
Stephen D. Behnke
Western Michigan University, steve.behnke@hotmail.com

Follow this and additional works at: http://scholarworks.wmich.edu/honors_theses

Part of the Political Science Commons

Recommended Citation
Stephen D. Behnke, having been admitted to the Carl and Winifred Lee Honors College in 1993, successfully presented the Lee Honors College Thesis on April 22, 1997.

The title of the paper is:

"US/Japan Trade Policy: A Defense of Limited Unilateralism"

Dr. William Ritchie
Political Science

Dr. David Flanagan
Management
US/Japanese Trade Policy:
A Defense of Limited Unilateralism

Steve Behnke
Lee Honor’s College Thesis Statement
Winter 1997 Graduate
Political Science Dept.
# Table of Contents

Introduction: From the Evil Empire to the Evil Import .................................. 1
Endnotes ............................................................................................................ 3
Chapter 1: Japanese Trade Practice ................................................................. 4
Endnotes ............................................................................................................ 16
Chapter 2: The American Response Under the WTO .................................... 18
Endnotes ............................................................................................................ 24
Chapter 3: Bilateral Trade Action with Japan ................................................ 25
Endnotes ............................................................................................................ 39
Chapter 4: Policy Proposals ........................................................................... 41
Endnotes ............................................................................................................ 46
Bibliography ..................................................................................................... 48
Introduction: From the Evil Empire to the Evil Import

With the end of the Cold War, the Soviet threat is no longer a factor in our formulation of trade policy with Japan. In days past, the State Department cited geopolitical concerns in its on-going battle with those sections of the government who were more willing to slap trade restrictions on Japan for alleged unfair trading practices.1 Until the early 1970s, United States trade policy was almost totally subjugated to winning the Cold War, our market was thrown open to imports even if others were not. Back then, though, this was not only a wise Cold War "military tactic," but it also made good economic sense. Japan and Europe were so economically decimated by World War II, that we needed to pull up their economies in order to have trading partners.2

The oil shortages and global slowdown in economic growth during the 1970s changed these policies, however. From that point until the collapse of the Communist bloc, trade relations between Japan and the United States grew increasingly tense. Even former President Ronald Reagan, a vocal supporter of laissez-faire government, slapped a 100% retaliatory tariff on $300 million worth of Japanese imports in 1987 because of an alleged violation of a 1986 semiconductor agreement.3

Mercantilism was abandoned by most economists in the 1700s, and most economists assert that imports are the most important part of free trade.4 Public opinion certainly does not always gel with "most economists," though. With the evil empire gone, we seem to be focused on the evil import. It has often been mentioned that we may be leaving the Cold War only to face a number of other international problems: many of
which will be caused by economic trends and international trade. These other problems are certain to affect US/Japan trade policy.

The multilateral trading regime, known as the General Agreement on Tariffs and Trade (GATT), finished its Uruguay Round in 1994. GATT is now known as the World Trade Organization (WTO). The major objective of the WTO is to make world trade freer by reducing trade barriers. One of the noteworthy aspects of multilateral negotiations, though, has been the absence of any discussion of the benefits of imports. Opening up one’s market to the evil import was put forth as the supreme sacrifice, only to be implemented if another market would make a similar sacrifice (i.e. open their market to imports.)

WTO members are quick to embrace the idea of increased exports, but not necessarily of increased imports.

Besides the new WTO, other trade issues have affected US/Japan trade relations. Among these issues are American unilateral action against Japan and bilateral negotiations between the two countries. Since such negotiations will be heavily discussed in this paper, all we need to mention here is that many people view bilateral negotiations and unilateral actions as a threat to the multilateral trading regime (the WTO). However, I hope to demonstrate in this paper that unilateral negotiations, threats, and retaliations, have accomplished progress that the GATT could not have achieved alone.

Another important issue bearing on US/Japan trade relations is that geopolitical concerns continue to be a part of trade relations, even though the Soviet threat is gone. There are still a lot of spots around the world where military conflict could flare up (e.g. the Middle East, China, Korea), so it is still immensely important that we stay on good
terms with Japan. Therefore, geopolitical concerns will, and certainly should, continue to temper rash decisions to impose our own trade barriers against Japan. Not only that, but just because the Soviet threat is gone does not mean that another threat will not rise up to take its place; many people believe that China could be that threat. Since Japan has such great historical, geographical, and political ties to China, this is another reason to allow geopolitical considerations to figure into our foreign trade policy.

Finally, the Japanese economy is struggling. In 1994 and 1995 the Japanese economy grew at an anemic 1% per year. In 1996 it seemed that the Japanese economy was finally coming out of the doldrums when it grew 3%. However, it is estimated that the economy will only grow at a rate just over 1% in 1997. The prolonged Japanese recession of the early 1990s is forcing changes in the Japanese system. It is the Japanese system as it has been known that we begin with now.

2 Prestowitz, in Free Trade vs. Protectionism, 1988, p. 131.
6 Business Week, January 27, 1997, p. 27.
Chapter 1: Japanese Trade Practice

Many economists are so wedded to the free trade religion that whenever America threatens retaliatory trade action, they accuse America of unfairly complaining. Furthermore, many of these same economists will not believe that it can be beneficial to deviate from the laissez-faire paradigm. Overall, free trade is beneficial, but some government intervention can also be beneficial. In Chapters 2 and 3, we will see that many elements of American trade policy are unfair; and, when making policies to improve our economy we should certainly place more emphasis on domestic policy than trade policy. However, as this chapter will demonstrate, many aspects of Japanese trade policy are unfair to American imports. The discussion cannot stop there, though, because Japanese trade policies are detrimental to more than just American exporters. Much more importantly, these policies are harmful to Japanese consumers, as well. This was even evident before the current Japanese recession.

Japanese Capitalism

It can be hard to define why Japanese trade practice is unfair. During the 1980s it was more common for people to believe that if the United States complained, we were complaining unfairly. Today, though, many people may not be able to define why Japanese trade practice is unfair, but they believe that it is unfair. Hopefully, we will be able to define Japanese trade policy in more exact terms, and a good place to start is with a description of their system of capitalism.

The economies of Japan, and South Korea and Taiwan for that matter, have used
protectionism to positively develop their own economies. Free trade, as Americans would define the term, can be an alien concept to them.\textsuperscript{1} The basic theory of free trade, David Ricardo's theory of comparative advantage, states that countries will produce what they are relatively better at producing. And, of course, the logical extension is that they will import those products which they are relatively less able to produce. Japan, on the other hand, sees comparative advantage as something to be conquered and developed.\textsuperscript{2} Carried to an extreme, this policy could justify using the infant industry argument in every part of the economy. Any product that Japan is less able to produce now, could be turned into a comparative advantage if they protect it long enough.

Another basic difference is that American economics is geared towards maximizing consumer welfare. This is evident in our strict antitrust laws. However, the Japanese system is geared towards producer welfare. Japan is not naturally wealthy because of its poor resource endowment. History has also played a role in Japan's producer welfare orientation. Ever since the Meiji Restoration, Japan has attempted to raise its economy up to the modern level of the rich Western countries. After World War II, Japan's economy was devastated. The focus further shifted to producers who, it was believed, were most able to repair the country.\textsuperscript{3}

For these reasons, economics is viewed as a matter of national security to many Japanese citizens. All elements of Japanese society are geared towards economic progress, from the workers on up to the Ministry of International Trade and Industry (MITI) and other prominent governmental agencies. Conflict arises because policies that
the United States views as protectionist are seen by Japan as its only way to survive as a first-class nation.4

High-technology industries have intensified and highlighted national differences in the models of capitalism. Since high-tech advantage can be created rather than inherited, as some would argue, conflict has focused on the way a country creates its advantage. In the past, trade conflicts were focused on border policies such as tariffs slapped on imported goods. GATT has been successful in eliminating most such barriers, especially among developed countries. The only noticeable tariffs that remain are on agricultural products because of the political power of farmers.5

Unfortunately, international trade negotiations have become more complex. Areas of trade negotiations which were once off-limits because they were considered the nation-state’s sovereign choice are now exactly those issues which generate so much conflict.6 Now we turn to many of these issues as we look at an area called competition policy.

**Competition Policy**

Tariffs, and non-tariff barriers (NTBs) such as quotas are well-known barriers to free trade. Japan employs few tariffs or NTBs so it can be difficult to pin down their unfair trading practices. However, several new areas of trade law have arisen in recent years, including intellectual property rights, labor standards, environmental standards, and competition law. Some of these standards are so new they have not even been codified; or, if they have, the process has just begun. Competition law falls into this category. In Chapters 2 and 3 we will see how competition policy affects multilateral and bilateral
negotiations. Now, though, we need to define competition law because it goes a long way towards explaining America's concern over the openness of Japan's market.

Collins and Bosworth define the problem of competition policy nicely. "The biggest trade friction problems have been arising in recent years and will continue to arise over issues of competition [which are] cartel-like activities; non-competitive business practices, informal arrangements between governments and companies; closed distribution systems, all of the so-called non-tariff barriers that have been so much in dispute over the past ten or fifteen years. Most of these do not fall under the rules of the new WTO." This is exactly why dealing with Japan in the area of trade can be so frustrating.

I'd like to deal with each of these issues in turn. To begin with, cartel-like activities are very rare in the United States. Such activities are an excellent example of the difference between the two forms of capitalism. Since the United States economic system is geared towards consumer benefit, the United States's strict antitrust laws would prevent cartelization among industries. In Japan, explicit or implicit cartels are not only informally approved, they are often encouraged.

There are also informal arrangements between governments and companies to keep out foreign competitors. The soda ash case is a good illustration of this problem. The production of soda ash is expensive and energy intensive. Soda ash occurs naturally in America, and it can be mined for $75 per ton or less. Despite this cost advantage the United States exported a mere 60,000 of the 1.4 million tons of soda ash used in Japan. The unloading charge for soda ash in prominent ports, such as Antwerp or Cape Town,
was $20 per ton. Japan charged $50-$75 per ton at its *one* unloading facility, the Toko Terminal owned by a consortium of Japan’s soda ash manufacturers and large trading companies.

Inevitably, the United States complained about this unfair treatment. Our complaints were met by Japanese officials’ claims that we were not trying hard enough, that we provided unreliable service, and that we produced a poor quality product. Eventually, some changes were made and sales increased to 200,000 tons per year.9

The soda ash case is an example of how elements of the Japanese business sector can work in tandem to prevent Japanese exports in more subtle ways than implementing non-tariff barriers such as quotas. The Kansai case is an example of how informal government practices can also limit imports. Here, the activities are restricting a service (construction), rather than a manufactured product.

Kansai was an airport that Japan was building. Japan did not allow American firms to bid on the construction of some parts of the airport. In order for foreigners to bid on those sections that were opened up to foreign bidding, they had to have experience in construction projects in Japan. Of course, this was experience that US firms did not have because they had been kept out of other Japanese construction projects.10

Perhaps the most well-known of Japan’s informal trade barriers, is the unfair treatment of US products in the distribution system. The ties between Japan’s domestic producers and retailers run deep and have heavy social obligations.11 The difference between this arrangement and the United States distribution system could not be more striking. For example, if an American manufacturer pressured dealers not to sell Japanese
cars, that manufacturer could be put in jail. In Japan such pressure against American made
cars is commonplace. The Japanese place a lot of emphasis on preserving long-term
relationships. This is also true in the producer-retailer relationships. The end result is that
foreign firms simply do not offer the benefits that local producers do. How can a
multilateral trade organization regulate the fact that Japanese producers pressure retailers
to sell their own products?

In 1994 about 51% of Japan's 1.5 million retailers were classic "mom-and-pop"
stores operated by one or two people. Large retail stores are discouraged in Japan for a
number of reasons. First of all, large retail stores could circumvent the ties between
producers and retailers we just discussed in the previous paragraph. Because of their size,
they are not dependent on wholesalers who are, in turn, dependent on manufacturers.
This is especially important in Japan, where it is common for products to pass through
three or four wholesalers before being sold at a retail store. In the United States products
usually pass through one wholesaler, while in Europe products usually pass through one
or two wholesalers. An important result of this practice is that the small stores are more
dependent on local (i.e. Japanese) producers. And, as you may have guessed, large
retailers would have more freedom to sell imported products.

A second, and, political reason for maintaining a large number of small stores is
that the distribution sector has served as a shock absorber for high unemployment. The
small shopkeepers are numerous and politically powerful. It is in their best interest to
prevent the emergence of large retail stores that could put them out of business.
A third reason is that the government, as we have already seen, emphasizes production over consumption. The Japanese government works to keep consumption low to encourage a high savings rate and to make production available for exports. What better way to keep consumption low then to prevent large retail stores which encourage spending.

The Large-Scale Retail Store Law, enacted in 1974, put in place numerous bureaucratic hurdles for business people wishing to start a large retail establishment. This law was the codification of the Japanese government’s policy of keeping out large retailers in favor of “mom-and-pop” stores. Fortunately for Japanese consumers and American exporters, this law is being relaxed. For instance, *Toys R Us* opened its first store in Japan in January 1991 to great media fanfare. Twenty-nine more *Toys R Us* stores were scheduled to open by late 1995. Other relaxations of legal restrictions have included allowing longer store hours and limiting the wait between application for a large store and approval of the project. Japan is likely to experience an increase in mergers of small and medium sized stores and the construction of more large retail establishments. This should drive down prices which would, in turn, improve the welfare of Japanese consumers.¹⁸

One final point which should be made before leaving this section is that many trade watchers argue that we simply need to try harder. Naturally, a country must try harder to establish itself in a foreign market. Many American companies have made mistakes in their attempts to market products in Japan. They may use American, rather than Japanese lettering; or, they may improperly re-engineer a car that must have the steering wheel on the right side. Despite these examples, though, the Japanese market is inordinately
difficult to penetrate. No one accuses Hong Kong or Taiwan of being poor traders, but they have just as much trouble as we do in penetrating the Japanese market.21 The "Made in Hong Kong" or "Made in Taiwan" labels are common in the United States, but relatively rarer in Japan.

Elements of unfairness in the Japanese economy lie on a spectrum. The fact that Japanese consumers are less likely to purchase foreign elements may justify the argument that we should try harder. The fact that members of the gaiatsu purchase from each other is a little harder to justify. And the fact that the Japanese government keeps foreign firms from bidding on non-military government contracts is hardest of all to justify.

To justify their argument that foreigners are not trying hard enough, critics may point to success stories. For instance, Citibank has done quite well in Japan. However, the role of foreign banks actually declined in the 1980s, and foreign banks account for only 2% of deposits. It may be that the Japanese government "allowed" Citibank to do well so they could have a foreign success story.19 This may seem like a cynical interpretation, but the Japanese government has bought off foreign pressure in other markets by allowing one firm to do well in the Japanese oligopoly.20

**Intra-Industry Trade**

The preceding discussion of Japan's alleged unfair competition policy begs an obvious question: Are these practices reflected in the trade statistics? The theory of intra-industry trade, or trade in similar manufactured products, helps answer this question.

A discussion of Japan’s balance of trade is not as straightforward as it was a mere
two years ago. As recently as 1994 it would have been difficult to defend Japan’s balance of trade, but the Japanese economy is slowly changing and becoming more open to foreign exports.

It is unlikely that Japan will ever have a trade deficit in manufactured products because they are forced to import so many raw materials due to their poor resource endowment. Even if we take this into consideration, Japan demonstrated many strange patterns of trade during the 1980s. It was the only major country to experience a decline in the ratio of total imports to GDP, and it was the only industrialized country to run large trade surpluses with the Little Tigers in East Asia. When Edward J. Lincoln analyzed Japan’s trade, he used several measurements and held different relevant variables constant. For example, he examined a study by Kazuo Sato which assumed that larger population bases (like Japan) import less, and considered the extensive intra-EU trading in Europe. His conclusion was blunt: “Any way the question is posed, Japan turns out to be different. Its pattern of behavior is seriously at odds with all the expectations generated by intra-industry trade theory.” In 1995, though, Japanese imports of manufactured products nearly doubled from just over $100 billion to almost $200 billion. Hopefully, this signifies that change is afoot.

Japanese Consumers

As I have hinted at earlier, the Japanese consumer has suffered because of Japanese trade practices. This is one of many reasons that Japanese trade policies do not only hurt American exporters. In some ways, their practices do harm our producers. But the affect on Japanese consumers has been much more devastating.
Edward J. Lincoln, paints a dark picture indeed of the plight of the Japanese consumer in his work *Japan’s Unequal Trade*. He explains that the Japanese standard of living continues to lag behind other industrialized nations for many reasons. The incessant emphasis on manufactured exports is a main cause of this. Low productivity in agriculture and services, and deficiencies in basic elements of social infrastructure have been a consequence of Japan’s blind emphasis on manufactured exports. Moreover, Japan has continued to expand exports despite a prohibitively strong yen.\textsuperscript{25}

Governmental policies to keep consumption low have also affected the Japanese consumer. Tax and land-use rules restrict housing space.\textsuperscript{26} These same laws also inflate urban land prices, forcing citizens into cramped dwellings where few consumer durables can fit.\textsuperscript{27} The situation is so bad that a college graduate’s anticipated life earnings will barely pay for one of these cramped one-room apartments in Tokyo. The average worker has a three to four hour commute because living space in the city is so expensive.\textsuperscript{28} Furthermore, according to some estimates, Japanese men work an average 2617 hours per year and Japanese women work an average 2409 hours per year; American workers average 1943 hours per year.\textsuperscript{29}

The Japanese worker suffers in other ways for the Japanese production behemoth. One reason that Japanese exports are so successful is because of its low prices. This is accomplished, in part, by holding worker’s wages below the productivity increases which should raise their salaries. It is further accomplished by imposing harsh demands on intensely loyal, but dependent and vulnerable subcontractors.\textsuperscript{30}
These subcontractors demonstrate the two-tier society prevalent in Japan. The large multinational corporations have been successful, but these subcontractors represent the dark underbelly of the Japanese economic machine. In fact, one of the reasons that the average hours worked per year is so high is that small and medium sized enterprises (often these very same subcontractors) are not covered by the Labor Standards Law which sets maximum hours. Yet, two-thirds of Japanese employees work in small-to-medium sized firms.31 It is no wonder that Japanese workers are more dissatisfied with wages and general working conditions than US, British, German, Australian, or Singaporean employees.32

To add insult to injury, the environment in which the average Japanese citizen works and lives is outwardly opulent. Gavan McCormack, in his 1996 work entitled, very accurately, The Emptiness of Japanese Influence, describes Kobe before the earthquake as "a city exclusively devoted to convenience and economic efficiency [which] betrayed the interests of its citizens and sacrificed its weak and poor."33 Mr. McCormack, a few pages later, quotes Morita Akio, Chairman of Sony as saying, "Until Japan proved ready to redefine itself, it cannot hope to be accepted on the same stage as Europe and North America."34 The recently coined term fukoku hinmin (Enrich the country, impoverish the people) symbolizes this development.35

Following World War II, as we have seen, the Japanese people worked in concert to rebuild its war-ravaged economy. It is unlikely that this generation, or subsequent generations, of Japanese will continue to sacrifice in this manner for their country. Recent developments in the behavior of Japanese consumers demonstrate that change is coming.
In the past the Japanese consumer was kept in the dark about imports; consumer behavior represented this. The Japanese term for imported products was *hakuraihin*, meaning “goods that come by ship.” These imports, which were usually displayed with a flag or sticker to signify that they are different, were seen by consumers as exotic products coming from far away.36

Western economists still think of Japanese consumers and producers reacting to supply/demand conditions. This is always modified by existing social norms.37 Not only that, but Japanese consumers often assume locally produced goods are better than equivalent foreign products. And these equivalent foreign products are quick to appear. Whenever a foreign product attracts a Japanese audience, local companies are quick to duplicate it with additions that will attract the Japanese consumer.38 Once again, the question this brings up is should this be regulated by a multilateral trading order? Hopefully, in time, this question will never need to be answered because Japanese consumption practices are starting to change.

Japanese consumers are Westernizing in that they buy rooms with tables and chairs rather than tatami mats, and they are buying bread, blue jeans, hamburgers, etc. In other words, their tastes are becoming more cosmopolitan.39 As the Japanese consumers’ tastes have changed, so have their spending practices. Because of the trade practices described earlier, the prices of products in Japanese stores are very expensive. Japanese travelers stand out overseas because of their heavy purchasing. That is because these products can be purchased cheaper abroad, *even Japanese products*.

An increasingly noticeable example of this trend is the increase in the use of over-
seas mail-order catalogs. One mail-order company said that they started their business after hearing many Japanese employees say that they would like to purchase the high-quality products they saw while traveling abroad as easily as they are able to purchase domestic products.40

---

1 Tyler, in *Free Trade vs. Protectionism*, 1988, p. 34.
8 *Japan's Unequal Trade*, 1990, p. 100.
10 *Regulating Unfair Trade*, 1993, p. 82.
17 *Japan's Unequal Trade*, 1990, p. 130
21 Ibid, p. 190.
23 *Japan's Unequal Trade*, 1990, p. 60.
26 Ibid.
29 Ibid, p. 80.
33 Ibid, p. 79.
34 Ibid, p. 82.
37 *Japan's Unequal Trade*, 1990, p. 100.
Chapter 2: The American Response Under the WTO

If the United States believes that Japanese trade policy is unfair, it can, basically, react in one of two ways. It can either act within the multilateral trading regime, or it can act outside of it by acting alone or only with Japan. This chapters will examine the former choice, while the next chapter will examine the latter choice. The multilateral trading order is organized under the World Trade Organization (WTO), formerly the General Agreement on Tariffs and Trade (GATT). We will look at the WTO first because we will examine the pros and cons of acting outside of the multilateral trading order in the next chapter.

The WTO

The United States has been very successful in leading the policy making direction of the GATT. As the largest and most influential economy since the end of World War II, other countries have followed the behavior of the United States in the multilateral trading order. As Patrick Low says in Trading Free, “[I]f the United States chooses a route different from multilateralism, the world will not be far behind.”

The current struggles of the WTO have caused some people to imagine a golden age of GATT that never really existed. The GATT has always been a struggle. The problem now is that the issues are more complex. The first ever meeting of GATT, which took place in 1947, mainly focused on tariff reduction. This was a struggle, but it was successful. In the United States tariff rates fell from 54% in 1930 to 12% in 1983. Then, starting in 1978 with the Tokyo Round of GATT, non-tariff barriers became a focus of trade talks. This has been a struggle, but has also led to a worldwide reduction in NTBs.
The Uruguay Round was a struggle to finalize, and the agreement reached will be a struggle to implement for several reasons. To begin with, the Uruguay Round of GATT dealt with a wide array of issues with which the GATT has never had to contend. The Uruguay Round implemented a General Agreement on Trade in Services (GATS). This is an issue the United States wanted to see put on the table, and the US was successful in seeing it implemented. The GATS is similar to GATT because it does not move to free trade in services, but will start the world down the path of freer trade in services. Another new issue dealt with in the Uruguay Round of GATT was intellectual property (IP) protection. Unlike the GATT or the GATS, the Trade Related Aspects of IP Rights (TRIPs), achieved a minimum standard of harmonization.\(^3\) The new WTO also includes a more powerful dispute resolution process. Many trade watchers, though, believe that the dispute settlement process was designed to be drawn out so that the sides could reach a settlement on their own.\(^4\)

These issues are not as straightforward as tariff or NTB reduction. The TRIPs is especially noteworthy because US IP law is very different from other countries. True, America's ability to negotiate a multilateral agreement in an area where there are so many differences among countries demonstrates the influence the United States has over the GATT. However, these differences are likely to be a source of heated conflict.\(^5\)

It will be interesting to see how effective the GATS and TRIPs are in dealing with their respective issues because there are so many issues with which the WTO could still take up. The WTO could deal with wage scales, worker's rights, working conditions, exchange rates, environmental controls, tax codes, banking regulations, \textit{ad infinitum}.\)
Where should the WTO draw the line? Should the WTO begin negotiations on competition policy?6

**Japan and the WTO**

Japan presents several unique difficulties for the United States in multilateral negotiations. The structure of the Japanese government and business sectors are very different from the United States. Some people believe that the Japanese government has a central organ; this is not true. The Japanese government is actually a balancing act between semiautonomous groups who share power. These include certain political groups, powerful bureaucrats, and industrialists.7

The economic sector is also different for two reasons. One is the two-tiered economy consisting of low wage and dependent subcontractors, and the large multinational corporations for whom these subcontractors work. The other major difference is the *keiretsu* relationship. The *keiretsu* relationship, or enterprise group, is defined nicely by Ozaki.

The enterprise group consists of a major bank, a major trading company, and a major manufacturing firm as the central core of the group, and of several large manufacturing firms in different product lines, below which lie pyramids of affiliated smaller subcontracting firms.

There are elements of cooperation among the *keiretsu* group which would be illegal in the United States. The best known, and perhaps most important, is cross-ownership of stock. For instance, a bank may own a large amount of stock in a company in its enterprise group. This is done so that the bank has a defined interest in the company to which it loans money. In the United States under the Glass-Steagall Act, it is illegal for banks to own stock.8
Of course, the differences between Japan and the United States are not limited to this. History, geography, resource endowment and everything else that goes into the development of a nation-state have created differences between the two countries. Perhaps this is what prompted John M. Culbertson to write that "national differences in circumstances, ideologies, and administrative capabilities, and other factors are too important to permit any uniform and general system for arranging international trade."

Competition policy (or antitrust rules) have not been formally dealt with by the WTO, but this will not prevent it from being a source of conflict. If (more likely when) there are competition policy negotiations, the negotiations will be very delicate. The question which will loom over the negotiations will be which Japanese practices are unfair, and which simply represent a fair, and welfare-increasing, element of the Japanese system of which Japan has every right to protest the removal. Many of these are simply an offshoot of the Japanese system of capitalism. For instance, Japanese companies are able to sell below cost for a time because of the keiretsu relationship. A company earning temporary losses in one market can be offset by profits in another sector of the keiretsu. Should this be considered a violation of antitrust or simply effective capitalism? There certainly is not as much consensus on the answer to this question as there is to whether quotas or tariffs should be reduced.

The Uruguay Round of GATT was successful in eliminating most tariffs on goods and setting up a mediation system. However, the United States, Japan, and Europe cannot decide where to take the WTO next, and whether this next step should include deliberations on competition policy. Japan is unlikely to agree to such a step. They have
always wanted the multilateral trading system to only focus on manufactured goods. Given Japan's balance of trade and economic system, this is not surprising. Japan would like foreign markets to be more open for its export machine, but Japan is dead last among industrialized nations in trade in services.

The United States and the WTO

Despite the many problems with the WTO, the United States and the rest of the world have much to gain from a successful multilateral trading order. Negotiations began in 1984 to begin a new round of GATT talks in part because it was estimated that global welfare would increase by $250 billion (1% of world GDP). And, as we have seen, there were many new, emerging issues with which the WTO could still take up. It may appear that it is bad news for the multilateral trading order that these new issues have arisen. Nothing could be further from reality. It is true that these new issues will make negotiations more complex and, possibly, less successful. These new issues arose, however, because of the vast increase in international trade; it was inevitable that new issues would arise as the world economies became more intertwined.

In spite of these potential gains from trade, the WTO is experiencing many problems. Many international political observers believe that a multilateral trading system can only survive with a hegemon. This theory proposes that a hegemon is necessary to produce the public goods and set the example for the rest of the world. As we discussed earlier, the United States was willing to open its market to imports during the Cold War even when other countries were not willing to do so. This occurred for many reasons, not
the least of which was that we were so economically strong that we could afford to wait on other countries to open up their markets.\textsuperscript{14}

Clearly, the United States is still the leader of the world economic community. Is its position still strong enough to permit it to play the role of hegemon? If it is not, then Japan’s role in the multilateral trading order will be a critical one. So far, though, Japan has not shown much interest in exercising political influence commensurate with its economic power. Moreover, Japan has never been particularly active in the GATT system. Some have gone so far as to argue that, for the most part, Japan considers its multilateral trading activity to be a necessary evil to improve its image in the international community.\textsuperscript{15}

The United States has had its problems with free trade, as well. Since, constitutionally, Congress can override the US’s WTO responsibilities, the impact that the WTO has on the United States will depend on the reactions of those in the trade war trenches: Congress, Courts, trade lawyers, and administrative agencies.\textsuperscript{16}

As we have seen the WTO gave teeth to the dispute resolution agreement of the multilateral trading order. If history is a guide, there may be trouble brewing; US agencies openly defied many decisions of US/Canadian panels in deciding trade disputes under the US-Canada Free Trade Agreement (the precursor of NAFTA).\textsuperscript{17}

At the risk of sounding redundant, the United States is better off with the multilateral trading order. Despite the hand-wringing about the threat of imports, our economic welfare is improved by keeping trade as free as possible. There is great political pressure in this country to protect threatened industries, even if such protection
decrease total economic welfare. The WTO permits politicians to resist these pressures by pointing to their duty under the multilateral trading order.

Foreign competition also forces domestic companies to improve efficiency. And, if a country has a comparative advantage in the production of an input, domestic companies will be better off purchasing the input from the cheapest source. Nonetheless, it may be necessary to act bilaterally to open a market that is closed. The libertarian argument that we are better off with an open market even if other countries’ markets are closed to our exports is not very popular, and it is certainly debatable. It is the argument over whether to use bilateral and unilateral negotiations that we turn to in Chapter 3.

---

1 Trading Free, 1993, p. 140.
4 Business Week, June 5, 1995, p. 35.
7 van Wolferen, in Free Trade vs. Protectionism, 1988, p. 110.
9 Culbertson, in Free Trade vs. Protectionism, 1988, p. 66.
12 Japan’s Unequal Trade, 1990, p. 136.
14 Trading Free, 1993, p. 18
15 Bid, p. 246.
16 Journal of World Trade, June 1996, p. 64.
17 Bid, p. 67.
CHAPTER 3: Bilateral Trade Action with Japan

It is important to remember that the trade conflict we are experiencing with Japan is not new. Since hindsight is 20/20 we can learn several lessons from previous trade responses. The high tariffs we imposed on Japan in the 1930s caused a fear and resentment still felt today.¹ We should note our successes and mistakes when dealing with other countries, as well. South Korea is especially noteworthy in this respect. Both Korea and Japan have poor resource endowment, abundant labor, and strong entrepreneurship.² When we retaliated against Korean color TVs in 1984, the shock to the Korean government, industry, and public, who considered the US a key ally, is similar to the reaction we get from Japan, who also considers us a key ally.

The Politics of Trade Policy

No trade policy decision we make, or choose not to make, occurs in a vacuum. As mentioned earlier, government organizations such as the State Department and the National Security Counsel are more concerned about global tranquillity than domestic jobs. There is no reason that this should not be a factor to consider when we formulate our national trade policy.³ We should not be upset that our trade policy is not precise. There are so many factors to consider, and there are no absolute truths.⁴

It is unfortunate, though, when politics get in the way of wise trade policy. Trade ceased to be a partisan issue a long time ago. Economic conditions are the best predictor of how a member of Congress will vote on a certain issue. For instance, if a Congressman lives in an affluent district where a high-tech export is important, that Congressman is very unlikely to support policies which would likely anger foreign countries. On the other
hand, if a member of Congress represents a district which produces an import sensitive product such as textiles, that representative is much more likely to support policies which are intended to protect the workers in that industry.

Another reason that politicians often make economically unwise decisions is that appearing tough on trade can improve one’s chance at reelection. First of all, low-growth sectors often suffer visibly because of layoffs and business losses in the industry. Obviously, this may have less to do with unfair trade, and more to do with a weak industry, or loss of comparative advantage. To be blunt, competition can be a scary thing. The first chairman of the US Tariff Commission once said that ‘Competition of any sort is unwelcome enough; competition from foreigners seems always to be regarded with particular dread.”

Of course, there are times when an industry comes back, and the protection earned by the representative helped that to happen. This is the essence of our representative democracy. However, if it seems that an industry representative is one of the only Congressmen pressuring for protection, we should only grant that protection after a very careful consideration of the facts.

This, in part, explains the protection of the automobile industry in the early 1980s. By early 1980 members of Congress recognized that auto industry distress had wide appeal as a political issue. There were a lot of autoworkers, and the perception was that their struggles were caused by unfair trade. Traditionally, Congress has been more protectionist than the President. Thus, in 1984 when President Reagan ceded trade policy power to Congress because of his own interest in tax relief and fighting communism, the
die was cast. A voluntary export restraint (VER) was negotiated in 1984 despite sharply increased prices and large executive bonuses. 7

Another reason that politicians have made some unwise economic decisions is that we have, unfortunately, a squeaky wheel policy. The industry that complains the loudest has gotten the most attention. In our representative democracy, those groups which organize most effectively are bound to receive the most attention. 8 For instance, in the debate over the North American Free Trade Agreement (NAFTA), many agricultural groups were harmed because of regional and commodity divisions. The sugar industry, however, was united and achieved a high level of protection. 9

Protectionism has been blunted in this country because of an underlying broad support for free trade. This has been a critical counter to organized pressure groups. A Democratic Congressman from North Dakota, Byron L. Durgan, said it is still considered “almost a shameful thing to be labeled a protectionist.” 10 It was this broad underlying support for free trade which helped NAFTA pass. As of 1997, America was experiencing prosperous economic times. When we have another recession, it is inevitable that protectionist sentiment will grow with the unemployment rate. But, hopefully, long-term support for free trade will continue.

There are some advantages to the inherently political aspects of our trade policy. It may be inevitable that there will be some protectionism. For the most part Congress leaves trade policy decision making to the executive branch. Occasionally, though, it may be necessary to buy off opposition to free trade in general with a few particular exceptions. 11 However, many economists believe that protection often postpones the loss
of jobs. Or, the added profits may increase executive bonuses rather than protecting jobs. If so, this argument is weakened.\textsuperscript{12}

Another advantage of bilateralism is that it may help open up Japanese markets when the WTO will not. The European Union EU has gone to the WTO more often than the United States, which has often dealt with lack of reciprocity to Japanese markets through bilateral negotiations.\textsuperscript{13} These bilateral talks allow the United States to appear tough to appease those groups interested in protection. It has been common practice during these talks to use a “good cop/bad cop” strategy. Congress, the bad cop, threatens to impose tough trade sanctions. Then, the good cop, the agency with which Japan actually cuts a deal, prevents Congress from carrying through with its threats. In this way, Congress knows it can talk tough without its policies being carried out. This is an inherently dangerous game since it may cause Japan to feel ill-will toward us, and poison the multilateral atmosphere. So far, we have been fortunate that a trade war has not broken out. It is for this reason that US negotiators bark louder than they bite. We may sacrifice quick, timely responses, but we have also prevented the onset of a trade war.\textsuperscript{14}

When we looked at Japan’s balance and terms of trade, we saw that Japan runs unusually large surpluses in intra-industry trade. When making unilateral threats, the United States does not run as high of a risk as Japan. Japan exports durable consumer goods with a high elasticity of demand. If Japan employs counterretaliatory protectionist measures that start a trade war, Japan has a lot to lose. The high elasticity of demand means that increases in prices will have a large impact on their export sales. Also, Japan
simply does not import as much as other countries. For example, in 1987 Japan exported 6.3 million of the 12.2 million cars it produced. However, they imported a mere one-hundred thousand cars. The math is simple. A trade war involving vehicles would affect 6.3 million Japanese units, and a mere hundred thousand foreign units.\(^{15}\)

**Trade Policy Choices**

United States trade policy is basically a waiting game; when an industry complains about alleged unfair trade, the government reacts. Section 301 of the 1974 Trade Act gave private parties the right to initiate complaint proceedings. This was the catalyst for a large increase in bilateral trade actions. The presidency, which has traditionally withstood protectionist calls, was badly weakened after Watergate.\(^{16}\) Moreover, many industries were weakened during the relatively poor economy of the 1970s. One opportunity to protect your hurting industry is to prevent trade, fair or unfair.

In 1979, Section 301 was mildly strengthened. Then, in 1984, explicit statutory definitions were given to the terms unreasonable, unjustifiable, and discriminatory in Section 301. Also, the definition of standing was loosened so that more businesses could bring unfair trade claims. Section 301 was also made more favorable to claimants when the rules relating to antidumping and countervailing duties (CVDs) were changed to favor claimants.\(^{17}\)

Some supporters of Section 301 have argued that it diverts protectionist sentiments away from closing our market and to opening foreign markets. There are many problems with this argument. First of all, if a Section 301 dispute is successful when it should not have been, then the focus is closing our market because some type of reaction,
such as antidumping duties, will occur.\textsuperscript{18}

Another problem with this argument is that Section 301 operates outside of the multilateral trading order. The United States appoints itself judge, jury, and executioner when it performs a Section 301 investigation. Not only does this circumvent the WTO, but it also makes it looks like the United States is appointing itself the good guys to take on the foreign bad guys.\textsuperscript{19} Many countries resist this because of our own sins against free trade. Japan and Korea will likely be especially angered by this. These two countries accounted for only 17\% of Section 301 investigations, but were responsible for one-half of all successful outcomes. Whether these results are justified or not, they make these two countries feel like they are being unfairly singled out by the United States.\textsuperscript{20}

In almost every unfair trade case, the US government finds the foreigners at fault. One element of the Uruguay Round of GATT stated that there was an “undertaking not to make unilateral determinations about the GATT-consistency of other countries’ policies.” This provision was directed at Section 301 and certainly made it harder to defend its continued use.\textsuperscript{21} However, such actions were inconsistent with the Tokyo Round, as well, so the United States is likely to continue to use Section 301, or some similar variant of it.\textsuperscript{22}

An even more aggressively unilateral trade law is Super 301. Super 301 makes the United States Trade Representative (USTR) submit an annual report to Congress on evidence of substantial progress towards eliminating unfair trade practices. Super 301 was taken off the books in 1990, but was reinstated in 1994 by President Bill Clinton. Super 301 tested the limits of Japanese responsiveness to unilateral threats. Rather than be put
on the “watch” or “priority” lists of Super 301, Japan was put into the broader Structural Impediments Initiative (SII). True, Super 301 is unilateral and illegal under the WTO. However, until the multilateral trading order addresses competition law we must have some way to help American businesses. Super 301 is one way to accomplish this. If Japanese unfair trade is not covered in the WTO, but American unfair trade is covered, there will be growing frustration with the trading order among American businesses.

In 1995 the United States had a dispute with Japan over auto parts. Those officials opposed to the WTO were likely pleased by the way this case played out. The United States alleged that Japan has kept out American auto parts by its use of cartel-like dealings and business-government collusion (i.e. the competition policy we have discussed.) If the United States imposes retaliatory tariffs, and Japan brings suit under the WTO, Japan will win because such US actions are clearly illegal under the WTO. 24

The Trade Act of 1974 included an escape clause to protect domestic industries from “fair, but injurious” foreign competition. Such filings are known as Section 201 trade cases. During the 1980s the United States alone processed about 350 unfair trade cases. However, Section 201 was only used for 26 cases from January 1958 until March 1987. In fact, Senator Ernest F. Hollings (D-South Carolina), reportedly said that “going the 201 route is for suckers.” 26

It is very unfortunate that Section 201 is so discouraged. It is inevitable that some industries will be affected by free trade. The basis of freer trade under the WTO is that some countries’ industries will gain and others will lose. But, in the end, total economic welfare increases by having free trade. Successful 301 cases lead to retaliations that
reduce free trade. If the decision to find the foreign company at fault was the “wrong” decision, then relations will likely sour and we lose the benefits of free trade.

Section 201 is a way to acknowledge that some industries suffer because of free trade, and we should help these industries. Once an industry demonstrates a successful 201 case, they could receive Trade Adjustment Assistance (TAA). A simple political reality lesson can demonstrate why this may be a beneficial, but unrealistic option. Let us say that a Section 301 retaliation leads to antidumping duties that raise the costs of products and decreases consumer welfare by $40 billion. On the other hand, we could provide $10 billion in assistance to an industry and save $30 billion. The problem is that the $40 billion is spread out and goes unnoticed, while the $10 billion is visible because it will have to come from increased taxes, decreased spending, or a higher deficit.

Furthermore, a country initiating a 201 investigation faces a heavy burden to prove to the ITC that it deserves help. Another benefit of Section 201 is that it gives the money directly to the industry to change. A Section 301 finding may lead to protection that merely delays the inevitable collapse of the industry. If we decide that Section 201 is the preferred route we need to make it easier to prove than Section 301 and Super 301 cases.

Antidumping has become an increasingly common method of protection. In Michael J. Finger’s book entitled Antidumping, he calls this “ordinary protection with a grand public relations program.” The Tokyo Round of GATT turned antidumping into a major, from a minor, instrument for restricting imports. Soon thereafter, antidumping became the major means for controlling imports in Australia, Canada, the European
Community, and the United States. This is quite a testament to the flexibility of antidumping as a weapon against imports.\textsuperscript{29}

It has been unfortunately rare for the government to ask if a problem is caused by dumping. Instead, industries ask how antidumping can be applied to their problem.\textsuperscript{30} Like other trade laws on the books in the United States, though, antidumping does serve more than one purpose. Surprisingly, it is meant to prevent dumping. However, since Section 301 is unlawful under the new WTO, antidumping laws are one of our best ways to retaliate against closed markets. And until the WTO deals with competition policy, US industries are likely to continue to use antidumping laws to challenge forms of unfair competition besides dumping.\textsuperscript{31}

Our current antidumping laws are unpredictable and are often arbitrarily applied. If a foreign company sets prices too high they will be uncompetitive, if they set prices too low they may face a costly antidumping suit.\textsuperscript{32} The countries of Taiwan, Hong Kong, and Korea are part of the Multi-Fiber Agreement (MFA) which puts limits on apparel exports. Despite the restriction imposed by the MFA, the USITC \textit{still} found that these three countries had dumped sweaters. This makes it painfully clear why other countries would complain that our antidumping laws restrict imports unfairly.\textsuperscript{33}

Besides antidumping, another common trade law we have applied against Japan is Countervailing Duties (CVDs). However, the perception is that the WTO put stricter controls on the use of CVDs, than on the use of antidumping. So we should not be surprised to see the continued use of antidumping.\textsuperscript{34}
The United States may not have realized it at the time, but we should be thankful that Voluntary Export Restraints (VERs) were made illegal under the WTO. Before they were made unlawful, the United States made common use of VERs. When we negotiated VERs with Japan on automobiles, steel, machine tools, and textiles, we managed to send economic rents to Japan.\(^{35}\) Not only that, but since VERs required Japan to reduce output, the industries colluded to decide who would get to export. This enhanced the power of the MITI bureaucrats, who set up the industry collusion. This was the opposite of what we desired, and we should be glad that VERs are a thing of the past.\(^{36}\)

**American Bilateral Actions Against Japan**

Now that we know how the United States retaliates against Japan, we can examine whether it has been effective or not. Patrick Low wrote that 27 out of 77 Section 301 cases from 1975-1990 had a trade liberalizing effect. It is difficult to measure if the trade liberalizing effect of this was worth the negative consequences of acting outside of the WTO.\(^{37}\)

If one measure of the effectiveness of unilateral action is the overall liberalizing effect, then another measure must be which industry is affected. Laura D'Andrea Tyson, for one, has argued that we must be more aggressive in protecting high-technology industries. The semiconductor industry is often mentioned in this regard. Since semiconductors are a downstream product (a product used by other firms in a finished product), many have argued that we should simply buy them from the cheapest source. We should not be angry that Japan is protecting semiconductors, we should be glad that we are getting a cheap product.
A similar argument is often made for national defense. The argument is that we are better off stockpiling and/or buying from the cheapest source rather than propping up an inefficient industry we deem necessary to the national defense. Finally, despite all the rhetoric about the need for a high-tech industry, the semiconductor dispute has followed the same political economy script of other US-Japan trade conflicts.38

It may be true that the dispute follows the same script, but high-tech industries are different. High-tech exporting companies provide unmeasurable contributions to a nation’s technological capabilities. By sacrificing the industry, a country may sacrifice these beneficial offshoots.

Bilateral negotiations have worked with Japan in other ways. Before the TRIPs agreement in the Uruguay Round, we threatened to cut off Japanese access to our market if they failed to protect our semiconductor patents. Eventually, Japan agreed to a 10-year protection of chip design. As in all negotiations, though, the threat of increased tensions must be balanced against actual or potential liberalizing effects.39

A dispute in the mid 1980s demonstrated another reason why bilateral action may be necessary. At this time, Japanese firms managed to drive several US producers out of the market, most of whom did not return. This left the field to six Japanese corporations who raised prices and raked in profits. These profits were put back into R&D which gave the companies a further advantage.40 American downstream users were left paying higher prices, and 42% of 59 companies interviewed in one study complained about delays in receiving chips from Japanese producers. Some delays in receiving state-of-the-art chips were longer than six months.41
The semiconductor trade agreement (STA) signed in 1986 eliminated competition among firms and allowed MITI to set up a cartel. This further increased profits. Eventually Japan signed an agreement mandating at least a 20% US share in the Japanese market. Thus, we had entered the very controversial area of managed trade. Inevitably, some people argued that this was a laudable step towards increasing sales in Japan. Others thought that setting a threshold amounted to dangerous tampering with the free market.\(^{42}\)

The 1985 recession in the semiconductor industry was severe. It may be possible to blame unfair Japanese trade for some of the domestic chipmakers’ problems. But Japan experienced similar layoffs and losses to US chip manufacturers.\(^{43}\) It may have been that the Japanese system of capitalism allowed the semiconductor firms to weather the storm, and sell at or near marginal cost for a longer time. Or, it may have been that Japanese firms were dumping chips and blocking imported chips. The record seems to indicate that all of these were taking place.

To this day, trade analysts are still unsure how to measure the affects of the semiconductor dispute on domestic industries. The record of the Cray corporation case seems to indicate that the Japanese were more at fault in supercomputers. Cray supercomputers are consistently ranked the best in the world. In the late 1980s they held an estimated 63% of the world market: 84% of the European market, 81% of the North American market, and only 15% of the Japanese market. Japanese companies held 85% of the Japanese market and 10% of the European market.\(^{44}\)

These numbers are hard to justify by anything except the infant-industry argument. Eventually, the Japanese did open their market to supercomputers, but only when
domestic producers were strong enough to compete. But by then, Cray had lost approximately $400 million in revenue and $54 million in extra research and development. Was Japan justified in its intervention. If not, what should we have done?

Steel, on the other hand, provides an example of why not to intervene. In the 1970s steel was experiencing a downward demand on pressure. If you can excuse the pun, the steel industry benefited from a "steel" triangle of producers, workers, and politicians who worked for import protection; steel has been the most common petitioner in antidumping and CVD cases. In fact, the steel industry filed such a flurry of antidumping cases in the 1980s that the government was forced to negotiate VERs because it could not process the cases in time to meet statutory deadlines.

By the late 1980s the steel industry experienced a comeback. This comeback was held up as proof of the voluntary restraint agreement's success. In reality, the steel industry improved its standing because of successful minimills and other restructuring programs. Thus, the steel case demonstrated a potential pitfall in analyzing trade policy: confusing cause-and-effect. Just because a retaliatory action preceded an industry's improvement does not mean that the action caused the comeback; it may have been other factors. The semiconductor case was really complex in this respect. The managed trade and retaliatory tariff may have led to a revival in the semiconductor industry, or it may have simply been changes in the industry itself. For instance, many firms came back into a niche market where they enjoyed greater price markups.

Regional Blocs

Europe has been in the process of integration since the end of World War II.
But since the end of the Cold War, we have also seen the United States grow closer to the Western Hemisphere, and we have even seen Japan grow closer to the Far East. Before the Cold War, the GATT members were united in their military opposition against the Soviet threat. It was a natural offshoot that they would be economic allies. A very pessimistic analysis of the situation could lead one to believe that the GATT merely codified the pre-existing anti-Soviet situation. Of course, economic gain and friendlier ties among nations surely played a large part. But it would be difficult to argue that the Cold War alliance did not help the process along. The new question is will the end of the Cold War alliance, and the rise in regionalism threaten the multilateral trading order.

Article XXIV of the WTO, dealing with customs unions and free trade areas, is of minimal significance. With the growth of importance in regional trading blocs, and the uncertainty about countries not meeting their WTO obligations because of possible regional discrimination, there will likely be future negotiations in this area.

Since the EU is the most advanced of the regional blocs, it will set the tone for the affect of regional integration on the world trading order. The United States would suffer the most from a trilateral trade war because it has a greater percentage of trade outside its bloc.

The potential for closer Japanese ties with Asia is an interesting case. Since World War II, the countries of East Asia have feared a Japan that tries to impose hegemony over the area. However, Japan has become an increasingly critical source of capital and technology to the NICs of East Asia. In fact, the prime ministers of Thailand and Malaysia have expressed support for a stronger Japanese role. America’s actions will play
a critical role in how East Asia reacts to a stronger Japanese presence. The NICs may grow closer to Japan if they become annoyed with American foreign economic policies. And, Japan may turn inward to the APEC if they feel they are being unfairly targeted by US trade policy. A key question will be whether the regional blocs provide an example and incentive on how freer trade leads to economic growth, or whether the regional organizations will discriminate against those countries not within their bloc.

---

2 Ibid., p. 82.
4 Ibid., p. 139.
5 Ibid., pp. 115-16.
6 *Antidumping*, 1993, p. 16.
8 Ibid., p. 199.
9 Ibid., p. 440.
10 *Regulating Unfair Trade*, 1993, p. 149.
16 *Trading Free*, 1993, p. 56.
17 *Trading Free*, 1993, pp. 69, 71.
18 Ibid., p. 96.
19 Ibid., p. 94.
20 Ibid., p. 91.
21 Ibid., pp. 229, 235.
23 *Trading Free*, 1993, pp. 91, 93.
25 *Antidumping*, 1993, p. 3.
27 Ibid., p. 252.
28 *Antidumping*, 1993, p. 34.
30 *Antidumping*, 1993, p. 27.
34 The New GATT, 1994, p. 73.
37 Trading Free, 1993, p. 89.
40 Regulating Unfair Trade, 1993, p. 33.
43 Ibid., p. 36.
45 Ibid., p. 79.
47 Ibid., p. 110.
49 Time, June 15, 1992, p. 46.
52 Japan’s Emerging Global Role, 1993, p. 165.
53 Ibid., p. 163.
54 Business Week, May 25, 1992, p. 27.
Chapter 4: Policy Proposals

When we choose to impose retaliatory tariffs or antidumping duties, we are raising the price of an import. It is absolutely critical that we pick the right battles. One way to do this is to separate parochial interest from national interests. Granted, it is hard to define the national interest, but we should still avoid parochial interests dictating our trade policy. For instance, angering the Japanese to appease California rice growers when Thai rice growers would benefit from a liberalized Japanese rice market is not a wise strategy.1

One way to make sure that national interests are taken into consideration is to consider downstream users of products. Since downstream users are, by nature, more dispersed than the initial makers of a product, they are less likely to be politically successful in their attempts to prevent protection. When an individual industry initiates an antidumping or Section 301 investigation, the government should be required to consider the interests of downstream users.

Of 16 industries granted relief from 1954-1988 only the bicycle industry grew.2 These unsuccessful results may have been caused by relief coming too late, or it may have resulted because the relief failed to open the Japanese market. However, in most cases, it was probably caused by loss of national advantage in an industry. Attempts to use managed trade to turn around the fortunes of industry that is failing for reasons other than unfair trade will cause a downward spiral as lack of gains lead to calls for more protection.3

What, then, should be the industries we protect. Some industries are bound to stick out. For instance, the numbers we examined in Chapter 3 about Cray's success in all markets except Japan demonstrated that they were more than likely being treated unfairly.
One trade analyst divided conflicts into two types. Automobiles and steel fall into the category of industries facing stiff import competition. He placed computers, telecommunications, construction, retailing, and financial services into the category of industries seeking access to a restricted Japanese market. He said that the semiconductor industry could be placed into either category.4

Once we decide whether to proceed with a retaliatory trade action, we must decide how to act. Libertarians would argue that we should not act at all. The Japanese will not save as much because the population is aging, and Japanese consumers are unlikely to continue to accept their current lot.5 Libertarians would also argue that we should not use CVDs to retaliate against unfair subsidization. In fact, we should consider foreign subsidies a gift that brings lower prices and new technological information free of charge. Finally, even if you believe that it is advantageous to pick industries to protect or subsidize, you may question our government's ability to do this effectively.6

Most policymakers are moderate free traders, though. They grudgingly accept that unilateral action is sometimes necessary.7 In the case studies we looked at for the Japanese market we saw some examples of where trade intervention is beneficial, but we also saw where it can be self-destructive. There is some evidence that investment capital is not made available in certain product areas, like computer displays, if investors believe it is a market that the Japanese are planning to target.8 Japan is also very protective of its own technology while obtaining bargain price licenses for foreign technology.9 Therefore, even if no industry gains from unilateral action, future industries may gain from the overall liberalizing affect our actions have on Japan.
To this end, the first major dispute between Japan and the United States involving the new WTO, provide some evidence, albeit limited, on the effectiveness of unilateral actions. As we have mentioned, the new WTO has a dispute resolution mechanism. However, many American trade analysts are opposed to this dispute resolution mechanism because the WTO does not ban Japan’s discriminatory competition policy, but the WTO does disallow America’s ability to unilaterally retaliate against such actions.10

In 1995, a little over a year after the ratification of the Uruguay Round of GATT, the United States threatened to impose high tariffs on Japanese luxury cars. Tokyo planned to take the US to the WTO for this unilateral action, and the US planned to go to the WTO to protest Japanese practices that keep out US auto parts.11 On June 28, twelve hours before the threatened tariffs were to go into effect, this potential trade war was averted. Even President Clinton mentioned these threatened tariffs in his explanation of how a compromise was reached.12

We have seen that sometimes Japan will allow one firm into the oligopoly to have an example of foreign success. If we have only one or two firms in a market (as in fiber optics or supercomputers), we should accept this. But we should attempt to achieve complete liberalization when there are several firms in an industry.13

We should always keep our eye on free trade and the multilateral trading order. Free trade promotes economic expansion and good will among nations. A large focus of this paper has been on competition policy. Although competition policy has not been dealt with in the WTO, we should have cooperative investigation and prosecution with Japan against restrictive trade practices. This will promote good will, begin the process of
harmonizing competition policies, and, hopefully, lead to some sort of multilateral agreement in the near future.\textsuperscript{14}

\textbf{Changing Japan}

The events of the past four years seem to indicate that Japan’s best interest lie in opening its market. The 1995 Japanese elections were a rejection of the candidates who symbolized work, accumulation, and progress.\textsuperscript{15} Also, but slowly, the Japanese government is changing. By the end of the 1980s, Japanese ministries were pressuring businesses to permit more imports. This symbolized that the Japanese government was focusing on the competition policy problems that have kept out imports.\textsuperscript{16}

In this essay I have said that our interests lie with the multilateral trading order. However, I have also emphasized the benefits that can come from acting bilaterally. This may not be a popular position with many economists, but the nature of our relations demonstrate that we can help nudge Japan towards opening up its markets.

\textit{Gaiatsu} is the Japanese term used to describe the process of foreign pressure acting to overcome political inaction and reluctance to liberalize. In April 1993 Prime Minister Kiichi Miyazawa explicitly asked Bill Clinton to apply pressure to get Japan to liberalize.\textsuperscript{17} Since World War II, Japan has looked to America for leadership. This is a delicate game, though. If we push too hard we end up looking lazy and self-righteous. If we do not push hard enough, Japan may not change.

There are many reasons to fear that Japan will not change. Noted Japanologist Chalmers Johnson once noted that “preoccupation with balance-of-payments problems runs through Japan’s modern history like a litany.”\textsuperscript{18} Whether or not, Japan can put forth a
concerted effort to contain their trade surplus is uncertain. There is no real center of power in Japan so decisions are made by a slow consensus. Not only that, but there are close social bonds between buyers and sellers, a strong sense of hierarchy, and a feeling that Japan must be protected from foreign products.19

The dynamics of group-centered decision-making, which Japan demonstrates, leads to slow change, and means that sharp breaks with history are rare, even if they are very necessary.20 We just saw that the Japanese government has been pressuring businesses to accept more imports. However, one government document stated that “Japan must become a leading importer of manufactured goods in order to fulfill its obligation toward the international community.”21 (author’s emphasis). Thus far, action has lagged behind the rhetoric of greater openness, but the fact they are talking is good. After all, their decision-making process dictates that they will move slowly.22

In the end it may be economics that provides the final push. The closed Japanese system prevents companies from purchasing the lowest priced inputs for their products. Japan may be able to import from its own companies stationed abroad, but that is simply not as beneficial as being able to purchase products from the cheapest source. Thus far, Japan has been able to use domestically produced imports because the worker’s incomes have been kept low. Japanese workers are unlikely to allow this much longer.

MITI has set the stage for Japanese industry by producing its 10-year “vision documents” at the beginning of each decade. The 1990 “vision document”, which included groundbreaking issues such as improving the quality of life, scarcely mentioned individual industries.23
The recent renewed downturn in the Japanese economy may provide another impetus for change. But the complex relationship between business and industry will be difficult to dismantle. The CEO of Itochu Corp., a Japanese trading company, said that "radical reform in Japan is really going to take many years."24

Conclusion

Although we may benefit from free trade, it can be necessary to deviate from a laissez-faire view of world trade. By applying pressure on the Japanese to open up its market, we may be able to help them overcome cultural and political obstacles to free trade. Though the WTO has been an important component towards freer trade, the fact that it currently does not deal with competition policy means that it will fall short of tackling some of the points of conflict between Japan and the United States. These obstacles are causing unnecessary hardship on the Japanese consumer, and some American producers; unilateral action may be necessary to overcome them.

The lessons we learn from our dealings with Japan should not be forgotten, either. The Japanese were successful in transforming itself into a modern country. Its method of achieving this success will likely be emulated by other countries. We should remember what has and has not worked with Japan when forming trade policy with these other countries.

1 Regulating Unfair Trade, 1993, p. 65.
7 Bid, p. 10.
8 Bid, p. 276.
16 *Regulating Unfair Trade*, 1993, p. 43.
18 *Japan’s Emerging Global Role*, 1993, p. 6.
19 *Japan’s Unequal Trade*, 1990, pp. 99-100.
20 *Bid*, 1990, p. 98


