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Recommendations for the U.S.–Japan Economic Dialogue

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U.S. Vice President Mike Pence and Japanese Deputy Prime Minister Taro Aso will meet in Japan on April 18 and 19 for a bilateral economic dialogue.¹ The meeting will highlight opportunities for direct economic engagement between the United States and Japan, as well as regional economic influences and areas for cooperation.

The two countries should seek to expand opportunities for trade and investment, both domestically and globally, with an eye to maintaining expanded market access. Framing any further engagement within the context of what the U.S. and Japan stand to gain from increased cooperation will also be important. Finally, there should be a proposal for a bilateral U.S.–Japan free-trade agreement.

The U.S.–Japan Economic Dialogue

During their first official visit in February, President Donald Trump and Prime Minister Shinzo Abe agreed to continued high-level talks regarding U.S.–Japanese economic relations.² The U.S. and Japan represent roughly 30 percent of the world's gross domestic product (GDP), and each continues to rely on the other's economic success.³ Domestically, both countries face sluggish growth: Annual GDP growth for the U.S. is a recovering 2 percent, while Japan's

stagnates at around 1 percent. Consequently, both countries are continuing to seek opportunities for growth abroad.

The U.S.–Japan economic dialogue is a great opportunity for the two countries to discuss further economic cooperation and share domestic policies at the leadership level. The bilateral meeting will focus on trade, investment, and other economic considerations such as monetary and fiscal policies that might further support growth.⁴ Prime Minister Abe has focused on these issues since taking office in 2012.

Opportunities for Discussion

Among hoped-for outcomes of the dialogue are a better understanding of the likelihood of cooperation on trade and investment and, possibly, some initial discussion of a free-trade agreement, although a trade agreement would take time. Prime Minister Abe has already made the Trans-Pacific Partnership a major focus, and President Trump is devoting resources to reviewing all previous trade agreements.

It is important to note that while the President has the ability to negotiate trade agreements, Congress has discretion over trade objectives through Trade Promotion Authority (TPA) legislation. In addition, any trade agreement reached would set the standard for future bilateral agreements between the U.S. and other Asia-Pacific countries.

The U.S. receives large amounts of foreign investment, and Minister Aso will likely want to talk about opportunities for Japanese companies to invest in the U.S.⁵ Japan is already the second largest investor in the U.S., which certainly should continue to welcome all types of investment.

This paper, in its entirety, can be found at
<http://report.heritage.org/ib4684>

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Both Trump and Abe want their countries' firms to be more competitive globally. In 2016, Prime Minister Abe reduced Japan's corporate tax rate from 36.99 percent to 29.97 percent. That change makes the U.S. corporate tax rate, now at 38.92 percent, one of the highest among the 34 advanced economies within the Organisation for Economic Co-operation and Development (OECD). Japan's tax reduction should serve not only as an incentive for the U.S. to reduce taxes, but also as an area of discussion for the dialogue.⁶

Another issue likely to be discussed is the impact of regional economic powers, particularly China. China aside, Vice President Pence should inquire about Japan's potential for participating in the Asia Infrastructure Investment Bank, which the U.S. should consider joining alongside Japan.

Not This Time

There are several economic policy issues that might be hard to discuss. For example, the independence of both countries' central banks would likely keep the discussion on monetary policy short, since neither administration has direct control over the policies of its banks.

With regard to interest rates, the U.S. and Japan have taken relatively different paths on monetary policy in response to economic downturns. The Bank of Japan has had a nearly 0 percent interest rate policy since Japan's economic malaise began over 20 years ago, with some assets now being purchased at a negative rate, and continues to purchase government bonds at 80 trillion yen a year. In contrast, the U.S. ended its seven-year quantitative easing measures two years ago, and interest rates have begun to increase slowly, most recently by 0.25 percent in March.

Conversations regarding currency, while a concern for the Trump Administration, are likely to be just as short. Trump and Abe have decided to leave the currency talks to Secretary of the Treasury Steve Mnuchin and his counterpart, Minister Aso, who is also Minister of Finance.⁷ This makes sense: Opportunities for future bilateral gains should not be overshadowed by difficult discussions about currency values.

One topic that probably will not (and should not) be discussed much now, but which eventually will have to be addressed, is the increasing debt caused by government expenditures and fiscal problems associated with aging populations. U.S. public debt now stands at 105 percent of GDP. For Japan, public debt is 250 percent of GDP. Neither is sustainable in the long run.

Issues for Consideration

At the meeting, Vice President Pence should seek to:

- **Encourage foreign direct investment and market-opening measures.** Japanese firms want to invest in the U.S., and U.S. firms want access to Japanese markets. Both countries should seek to ease any difficulties that impede investment in each other's economies.
- **Propose a U.S.–Japan bilateral free-trade agreement.** Free-trade agreements can boost U.S. economic prosperity. A U.S.–Japan agreement does not have to be signed on day one, nor do negotiations even have to be considered. However, Vice President Pence and Minister Aso should agree to pursue the idea of a bilateral agreement actively within their governments.

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1. News release, "Vice President of the United States to Visit Japan," Ministry of Foreign Affairs of Japan, April 7, 2017, http://www.mofa.go.jp/press/release/press4e_001538.html (accessed April 7, 2017).
 2. Transcript, "Remarks by President Trump and Prime Minister Abe of Japan in Joint Press Conference," The White House, February 10, 2017, <https://www.whitehouse.gov/the-press-office/2017/02/10/remarks-president-trump-and-prime-minister-abe-japan-joint-press> (accessed April 12, 2017).
 3. The World Bank, "Gross Domestic Product Ranking Table," last updated February 1, 2017, <http://data.worldbank.org/data-catalog/GDP-ranking-table> (accessed April 4, 2017).
 4. Transcript, "Remarks by President Trump and Prime Minister Abe of Japan."
 5. Mitsuru Obe, "Abe to Tout Japan's U.S. Investment Plans in Trump Meeting," *The Wall Street Journal*, February 6, 2017, <https://www.wsj.com/articles/abe-to-tout-japans-benefits-to-u-s-in-trump-meeting-1486373098> (accessed April 12, 2017).
 6. Organisation for Economic Co-operation and Development, "Table II.1. Corporate Income Tax Rate," 2016, https://stats.oecd.org/index.aspx?DataSetCode=Table_II1 (accessed April 12, 2017).
 7. Transcript, "Remarks by President Trump and Prime Minister Abe of Japan."
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■ **Inquire into greater regional cooperation.**

U.S. and Japanese firms are invested in many countries, and both countries should consider greater regional cooperation. Withdrawal from the Trans-Pacific Partnership should not deter the U.S. from seeking such cooperation.

■ **Define priorities in the bilateral relationship.**

For this first meeting, it is important to cover the most pressing issues and areas that present the greatest opportunities for our bilateral relationship. Government debts, aging populations, and currency and monetary policies should be reserved for later economic dialogues.

Vice President Pence and Minister Aso's bilateral meeting will set the tone for U.S.–Japanese economic engagement over the next several years. It is important to focus on the essentials and highlight the mutual engagement that has allowed both countries to prosper up to this point.

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