is even more crucial because of the impossibility to achieve such an ambitious scope within the WTO. And even if the Doha Round had not failed, the WTO might still not be the most adequate arena to pursue broader issues, such as regulatory aspects and important ‘behind-the-border’ measures: “existing WTO rules and member-specific obligations are perceived as being unsatisfactory, as they often tend to reflect the lowest common denominator”.<sup>64</sup> At the multilateral level, there are areas not appropriately covered yet, such as trade in services, investments, technical standards, and regulatory issues (referred to as WTO+ and WTO-x, see below).<sup>65</sup> Behind this lack of multilateral coverage are the consensus-based processes at the WTO, as, according to the ‘single undertaking’ principle, “nothing is agreed until everything is agreed”.<sup>66</sup> Therefore, outside of the WTO the “transaction costs for negotiating a wider agenda shall be lower”.<sup>67</sup> Potential hubs created by mega-regionals could open the way towards provisions of unprecedented scope, ranging from intellectual property and

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<sup>63</sup> A.R. Young, *The New Politics of Trade: Lessons from TTIP*, Newcastle upon Tyne, Agenda Publishing, 2017, p. 123.

<sup>64</sup> Griller, *op. cit.*, pp. 4-5.

<sup>65</sup> Akman, *op. cit.*, p. 88.

<sup>66</sup> World Trade Organisation, *How the negotiations are organised*, WTO website, 2020, retrieved 26 June 2020, [https://www.wto.org/english/tratop\\_e/dda\\_e/work\\_organ\\_e.htm](https://www.wto.org/english/tratop_e/dda_e/work_organ_e.htm).

<sup>67</sup> Akman, *op. cit.*, p. 88.

labour standards to environment, climate change or food security. This is why Velut refers to mega-regionals as “no longer confined to trade and investment, but ... (as) international regulatory regimes in their own right”.<sup>68</sup> In an increasingly interconnected economy, with the nature of economic exchange developing and taking new forms, behind-the-border issues are extremely important to address.<sup>69</sup> Therefore, the EU has a strong motivation to ride the new wave of digital globalization and demonstrate its awareness that former trends in financial and trade flows are being overshadowed by “the exponential growth of global data flows”.<sup>70</sup> Within this context, the EU is particularly motivated to follow the mega-regional path because of the opportunity to address non-trade concerns, such as sustainable development and climate change.

At the same time, a key motivation to negotiate mega-regionals are the economic and commercial gains of the partners to such an agreement.<sup>71</sup> The economic impact of mega-regional initiatives is significant, considering that often major actors negotiate these agreements which represent a substantial share of the world GDP.<sup>72</sup> Furthermore, such agreements can improve the competitiveness of industries for both sides of the deal. All in all, the overall positive welfare effects serve as one of the core motivations for the conclusion of mega-regionals.<sup>73</sup>

### Summary

So far, it has been argued that the EU negotiates mega-regional trade agreements for a number of political, economic and systemic/institutional reasons. The stalemate in the WTO Doha Development Round triggering the subsequent 2006 Global Europe strategy was identified as a critical juncture. Moreover, the EU’s standard-setting approach through its trade policy, as well as the use of CETA as a template were identified as important path dependences, keeping the EU at the forefront of the sequencing game and acting as substantial motivations for the conclusion of mega-regionals. Finally, the role of power asymmetries has been elaborated, as the

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<sup>68</sup> J.B. Velut, “Introduction: The political and economic governance of new cross-regionalism”, in J.B. Velut *et al.* (eds.), *Understanding Mega Free Trade Agreements: The Political and Economic Governance of New Cross-regionalism*, London, Taylor and Francis, 2017, p. 10.

<sup>69</sup> *Ibid.*, pp. 4-5.

<sup>70</sup> *Ibid.*, p. 15.

<sup>71</sup> Schwab & Bhatia, *op. cit.*, p. 18.

<sup>72</sup> Griller, *op. cit.*, p. 6.

<sup>73</sup> *Ibid.*



bargaining game with like-minded partners allows the EU to adopt a much wider scope of provisions, while enabling deeper economic benefits to be reaped by both partners.

The following case study illustrates these motivations by discussing to what extent they are valid in the case of the EU-Japan EPA. It complements the analysis with additional elements that are specific for this case.

### **EU-Japan EPA: A historical institutionalist case study**

First of all, it will be examined to what extent previous mega-regionals and especially CETA, but also TTIP and TPP have acted as a critical juncture, creating a path towards the conclusion of the EU-Japan EPA. Second, the importance of the sequence of events will be illustrated by discussing the role of Brexit and the EU-South Korea FTA. The path dependence of the EU as promoter of values and standard setter will be elaborated against the background of a rising China and of the protectionism advocated for by the Trump administration. Third, the role of power asymmetry in trade negotiations will be highlighted by analysing the comprehensive agreement achieved.

#### *TTIP, TPP and CETA as a critical juncture for the EPA*

As discussed above, critical junctures are “initial markers of path-dependent processes”.<sup>74</sup> It will be argued that TPP and TTIP, and in particular the withdrawal of the US from both, pushed the EU and Japan towards the path of concluding the EPA, after a period of ‘functional distance’ between them.<sup>75</sup>

TTIP is well suited to illustrate the positioning of Japan vis-à-vis the US. Historically, there has been a “deeply embedded American bias” in Japanese economic and security relations, and for this reason, Suzuki argues that “Japanese trade relations have been and will be decided through the prism of US-Japanese relations”.<sup>76</sup> When the US

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<sup>74</sup> Fioretos *et al.*, “Historical Institutionalism in Political Science”, in O. Fioretos *et al.* (eds.), *The Oxford Handbook of Historical Institutionalism*, Oxford, Oxford University Press, 2016, p. 11.

<sup>75</sup> M. Okano-Heijmans & T. Terada, “EU-Japan Relations in the Age of Competitive Economic Governance”, in A. Berkofsky *et al.* (eds.), *The EU-Japan Partnership in the Shadow of China: The Crisis of Liberalism*, London, Routledge, 2018, p. 113.

<sup>76</sup> H. Suzuki, “The New Politics of Trade: EU-Japan”, *Journal of European Integration*, vol. 39, no. 7, 2017, p. 881.

approached the EU to negotiate TTIP, this was a “wake up call for Japan” to engage in discussions with the EU.<sup>77</sup> Furthermore, TTIP motivated Japan to participate in the TPP negotiations, as a successful EU-US deal without the participation of Japan in TPP would reduce Japan’s importance and its overall position in global trade.<sup>78</sup> Japan first entered into TPP negotiations in July 2013.<sup>79</sup> Prime Minister Abe had initially prioritized TPP negotiations over all other trade initiatives, as part of his ‘Abenomics’ policy, which, among others, envisaged reaching a total share of trade covered by FTAs of 70% by 2018, from 19% in 2013.<sup>80</sup> After the withdrawal of the US from TPP in January 2017, Japan could no longer reach the 70% target.<sup>81</sup> At the same time, the “new regional economic architecture” in the Asia-Pacific centred on TPP was projected to negatively affect the EU, if the EU would not conclude an FTA with Japan.<sup>82</sup> Thus, according to the Commission’s trade sustainability impact assessment for the EU-Japan EPA, the EU needed to improve its access to the Japan market in order to retain its current level of economic benefits from trade.<sup>83</sup>

The failure of TTIP reinforced the critical juncture for the EU to pursue the path towards the conclusion of an agreement with Japan. Moreover, TPP and the withdrawal of the US also pushed Japan and the EU closer together, demonstrating their need to step up and create the rules of the game among them. Thus, both TTIP and TPP acted as a critical juncture opening the path towards the EU-Japan EPA.

Moreover, the previous section of this paper argued that CETA has served as a template for subsequent EU trade agreements. To assess whether this argument is valid in the case of the EU-Japan EPA, I will compare the two agreements with regard to their WTO+ (building on existing WTO commitments) and their WTO-x commitments (issues beyond WTO’s current scope).<sup>84</sup>

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<sup>77</sup> R. Tyszkiewicz, “Towards New Political and Economic Agreements with Japan: Bringing New Dynamism into the Strategic Partnership between the EU and Japan”, *PISM Policy Paper*, vol. 57, no. 9, April 2013, p. 3.

<sup>78</sup> Tyszkiewicz, *op. cit.*, p. 3.

<sup>79</sup> Y. Watanabe, “The Japan-EU Economic Partnership Agreement (JEEPA) and its Potentials”, *ECIPE Seminar*, Brussels, 22 November 2018, retrieved 17 June 2020, <https://ecipe.org/wp-content/uploads/2018/11/EU-Japan-EPA-ECIPE-Seminar-22-11-18-Prof.-Watanabe.pdf>, p. 11.

<sup>80</sup> Solis & Urata, *op. cit.*, pp. 106, 113.

<sup>81</sup> *Ibid.*, pp. 113-114.

<sup>82</sup> European Commission, *Impact Assessment*, *op. cit.*, pp. 49, 248.

<sup>83</sup> *Ibid.*, p. 49.

<sup>84</sup> Chowdry, *op. cit.*, pp. 8, 22 et seq.

Regarding WTO+ issues, CETA and the EU-Japan agreement are similar in their high degree of commitments on services trade, technical barriers, public procurement and intellectual property.<sup>85</sup> Both differ, however, substantially from older agreements (e.g. CARIFORUM or Israel), as, they cover new policy areas, such as trade-related investment measures and the elimination of export taxes.<sup>86</sup> This supports the argument that CETA indeed set a precedent.

Concerning WTO-x commitments, both agreements pursue the objective of expanding market access, while “promoting equitable and sustainable trade”, as they include provisions on environmental law and labour market regulations.<sup>87</sup> Moreover, both CETA and the EU-Japan EPA include provisions specific to small and medium-sized enterprises, as well as cooperation on research, technologies and energy.<sup>88</sup> A novelty of the EU-Japan EPA is its mention of the commitments under the Paris Agreement, as well as a chapter dedicated to corporate governance.<sup>89</sup>

There is, however, one key difference between the EU-Japan EPA and CETA, as the EPA only covers issues under the exclusive competence of the EU and requires approval from the Council and ratification by the European Parliament.<sup>90</sup> CETA, on the other hand, covers portfolio investment and investor protection disciplines and is therefore a mixed agreement, which must be approved by national and regional parliaments, according to Singapore Opinion 2/15 of the European Court of Justice.<sup>91</sup> Concretely, CETA was the first EU trade agreement to replace the earlier Investor-State Dispute Settlement (ISDS) mechanism with the Investment Court System (ICS).<sup>92</sup> The Singapore Opinion set a precedent for the EU, opening the path of splitting investment agreements from the FTAs in the future, in order to facilitate the FTA’s ratification. Therefore, in the case of the EU-Japan EPA, while the trade agreement has entered into force, an agreement on investment is still under negotiation, as

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<sup>85</sup> *Ibid.*, p. 22.

<sup>86</sup> *Ibid.*

<sup>87</sup> *Ibid.*, p. 24.

<sup>88</sup> *Ibid.*

<sup>89</sup> Interview with EU Delegation in Tokyo, *op. cit.*

<sup>90</sup> European Parliament, *Bilateral Trade Deal with Japan: Largest to Date for EU*, European Parliamentary Research Service, PE 633.164, February 2019, p. 7.

<sup>91</sup> Court of Justice of the European Union, Press Release no. 52/17, *op. cit.*

<sup>92</sup> K. Hübner *et al.*, “EU and trade policy-making: The Contentious Case of CETA”, *Journal of European Integration*, vol. 39, no. 7, 2017, pp. 843 *et seq.*; Chowdry, *op. cit.*, p. 18.

Japan prefers the ISDS mechanism and not the ICS proposed by the EU.<sup>93</sup> Overall, with the exception of this last point, it is safe to conclude that the provisions of CETA have to a large extent been replicated in the EU-Japan EPA. Therefore, CETA indeed created a template for the EU-Japan case.

*Beyond CETA: Brexit, South Korea and the importance of sequencing for the EPA*

The sequence of events, meaning the order in which things happen, can “affect the interests of political actors” and shape the direction of subsequent developments.<sup>94</sup> Beyond the CETA template, case-specific motivations for the EU-Japan EPA were the 2016 Brexit referendum and the EU-South Korea FTA signed in 2010, which demonstrate the role of sequence of events pushing the EU and Japan closer to each other.

Apart from the withdrawal of the US from TPP, the EU-Japan negotiations have also been pushed by Brexit.<sup>95</sup> While Brexit may have contributed, as will be shown, to the negotiations with Japan, in the case of TTIP it made an agreement with the ‘EU minus the UK’ less attractive to the US.<sup>96</sup>

For Japan, on the other hand, the UK is an important base for Japanese firms in Europe, such as the motorcar industry (Nissan-Renault, Toyota and Honda) operating plants in the country.<sup>97</sup> Many of the more than one thousand UK-based Japanese companies consider the possibility of relocating to EU territory to adapt post-Brexit.<sup>98</sup> Brexit further demonstrates how the sequence of events plays a substantial role. Both Japan and the EU wished to conclude the EPA before the UK entered a transition phase on 31 January 2020, in order to use the EPA as a bargaining chip vis-à-vis the

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<sup>93</sup> P.A. Nelson, “Taking the Lead in Current and Future Trade Relationships”, in A. Berkofsky et al. (eds.), *The EU-Japan Partnership in the Shadow of China: The Crisis of Liberalism*, London, Routledge, 2018, p. 130. For more information on the benefits of ICS over ISDS see Chowdry, *op. cit.*, pp. 18-19.

<sup>94</sup> Fioretos (2011), *op. cit.*, p. 382.

<sup>95</sup> Gstöhl & De Bièvre, *op. cit.*, p. 153.

<sup>96</sup> Young, *op. cit.*, p. 112.

<sup>97</sup> Suzuki, *op. cit.*, p. 885.

<sup>98</sup> K. Holton, “More Japanese companies could leave UK over Brexit – ambassador”, *Reuters*, 4 March 2019, retrieved 22 June 2020, <https://www.euronews.com/2019/03/04/more-japanese-companies-could-leave-uk-over-brexit-ambassador>.

UK.<sup>99</sup> For the EU the agreement served as a demonstration of strength in its negotiations with the British government.<sup>100</sup> For Japan, a deal with the EU is also a bargaining chip, which can buy it more time to negotiate a separate trade agreement with the UK.<sup>101</sup>

A further case in point for the significance of the sequence of events is the EU-South Korea FTA, the first EU trade agreement with an Asian country, which entered into force in July 2011.<sup>102</sup> The market access granted to Korean firms in the EU under the FTA challenged Japanese business interests, especially those competing with Korean firms in European markets for electronics and automobiles, which through the FTA had gained a competitive advantage.<sup>103</sup> Thus, the EU-South Korea FTA has created momentum, mobilising Japan and the EU to achieve at least a similar agreement.<sup>104</sup> The unprecedented economic impact of the 'triple disasters' of 2011 in Japan – the earthquake, tsunami and nuclear reactor meltdown in Fukushima – added to the pressure to negotiate the EPA.<sup>105</sup> On the whole, the FTA with South Korea was a major catalyst for the advancement of the EU-Japan EPA, setting into motion a domino effect that brought Japan and the EU closer to an agreement.<sup>106</sup>

### *Path dependence and the influence of China and Trump*

The EU's values-based, standard-setting approach has been identified above as an important path dependence that can explain the motivations of the EU to conclude mega-regionals. This section examines how China and the US influenced the EU's and Japan's chosen path.

China became a member of the WTO in 2001.<sup>107</sup> Ever since, despite expectations to the contrary, China has become less of a market economy and more state-

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<sup>99</sup> P. Blenkinsop, "EU, Japan seek to push through trade deal before Brexit", *Reuters*, 28 February 2018, retrieved 10 July 2020, <https://www.reuters.com/article/us-eu-japan-trade/eu-japan-seek-to-push-through-trade-deal-before-brex-it-idUSKCN1GC2CA>.

<sup>100</sup> Suzuki, *op. cit.*, p. 885.

<sup>101</sup> Blenkinsop, *op. cit.*

<sup>102</sup> Tyszkiewicz, *op. cit.*, p. 3.

<sup>103</sup> Nelson, *op. cit.*, p. 118.

<sup>104</sup> Tyszkiewicz, *op. cit.*, p. 3.

<sup>105</sup> Nelson, *op. cit.*, p. 119.

<sup>106</sup> Ponjaert, *op. cit.*, p. 91.

<sup>107</sup> World Trade Organisation, *China and the WTO*, official WTO website, updated 2020, retrieved 20 June 2020, [https://www.wto.org/english/thewto\\_e/countries\\_e/china\\_e.htm](https://www.wto.org/english/thewto_e/countries_e/china_e.htm).

dominated, creating significant irritants to trade, including industrial subsidies, state-owned enterprises and overcapacity issues.<sup>108</sup> Even though they do not often explicitly refer to China in their interactions, both the EU and Japan are affected by Chinese attempts to reshape global economic governance and to reform institutions such as the World Bank, the WTO or the International Monetary Fund.<sup>109</sup> China seeks to create new networks with its 'Belt and Road initiative' and a number of regional and bilateral trade deals.<sup>110</sup> The rise of China has been identified as a challenge for the US, referred to as "avoiding the Thucydides trap".<sup>111</sup> In this context, Japan has as a US ally been taking a zero-sum approach towards Beijing, whereas the EU recognises the growing role of China in global economic governance and wishes to positively engage with it, always "with emphasis on rules and regulations that China should comply with".<sup>112</sup>

The US, an ally of both the EU and Japan, has been following a more and more protectionist approach, resetting US trade policy and challenging the multilateral system of the WTO by 'trade wars' and by blocking the appointment of judges at its Appellate Body.<sup>113</sup> To reduce bilateral trade deficits, the US increasingly uses tariffs and quotas as a tool.<sup>114</sup> By contrast, Japan and the EU, having benefitted from openness so far, are making the case against this rise of protectionism.

#### *Power asymmetry and the EPA*

The EU and Japan are among the four largest economies in the world.<sup>115</sup> When it comes to the export of goods, the deal was comparatively more important for Tokyo,

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<sup>108</sup> "A new dawn for protectionism? From trade wars to mega-regional trade agreements" [video-recorded event], Washington, DC, Brookings Institution, 8 October 2018, , retrieved 15 July 2020, <https://www.brookings.edu/events/a-new-dawn-for-protectionism-from-trade-wars-to-mega-regional-trade-agreements>.

<sup>109</sup> Okano-Heijmans & Terada, *op. cit.*, p. 97.

<sup>110</sup> *Ibid.*, p. 98.

<sup>111</sup> B.S. Glaser, "US-China Relations: Managing Differences Remains an Urgent Challenge", *Southeast Asian Affairs*, 2014, p. 82. In the example of Sparta and rising Athens in the 5<sup>th</sup> century BC, the historian Thucydides identified as a trap the situation, in which "when one great power threatens to displace another, war is almost always the result". See G. Allison, "The Thucydides Trap", *Foreign Policy*, 9 June 2017, retrieved 16 July 2020, <https://foreignpolicy.com/2017/06/09/the-thucydides-trap>.

<sup>112</sup> Okano-Heijmans & Terada, *op. cit.*, pp. 99, 101-102.

<sup>113</sup> T. Miles, "U.S. blocks WTO judge reappointment as dispute settlement crisis looms", *Reuters*, 27 August 2018, retrieved 10 July 2020, <https://www.reuters.com/article/us-usa-trade-wto/u-s-blocks-wto-judge-reappointment-as-dispute-settlement-crisis-looms-idUSKCN1LC190>.

<sup>114</sup> Brookings, *op. cit.*

<sup>115</sup> Okano-Heijmans & Terada, *op. cit.*, p. 97.

as 10% of Japanese exports go to the EU, which is more than twice the amount of EU goods exported to Japan.<sup>116</sup> Furthermore, the withdrawal of the US from TPP negatively influenced the Japanese position, as “preferential U.S. market access in Japan would provide Tokyo with additional leverage over its European counterparts”.<sup>117</sup> At the same time, the sequence of events and previous agreements influenced concessions on both sides. On the one hand, Japan conceded to tariff reductions on chocolate and pasta, as it had previously done in TPP.<sup>118</sup> The EU’s concessions to Japan, on the other hand, resemble those in the EU-South Korea FTA.<sup>119</sup>

Yet, all things considered, it was rather the convergence of interests that motivated the two sides to achieve a comprehensive agreement. This is in line with the general motivations identified above, where it has been concluded that a mega-regional can be all the more comprehensive, the stronger the convergence of interests and domestic agendas of the two sides.<sup>120</sup> This was indeed the case for the EU and Japan, achieving a transformation from “de-facto business-driven integration” to “de-jure EPA-driven integration”.<sup>121</sup>

Even though the EU uses the term ‘EPA’ for agreements with the African, Caribbean and Pacific states, the EU-Japan agreement is called EPA instead of FTA because Japan uses the term for its recent trade agreements that include many issues, such as trade in goods, trade in services, direct investment, government procurement, intellectual property and competition,<sup>122</sup> as shown in Figure 1.

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<sup>116</sup> J. Brunsden & V. Romei, “Why the EU’s agreement with Japan is a big deal”, *Financial Times*, 6 July 2017, retrieved 20 April 2019, <https://www.ft.com/content/572fef42-6260-11e7-91a7-502f7ee26895>.

<sup>117</sup> D. Kleimann, “Negotiating in the Shadow of TTIP and TPP: The EU-Japan Free Trade Agreement”, *The German Marshall Fund of the United States, Asia Program, Policy Brief*, 20 June 2015, p. 6.

<sup>118</sup> Suzuki, *op. cit.*, pp. 881-882.

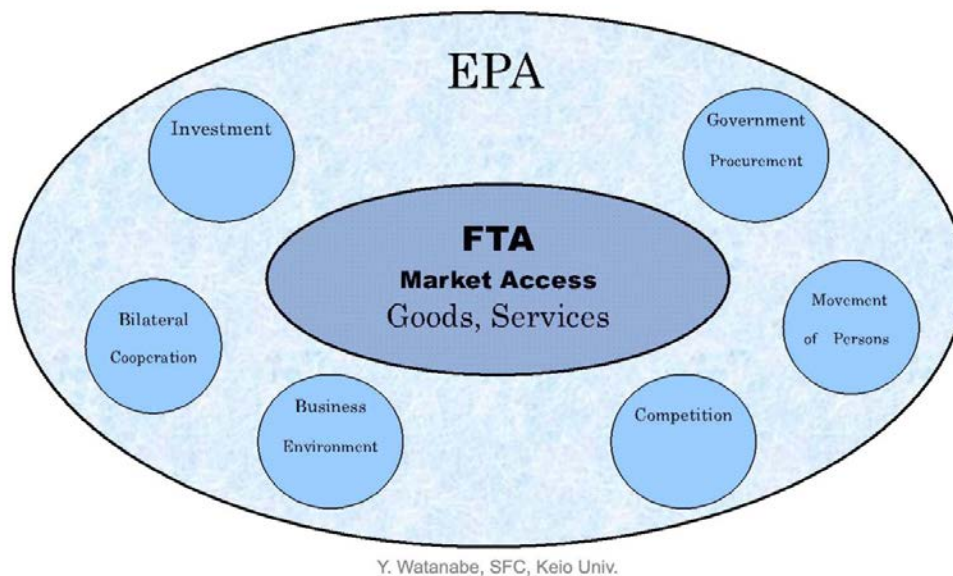
<sup>119</sup> Kleimann, *op. cit.*, p. 6.

<sup>120</sup> Ponjaert, *op. cit.*, p. 88.

<sup>121</sup> Watanabe, *op. cit.*, p. 4.

<sup>122</sup> C. De Prado, *Prospect for the EU-Japan Strategic Partnership: A Global Multi-level and Swot Analysis*, European University Institute & EU-Japan Centre for Industrial Cooperation, Florence & Tokyo, December 2014, pp. 29-30.

Figure 1 Elements of a Japanese FTA and the EU-Japan EPA



Source: Watanabe, *op. cit.*, p. 5.

Simplistically referred to as the “cars for cheese” deal, the EPA decreases Japan’s tariffs on meat, wine and dairy products in return for an end to EU import duties on Japanese cars.<sup>123</sup> In terms of liberalisation, “97% of tariff lines and 99% of imports from Europe are liberalised and on the 3% of tariff lines not fully liberalised, Japan has given the EU significant concessions in terms of tariff rate quotas and/or tariff reductions”.<sup>124</sup> According to the European Commission, “by removing billions of euros of duties, simplifying customs procedures and tackling behind-the-border barriers to trade, [the EPA] will offer opportunities for companies on both sides to boost their exports and expand their business”.<sup>125</sup> Going beyond its economic provisions, the agreement also has significant non-economic implications on sustainability, labour and climate change.<sup>126</sup> The EPA will further enable the EU and Japan to shape the course of global developments, reflecting their values and “their commitment to a rules-based global trade system and the fight against global warming”.<sup>127</sup> Indeed, as Yeo argues, in partnership, the EU and Japan are able to “leverage on each other’s capacities”

<sup>123</sup> Brunsden & Romei, *op. cit.*

<sup>124</sup> Interview with EU Delegation in Tokyo, *op. cit.*

<sup>125</sup> European Commission, *EU-Japan Summit: A landmark for trade and cooperation*, Press Release, Brussels, 17 July 2018.

<sup>126</sup> A. Poidevin & H. Lee-Makiyama, “The EU-Japan EPA Freer, Fairer and more Open Trading System”, *ECIPE Policy Brief*, no. 10/2018, Brussels, December 2018, retrieved 17 June 2020, [https://ecipe.org/wp-content/uploads/2018/12/ECI\\_18\\_PolicyBrief\\_EU-Japan-EPA\\_10-2018\\_LY05.pdf](https://ecipe.org/wp-content/uploads/2018/12/ECI_18_PolicyBrief_EU-Japan-EPA_10-2018_LY05.pdf).

<sup>127</sup> Chowdry, *op. cit.*, p. 1.



in order to share the responsibility of leadership on transnational challenges, such as climate change.<sup>128</sup>

### Summary

An untapped potential in the relations between the EU and Japan, both politically and economically, was at the core of the decision to engage in negotiations for a trade agreement.<sup>129</sup> The case study confirmed that the motivations identified above also apply to the EU-Japan EPA. More specifically, it has been shown that TTIP, TPP and CETA served as a critical juncture towards the negotiation and conclusion of the EU-Japan EPA. The crucial role of sequence has been shown with the examples of Brexit and the EU-South Korea FTA. Path dependences were discussed against the background of a rising China and the uncertainty surrounding the policy of the Trump administration. Finally, this section elaborated how relative power asymmetries between the two large economies allowed for a comprehensiveness deal.

In the global context of rising protectionism and geopolitical uncertainties, the EPA sends a signal that the EU and Japan stand together for sustainable cooperation and for preserving the benefits of openness.<sup>130</sup> Finally, a stronger EU-Japan partnership could also reinforce the strength and capacity needed to potentially reinvigorate the multilateral trading system.<sup>131</sup> This, along with other potential impacts of mega-regional agreements for the parties, for the 'outsiders' (non-parties to the agreements) and for the multilateral trading system, will be elaborated in the subsequent section.

### Likely implications of EU mega-regionals

As the spread of EU mega-regional agreements is a recent phenomenon, evidence of the effects of such agreements is still inconclusive.<sup>132</sup> Furthermore, these new

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<sup>128</sup> L.H. Yeo, "The EU-Japan Economic Partnership Agreement: Filling the Leadership Void?", *Brink Asia*, place?, 12 August 2018, retrieved 20 June 2020, <http://www.brinknews.com/asia/the-eu-japan-economic-partnership-agreement-filling-the-leadership-void/>.

<sup>129</sup> Interview with EU Delegation in Tokyo, *op. cit.*

<sup>130</sup> P. de Taxis du Poët, "A new era for the EU and Japan starts now!", *EU-Japan Centre for Industrial Cooperation*, 2019, retrieved 29 June 2020, <https://www.eu-japan.eu/news/new-era-eu-and-japan-starts-now>.

<sup>131</sup> Yeo, *op. cit.*

<sup>132</sup> J. Ravenhill, *Global Political Economy*, Oxford, Oxford University Press, 5<sup>th</sup> edn, 2017, p. 168.

agreements have been designed as “living agreements” because regulatory cooperation is supposed to continue after the conclusion of the negotiations.<sup>133</sup> What is more, as has been established above, mega-regionals are very comprehensive agreements, going beyond tariffs into writing “rules that underpin global value chains”.<sup>134</sup> This, in turn, renders the analysis of the implications of mega-regionals all the more challenging, as these new agreements, according to Velut, blur the boundaries between regionalism and multilateralism, have substantial economic significance and can potentially set new precedents for worldwide regulation.<sup>135</sup>

*Implications for ‘insiders’: positive feedback effects and path dependence*

The path of mega-regional agreements can create ‘positive feedback effects’, which in turn render a departure from the path less likely and ultimately contribute to a given path dependence.<sup>136</sup> The opening of markets and the reduction and elimination of tariffs can bring significant economic benefits to both sides of an agreement. Mega-regionals facilitate existing and build new trade patterns, while achieving a “higher common-denominator trade agreements”, setting standards and proactively responding to challenges.<sup>137</sup> On a global level, the large number of preferential agreements, which include a multiplicity of rules and tariffs, have been described by Bhagwati as a “spaghetti bowl effect” since the agreements are “intertwined and reaching out to different directions”.<sup>138</sup> Thus, a further positive feedback effect of mega-regionals is organising this spaghetti bowl, or what Baldwin describes as “making the spaghetti into lasagne plates”.<sup>139</sup> As Schwab and Bhatia put it, mega-regionals “may be the inevitable direction taken by like-minded countries in a globalized world”.<sup>140</sup>

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<sup>133</sup> Velut, *op. cit.*, p. 1.

<sup>134</sup> R. Baldwin, “The Economic Impact”, in *Mega-regional Trade Agreements: Game-Changers or Costly Distractions for the World Trading System?*, Report, World Economic Forum, July 2014, p. 22.

<sup>135</sup> Velut, *op. cit.*, p. 5.

<sup>136</sup> Fioretos *et al.*, *op. cit.*, p. 11.

<sup>137</sup> Schwab & Bhatia, *op. cit.*, pp. 19-20.

<sup>138</sup> J. Bhagwati, “US Trade Policy: The Infatuation with FTAs”, *Columbia University Discussion Paper Series*, no. 726, Department of Economics, Columbia University, April 1995, p. 4.

<sup>139</sup> Baldwin, *op. cit.*, p. 26.

<sup>140</sup> Schwab & Bhatia, *op. cit.*, p. 19.

*Implications for 'outsiders': domino effects and unintended consequences*

The likely impact of mega-regional agreements for – especially smaller – non-members to the agreements concern potentially discriminatory effects.<sup>141</sup> In particular developing and least developed countries fear that their interests will be overlooked by large trading powers in smaller groups and that mega-regional agreements are not sufficiently inclusive.<sup>142</sup> In response to this, it may be argued that there are positive spill-over effects for third countries “thanks to increased economic activity and the overall reduction in the number of standards that require adaptation of third-country companies”.<sup>143</sup>

Moreover, the mega-regional trend could eventually motivate other countries to participate and conclude comprehensive agreements of their own. According to Cai, “being involved in the process of mega-negotiations undoubtedly benefits China by providing chances for it to abide by and create new rules”.<sup>144</sup> As the negotiations at the WTO are not progressing, mega-regionals can regulate issues such as cross-border data flows or investment protection, with the hope that these regulations will become global standards.<sup>145</sup> If the EU and its partners succeed as standard-setters, this could create a “domino effect”<sup>146</sup> if the conclusion of a mega-regional agreement induces non-members to join the trade bloc.<sup>147</sup> In essence, countries could adopt the competitive trade-liberalising standards if they see that negotiations going on around them create the risk of them being “locked out”, at a competitive disadvantage.<sup>148</sup>

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<sup>141</sup> R. Meléndez-Ortiz, “Discriminatory and Multilateralizing Potential of TPP and TTIP Provisions”, in *Mega-regional Trade Agreements: Game-Changers or Costly Distractions for the World Trading System?*, Report, World Economic Forum, July 2014, p. 22.

<sup>142</sup> European Parliament study (February 2017), *op. cit.*, p. 27.

<sup>143</sup> Riffel, *op. cit.*

<sup>144</sup> P. Cai, “China’s Responses to Mega-regional FTAs: A Chinese Perspective”, *Asian Survey*, vol. 56, no. 6, p. 1142.

<sup>145</sup> B.M. Araujo, “Brexit and the promised land of Free Trade Agreements”, *Queen’s Policy Engagement*, Queen’s University Belfast, 28 June 2016, retrieved 20 June 2020, <http://qpol.qub.ac.uk/uk-brexit-free-trade-agreements>.

<sup>146</sup> Griller, *op. cit.*, p. 8.

<sup>147</sup> R. Rieder, “Playing Dominoes in Europe: An Empirical Analysis of the Domino Theory for the EU 1962-2004”, *IHEID Working Papers*, no. 11-2006, The Graduate Institute of International Studies, Economics Section, Geneva, revised June 2006, p. 1.

<sup>148</sup> Schwab & Bhatia, *op. cit.*, p. 19.

A further question related to this effect is whether the EU mega-deals can provide an “incentive structure” for the US’s return to open and comprehensive trade deals.<sup>149</sup> Trump’s protectionism is a highly political tool meant to achieve short-term advantages and eventually get re-elected: “with protectionism you can create domestic manufacturing, you can pull inward FDI [foreign direct investment], you can bring manufacturing business back home”.<sup>150</sup> The rise of protectionism might be further enhanced by mega-regionals because, unintendently, they may “encroach too much on the regulatory freedom of national legislatures. If those legislatures are democratically legitimized, the conclusion of ever more integrative agreements might come into conflict with the principle of democracy”.<sup>151</sup> Moreover, Vandebusch observes a cultural shift in the younger generation, coupled with the evolution of societies: people today have seen the world and seem to be valuing the local sourcing patterns more; “we care about higher values in life, once our material values have been satisfied”, forgetting that the growth of today is thanks to the global value chains and globalisation.<sup>152</sup> All in all, for the first time in 75 years, “there is no international consensus in support of trade”.<sup>153</sup> Against this background, it might be more difficult than in the past for mega-regionals to achieve the domino effects and the global standards-setting envisaged.

Finally, the departure of the UK from the EU also means a withdrawal from its mega-regionals. According to the Organisation for Economic Cooperation and Development (OECD), the UK will lose its preferential access to 53 non-EU markets, including the access granted under mega-regional agreements.<sup>154</sup> Concluding new trade agreements with non-EU countries might be more modest in content and take long to finalise.<sup>155</sup> Moreover, as explained above, due to the sequencing game and asymmetrical bargaining power, the UK will find itself “at the back end of the sequence of trade”.<sup>156</sup> Thus, it will be unable to “demand the type of market access concessions and regulatory reforms the EU typically secures in the context of its own

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<sup>149</sup> Solis & Urata, *op. cit.*, p. 120.

<sup>150</sup> Brookings, *op. cit.*

<sup>151</sup> Riffel, *op. cit.*

<sup>152</sup> cited in Brookings, *op. cit.*

<sup>153</sup> F. Lavin & O. Guinea, “Learning to Love Trade Again-Time to Think Small”, *ECIPE Occasional Paper*, no. 03/2020, European Centre for International Political Economy, Brussels, June 2020, retrieved 21 June 2020, <https://ecipe.org/publications/learning-to-love-trade-again>, p. 3.

<sup>154</sup> Organisation for Economic Cooperation and Development, *The Economic Consequences of Brexit: A Taxing Decision*, OECD Economic Policy Paper, no. 16, Paris, April 2016, p. 6.

<sup>155</sup> *Ibid.*, p. 17.

<sup>156</sup> Interview with P. Lamprecht, *op. cit.*

trade negotiations".<sup>157</sup> If mega-regionals are successful in competing with other standards around the world, they can create the regulatory rules that the UK would have to adhere to, given its limited bargaining power outside of the EU. Thus, post-Brexit the UK might have to "subscribe to a set of rules that have been developed by a small number of trade powers, including, ironically, the EU", essentially turning the UK "from a rule-maker to a rule-taker".<sup>158</sup>

#### *Unintended consequences for the multilateral trading system*

Mega-regionals are comprehensive agreements, ultimately aiming at rewriting the rules of trade. Analysts have inquired to what extent this rule-writing among a few countries poses a threat to the multilateral trading system, that is, whether comprehensive trade agreements constitute "steppingstones or stumbling blocks to multilateralism".<sup>159</sup>

This paper has established the stalemate of the Doha Development Round as a critical juncture opening the path towards mega-regional agreements. However, as Hoekman argues, "the lack of progress in the Doha Round should not be taken to imply lack of relevance of the WTO".<sup>160</sup> This has been explicitly defended by the EU. The 2006 Global Europe strategy declares that "there will be no European retreat from multilateralism".<sup>161</sup> Moreover, the 2017 EC Communication affirms that "the EU's multilateral obligations in the WTO are the basis of [the EU's] trade relations around the world".<sup>162</sup>

According to a first approach, analysts suggest that mega-regionals and multilateralism can indeed coexist, with the former taking steps towards the advancement of the latter. Research of the OECD suggests that, especially with reference to WTO+ measures, provisions in regional agreements have become "more widespread and similar over time", suggesting not just that these agreements have the capacity to achieve higher levels of commitment, but also that they create

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<sup>157</sup> Araujo, *op. cit.*

<sup>158</sup> *Ibid.*

<sup>159</sup> Lamy, *op. cit.*, p. 64.

<sup>160</sup> B. M. Hoekman, "Sustaining multilateral trade cooperation in a multipolar world economy", *Review of International Organizations*, vol. 9, no. 2, February 2014, p. 258.

<sup>161</sup> European Commission, *Global Europe, op. cit.*, p. 8.

<sup>162</sup> European Commission, *Communication 2017, op. cit.*, p. 3.

potential to serve as “building blocks for future multilateral policy-making”.<sup>163</sup> The analysis of the World Economic Forum also suggests that mega-regionals can create “potential precedents for future multilateral agreements”.<sup>164</sup> Finally, according to the WTO, regional and multilateral initiatives are complementary and can “coexist and cohere in a kind of ‘multispeed’ or ‘variable geometry’ system” of global trade architecture.<sup>165</sup>

However a second approach argues that mega-regionals could undermine the multilateral trading system. Today’s nature of trade obstacles, as Lamy points out, has moved from traditional trade barriers (i.e. tariffs) to differences in standards and regulatory regimes.<sup>166</sup> By ‘preferentially’ leveling the playing field between the partners to a mega-regional, the EU would essentially create a “bloc that benefits insiders more than outsiders”.<sup>167</sup> Thus, concluding EU mega-regionals could have as an unintended consequence the undermining of the centrality of the WTO.<sup>168</sup>

To avoid this, mega-regionals ought to be designed with an “open architecture” that allows for third countries to eventually become members.<sup>169</sup> To further facilitate the relationship between mega-regionals and multilateralism, a “supervisory role over regulatory convergence” could be given to the WTO.<sup>170</sup> Best practice exchanges have also been suggested as an invaluable way of ‘multilateralising’ WTO+ and WTO-x issues, along with confidence-building measures to improve the capacities and infrastructure of third countries, facilitating regulatory cooperation.<sup>171</sup>

A third approach to the effects of mega-regionals for the multilateral trading system has been put forward by Baldwin: for larger markets staying outside the mega-regionals, the “soft preferences arising from the mega-regionals may not prove very damaging”, given that larger outsiders “can use their market size and unilateral

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<sup>163</sup> Organisation for Economic Cooperation and Development, *Regional Trade Agreements*, Trade Policy Brief, Paris, February 2019, retrieved 30 June 2020, <http://www.oecd.org/trade/topics/regional-trade-agreements>.

<sup>164</sup> Schwab & Bhatia, *op. cit.*, p. 19.

<sup>165</sup> World Trade Organisation, *World Trade Report 2011 – The WTO and Preferential Trade Agreements: From Co-existence to Coherence*, Geneva, 2011, p. 54.

<sup>166</sup> Lamy, *op. cit.*, p. 68.

<sup>167</sup> *Ibid.*

<sup>168</sup> Lamy, *op. cit.*, p. 71.

<sup>169</sup> Schwab & Bhatia, *op. cit.*, p. 20.

<sup>170</sup> Lamy, *op. cit.*, p. 75.

<sup>171</sup> Akman, *op. cit.*, p. 91.

harmonization to offset the negative effects".<sup>172</sup> For smaller outsiders, the domino effect described above, pushing them to participate in the mega-regionals, is a probable scenario; "live and let live within this two-pillar system is a very likely outcome".<sup>173</sup>

Within this complexity, only a few members of mega-regionals alone might not be enough to address crucial international issues, such as climate change.<sup>174</sup> To mitigate possible unintended consequences of mega-regionals undermining the multilateral system, it is necessary to create an infrastructure that allows for the rules decided among mega-regional partners to be adopted by many more. At the same time, multilateralism at the WTO is not and should not be power-based, it is about giving small actors equal chances.<sup>175</sup> It remains to be seen how mega-regional agreements, such as the EU-Japan EPA, can find their way into the multilateral trading system without leaving anyone behind. As Lamy rightly puts it, "connecting the bilateral and multilateral 'brains' of trade negotiators remains a challenge for the future".<sup>176</sup>

### Summary

This section found that mega-regional FTAs can have positive feedback effects for the partners to the agreements, as opening the markets can lead to significant economic benefits, and allow the EU and other like-minded partners to create new trade patterns and set global standards which can (proactively) respond to global issues such as climate change, sustainability goals or labour rights. At the same time, these ambitious standards could lead to domino effects, inducing non-members to join the bloc. Finally, the section discussed (unintended) consequences for the multilateral trading system and the open architecture these agreements need so that they may co-exist without undermining the multilateral system of the WTO.

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<sup>172</sup> R. Baldwin, "The World Trade Organization and the Future of Multilateralism", *Journal of Economic Perspectives*, vol. 30, no. 1, 2016, p. 114.

<sup>173</sup> *Ibid.*

<sup>174</sup> Ravenhill, *op. cit.*, p.137.

<sup>175</sup> M. Demertzis & A. Sapir, "Director's Cut: Resuming the EU-US Trade Talks" [podcast], *The Sound of Economics – Podcast channel of Bruegel*, 23 April 2019, retrieved 24 June 2020, <http://bruegel.org/2019/04/directors-cut-resuming-the-eu-us-trade-talks/>.

<sup>176</sup> Lamy, *op. cit.*, p. 77.

## Conclusions: what future for mega-regionals?

Drawing on historical institutionalism, the present work examined why the EU negotiates mega-regionals and what the likely implications of such agreements are. The study found that the EU turned towards the mega-regional path due to the critical juncture of the WTO stalemate which triggered the EU's shift in trade strategy under the 2006 Global Europe. The EU's long-standing path dependence of promoting values, standards and rules according to the principles guiding its external action, also served as motivation towards the negotiation of mega-regionals. Furthermore, it has been argued that CETA marked the starting point of a new path dependence of the EU utilising CETA as a template in its subsequent comprehensive agreements. Finally, the role of power asymmetry and bargaining has been discussed. While there is less power asymmetry in the EU's bilateral relations with large countries (such as the US, Japan, Canada), this bilateral approach allows for more room to achieve deeper mutual concessions. In a nutshell, "mega-regionals can go more comprehensive, deeper and faster than the WTO".<sup>177</sup> The EU was thus motivated by the possibility of not only achieving deep economic benefits, but also of promoting issues such as climate, labour standards or corporate governance.

The EU-Japan case study presented further motivations that are case-specific to the EPA. Particular focus was placed on explaining the role of previous mega-regional negotiations – TTIP, TPP, CETA – as critical junctures for the EU-Japan EPA. Insights on the importance of sequence were given with regard to the EU-South Korea FTA and the UK's withdrawal from the EU. Against the geopolitical background of a decoupling between the US and China, a further reason behind the conclusion of the EU-Japan EPA is the need to counteract the rise of protectionism and promote an open, rules-based trading system. Finally, bargaining and power asymmetries were used as factors to explain how the EU succeeded in including pioneering provisions in the EPA.

The likely implications of mega-regionals include positive feedback effects for the partners and for the global 'spaghetti bowl' of trade agreements. Domino effects and possible discriminatory effects for third countries were discussed, along with unintended consequences, focussing especially on the rise of protectionism, as well

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<sup>177</sup> Akman, *op. cit.*, p. 90.



as on Brexit. Finally, with regard to the potential impacts of mega-regionals on the multilateral trading system, unintended consequences such as mega-regionals weakening multilateralism were discussed. It was concluded that mega-regionals are not to replace the WTO but should be constructed with an open architecture that would allow them to become building blocks towards the evolution of the multilateral trading system.

The discussion presented in this work is not exhaustive, as further motivations and implications of mega-regionals certainly exist. The decision to focus on the ones mentioned above is largely based on the choice to discuss geopolitical and institutional changes over time through the lens of historical institutionalism.

To date, the EU remains on this ambitious path and hopes to add to the already rich network of preferential trade agreements in the future.<sup>178</sup> Nonetheless, as the EU is one of the biggest trading entities in the world, bilateral agreements with smaller countries will in all likelihood also remain a parallel strategy, as the EU can exert more bargaining power.<sup>179</sup> What is more, perhaps more pressing than the impact of mega-regionals are a different set of challenges identified above, namely the low trade growth and the public opinion turned against global trade, as well as the weakening of multilateral institutions coupled with the rise of protectionism and increased state intervention.<sup>180</sup> Moreover, the Covid-19 emergency health crisis came to add to this already challenging moment for trade. The EU clearly expressed commitment to use trade, its “main geopolitical instrument of influence in the global economy”, as the “only non-budgetary instrument to get us out of the crisis”.<sup>181</sup> Within this complex environment for trade policy, the EU remains committed to setting ambitious standards together with like-minded partners, with agreements with partners such as Australia and New Zealand being currently negotiated. Inducing further countries to follow suit on this path and finding ways to ensure that the advanced standards set bilaterally ultimately also find their way into the multilateral trading system of the WTO remain two of the key challenges and open questions for the future existence of mega-FTAs.

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<sup>178</sup> S. Weyand in “EU Trade Policy for a Post-COVID World”, [zoom-recorded webinar], European Centre for International Political Economy, 28 May 2020, retrieved 2 June 2020, <https://ecipe.org/blog/eu-trade-policy-post-covid>.

<sup>179</sup> Interview with P. Lamprecht, *op. cit.*

<sup>180</sup> Similarly: Akman, *op. cit.*, p. 91.

<sup>181</sup> Weyand, *op.cit.*

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