



UKRAINE-JAPAN-EU TRADE CONNECTIVITY:

MUTUAL IMPACT
AND NEW OPPORTUNITIES





Analytical
commentary

UKRAINE-JAPAN-EU TRADE CONNECTIVITY: MUTUAL IMPACT AND NEW OPPORTUNITIES



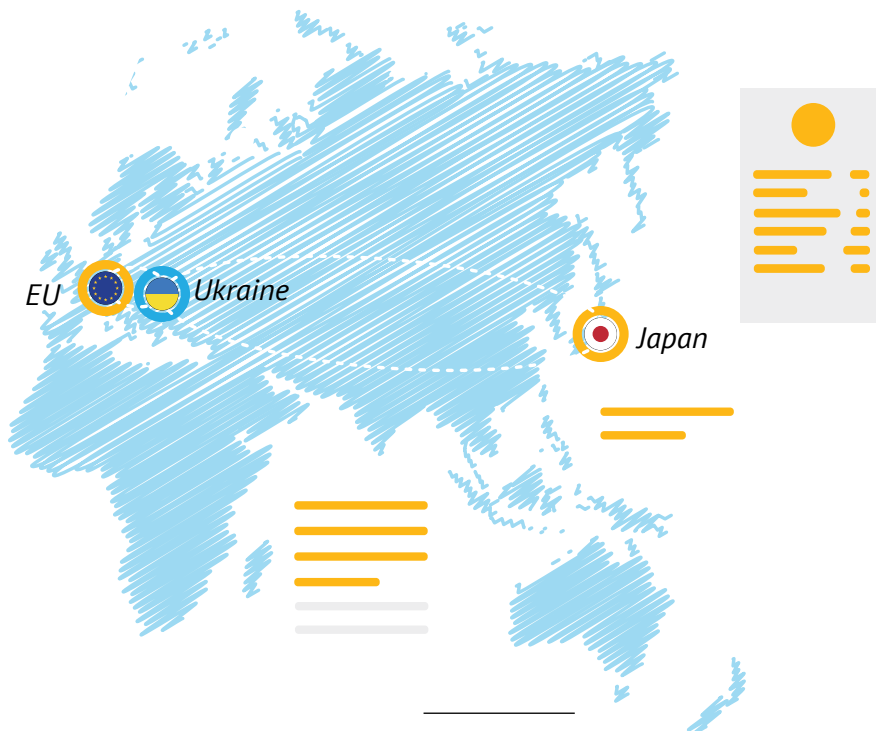
Daisuke KITADE,
Researcher, Mitsui & Co. Global
Strategic Studies Institute, Japan



Sergiy SOLODKYY,
New Europe Center, Ukraine

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Economization has become a defining feature of Ukraine's foreign policy. With the advent to power of Volodymyr Zelensky, approaches to the work of Ukrainian diplomacy have been adjusted, with a special emphasis recently placed on finding opportunities for domestic businesses in foreign markets. Therefore, it is not surprising that Ukrainian diplomacy today pays considerable attention to the development of business cooperation with Japan. Ukraine-Japan trade relations indeed have untapped potential¹. To improve the situation, Kyiv has been nourishing an idea of creating a free trade area between Ukraine and Japan. With the latter being an important hub at the intersection of strategic trade agreements, this move is expected to foster Ukraine's integration into global trade flows. Japan, however, is more cautious about launching new free trade areas. At the same time, Japanese observers note that the deep and comprehensive free trade area between Ukraine and the European Union has a positive effect on Ukraine-Japan trade. Moreover, Japan is gradually opening its market to Ukrainian producers on certain trade items.



¹ Korsunsky Sergiy. "Analiz potochnoho stanu vidnosyn Ukraina-Yaponiia." Portal zovnishnoi polityky. <http://fpp.com.ua/analiz-potochnogo-stanu-vidnosyn-ukrayina-yaponiya/>



WHY IS IT IMPORTANT FOR UKRAINE?

Winning markets for Ukrainian producers is one of the highest expectations that ordinary Ukrainians associate with foreign policy in 2021. This is suggested by the opinion poll conducted by Info Sapiens and ordered by the New Europe Center in the fall of 2020². Almost half of citizens (45.3 percent) support the implementation of the economic dimension in the country's foreign policy. President Volodymyr Zelensky has also repeatedly stressed in his speeches that the effectiveness of diplomats' work would be measured by achievements in the trade and economic field. Accordingly, the search for foreign investors who would invest in developing Ukrainian enterprises, and lobbying the interests of Ukrainian business have become part of the usual daily activities of Ukrainian embassies.

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Therefore, it is no wonder that Ukraine has come up with the idea of establishing a free trade area between Ukraine and Japan. As one plan has it, the creation of favorable conditions for Ukrainian enterprises to enter the Japanese market should balance the rather significant disparity between Japanese imports to Ukraine and Ukrainian exports to Japan. According to the State Statistics Service of Ukraine, Japanese imports of goods to Ukraine last year stood at \$ 1.1 billion, while Ukrainian exports to Japan amounted to \$ 182 million³. Over the past ten years, Ukraine has barely managed to break the \$ 200 million mark. Outstanding against the general background of the last decade was the pre-revolutionary year of 2013, when Ukrainian exports reached \$ 458 million. The structure of Ukrainian merchandise exports has traditionally been dominated by low added-value goods, such as iron ores and concentrate thereof, tobacco products and industrial tobacco substitutes⁴. Japan primarily exported to Ukraine mechanical engineering products, such as automobiles. Exports of heavy engineering and electrical machinery accounted for 8.5 and 4.6 percent of the trade turnover, respectively.

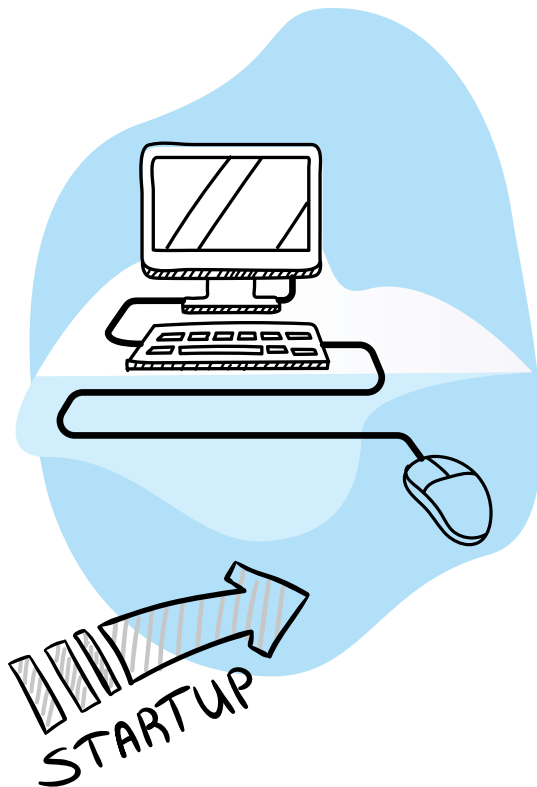
² *Diplomacy 2021: Government's priorities, expectations of society*, New Europe Center, December 16, 2020. <http://neweurope.org.ua/en/dyplomatiya-2021-priorityty-vlady-ochikuvannya-suspilstva/>

³ *State Statistics Service of Ukraine*. <http://www.ukrstat.gov.ua>

⁴ *Korsunsky Sergiy. "Analiz potochnoho stanu vidnosyn Ukraina-Yaponiia."* Portal zovnishnoi polityky. <http://jpp.com.ua/analiz-potochnogo-stanu-vidnosyn-ukrayina-yaponiya/>

It should be noted, however, that the statistics of the Ministry of Finance of Japan have serious discrepancies with Ukrainian data, which Kyiv ascribes to different calculation approaches. Thus, according to Tokyo, the bilateral trade turnover amounted to \$ 1.02 billion, with \$ 498 million of Japanese exports to Ukraine and \$ 523 million of Ukrainian exports to Japan⁵. As shown by this data, Ukrainian indicators are even slightly higher than Japanese ones. However, regardless of the discrepancies in calculation, it is obvious that the potential for cooperation between the parties is much greater.

According to the 2017 Export Strategy of Ukraine, Japan is among the top five most “undertraded” partners of Ukraine after the United States, United Kingdom, Germany and France. The free trade area, according to Kyiv, could alter the situation. According to the Export Strategy, Ukraine has concluded a total of 18 free trade agreements covering 45 countries and opening access to 800 million potential consumers (as of 2017, in particular, these included the EU, CIS, EFTA, GUAM, Canada, Georgia, Montenegro and Macedonia)⁶. On January 1, 2021, the free trade area between Ukraine and Israel was also launched into operation. The implementation of the provisions of the Free Trade Agreement



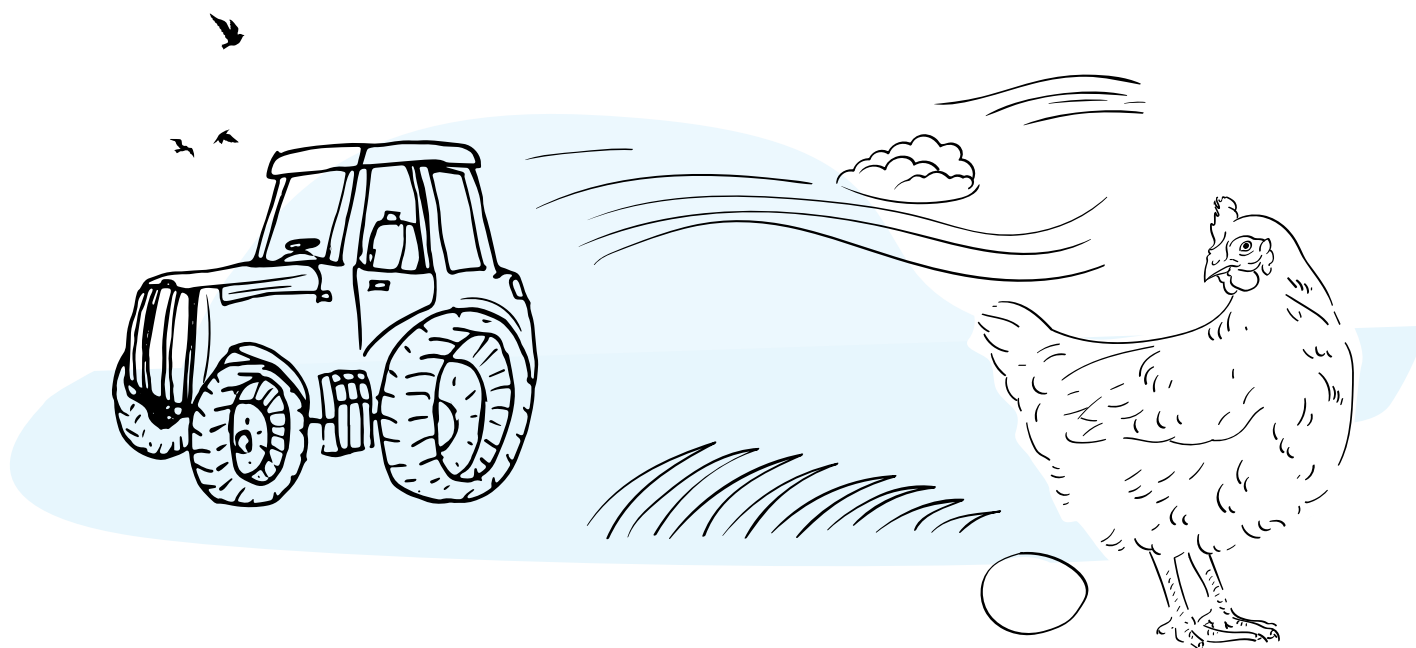
between Ukraine and Israel is expected to increase mutual trade to \$ 2 billion⁷. Kyiv and Ankara are also negotiating to create a free trade area between Ukraine and Turkey⁸. As can be seen, the Ukrainian government is keenly interested in establishing free trade areas, which, according to Kyiv, should contribute to the development of the Ukrainian economy.

⁵ Trade Statistics of Japan. <https://www.customs.go.jp/toukei/srch/index.htm?M=23&P=0>

⁶ Cabinet of Ministers of Ukraine. Order dated December 27, 2017 No. 1017-p, Kyiv, “On the Adoption of the Export Strategy of Ukraine (the “roadmap” of the strategic development of trade) for 2017–2021.” <https://zakon.rada.gov.ua/laws/show/1017-2017-p#n13>

⁷ Ukrinform, “Uhoda pro ZVT mozhe zbilshyty tovaroobih z Izrailem do \$2 miliardiv – Zelensky,” January 24, 2020. <https://www.ukrinform.ua/rubric-economy/2862204-ugoda-pro-zvt-moze-zbilshyti-tovaroobig-z-izrailem-do-2-milardiv-zelenskij.html>

⁸ Radio Svoboda, “Zelensky rozrakhovuiе, shcho Ukraina pidpyshe Uhodu pro vilnu torhivliu z Turechchynoiu ‘naiblyzhchym chasom,’” October 16, 2020. <https://www.radiosvoboda.org/a/news-ukrayina-turechchyna/30896717.html>



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In Ukraine and Japan, it is believed that the most promising areas of cooperation are agriculture and IT. Some items of Ukrainian agricultural exports have already confirmed this calculation. For instance, the export of Ukrainian honey to the Japanese market is showing rapid growth. Japan is gradually granting permits for Ukrainian agricultural exports, which to some extent can be considered a major step towards the liberalization of mutual trade (albeit presently not leading to the creation of a free trade area). In March

2021, Ukraine and Japan agreed on a certificate form for raw milk and dairy products⁹. Earlier, the so-called health certificates were approved for exporting chicken and fresh eggs from Ukraine¹⁰.

⁹ Cabinet of Ministers of Ukraine, "Yaponia vidkryla rynek dlia ukrainskoho moloka," March 9, 2021. <https://www.kmu.gov.ua/news/yaponiya-vidkrila-rinok-dlya-ukrayinskogo-moloka>

¹⁰ Ukrinform, "Ukraina i Yaponia pohodyly vetsytyfikat na eksport yaiets," January 8, 2020. <https://www.ukrinform.ua/rubric-economy/2851425-ukraina-i-aponia-pogodili-vetsytyfikat-na-eksport-aec.html>

A WIDER CONTEXT

During the forum “Asian Strategy in Action. The Role of Ukraine-Japan Cooperation,” organized by the New Europe Center on February 16, 2021, the participants highlighted the need to develop relations between Kyiv and Tokyo with due regard for the global and regional context. In other words, the discussion revolved around the importance of cooperation between the two countries in the framework of international organizations, where Japan’s voice plays a significant role; also stressed the need for a tripartite partnership – for example, between Japan, Ukraine and the EU. One of the key takeaways from the New Europe Center’s forum was “the necessity to move, as appropriate, from ‘triangles’ to ‘quadrangles’ in cooperation, taking into account the wider context, with collaboration developing between three, four or more countries.”

The application of the so-called multilateral approach can be quite useful for the development of economic cooperation between Ukraine and Japan. In some measure, the Ukraine-EU-Japan triangle already exists in terms of trade, with the only question being how it can be used to give new impetus to the dialogue between Kyiv and Tokyo. For example, if to talk about trade cooperation, in Ukraine and the EU it is based on the Association Agreement, which includes a deep and comprehensive free trade area. The free trade area has recently been created between Japan and the EU – the relevant agreement entered into force on February 1, 2019. This agreement (referred to as the Economic Partnership Agreement) creates additional

opportunities for European farmers and food producers. The EU has also gained access to one of the world’s largest public procurement markets¹¹.

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In her discussion note *Ukraine-Japan: how to secure an effective global partnership?*, Alyona Getmanchuk indicates that there is currently insufficient evidence to understand the extent to which the Ukraine-EU free trade area facilitates the entry of Ukrainian products into the Japanese market and the opening of Japanese enterprises in Ukraine¹². That said, the analyst notes that in order to enter the Japanese market, Ukrainian products must meet specific and rather stringent requirements (which, according to some information, are stricter than those in the EU countries). According to Alyona Getmanchuk, Ukrainian products today “win” the Japanese buyer in terms of price and quality thanks to their average price. Nonetheless, once the Japan-EU free trade area is fully

¹¹ *EU-Japan, Economic Partnership Agreement*. <https://ec.europa.eu/trade/policy/in-focus/eu-japan-economic-partnership-agreement/>

¹² *Getmanchuk Alyona. “Ukraine-Japan: how to secure an effective global partnership?”* New Europe Center, February 2021. <http://neweurope.org.ua/analytics/ukrayina-yaponiya-yak-zabezpechyty-efektyvne-globalne-partnerstvo/>

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operational, the price of European goods will get closer to those in Ukraine due to the abolition of 25 percent import duties in five years. Ukraine's understanding is that the way out in this situation may be to conclude its own Free Trade Agreement with Japan. It would also be preferable to analyze the extent to which certain provisions of the Japan-EU Free Trade Agreement might be taken into account in the process of updating the Ukraine-EU Association Agreement¹³.

At the same time, during the forum Japanese experts assured that the existence of the Ukraine-EU free trade area had already made Ukraine more attractive in Japan. Atsuko Higashino, Associate Professor at the

University of Tsukuba, stressed the differences in Japan's and China's perceptions of Ukraine¹⁴. According to the researcher, for Beijing, Ukraine is more interesting as a country with a communist experience than as a non-EU country. By contrast, for Tokyo, Ukraine is valuable for its rapid measures aimed at integrating the country into the European Union – i.e., the fact that Ukraine is a European country. Atsuko Higashino noted that Japan perceived Ukraine as a European country with which it could share experiences and with which “we share many values.”

¹³ *Ibid.*

¹⁴ Higashino, A. “Asia Strategy in Action. The Role of Ukraine-Japan Cooperation” forum, organized by the New Europe Center. February 16, 2021. <https://www.facebook.com/UkraineMFA/videos/482510059578338/>

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In turn, Sergiy Korsunsky, Ambassador Extraordinary and Plenipotentiary of Ukraine to Japan, stressed that “it is the economy that should become an important aspect of bilateral cooperation, which will lay a basis for growing the interest of Japan’s political leaders in developing a security component in the cooperation with Ukraine”¹⁵.

In particular, the Ambassador said that he had already held dozens of meetings with representatives of the Japanese authorities to begin negotiations on a free trade agreement and update the Convention on the Avoidance of Double Taxation (currently the old document of 1986; the draft convention has already been transmitted to Japan).

The outdated convention has long raised reservations in Japan. According to Japanese business circles, legal entities of Japanese origin must pay a 15 percent tax when sending dividends to their parent company in Japan. Representative offices of other G7 countries have to pay

dividend tax of only 5 percent (Chinese and Korean companies pay the same share). Japanese business has drawn attention to the fact that the 15 percent tax is provided only for companies from Japan and Belarus. Japan has already revised the old convention with other countries of the former Soviet Union; consequently, its companies in Russia, Kazakhstan and Uzbekistan pay only five percent. The agreement with Georgia was renewed on January 29, 2021. The settlement of this issue may have a positive impact on attracting Japanese investment. During the New Europe Center’s forum, the Ukrainian Ambassador drew the participants’ attention to the fact that Japan was the world’s biggest investor: last year, it invested \$ 170 billion in the economies of other countries, with Ukraine receiving as little as \$ 170 million (it should be mentioned, however, that this figure too may be higher due to limitations in the methodology for calculating the volume of foreign direct investment in Ukraine). One of the key messages of the Ukrainian Ambassador was that “in fact, there is much more Japan in Ukraine than the official statistics show”¹⁶.

Ukraine can also expect a positive effect from the Strategic Partnership Agreement¹⁷ and the Partnership on Sustainable Connectivity and Quality Infrastructure between the EU and Japan in the form of coordinated investments in the development of transport, energy and digital systems.

¹⁵ Korsunsky Sergiy. “Asia Strategy in Action. The Role of Ukraine-Japan Cooperation” forum, organized by the New Europe Center. February 16, 2021. <https://www.facebook.com/UkraineMFA/videos/482510059578338/>

¹⁶ *Ibid.*

¹⁷ <https://www.mofa.go.jp/mofaj/files/000381942.pdf>



A ROOM FOR IMPROVEMENT

Japan attaches a certain attention to the development of trade cooperation in Eastern Europe, although currently the relevant indicators of both trade and investment are fairly modest. Still, growth in the next decade may be properly expected if certain conditions are in place¹⁸. A free trade agreement and other agreements that would eliminate trade barriers and deepen trade liberalization are just one such tool. For instance, the aforementioned Japan-EU Economic Partnership Agreement led to an increase in EU exports to Japan by 6.6 percent and of Japanese exports to the EU by 6.3 percent only in the first ten months of its implementation¹⁹. In general, however, Japan negotiates and signs free trade agreements only with the countries with which it already has a significant trade turnover. Japan currently has 18 such agreements signed with partners in 21 countries and regions. The share of trade with these countries is 51.6 percent, which number is even higher – 86.2 percent – taking into account trade with partners with whom Tokyo is currently negotiating a free trade agreement²⁰.

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The 2018 statistics showed that the share of Japan's trade turnover with the six Eastern Partnership countries as a whole (Ukraine, Belarus, Georgia, Moldova, Azerbaijan and Armenia) was only 0.11 percent, therefore necessitating strong arguments for Tokyo's consent to negotiate a free trade area in the short or medium term. It is possible that political and security arguments will be more convincing for the Japanese side than purely trade-related ones. Initially, Japan seeks to increase trade not through FTAs (as such negotiations are effort- and time-consuming) but through improved business conditions (tax cuts or enhanced business environment) as well as partial and gradual market opening (certification, etc).

The Ukraine-EU deep and comprehensive free trade area is also expected to have a further positive effect on trade between Ukraine and Japan, primarily due to the higher quality of products and the gradual introduction of European standards and legislative harmonization with the European Union. Some Japanese companies have already begun to take advantage of the FTA between

¹⁸ Kitade, D., *The Butterfly Effect. Why does Eastern Europe matter to Japan?* / Brief #12, May 2020. <https://www.jstor.org/stable/resrep25018>

¹⁹ European Commission, "First year of EU-Japan Economic Partnership Agreement shows growth in EU exports", 31 January, 2020. <http://trade.ec.europa.eu/doclib/press/index.cfm?id=2107>

²⁰ Ministry of Foreign Affairs of Japan. <https://www.mofa.go.jp/policy/economy/fta/index.html>

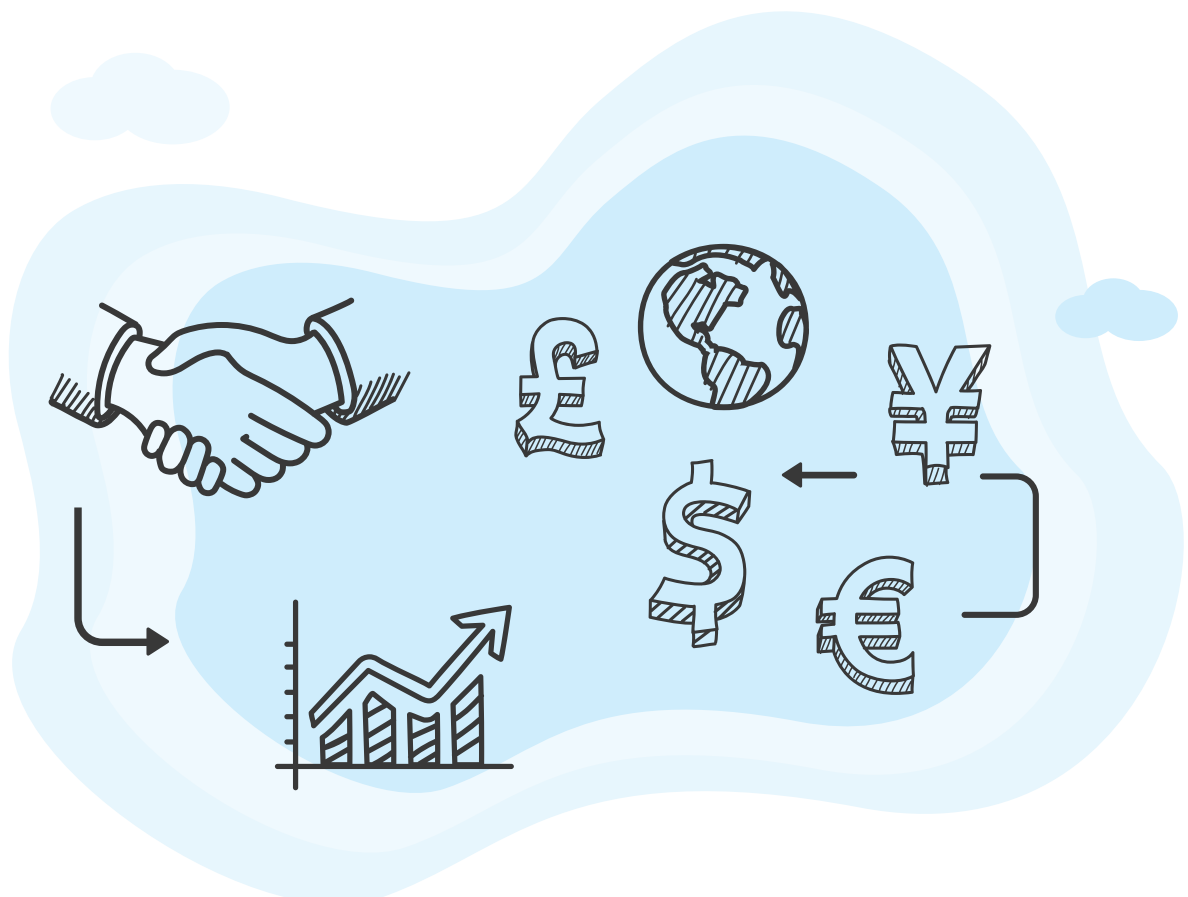
individual Eastern Partnership countries and the EU. For instance, Japanese automotive parts manufacturers export products from Ukraine and Moldova to the EU market²¹.

Japanese investments in the Eastern Partnership countries also remain limited. According to the Japan External Trade Organization, as of August 2019, there were 38 companies operating in Ukraine (for comparison: 11 – in Azerbaijan and Belarus, respectively, six in Georgia, five in Armenia and four in Moldova). The highest level of investment was also found in Ukraine – almost \$ 140 million (2019). This amount is more than ten

times less than the volume of Japanese direct investment in Russia, amounting to \$ 1.92 billion (2019), which may also be due to market size and geographical proximity. Even more Japanese companies could expand their business in the Eastern Partnership countries, not only in terms of cheap and skilled labor but also because of the benefits of FTAs for all three parties – Japan, the Eastern Partnership countries and the EU.

Another important factor for Japanese companies is the size of the market: in this respect, Ukraine is a hands-down winner compared to other Eastern Partnership countries. Ukraine

²¹ Fujikura Automotive Ukraine Lviv, LLC and Fujikura Automotive MLD S.R.L.





attracts Japanese investment primarily because of its potential, being the largest economy and market among the Eastern Partnership countries, with long-established economic ties with Japan (besides, it also has geographical proximity and economic integration with the EU). Strengthening the rule of law and eradicating corruption are the incentives that can spur Japanese investors even more. At the same time, the lack of reform will continue to deter foreign business from more serious cooperation.

Ukraine and Japan have the same understanding of the importance of developing trade and economic cooperation. Tokyo is already showing willingness to open its market to Ukrainian goods, but at this stage Japan is wary of an ambitious project of establishing a mutual free trade area. At the same time, Tokyo appreciates the country's course towards the EU by noting the positive impact of the Ukraine-EU Association Agreement on the interest of Japanese business to work in the Ukrainian market. The faster the reforms in Ukraine are carried out and the more attractive Ukraine is for Japanese business, the more buoyant will be the growth of trade turnover and investment.



ABOUT NEW EUROPE CENTER

The New Europe Center was founded in 2017 as an independent think-tank. Despite its new brand, it is based on a research team that has been working together since 2009, at the Institute for World Policy. The New Europe Center became recognized by offering high-quality analysis on foreign policy issues in Ukraine and regional security by combining active, effective work with advocacy.

The New Europe Center's vision is very much in line with the views of the majority of Ukrainians about the future of their country: Ukraine should be integrated into the European Union and NATO. By integration, we understand not so much formal membership as the adoption of the best standards and practices for Ukraine to properly belong to the Euroatlantic value system.

More about New Europe Center: neweurope.org.ua

