

As the table below shows, the United States has an enormous bilateral merchandise trade deficit with Japan. Much of the deficit reflects the fact that the United States tends to export raw materials and a few military goods to Japan, while importing large amounts of manufactured items. The deficit in automobile vehicles, parts, and engines alone is equal to about 57% of the total U.S.-Japan trade deficit. That deficit is in turn equal to roughly 43% of the total U.S. trade deficit.

Efforts to lower the U.S. deficit include President Nixon's threat to invoke the Trading with the Enemy act to get Prime Minister Tanaka to set "voluntary" textile quotas in 1968, the 1971 Smithsonian Agreement which allowed the value of the yen to float upwards, a 1981 agreement to limit Japanese automobile imports, the MOSS (Market Oriented Sector Specific) talks begun in 1985 to solve specific trade problems, the 1986 Semiconductor Trade Agreement wherein the Japanese government stated privately that it "expects" the U.S. market share to reach 20%, the SII (Structural Impediment Initiative) of 1988 under which Japan pledged to deregulate and spend more so that customers might benefit while the U.S. pledged to improve its schools and cut deficit spending, and the 1993 U.S.-Japan Framework for a new economic partnership under which "baskets" of specific agreements would help us trade. In June, 1995, after tense and often angry talks, the automobile "basket" was finally woven. Americans claimed that the agreement committed Japan to opening domestic markets to U.S. cars; Japanese claimed that they had defeated an American request for numerical sales targets.

To help provide materials for classroom discussion of these issues, *Education About Asia* has asked two experts to comment. In the first interview, Associate Editor Peter Frost discusses the U.S.-Japan trade problem with his sister, Ellen Frost, former counselor to U.S. Trade Representative Mickey Kantor. In the second interview, *Education About Asia* Editor Lucien Ellington discusses the trade problem with Professor Kiyoshi Kawahito, who closely follows U.S.-Japan trade issues.

U.S. Merchandise Trade with Japan (1994)

CATEGORY	EXPORTS	IMPORTS	DIFFERENCE
Food, Feed, Beverages	10,335	385	+ 9,950
Industrial Supplies	13,429	10,763	+ 2,666
Capital Goods	17,379	53,112	-35,733
Automotive	3,405	40,717	-37,312
Consumer Goods	6,888	12,381	- 5,493
Other	2,052	1,797	+ 255
TOTAL:	53,488	119,155	-65,667

In millions of dollars, f.a.s. value basis. Note that "other" for the U.S. consists of military equipment. Also, even the JETI source listed below gives slightly different figures according to the standard of measurement used, rounding off, and the like.

Source: Japan Economic Institute, Statistical Profile: International Transactions of Japan and the United States in 1994. The total of imports to the U.S. is listed on page 32 as 119,156. The Japan Institute is affiliated with the Japanese government. Its address is 1000 Connecticut Avenue, Washington, D.C. 20036.

PART 1 WITH ELLEN FROST

PETER

Let's take automobiles first. When Japanese claim that U.S. auto makers can't sell cars in Japan because they have not made (until recently) either right-hand drive cars or cars at the low horsepower level (under 2,000 cc) that constitute 80% of the Japanese market, don't they have a point?

ELLEN

The primary issue is not engine size or steering wheels. It so happens that American manufacturers have been making cars with steering wheels on the right side for some time. But that is not the point. The point is that Japanese consumers should have the right to choose which car suits them best, and to purchase competitively priced parts, just as American consumers do.

The overarching issue is the control exercised by Japanese vehicle manufacturers over both dealer networks and the auto parts replacement system. Those twin problems are the focus of the June 28 agreement announced by Ambassador Kantor and MITI Minister Hashimoto. In a number of concrete, measurable ways, the Japanese government agreed to open and deregulate the market for both automobiles and auto parts.

Building on this agreement, U.S. manufacturers have stated that they plan to export 300,000 vehicles to Japan by the year 2000. By then they anticipate 1,000 new outlets for foreign cars.

PETER

But the Japanese government claims that the dealers are legally free to market U.S.-made cars.

ELLEN

The Japanese system doesn't operate the way ours does. What the law says is much less important than what happens behind the scenes. Japanese automobile manufacturers maintain control over their dealers through financial ties as well as certain forms of cooperation and technical support. In effect, dealers have been functioning as captive distributors, highly dependent on a single manufacturer. In the past, dealers interested in selling foreign cars have expressed fears of retribution from their affiliated manufacturer.

TEACHING THE TRADE WAR

PETER

Well, how come the Europeans seem to be doing at least marginally better (4.9% of the market versus 3.2%) than we are?

ELLEN

The Europeans have targeted the luxury car market. This doesn't threaten the manufacturers to the same degree as our vehicles. Even so, many Europeans privately complain about many of the same practices that we have criticized.

PETER

What about auto parts? If, as the United States claims, our auto parts are 15-30% cheaper, why do Japanese buy 80% of their replacement parts (versus only 20% in the U.S.) from the original manufacturer? Why can't U.S. auto parts manufacturers break into this lucrative market?

ELLEN

The problem here is the strict and frequently obscure government regulations governing the repair, inspection, and modification of vehicles. The effect of these regulations has been to channel repairs to automobile dealerships and other certified garages which tend to use the manufacturers' replacement parts almost exclusively. Needless to say, Japanese consumers pay through the nose. A shock absorber, for instance, might cost \$225 in the United States, but over \$600 in Japan.

PETER

What about Japanese government claims that it cannot interfere in these privately negotiated areas?

ELLEN

This is fine, in theory, but the Japanese government has implicitly encouraged or tolerated an anticompetitive system for decades. The Clinton Administration, like its predecessors, is trying to introduce genuine competition into the market. In the near term, this requires the cooperation of the government, for instance, in enforcing Japan's own antitrust laws.

PETER

How about the Japanese argument that the trade problem is really rooted in the United States? After all, we have promised for some years now to cut our deficit, encourage savings, and improve our work force.

ELLEN

It's important to distinguish between

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the size of the overall U.S. trade deficit and the composition of U.S.-Japan trade. We have a large global deficit because as a nation we spend more than we save. If the Japanese are saying that our global trade deficit is rooted in the United States, they are in large part correct.

The bilateral deficit with Japan is quite a different issue. In normal circumstances, it does not particularly matter whether we run a deficit or a surplus with any particular country, provided that market forces are at work. In the case of Japan, however, the bilateral imbalance has ballooned out of all proportion because of pervasive barriers in the Japanese market. In a number of

important sectors employing skilled and disciplined U.S. workers, U.S. companies have gone through a productivity revolution and are highly successful in competing with Japanese companies in third markets. Nevertheless, penetrating the Japanese market is like chipping stone.

PETER

You've talked before about how each side is building its case from a totally different starting point. Can you elaborate?

ELLEN

We shouldn't forget that there are many competing interests on each side. There is no single Japanese or American voice. But in simple terms, the Japanese case is that a truly competitive product can be sold in Japan, whereas the American case is that certain key products that are now competitive—including autos and auto parts—face a wide range of subtle and pervasive barriers in the Japanese market.

PETER

Is this just a game, or are we headed for deep trouble?

ELLEN

I come out somewhere in between those two poles. I think that this tension is serious. Friction of this kind cannot help but erode the kind of trust and good feeling on which an alliance depends. Long-time friends of Japan who suggest that the trade problem will simply go away are not doing the Japanese a favor. At the same time, the two countries have so many interests in common, and so many areas where they cooperate closely, that I'm not worried about the fundamentals of the relationship. What I'm hoping is that the pro-reform forces in Japan will gather strength, so that foreign pressure will become less and less necessary.

PETER

What do you think of the plausibility of the argument that the Clinton Administration has been particularly bellicose with Japan on trade because Japan-bashing is popular with certain groups such as organized labor that are hostile toward Japan?

ELLEN

I challenge the word "bellicose." The Clinton Administration's Japan initiative arose because of widespread frustration, but it is not tantamount to war! The question is therefore off the mark. What is plau-

PART 2 WITH KIYOSHI KAWAHITO

sible is that the Clinton Administration recognizes that a firm stance toward opening the Japanese market lends credibility to overall U.S. trade policy. You cannot go to the Congress and say that you believe in open trade and investment and then overlook the second biggest national market in the world. You cannot say that trade is good because it shifts the composition of U.S. jobs toward the high-wage, high-skill end of the spectrum and then ignore a major market for the goods and services produced by that labor. You cannot urge U.S. firms to be globally competitive without giving them a chance to compete against Japanese firms in their home market. It just doesn't work. For that reason, any U.S. President is going to have to be resolute vis-a-vis Japan. It isn't just labor union members who believe that Japanese resistance to market-opening measures justifies extra foreign pressure.

PETER

Since the entire issue of Japan-U.S. trade seems to be both controversial among experts and highly emotional, what is your opinion on how high school and university instructors should approach the issue?

ELLEN

I favor a multidisciplinary approach to the trade problem. Students should acquire a historical perspective by learning about the goals of the Meiji Restoration against the backdrop of what was happening in Asia at the time. They should reflect on the lingering consequences of two and a half centuries of isolation during the Tokugawa era, as well as the impact of defeat in World War II. They should have a grasp of Japanese geography so that they understand Japan's sense of vulnerability and somewhat insular mentality. They should learn the basics of economics so that they understand the sources of the U.S. trade deficit and concepts like comparative advantage. They should look at how Japanese society is changing and how those changes will affect trade. They should be exposed to the Japanese political system and bureaucratic decision making. All this presumes that students are fully aware of the peculiarities of our own history, geography, economy, society, and politics—a sine qua non for understanding another culture. ■

LUCIEN

Let's take automobiles first. Why don't more U.S. made cars sell in Japan?

KIYOSHI

Essentially for the same reason that they have not been selling well elsewhere in the world except in North America; namely, they have not been adapted to the conditions and requirements of the market.

Although more than 50 models of U.S.-made large cars (engine capacity of more than 3,000 cubic centimeters) are introduced and collectively selling well, that segment in the total Japanese market is very small (3%). In the biggest segment, which accounts for 80% of the total market and entails small cars with the engine capacity of 2,000 cc or less, no U.S.-made cars are introduced; obviously they cannot compete with Japanese and European cars here because they are not adjusted to Japanese tastes (e.g., European styling), customs (e.g., left-side driving), and standards (e.g., power control rear mirrors). I believe that European-made American cars should have been introduced in Japan.

Moreover, American automakers, with the exception of Ford, have little invested to develop their own distribution, service, and training systems, as compared with their European counterparts. In this connection, note that European cars have captured a larger auto market share in Japan than in the U.S.

Very good news is that the Big Three of the U.S. have very recently taken definitive steps to develop their own dealerships and to market smaller cars. Other positive news is that the Japanese government and its affiliates are ready to provide American automakers with some assistance, including low-interest loans to develop left-side drive cars.

LUCIEN

What about U.S. claims that Japanese car dealers don't dare market U.S. cars?

KIYOSHI

Such claims are very misleading. In the first place, some Japanese car dealers, notably the Yanase network, have been marketing imports, including U.S. cars.

Secondly, domestic car dealers have long-term business relationships with spe-

cific car makers, and they wouldn't easily switch. If, say, a Toyota dealer switches to be a Nissan or Honda dealer, that would be national news. Certainly, it is not easy either to convince any of them to break the long-time tie and market a U.S. car.

It is possible that in some cases Japanese car dealers, despite their wish to switch to another car-maker or become a dual agent, do not dare to do so in fear of retaliation. The Japanese government seems to be increasingly determined to protect such dealers through the application of antitrust laws and other measures.

Incidentally, I understand that a similar exclusive dealership system exists in Europe and that U.S. automakers have long been doing in Europe as Europeans do.

LUCIEN

Even with the promised changes, won't it take a lot of time for traditional Japanese business relationships and existing regulations to change?

KIYOSHI

In general, reforms tend to take more time in Japan than in the U.S. for various reasons, including the preference to use consensus instead of majority ruling and the concern to minimize hardships on affected parties during the transition. On the other hand, when promises for change are made internationally, the Japanese tend to implement these faster than Americans because they are more sensitive to world opinions. Incidentally, such expressions as "plan," "expectation," and "hope" should not be confused with "promise."

Over the years, many government regulations in Japan have become obsolete, only protecting the privileged, and some business practices have apparently been fraudulent or illegal by Japanese and international standards. In these areas, reform campaigns seem to have been accelerating; for instance, nowadays a day hardly passes without some new de-regulations and antitrust actions. On the other hand, it is also realistic to assume that some meaningless regulations will remain for a long time.

It is important, in this connection, for Americans dealing with Japan or any other country to recognize the difference be-

TEACHING THE TRADE WAR

tween unfair regulations or practices that should be removed and uncomfortable cultural elements to which they must adapt themselves patiently.

LUCIEN

What about auto parts? Is the Clinton administration correct when it claims that Japan's unnecessarily strict auto inspection regulations shut out U.S.-made replacement parts?

KIYOSHI

Partly correct, in the past, I believe, although the expression "shut out" is misleading.

The strict auto inspection system has existed in Japan for a long time for safety, traffic control, environmental protection, and other purposes not associated with any economic protectionism. However, it has had the unintended side effect of discouraging the use of less known brand parts. The U.S. proposed changes of regulation in this area, and Japan not only accepted most of such proposals but incorporated additional reforms. These deregulations have either been implemented or are about to be implemented.

LUCIEN

Breaking up these cozy government and business relationships will require strong political leadership. Do you think that the Japanese government is up to it?

KIYOSHI

The government and business relationships in Japan have been based on philosophical principles and historical backgrounds different from those in the U.S. Moreover, they are similar to practices in many Asian and European countries. They do not need to be broken up just because they are different from those in the U.S. or uncomfortable to newcomers in the system. Only those obsolete practices which are just protecting the privileged in discrimination against others and causing economic and social inefficiency should be removed.

Given the Japanese political system, it is difficult for a strong political leadership, as understood in the U.S., to develop, and as a result substantive reforms may take a long time in some areas. On the other hand, many reforms can materialize without strong leadership, as a combined

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effect of mounting pressures from the public and efforts of conscientious bureaucrats and politicians.

LUCIEN

In your opinion, does Japan have an obligation either to its own consumers or other nations to reduce its large current account trade surplus? Please elaborate.

KIYOSHI

Japan, the U.S., and any other country should be concerned with the welfare of people at home and in the world. If the large current trade surplus of Japan is caused by unfair trade barriers and imposing hardship on people, Japan should by all means reduce and eliminate the surplus. If the surplus is caused by inter-

national differences in income spending, all relevant countries' concerted efforts are necessary. If the surplus is a natural development caused by international differences in product innovations, recycling of the surplus to benefit people in the world is in order.

Japan should continue to aggressively remove those government regulations and business practices which unfairly discriminate against newcomers in the market, native or foreign, because that is the right thing to do. And I want to emphasize this point. It should be noted, however, that most economists in the U.S. and Japan see this factor as relatively insignificant in reducing the trade imbalance. More important are the correction of the overspending habit of the U.S. and underspending habit of Japan, and the generation of more product innovations in America.

These discussions may be difficult for non-economists to digest. The following list of basic facts may be helpful:

1. The average Japanese has been buying slightly more American products than the average American has been buying Japanese products, but the American population is twice as large as the Japanese.
2. The American market is open, but not as open as uninformed people think; Japan fares better than the U.S. in terms of the three major "traditional" yardsticks, namely the average rate of tariff, number of quantitative import restriction categories, and the extent of "buy-national" requirements.
3. The U.S. developed a national overspending habit in the early 1980s when income taxes were cut as much as 25% while keeping the level of government spending high; the more spending, the more imports.
4. While the U.S. still overwhelmingly leads the world in the number of Nobel-Prize-winning technological breakthroughs, Japan now overwhelmingly leads the world in the number of patented product innovations.

5. Measured by the ODA (Official Development Assistance), the average Japanese today provides twice as much foreign aid as the average American.

LUCIEN

What future do you see for the U.S.-Japan trade balance?

KIYOSHI

Some but not sizable improvement in the bilateral balance in the near future. Just as in the past ten years, the dollar value of Japanese imports from the U.S. will increase significantly, but the increase will be largely offset by a rise in American imports from Japan.

I believe that the 21st century solution to the trade dispute is to liberalize the movement of people between the two countries. Today, goods and money move freely internationally, world operations without specific national identification are everywhere, and trade statistics have become substantially misleading. Yet people cannot freely reside, work, or start businesses in each other's country.

Let American workers obtain jobs in Japan and let American businessmen freely start businesses in Japan, selling American products directly to consumers. Let the Japanese, who must pay exorbitant prices for housing and space, freely live in the U.S. and contribute to product innovations. Let us restore this human right which we lost to immigration laws and other regulations about a century ago.

LUCIEN

What do you think of the plausibility of the argument that Japanese high-level bureaucrats such as Minister Hashimoto are being particularly bellicose and tough with American trade negotiators because they will gain domestic political advantage?

KIYOSHI

Little credence can be given to such an argument, which assumes the American type political setting. Under the political system of Japan, which is much less democratic than that of the U.S., one's political party and faction affiliations, past positions, and seniority are far more important than the image projected to the public. A John Kennedy, for instance, would not become

Prime Minister in Japan unless he is at least 55 years old.

Hashimoto, regarded as a talented and promising politician by analysts for more than two decades, was expressing, somewhat rhetorically, the Japanese position on the trade issue that had been a near consensus for some time. His popularity did increase recently, not because of his outspoken manner, but because his capabilities happened to be recognized more widely through mass media exposures.

As a matter of fact, American and Japanese professional trade negotiators are surprisingly courteous and friendly to each other. High-level politicians' public remarks give a different impression. Incidentally, it may be interesting if third-country observers are asked which appeared more bellicose over the trade dispute, the Murayama-Hashimoto team or the Clinton-Kantor team.

LUCIEN

Since the entire issue of Japan-U.S. trade seems to be both controversial among experts and highly emotional, what is your opinion on how high school and university instructors should approach the issue?

KIYOSHI

They should remind their students that there are two sides on any controversial international issue, just as on domestic issues. They should try to present a balanced picture of the issue. They should also stress that for mutual understanding and cooperation the sensitivity to be able to see the issue from the other side's point of view is important, just as it is with respect to gender, race, and other domestic issues.

The difficult part for the instructors is to find the time and means to develop a balanced picture themselves. Obviously, relying on American television news and newspaper reports is inadequate, as most (but not all) American newspapers and television stations tend to depend on English-language sources of information and incorporate remarks of only American politicians. Even the largest newspaper in most states does not seem to have a single

reporter who can read Japanese-language newspapers for checking the other view. In this circumstance, I suggest that they call the Japanese consulate or JETRO (Japan External Trade Organization) in their district.

Finally, tell the students that, like Americans, most people in the world are good natured and conscientious and that lack of informational objectivity and cultural sensitivity often make good people bad. Tell them to maintain confidence but drop arrogance. Encourage them to learn a foreign language, travel, and open their hearts. ■

Editor's Note:

Since the time of the interview Mr. Hashimoto has become Japan's Prime Minister.

EAA Interviews

Editor's Note:

Each of the interviewees was unaware of the identity of the second interviewee or of the interviewee's comments. Ellen Frost and Kiyoshi Kawahito have been invited to provide their reactions to this article for publication in the August 1996 EAA.