

Impact of JTEPA on the bilateral relationship between Japan and Thailand

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Introduction

Economic relations between Japan and Thailand date back at least 600 years. Indeed, the first recorded ‘trade negotiations’ between governments can be dated to 1419. The King of Ryukyu sent a letter to the King of Siam complaining that a previous Ryukyu trading mission had been unable to buy sappanwood because Siamese officials judged the accompanying gifts were insufficient. We might call this an early example of non-tariff barriers. To overcome them, the Ryukyu king sent more gifts including large quantities of woven-gold satin, white linen, sulphur, swords, big blue vases, folding paper fans, and small blue bowls (Hamashita, 1995; Ishii and Yoshikawa, 1999: 11).

The records do not tell us whether this particular negotiation was successful, but certainly the Siam-Ryukyu trade flourished.

Over the intervening six centuries, trade and economic relations between Thailand and Japan have waxed and waned in different periods, but there is a strong overall continuity. In the negotiations of 1419, the issue was Ryukyu’s access to rare goods for import back to Japan. The negotiations that resulted in the JTEPA were much more wide-ranging. They include trade in commodities in both directions; trade in services in both directions; and investment in both directions.

In recent years, the regional and global context has become more complex, with the rise of China and India, and the failure of the multilateral agreement on trade and investment under the WTO. Many countries, Japan and Thailand included, have been using trade agreements to enhance competitiveness.

I have been asked to focus on the impact of JTEPA on the bilateral relationship between Japan and Thailand. In this talk, I’m going to look at the agreement from the Thai point-of-view. I will summarize its main provisions for commodity trade, services, and investment. After that, I will look at the main controversies which arose during the negotiations and how they were resolved. Finally, I will make some suggestions and predictions about how this agreement will be judged – as a success or failure – by the Thai side in the future. These are my own views as an economist and observer of Thai-Japanese relations.

Background: recent Thai-Japanese economic relations

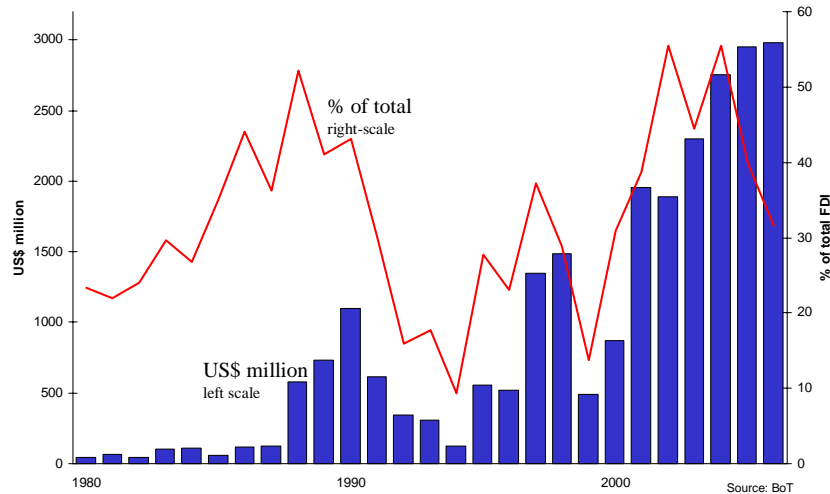
But first a little background.

For Thailand, there is no doubt that Japan is our single most important economic

partner. This has been especially true since the Plaza Accords of 1985 sparked a flow of Japanese investment in manufacturing in Thailand.

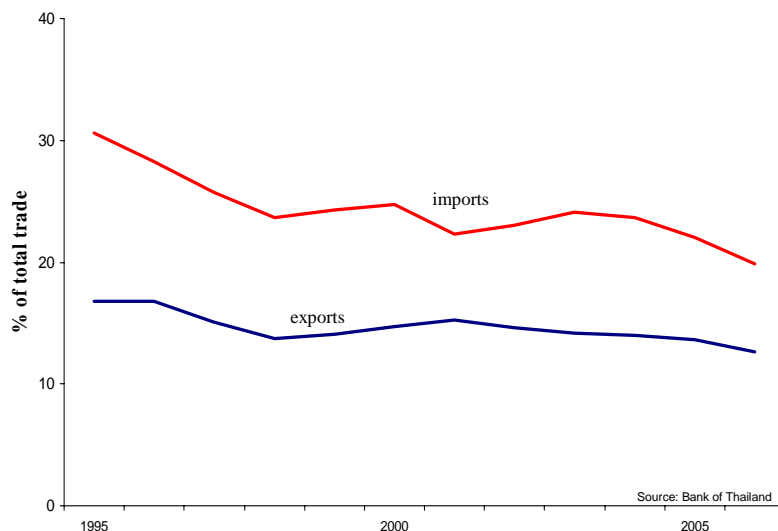
Since the crisis of 1997, that investment flow has recovered and reached new heights. Last year, it was almost 3 billion US dollars. Over recent years, Japan has contributed between a third and a half of all our foreign investment (see Fig. 1).

Japanese Direct Investment in Thailand, 1980-2006



It is no exaggeration to say that the health of our economy depends crucially on the exports of manufactured goods made in Japanese plants in Thailand including automobiles and parts, electronics, machinery, rubber products, chemicals, and plastics. Because of Japanese direct investment, Thailand now counts among the top ten exporters of automobiles in the world.

Japan's share of Thailand's trade, 1995-2006



Japan is our single largest trading partner. Japan's shares of our imports (around 20 percent) and exports (around 15 percent) are declining slightly as we diversify our trade, but are still of major significance (Fig. 2). The US takes a slightly higher share of our exports, but Japan's share of our imports is two to three times that of the US.

Japan is also an important friend-in-need, as was shown during the Asian crisis of 1997. Japan contributed generously to the IMF rescue program, and then went further by providing the Miyazawa Fund to help stimulate a recovery. This is well remembered and appreciated.

From the Japanese side, Thailand is not important on the same scale. Thailand accounts for only 3-4 percent of Japan's total trade. Among export destinations, Thailand ranks around sixth, and among import sources, around tenth. Yet Thailand is far from insignificant to Japan. For many Japanese firms, their investments in Thailand have helped them to retain their profit levels and their world market shares in the face of new competition.

Given the strong economic links between the two countries, it's befitting that the agreement between Japan and Thailand is called the Japan-Thailand Economic Partnership Agreement or JTEPA.

The JTEPA in brief

Commodity trade¹

Tariff reductions to promote freer and increased trade are the stock-in-trade of most bilateral trade agreements, and the JTEPA is no exception.

On Japan's side the average tariff rate is already at the low level of 2.67 percent.

¹ This section is largely based on TDRI, 2006.

This will be reduced to 0.8 percent in the first year, and more gradually thereafter until it reaches 0.17 percent in year 16 (2024). For several agricultural products from Thailand, the tariff rates will be reduced to zero in the first year. This applies to prawns, fresh fruits, vegetables, processed fruits, and canned fruits. For cat and dog foods and squid the tariff will be zero within 5-10 years.

On Thailand's side the average tariff rate is currently higher at 9.09 percent. This will be reduced to 7.18 percent in the first year and will eventually reach 0.55 percent by year 11 (2019), a shorter time frame than in the case of Japan.

The Thailand Development Research Institute (TDRI) estimates that the cost of imports from Japan into Thailand will drop by 1.91 percent in the first year, rising to 8.55 percent in the 11th year. Meanwhile, the cost of imports from Thailand into Japan will drop 1.98 percent in the first year, rising to 2.61 percent in the 16th year. In fact, the savings are likely to be higher as these calculations are based on past data. These reductions should stimulate mutual trade.

Thai manufacturers in garments, jewelry, and processed foods are said to be satisfied with the JTEPA as they see prospects of advancing into the Japanese market, even though they will still face fierce competition from other countries.

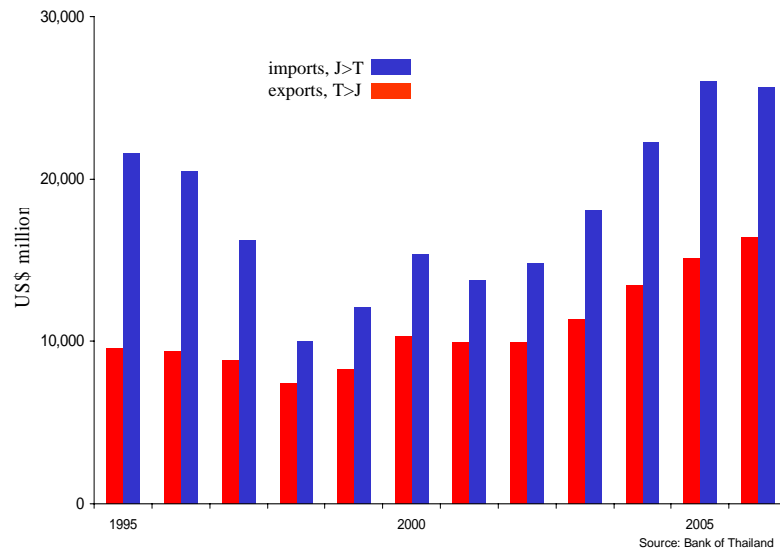
The Thai Ministry of Foreign Affairs announced that 'Thai farmers will benefit when the JTEPA is effective from opportunities to sell [to Japan] more agricultural products such as sweet peppers, bananas, mangosteens, pineapples, flowers, chicken, prawns, and seafood. The standard of products will be better. Thai co-operatives will be able to contact and sell direct to Japanese co-operatives. Products will not face obstructions and middlemen profits will be reduced... The fear that there will be an influx of Japanese goods to compete with Thai agricultural goods is unfounded because ...fruit such as apples from Japan are very expensive.'

According to the Ministry, Thailand will also benefit in manufactured goods since 'Japan will immediately remove tariffs on jewelry, textiles and chemical products; and for shoes and some leather products, the tariffs will be zero within 5-10 years' (MOFA, 2007).

On first glance, Japanese exporters seem to benefit more than their Thai counterparts as the fall in tariff rates is steeper and faster. Moreover, Japanese exporters should be able to realize the benefits of the tariff reduction immediately, while Thai firms may have to spend time and money to improve product quality in order to meet Japanese standards.

Thailand already has a trade gap with Japan, which has increased in recent years (see Fig 3). From the Thai side, this gap is not considered to be a problem as much of it represents imports of Japanese capital goods which Thailand uses to generate an export surplus with the rest of the world. But Thailand will certainly be watching the future trends of trade between the two countries to gauge whether the Agreement benefits both parties in roughly equal measure in the area of commodity trade.

Thailand's trade with Japan, 1995-2006



Services

Under the Agreement, Japanese firms are allowed to hold a higher equity share than the 50 percent allowed under local law in a number of service areas. These include consulting; logistics (excluding all transport); maintenance and repair; and wholesale and retail in household electrical appliances and automobiles produced or wholesaled by Japanese firms under the same brand either in Japan or in Thailand.²

During the 1997 crisis, Thailand relaxed its restrictions on equity participation in order to allow Japanese parent companies to inject funds to keep their local joint ventures afloat. These investments were in manufacturing plants, but also in a range of service firms to support this manufacturing – including logistics, consultancy, and dealerships. This provision in the JTEPA seems designed to safeguard Japanese investments in these services against any future change in Thailand's investment laws. These provisions represent an assurance to Japanese investors of Thailand's commitment to the economic partnership. Hopefully this will make Thailand become more attractive to Japanese investors

In return Japan opens up trade in services under the JTEPA for Thailand including allowing Thai firms to provide services such as advertising, hotels, restaurants, event organizing, tour organizing, security services, interpreting, caring for the elderly, teaching Thai language and Thai dancing, spas, and professional services including taxation, legal, architectural and engineering consultancy.³

In practice, entry into many of these areas in Japan requires professional

² Curiously the agreement limits the Japanese share in advertising and general management consultancy to a proportion *below* that allowed under local law. In effect JTEPA is a safeguard on these activities against possible future more restricted change in the Thai law.

³ These provisions are no different from those in the Japan Malaysia Economic Partnership (JMEPA).

qualifications and other conditions. Here the Agreement has also made things a little easier. Thais with a BA degree from Thailand may apply for an equivalent degree in Japan (*Thiep wut*), which would make it easier for them to provide some types of professional services in Japan. For Thai cooks, the Agreement reduces the required work experience from 10 years to 5 years (time to study for vocational education is included as part of the experiences). But for other occupation in the non-BA degree category, such as spa-workers and elderly care workers, provisions are made for renegotiation at a later date.

Japanese can already apply for a refund of up to 70 percent of their medical expenses incurred abroad from the Japanese medical insurance scheme. The Agreement reaffirms this arrangement. This in effect gives assurance to investors in private health service providers in Thailand.

On first reading, the arrangements on services appear to benefit Thailand more than Japan. The Thai Ministry of Foreign Affairs (2007) shows that Thailand provides more liberal treatment than that specified under WTO in just 14 areas, while Japan provides more liberal treatment than that specified under WTO in 135 areas. However there are concerns whether Thai service providers will truly be in a position to take advantage of this liberalization.

For this reason, one of the most important features of the JTEPA is the chapter on cooperation which was elaborated further in the Implementing Agreement. Such cooperation is intended to overcome barriers to realizing the full benefit of the Agreement in the areas of both commodity trade and services. This Implementing Agreement sets a framework for cooperation in many fields such as agriculture, forestry and fisheries; education and human resource development, information and communication technology under the principle that the parties shall develop and enhance partnership and co-operation in these various fields for mutual benefits.⁴

For example, Thai farmers may not benefit from JTEPA if they cannot overcome technical barriers to trade such as sanitary phytosanitary (SPS) measures in Japan. Under the Implementing Agreement, the Thai Ministry of Agriculture may push for assistance from Japan including technical inputs and help with licensing procedures. This type of facilitating cooperation is very important, especially to aid small-scale exporters, and to facilitate the entry of more Thai agricultural products into the Japanese market.⁵

I gather that various local bodies in the private sector in Thailand, including some local agricultural co-operatives,⁶ have also shown enthusiastic interest in pursuing cooperation under the Implementing Agreement.

Investment agreement

Thailand and Japan have never had a bilateral investment treaty (BIT). As a result, Japanese investors in Thailand and Thai investors in Japan are governed by the laws of

⁴ Such cooperation is not binding on the two parties, however. The Agreement just sets out a framework for possible cooperation.

⁵ In automobile, steel and SMEs, technical and human resource development cooperation between the two parties has already taken place before JTEPA.

⁶ Thailand's FTAs with many other countries, including China and Australia, have brought in cheaper non-tropical fruits and vegetables (previously luxuries), leading to a situation where local fruits face a glut and plunging prices. JTEPA provides an avenue of hope for Thai fruit and vegetable producers.

the respective countries. The Agreement (article 91) gives investors on both sides added advantages beyond the provisions in the respective countries' local laws. The Agreement safeguards them from expropriation, nationalization, or indirect expropriation, with compensation procedures in the case of expropriation for public purposes. There is a provision for protection against strife due to armed conflicts, state of emergency, revolution, or civil disturbances. The range of assets covered includes shares, equity, bonds and other debt instruments, reinvested earnings, supplier and buyer credits, intellectual property rights, concessions, licenses and permits, tangible and non-tangible property, and property rights.

Some NGOs questioned whether the scope of these provisions is so broad that it may cause difficulties in the future. For example, the protection of intellectual property rights under this clause could obstruct the Thai government's policy to use compulsory licensing for pharmaceuticals.

Another provision of this section also created concern. Investors may sue the government for compensation on grounds their business has suffered as a result of changes in government policy. The case will be heard by a Dispute Settlement Panel consisting of three arbitrators, two being appointed each by the dispute parties and one appointed jointly by the two parties. The ruling of this Panel is final with no avenues for appeal. In the FTAs which the US concluded with Chile, Singapore, and Morocco, the US allowed either party to appeal the initial judgment to a Bilateral Appellate Body. TDRI suggested that the JTEPA should adopt this system in the future. TDRI also cautioned about the lack of clarity in the Article which allows compensation in cases where taxation amounts to expropriation (TDRI, 2006).

Sensitive issues

During the negotiation of the JTEPA, certain key points became a matter of public concern. Undoubtedly, the resolution of these key points will crucially affect whether the Agreement is subsequently judged a success or failure from the Thai point-of-view. Let me briefly review these issues.

Process

The first issue concerned the process of negotiation itself.

Bilateral trade and investment agreements are made for mutual benefits. No one party receives all the gains and no one party bears all the loss. In international agreements, the imbalance of power between the two parties can determine the distribution of gains. The skill of the respective negotiating parties is very important. Where the negotiation process is secretive and non-transparent, there may be a mismatching between what the negotiators consider beneficial and what the society at large might consider beneficial.

In Thailand, the process was criticized for not having sufficient transparency. While official negotiations proceeded from early 2004 to 2006, some important information was not made publicly available. Under Thai law, there was no requirement for the Agreement to be submitted to parliament. Shortly prior to the eventual signing, the Agreement was debated in the Legislative Assembly, but legislators were provided with little information on the details of the Agreement, had only a short time to analyze that information, and had no power to vote.

Inevitably, this procedure generated suspicion. For example, it emerged that Japan had excluded rice and some 230 other items from the scope of negotiation, while Thailand's exclusion list had about 10 items.⁷

This left doubt whether the Agreement truly reflects Thailand's best interests, since there was no mechanism to ensure those interests were properly articulated and taken into account. Everything depended on the negotiators who might have been poorly informed, or susceptible to vested interests.⁸ In Japan, the FTA sailed through parliament and excited no public controversy. In Thailand, civil society was left with suspicion.

This is, of course, Thailand's own internal problem, and steps have already been taken to overcome it. As a result of lobbying by civil society, the new constitution of 2007 requires that such Agreements are aired in a public hearing, submitted for parliamentary approval, and governed by a new law currently under discussion.

Intellectual property

When details of the Agreement were revealed to the public early this year, NGOs questioned why a clause on intellectual property rights seemed to provide Japan with more benefits than those available under TRIPS, and more benefits than appear in Japan's similar EPA with Malaysia.

The controversial issue is this. Under Thai law, it is difficult to gain intellectual property rights over a natural organism. Under TRIPS, individual countries are allowed to protect themselves by such a law. But a clause in the JTEPA⁹ states that 'Each party shall ensure that any patent application shall not be rejected solely on the grounds that the subject matter claimed in the application is related to a naturally occurring micro-organism.' The question arose of *why* this clause should appear in the JTEPA. What sort of substance was envisaged? Thai NGOs argued that it would be safer to drop this clause and allow the TRIPS framework to apply. The negotiators refused this suggestion so the clause remains, and so too does the suspicion of why it is there.

Waste

The second controversy which arose when the details of the Agreement were revealed concerned waste. Under the Agreement, Thailand will reduce the tariff on several categories of waste. This raised suspicion that the Agreement would promote Japan's ability to use Thailand as a dump for unwanted waste. Officials from Thailand and Japan protested that this was not true as the movement of waste was strictly controlled by laws in both countries. In addition, both Thailand and Japan had signed the Basle Convention of 1989 which controls the inter-country movement of hazardous waste. The Ministers of Foreign Affairs of the two countries have exchanged official communications (dated 3 April 2007) to reaffirm their common understanding 'that they will continue to enforce strict control on the export and import of hazardous and other wastes.... in accordance with the Basel Convention.... They also reaffirm that JTEPA does not in any way encourage trafficking of hazardous wastes between Japan and the

⁷ This discrepancy may reflect a finer classification on Japan's side as compared to that of Thailand's.

⁸ This is stated at a theoretical level and does not imply that the Thai negotiators were at fault in any way. There is no doubt that they had Thailand's interest as their main objectives and tried their best to achieve this.

⁹ Article 130(3) of the JTEPA.

Kingdom of Thailand.’

But if the import of hazardous waste is thus strictly controlled, why bother to adjust the tariff levels? Though Thailand may have a system of control on paper, the enforcement of law is often inefficient.¹⁰ Currently there are problems that waste is imported to Thailand, earmarked for re-export to other countries, but never leaves. The Thai negotiators do not seem to have thought that the waste issue might be a problem. But civil society is more suspicious, and there remains a big question mark over why this tariff reduction should appear in the agreement.

While both Japan and Thailand have signed the 1989 Basle Convention which *controls* the movement of hazardous wastes, neither country has signed the 1998 Convention which effectively *bans* such movement.¹¹

Steel

The fourth issue aired in public debate concerned the steel industry. This was largely a matter of commercial competition rather than public interest. Thailand’s downstream steel industry opposed reduction in tariffs on grounds that their businesses would be wiped out as their profit margins are slim. Japan auto-makers in particular lobbied hard for the reduction on grounds that the Thai firms are unable to make steel of the type and quality required now that these firms use their Thai plants to make vehicles for export to world markets. This issue was resolved by reducing tariffs to zero on some items which are not yet produced in Thailand, or produced with inadequate quality or quantity, while delaying the schedule of tariff reduction for other steel products. The Thai steel firm, Sahaviriya, plans to use this delay to build a plant capable of making steel of the required capacity, but this project is not yet ensured of success. Nippon Steel is also considering whether to invest in a plant in Thailand.

Criteria for judging JTEPA from the Thai side

Given the massive importance of Japan for the Thai economy, it is vital that Thailand concludes such an agreement with Japan, particularly in view of the parallel negotiations between Japan and other Asian neighbors.

But the very extent of Thailand’s dependence on Japan gives rise to fears that the weaker party may not have done so well out of the negotiations. These fears are aggravated by concerns over the process of negotiation on the Thai side. How then will the Thai public assess the success or failure of the Agreement over the years to come?

In January of this year, the Thai Ministry of Foreign Affairs listed its own assessment of the good and bad points of the Agreement on its website (MOFA, 2007). In brief, the Ministry lists the good points as: lower tariffs for farmers and manufacturers exporting to Japan; liberalization of 135 service items by Japan as against 14 by Thailand; more openings for Thais to work in Japan; and the opportunities for

¹⁰ In 1991 a fire involving toxic waste stored at Bangkok’s port caused terrible injuries to many people. The provenance of the waste responsible has never been properly explained.

¹¹ A Japanese Citizen Group has urged the Japanese government to remove clauses on waste from EPAs with developing countries and to seek national self-sufficiency in waste management. This group claims that Japan’s refusal to be party to the second Basle Convention shows that it hopes to weaken or circumvent the Convention.

cooperation under the Implementing Agreement. The bad points are: the need for adjustment in such industries as steel and auto parts which will face greater import competition; the drop in government revenue resulting from lower tariffs; and the possible adverse trend in the Thailand-Japan trade gap.

The Ministry argues that these bad points are not really bad. Import competition presents a challenge for Thailand's corporations and government agencies to overcome. Reductions in trade taxes can be offset by increased revenues from value-added taxes and corporate income taxes due to increased economic activity. The trade deficit is not a problem if it is covered by Thailand's surplus with the rest of the world.

I would like to propose a list of nine points which may be used for monitoring the result of the agreement.

1. *Have the commodity exports of Thailand to Japan increased at higher rates after the JTEPA?*

2. *Have the service receipts of Thailand from Japan increased at higher rates after the JTEPA.*

3. *Are more professional Thais with BA able to obtain licenses to provide services in Japan?*

4. *Are more cooks, health-care providers, and others in categories listed in the Agreement able to go to work in Japan?*

5. *Have additional hazardous wastes been imported into Thailand from Japan? And what has been done to them?*

6. *Have there been significant increase in patents on natural organisms being registered after JTEPA?*

7. *Have more small producers been able to export to Japan? For example have more agricultural cooperatives been able to export agricultural products to Japan?*

8. *Has the cooperation framework outlined in the Implementing Agreement facilitated new efforts to overcome practical problems, especially for small agriculturalists and SME?*

9. *Has the Agreement played a positive role in encouraging continued Japanese investment in Thailand?*

To the extent that the success of the agreement has implications on Japan-Thailand relations in the future, it will be a good idea to set up a joint body not only to implement the agreement but also to monitor and evaluate the outcome of the JTEPA for both partners.

Concluding remarks

Of course, much of the responsibility for the success or failure of the Agreement depends on us. Such agreements should act as a spur for improvement in areas including research and development, education and training, government's institutional support, systems for environmental protection, and so on. But Japan can also help a lot on the technical side.

Negotiators for the JTEPA expect it to enhance trade and investment between the two countries for mutual benefits, and to improve the competitiveness of the two countries in the context of globalization. It is also a very important document for another reason. It provides a framework for further discussion on old and new economic issues where there may be opportunities to enhance mutual benefits.

Perhaps the single most important thing about the Agreement from the Thai point-of-view is that it has reaffirmed the commitment of both countries to evolve an economic relationship which benefits both sides. In a world economy which seems to become more complex, more competitive, and less stable as time passes, this is a relationship which both sides need to nurture.



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