

**Agenda for a Pacific Partnership:
A Japanese-American Dialogue**

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Akao: Today's topic, "Agenda for a Pacific Partnership: A Japanese-American Dialogue", is a very positive and forward-looking one and it expresses what U.S. - Japanese relations ought to be. Working in Washington, D.C., however, I often wonder what the current status of our relationship is, because the perception of Japan held by many Americans is not necessarily good. In a poll taken a few months ago, Americans were asked which poses a more significant threat to the United States: the threat from Soviet missiles or the threat from the Japanese economy? More Americans answered that the Japanese economy is a more serious threat to the United States than Soviet missiles. This astonishes and discourages us. It is based on misconceptions among Americans about the importance and current status of cooperative relations between the two countries.

Japan and the United States have very close security ties; in fact, Japan has a security treaty with only one foreign country and that is the United States. Japan is protected by the United States, but the U.S. also has profited greatly from the maintenance of its military forces in Japan for its own security. Japan pays approximately \$45,000 per U.S. serviceman stationed in Japan. We share, in addition, the same values of freedom and democracy and the same free enterprise system. This system is the very basis on which Japanese economic development has been made successful; Japan has depended on this system for what it has achieved. Despite our similarities and interdependence, however, the perception of Japan held by many Americans is not necessarily good. Working in Washington we hear a lot of criticism, especially from Congress, regarding Japan's trade barriers, unfair trade practices, and so on.

A year ago, Japanese and U.S. trade officials were busy negotiating specific trade

issues, such as beef, citrus, and construction. In comparison, there are very few specific trade issues today. However, the psychological pressure we feel now, and in particular that those of us in Washington feel, is much greater than it was a year ago.

There are several reasons for this, one being the American political cycle. The Bush administration, in power only since January 1989, is still in the process of nominating senior officials and awaiting Congressional approval of the nominations. United States trade issues have been the focus of intense discussion at the confirmation hearings for these appointments, and much criticism of Japan has been expressed in the process. Once appointments are completed much of this discussion may subside.

Second, many Americans fear that the United States is losing its technological edge to Japan -- especially in the areas of advanced and high technology. To what extent are these concerns and fears warranted? A typical result of such concern is the debate over the FSX. As you know, Japan intends to develop a fighter support plane to be placed in service in about ten years. Because the United States does not yet have this kind of advanced fighter plane, Japan had originally planned to develop it on its own. The United States, however, offered to develop and sell planes to Japan. After three long years of discussion, an agreement to co-develop the plane was reached last fall. This debate reflects American fear of competition with Japan in high technology areas.

Third, the new trade act, which went into effect last August, requires the Administration to report and take action on many economic and trade issues. As the deadline for action by the Administration nears, as now is the case with Super 301, more attention is drawn to various trade issues, causing unnecessary friction between our two countries.

The most important issue, however, is the continued external trade imbalance facing

both the United States and Japan. The United States has huge trade deficits, both bilaterally with Japan and globally. Though the trade imbalance has gradually improved for both the United States and Japan, the rate of improvement slowed last fall, frustrating Americans and especially Congress. I want to further elaborate on this subject.

In Professor Jagdish Bhagwati's recent statement on U.S.-Japan trade issues, he stresses that the United States trade deficit is primarily caused by macroeconomic factors, such as fiscal policy, monetary policy, exchange rates, and so on. I fully agree with him. Macroeconomic policy coordination among major countries has been going well since September 1985 and the United States trade deficit has declined as a result. Some economists say that if the dollar had not been adjusted the United States trade deficit would have reached \$400 billion annually by now.

The Japanese economy has traditionally been heavily dependent upon exports for its growth. After a few years of this macroeconomic policy coordination, however, Japan's economic structure drastically changed and the nation now relies more on the expansion of domestic demand for its economic growth. Japan's external demand has been showing negative contribution to GNP growth since 1987 while domestic demand has increased. Japan's tradition of importing raw materials and exporting manufactured goods has changed. For instance, imports have greatly increased in the last three years; in 1988 alone, imports from the United States increased by \$10 billion and imports as a whole increased by approximately \$38 billion. In comparison, imports in the United States increased by about \$35 billion in 1988: that is, Japan's import growth last year was larger than that of the U.S. despite the U.S. economy being roughly twice the size of the Japanese economy.

The import growth of Japan is to a large extent attributable not to the import of raw materials, but to a sharp growth in the import of manufactured goods. In the early 1980's,

Japan's ratio of manufactured imports to total imports was very small, manufactured goods having been only about twenty percent of total imports. Since 1985, however, this has dramatically changed: forty-nine percent of imports in 1988 consisted of manufactured goods. Much of this increase came from neighboring Asian countries, but also from the European community, and in particular in 1988 from the United States.

Japan is on the right track, but in spite of the rapid increase in imports of manufactured goods in Japan, exports have also increased in value, making it very difficult for the trade surplus to be substantially reduced. This, in part, is because products that the United States does not manufacture -- such as VCR's and facsimile machines -- have to be imported from Japan. In addition, the rush of Japanese investments in the United States, in the automobile and electronics industries for example, have contributed to the increase of exports of machinery and components to the U.S. In the initial stage of Japanese companies transferring their production facilities to the U.S., exports of machinery and components increase. This contributes to a decrease in exports over the longer run, however, as local production by the Japanese companies gradually replaces imports into the United States from Japan. In the future, Japanese investment in the U.S. should also promote an increase in the export of U.S.-manufactured goods to Japan and other countries, and thereby alleviate the need for so many Japanese imports. This, however, will require time and patience.

The United States also needs to make better progress in this area of macroeconomic coordination. Most importantly, the huge federal budget deficit needs to be steadily reduced. Most economists agree that if this deficit remains, if consumer spending does not decline, and if the savings rate does not improve, the United States will have difficulty reducing its trade deficit. Japan alone cannot be made responsible for the external trade imbalances existing among major countries, nor is it possible for Japan alone to improve them.

This does not mean that Japan needs to do nothing. We believe that much needs to be improved, especially on a long-term basis. Japan has been fairly successful, for instance, in carrying out economic and industrial structural adjustment: Japan privatized the telecommunications company NTT and the National Railways, and liberalized financial markets. We have either simplified or eliminated many government regulations and standards. There is still room, however, for Japan to implement deregulation and reduce government intervention in economic activities.

The distribution system is alleged, especially by the United States, to be a major barrier to imports. To what extent our distribution system actually poses a barrier to imports I am not sure, but we can make some changes. Land use and housing are important areas in this respect. It is very difficult for many Japanese to own large houses as Americans do. If such ownership were easier, housing and construction demands would greatly increase, contributing to a further expansion of domestic demand and imports. There is still much Japan can do, but it takes time and patience.

Before concluding, I would like to speak about managed trade. The U.S. has been successful in reducing its trade deficit with European countries, but not with Japan. Some people say that Japan is unique and different from other countries and that the U.S. should use a different approach with Japan. Managed trade is one of the options proposed for dealing with Japan. The most typical of such proposals appears in a recent report by the Advisory Committee on Trade Policy and Negotiations, presented to President Bush in February. The committee proposes an option somewhere between free trade and managed trade, but it actually suggests the setting of targets for U.S exports in several sectors of industry where the U.S. is competitive. This is managed trade.

Former Secretaries of State Vance and Kissinger made another proposal last

summer. They proposed that Japan and the United States come to an agreement on the amount of the annual trade imbalance. How can we agree to set an annual level of trade imbalance under a free enterprise system?

A third proposal comes from a trade group called the Emergency Committee of American Trade, a group consisting of free-trade enterprises in the United States that are traditionally noted for their fight against protectionist legislation. This group will shortly issue a report proposing that the current \$52 billion trade imbalance between the Japan and the U.S. be halved within five years. This is similar to a proposal that Congressman Gephart presented a year ago during the Presidential campaign.

None of these proposals will work because both the United States and Japan have a free-enterprise system. Could Japan ask the U.S. electronics industry, or the computer industry, or any other industry to set and achieve import targets? Under the U.S. and Japan's system of free-enterprise, individual companies determine the origin and amount of imports. These same groups now propose that Japan should be doing something which American companies could not possibly do.

The case of semiconductors is a typical example of where the United States government, under strong pressure from Congress and the semiconductor industry, tried to apply managed trade and failed. The U.S. government had asked Japan to ensure that twenty percent of Japan's semiconductor market be given to U.S. imports. This is impossible for the Japanese government to achieve, however, because individual companies decide which semiconductors, whether domestic or foreign, to use. Japan was penalized two years ago because we were not living up to the U.S. interpretation of this agreement. Japan is still subject to trade sanctions, according to the United States, because the market share has not yet been achieved. This simply does not work, and I hope the United States government and

the Congress will understand that. I hope that the United States government does not succumb to the temptations of managed trade. If the U.S. does succumb, many other countries, especially in Europe, will follow suit. Some of them will be looking for an excuse to justify their practices. They are not openly practicing managed trade now, or if they are, they are doing it in a disguised form. If the United States initiates managed trade, they will willingly follow suit and it will bring about the collapse of a free-market economy.

Patrick: Thank you very much, Mr. Akao. I now turn it to Mr. Massey for his comments.

Massey: Thank you, Professor Patrick.

If I were to do this discussion in Japanese, how many of you could understand?
"Nihongo de yarimasho-ka?"

I ask this question because I want to indicate that there are two audiences here. I am going to talk to two audiences, and the message is slightly different to each. There are the Japanese students among you, and a few American students who can converse in Japanese. Then there are ordinary Americans.

This involves a couple of dichotomies. One is the audience. The Japanese audience here today is probably overwhelmingly older and more corporate in background; most are sponsored by various Japanese companies. I want to talk to you about your companies' role in U.S.-Japan trade relations.

The other dichotomy is the macroeconomic versus microeconomic dichotomy. There has been much discussion so far about macroeconomics, and some macroeconomic myths about trade. The fundamental trade decision is the decision made within a corporation or within a

person's mind, and that is a microeconomic decision: I am going to buy this product versus that product. Trade policy addresses trade policy related problems. This is why there is a Treasury Department or an Okurasho on the one hand, versus a USTR or a Economic Section of the Gaimusho on the other.

Believe it or not, the trade deficit is not the province of trade policy. As Mr. Akao pointed out, most of what is involved in the trade deficit -- whether it is our global, aggregate deficit, Japan's global trade surplus, or the bilateral of those two things -- can be accounted for by macroeconomic factors. Trade issues are access to markets, participation in foreign markets, and the factors that either facilitate or impede that access. The deficit, the relationship between the yen and the dollar, or the savings investment rate in the U.S. and Japan are not policy issues in trade negotiations. Does the Japanese Government make it possible for foreign firms to get into telecommunication services? Does Mitsubishi make it possible for some American company to get into a long term supplier-purchaser relationship? Those are trade policy issues. Trade policy issues are more nitty-gritty than macroeconomic issues, and they involve both audiences.

Trade policy is fundamentally microeconomic. The fact that the American savings rate is less than the Japanese is significant; fundamentally, however, "the purchase decision" is the key element in trade policy: the factors that affect the ability of the seller to make a sale to the purchaser. United States trade negotiators negotiate with the Government of Japan to make it possible for Americans to sell their wares in Japan. The Administration -- and if you look carefully you will discern a rather dramatic difference between the Administration and Congress on this -- does not define the Japan problem by the size of the bilateral deficit. That is basically a political problem. The real problem is politics because international trade is basically domestic politics. When goods and services flow across borders, the factors affecting them most profoundly are political, and the first rule of politics is that foreigners do not vote.

The first rule of economics is to avoid competition, and that applies to trade as well: competition affects the decisions made by politicians in Japan, the United States and the rest of the world. The Japanese have been somewhat more efficient in translating that economic law into the politics of trade.

Despite the fact that the bilateral deficit with Japan has declined so dramatically slower than our deficits with other countries around the world -- in 1988 over '87, our deficit declined seven percent vis a vis Japan while it declined forty-seven percent, vis a vis the EEC - - there has actually been a lot of progress made in our trade relationship with Japan. The Reagan Administration has a record of accomplishment in identifying and removing formal barriers to the Japanese marketplace. It took a long time and a lot of intensive negotiation. The Japanese are proud of having the lowest trade tariffs in the world: 2.3 percent. After years of negotiating, Japan said: Be patient, be patient. Americans are very patient people. We negotiated over beef and citrus for twenty-five years. We negotiated over tobacco for fourteen.

Rice is an example of trade as politics. Surpluses and deficits do not have a lot to do with trade policy. Rice policy is trade policy: put simply, there is no trade in rice in Japan. The tariffs on beef and oranges are trade policy. They are very high. They are better than the quotas, however, because quotas are illegal under the GATT.

The United States and Japan's other trading partners are not impatient. They merely ask that Japan live up to its international obligation. When Japan signed the general agreement on tariffs and trade they agreed that the only legitimate barrier to trade would be a tariff. The import ban on rice is against the law in international trade. The reality is that the U.S. has gone through a long list of formal barriers to trade with Japan: tariffs, quotas,

standards and certification barriers.

Remember the story about the Pennsylvania company, Easton Aluminum, that was unable to sell its softball bats to Japan because of the very deep set of layers to the onion of protectionism. First, the Japan Soft Baseball Association maintained a rule against the use of foreign equipment. This was at the time when Mizuno gloves were being widely used in the big leagues in the U.S. When the U.S. prevailed upon Japan to change that rule, we discovered an incredibly nontransparent set of requirements, all of which had either the clear intended or, in some instances, unintended, but nevertheless real, effect of denying access to the market for foreign products. It was impossible to know the standards governing a product and it was impossible to find out how to get it certified.

In 1983, after very intensive negotiations over this little product called "a soft baseball bat," a network of nontransparent, invisible, bureaucratic barriers to trade was unraveled. Sixteen laws in Japan, including the equivalent of the Consumer Product Safety Law, were changed to make it possible for foreign products to be treated on terms roughly equal to their Japanese counterparts. It is now possible for foreign firms to be treated on relatively equal terms in Japanese telecommunications services, an area in which many American and other foreign companies are extremely competitive. After eight years of intensive negotiations, formal trade barriers are no longer the key problem in Japan. We can shake our Japanese friends' hands and say we have done a good job.

That does not mean there are no remaining trade barriers. To the contrary, many informal barriers remain. Japan is now the second largest market in the world for everything except imports, particularly imports of manufactured products. Relative to income, and relative to consumption of manufactured goods, Japan is an "outlier in world trade." Manufactured imports as a share of GNP are half those of the United States and less than a third of all the

European countries. Japan is a huge marketplace in which the range of choice of products is substantially lower, and consumer prices higher, than those in any other industrialized country.

It is interesting to see the studies repeatedly done by Japanese, American and Western European organizations which demonstrate that Japanese consumer electronics and optical goods can be bought cheaper in New York than in Tokyo. Why is this? It is because there is too little pressure from imports on price. The range of choice in the marketplace is restricted, the price of goods is high, and the quality of life, as a consequence, is lower than it ought to be.

This is a problem not only for the United States, but for many of Japan's trading partners. In fact, Japan's ratio of exports to imports in manufactured products with all her trading partners is substantially positive. Hong Kong, Taiwan, Korea and Singapore all run manufactured goods deficits with Japan. Compare the share of products from those countries that Japan imports with the share that the U.S. imports: Japan's imports have grown. Manufactured imports have grown as well, but from a remarkably small base for such a large industrialized country. The world, no doubt, has a trade problem with Japan, but it is not a macroeconomic problem, it is not an American problem, and it is not a bilateral problem, except for Japan. Intact in Japan is a set of informal, invisible, and in some cases unintended barriers to manufactured imports. They are related to corporate strategy, national policy, industrial policy, and they are microeconomic rather than macroeconomic in character.

The issue involves three key elements. There are fundamental myths in the minds of Japanese that revolve around the notion that you break your neighbor's rice bowl by importing manufactured goods. The first is the myth that Japan is a small island nation, devoid of natural resources and unable to afford manufactured imports: the myth of poverty. This

myth is still maintained, but by fewer and fewer Japanese today.

Why then is Japan not importing more manufactures? Why then is Japan's standard of living not increasing as a result of trade? Because of the second myth, the myth of quality: the myth that everything Japan makes is better than anything made in a foreign country. Japan has indeed given the world a new focus on quality. In the meantime, however, many companies maintained the quality of their products all along. Kodak film, for example, is the best in the world; so are IBM computers. In a Japanese restaurant, four brands of beer are offered: Kirin, Suntory, Asahi, and Sapporo. Why not Dos Equis or San Miguel? There are millions of other high-quality products and their absence from the Japanese marketplace deprives the Japanese consumer.

The third myth is "the myth of the lazy foreigner": foreigners do not try hard enough. They do not learn the Japanese language and they do not tailor products to the Japanese marketplace. This is true; all these myths, by the way, contain a grain of truth. It is indeed necessary to make high-quality products and conduct more market research. The reality of trade, however, is that the fundamental galvanizing principle is import pull, not export push. That is the way most markets work. It is not principally because of an exporter's effort that a product from one country enters the market of another: it is the pull of demand in the market, demand that is channeled by and through imports. American manufacturers are importers. They scour the world's marketplaces, looking for products or components that are high in quality and low in price. The procurement is economically rational.

A final point to the Japanese audience: the world is a world marketplace and Japan needs to be part of that world marketplace -- not only as the source of goods, but as a market for goods and parts. With the Yen low, a rich Japanese population, and a financially powerful and secure Japan, many a fortune is going begging. When a constituency of Japanese

importers emerges in Japan, there will be a profound domestic political constituency for free trade. Foreigners do not vote; only a certain degree of pressure can be put on Japan from the outside. Not only *gaiatsu* for free trade, but *naiatsu* for free trade is necessary. Pressure is needed from inside Japan and importers need to give that pressure. The bottom line is profit. There are fortunes waiting. Japan is now a rich country and a country that prides itself on quality. There are many quality products that have not reached the Japan marketplace. If you believe it is the fault of the lazy foreigner for not selling his wares adequately in Japan's marketplace, you ought to prove to him that you are the hard-working importer. In doing so, you can help solve Japan's bilateral trade problem, which is in fact a multilateral problem, not only with the U.S., but the whole rest of the world.

Patrick: Our speakers have addressed the respective strong points of their case: Japanese arguments about national economic issues and the overall trade imbalance, and the American focus on not the trade imbalance, but the problems of market access. I would like each of you to speak for about five minutes, and if you do not mind Mr. Akao, please address this issue of invisible barriers, because it seems to be a very important one.

Why should not the United States impose the Super 301 on Japan and insist that negotiate simply because you do have invisible barriers?

Akao: Japan is ready to negotiate specific trade problems with the United States, as it has always done in the past. Simply criticizing Japan for maintaining "informal" or "invisible" barriers, however, does not contribute to the solution of the problem. If a problem is identified, Japan is prepared to negotiate. Of course, some things are not subject to negotiation -- the distribution system, for instance. If there is a barrier to imports in the distribution sector because of government regulations, it is easier for government to remove such a barrier. But if the barrier is based on the Japanese social and cultural system then it

is very difficult for the Japanese Government to negotiate such a matter with any other government.

Japan is also not prepared to accept being placed on the Super 301 list. This is a fundamental issue. Super 301 is a U.S. domestic issue -- part of the United States policy enforced by Congress upon the U.S. Government. Japan does not care about U.S. domestic decisions, but if and when its policies involve foreign countries, Japan cares very much. This kind of unilateral approach to trade issues is unwise, especially as we have resolved many trade issues through joint cooperative efforts. It also is counter to the spirit of the GATT.

Macroeconomics must be mentioned too. Mr. Massey distinguishes between macroeconomics and microeconomics, but this is impossible. When tension has been heightened between the two countries in the past, there have always been macroeconomic policy problems. In the early 1970s, from '71 to '73, when Japan accumulated a surplus against the United States, we had trade problems because of macroeconomic factors. Again in 1977, '78 and '79, we had a trade surplus due to macroeconomic factors. Now in the mid to late '80s we have similar problems. When macroeconomic problems disappeared, however, microeconomic trade issues also disappeared. They are very closely linked. The primary cause of trade imbalance lies in the macroeconomic area.

Massey: What Mr. Akao has just outlined is an interesting example of what statisticians call "spurious correlation." The fact that micro issues diminished at the same time that macro issues went away should not be taken to imply causation. Simultaneous with the changes in the macroeconomic circumstances were ongoing negotiations concerning trade barriers. For instance, the macroeconomic fact that the Yen is 132 to the dollar makes absolutely no difference with respect to rice. No more rice can be sold in Japan at 132 Yen to the dollar than could be at 268 Yen to the dollar. This is a microeconomic reality.

Akao: Your example is wrong, though. Rice is only a very small portion of Japan's imports.

Massey: That depends on how the problem is defined. If it is defined in terms of deficits versus imports, then you may be right. Rice might be a drop in the bucket for resolving the bilateral trade deficit that the United States has with Japan, or the global trade surplus that Japan has with the world. The U.S. trade negotiators do not define the problem in these terms. There is a barrier to market access that makes it impossible for competitive rice growers to participate in the Japanese market. The U.S. and Thailand can make a better product at a lower price and take the Japanese market in rice. It is outrageous what Japanese consumers pay for rice. Japanese rice, like many other products, is much more expensive than it ought to be, and this has consequences. The price of land is another example. There are many structural rigidities in Japan, such as rice policy, which have substantial trade effects. These are among the informal or invisible trade barriers.

Think, for instance, of the sunshine laws. The average height of a building in Tokyo, which is the largest metropolitan area on the face of the earth, is two-and-a-half stories. Is it because of rice policy? In part. It is also because of the tax laws involving the transfer of property and because of the sunshine laws. Many things in the Japanese economic context have substantial trade effects that are not either macroeconomic policies nor trade policy per se, and they need to be addressed. For instance, the Japanese are experiencing a severe housing problem. This in part arises because of structural rigidities. These function as trade barriers in that if the laws change and Japan has a housing boom, which would benefit Japan, there would be a substantial increase in demand for products that Japan itself can not supply. Plywood, paper products or wall paper, for instance: the U.S. is much more competitive than Japan in these products. If it were not for odd, anachronistic and, over the long run, quite

irrational policies that suppress housing building, Japan's trading partners could help Japan provide more adequate housing for its citizens. Those are examples of policy-based, informal or invisible barriers. Laws can be barriers as well; for example, the large-scale retail store law which impedes the ability of large stores to open branches in Japanese neighborhoods because they have to get prior consent from the mom-and-pop stores whose proprietors are on the local community council. Although they are not trade policies, these laws still need to be confronted and negotiated.

Non-policy and non-law practices also need to be addressed. Japan has seventeen large industrial groups that control a very substantial proportion of the nation's total economic activity. What are the policies of the companies inside those groups? On what basis are procurement decisions made? For instance, if a company is like Sumitomo Electric in their relationship to NEC, how does that relationship effect the economics of fiber-optics purchases? How does it impact upon Corning Electric? Those are key issues. Are those decisions made on economic grounds? Cultural grounds? Structural grounds? What is the impact on imports? The impact on imports is very substantial. Fiber optics is an area in which the U.S. market share worldwide is eighty percent. In Japan it is three percent, and if it were not for NTT, it would be nothing. That does not make economic sense because it is not economics that has led to that outcome: it is a structural reality of the Japanese marketplace. It is an invisible, very real trade barrier.

Patrick: Both the difference and the interrelationship between the macro and the micro are very important when politics is considered. Clearly, at the micro level, there are always going to be issues of trade access because no country except Hong Kong -- and Hong Kong is not a country -- is completely open. Part of that reflects the history and the creation or rise of political interest groups that succeed in protecting their turf. At the same time, it is true that the overall tension in the U.S.-Japan relationship does wax and wane with macroeconomic

conditions in the United States. It depends on whether the U.S. economy is growing well or poorly, whether there is a recession or boom, whether unemployment is high or low, and whether the U.S. has a large or small global trade deficit. That has to do with the political capability of interest groups to capture a wider audience. It is very hard for a particular industry, textiles or steel for instance, to capture Congress. If, however, it can approach Congress at a time when the American people are concerned about broader issues, and steel or textile is considered part of that broader problem, then an industry does have a greater political capability. Mr. Massey has rather skillfully, though, focused on an ongoing set of market access issues that are present regardless of the macro condition.

In the 1988 Trade Act, Congress both empowered and forced the Administration to take the initiative in opening up market access to other countries by requiring the Administration to report to Congress on the trade practices of other countries, indicating which of those were unsatisfactory. Countries would be listed as a priority target for bilateral negotiations with the implication that if negotiations were not successful bilateral restrictions would be imposed on those countries. Certainly the matter of whether Japan is listed or not will come up soon. Japan is so highly visible that it must be considered.

The importance of Japan living up to GATT law has been stressed, yet some people have said that the Super 301 is a unilateral, U.S. law that is inconsistent with GATT law.

Massey: In the first place, Section 301 of the Trade Act of 1974 empowers the President to impose restrictions on access to the U.S. marketplace against countries which engage in unfair trading practices. Unfair trading practices include discrimination or unjust practices, and practices that impose burdens on U.S. commerce.

The law permits companies or industries to petition USTR seeking a determination

by the U.S. Trade Representatives that such an unfair trade practice does exist, and a recommendation to the President to take retaliatory action.

In 1988 the Congress decided that Section 301 should play a more central role in U.S. trade policy and trade negotiations, so they built into the Omnibus Trade Act a section called "Super 301," which requires the Administration to determine the priority practices and priority countries around the world in terms of unfair trade practices. By the 30th of May, those trade practices that have the greatest impact on U.S. trade have to be identified, and the countries that have the largest number and the greatest impact in terms of their unfair trading practices must be determined. This particular section of the Trade Act of 1988, called Super 301, continues in effect for two years. Once a country is determined to be a priority country, all of the practices that have been identified as priority practices for that country are required to be individual Section 301 negotiations. First there will be an investigatory period in which information is collected, public hearings held, and so forth, about the practices. Next, the USTR will consult with the foreign government in question. At the end of the period the U.S. Trade Representative will make a determination as to the fairness or unfairness of the trading practice. The authority which had formally been in the hands of the President is now delegated directly to the U.S. Trade Representative.

A second element of the Trade Act related to this is the "Special 301," which concerns intellectual property. An issue for the U.S. right now with Japan and many other countries is protection for intellectual property. Do the intellectual property regimes of our trading partners maintain protection for patents, copyrights, software, and so forth? Do they adequately and effectively protect the rights of those that create the intellectual property? If they do not, the USTR must make a similar 301 determination.

If Japan or any other country is found to be violating Section 301, then the extent

of the damages to American interests would have to be determined and retaliations imposed. Retaliation typically would be restrictive tariffs.

Akao: It is up to the U.S. to put certain practices or countries on the Super 301 list, but the U.S. can not retaliate simply because other countries did not live up to their expectations. Under the Super 301, the United States intends to play the role of a prosecutor, a juror and a judge. We can never accept this kind of unilateral approach.

Massey: One of the nice things about the world of trade is the international set of rules called the GATT. If it is believed that a party is in violation of its obligations under the rules of the GATT, another party can go to GATT to settle the dispute. In the meantime, the U.S. thinks that the actions we take are GATT consistent. That is one of the fundamental premises upon which the U.S. acts, and Japan takes issue with that. We would love to see you in Geneva.

Akao: I think if the U.S. takes measures against Japan, Japan shall retaliate first. We should retaliate, and then negotiate. Otherwise, we do not have much bargaining power, as is the case with the semiconductor issue.

Massey: Ok. Is that GATT consistent?

Patrick: It is GATT consistent to retaliate.

Massey: Right.

Patrick: Technically it is GATT consistent. It does not sound very friendly, but no foreign country regards Super 301 as a friendly technique.

Massey: Right.

Audience: Why does Japan have two missions? One is to expand economically -- globally, and the other is to prevent foreigners from penetrating Japan.

Akao: Japan does not have a mission to expand. Expansion is simply the result of active business activities. And Japan does not intentionally maintain barriers. Of course, barriers exist, especially the formal barriers that Mr. Massey mentioned earlier. Rice is a barrier. Japan has never denied the fact that it does not import rice. Every country has its own slant to trade issues and for Japan it is rice. Rice is the only major item under import control in Japan. There are fourteen agricultural products under import controls in the U.S.

Japan became a member of GATT in 1955. The United States, however, was the original member and, taking advantage of that, they got a waiver on these items. Once a nation becomes a member of GATT, imports are supposed to be liberalized, but Japan could not liberalize certain items, such as beef, citrus and rice. The United States has maintained import quotas on more than ten items, including sugar, butter, cotton, and peanuts. There is an invisible barrier for beef imports in the U.S., and less than one percent of U.S. consumption of peanuts, butter and raw cotton, are imported.

Japan does not intend to maintain invisible import barriers. For instance, the issue of baseball bats is an old one. Although it was solved a long time ago, the American perception of the issue lags far behind the reality.

There is a difference between American and Japanese safety standards. In Japan, consumers believe the government protects their safety. In the United States, if a

manufacturer should sell a defective product the consumer sues the company or the manufacturer. In Japan, however, because of safety standards, it is the government which is sued, not the manufacturer. Japan is making some progress in trying to deregulate or simplify these safety standards.

Americans claim that distribution is an import barrier, but the Japanese system of distribution developed over hundreds of years of economic activity. It is not a new invention. Japanese companies actually utilize the same distribution system as many American companies.

Patrick: With respect to distribution Mr. Akao, it is very important to understand that the distribution system in Japan is a barrier to market entry, not only for American firms or foreign firms, but for new Japanese entrants as well. If a consumer wants to buy a toaster in Japan, they have a choice of Hitachi and Toshiba toasters. For GE, or Black & Decker, or any company who makes better toasters than Hitachi or Toshiba, it is hard to get into that marketplace. Japanese manufacturers have significant control over the wholesalers and distributors who have significant control themselves over the retail outlets. The fact that the principle role of the distribution system in Japan is that of a social welfare network is significant. However, the distribution system also functions as a barrier to new entrants into the marketplace. Consider the large-scale stores law: if an individual or a corporation wants to establish a new retail store in an area that does not have one, and that store is going to have more than 1500 square meters of floor space, the consent of the local council is needed. The local council, of course, has significant representation among the mom-and-pop stores that are already there. This requirement has significantly slowed the expansion of large stores around the country. It impacts upon imports because large stores have the capacity for large inventories and also are not financially tied to existing Japanese manufacturers. Large stores can afford to put imports on the shelves on a scale that the little mom-and-pop stores can not match.

Audience: Rice is more than an economic commodity in Japan and if Americans exert too much pressure on the rice issue it could lead to more America-bashing in Japan, which is potentially more detrimental to our economic relationship. Rice is an extremely sensitive topic for Japan, just as the fourteen agricultural products on the list are to Americans. I get the impression that this is an adversarial rather than a friendly conversation.

Patrick: That is the nature of the relationship. The American perception of the problem is that the Japanese market is not open in certain respects. If Japan had a trade deficit with the United States and with the world, the non-openness of the American market would be the focus of discussion. The political reality of the bargaining process is that the country with the large deficit is in a powerful bargaining position.

Massey: The U.S. gave Japan a good deal on rice. The U.S. asked Japan to put rice barriers on the multilateral negotiating table of the new round of GATT talks. Japan is a contracting party to the GATT, and does not have a special exemption. The only legitimate barrier to trade is a tariff according to GATT, and Japan was permitted to impose very substantial tariffs - seventy-five percent - in place of illegal barriers to the import of beef and citrus. We now have to see whether Japan, having agreed to multilateral negotiations on rice, engages in them.

Audience: Mr. Massey, although there are not too many American cars in Japan, there are BMWs and Mercedes-Benzes. Are you saying the Japanese have to change their taste to reduce United States trade deficits?

Massey: No one in the United States would argue that Japanese consumers should change their tastes to accord with American demands. The U.S. would like to see the Japanese marketplace open to a range of products so that taste can be rewarded with the ability to buy.

Audience: What has the American Government or American business community done to improve American competitive consumer excellence?

Massey: Countries have various kinds of comparative advantage. Europeans have a specific sort of comparative advantage in luxury consumer items. The U.S. comparative advantage tends to lie in producer and capital goods -- Caterpillar tractors, IBM computers, software, semiconductors -- a whole range of products, the marketplace for which is corporations. That is why the U.S. has particular difficulty in Japan. The Japanese marketplace ought to be open, not specifically for American exports, but for the exports of all of Japan's trading partners. The U.S. does not argue against Japanese imports into the American marketplace. Expanded world trade is good for us all.

Audience: It seems as if the problematic issues for each side are functions of microeconomic issues, and each of you has implied that the solutions are tied to macroeconomic decisions. Given the spirit of this dialogue, please first comment on the constructive actions your own country could take? Secondly, what is the nature of the U.S.-Japan partnership?

Massey: One constructive action that the U.S. could take would be to get our manufacturing back up to a world standard. The U.S. ought to be competitive in all areas; there ought to be a focus on competitiveness. Many government policies need to be reviewed. Many practices of American companies need to be reviewed. Fundamentally, however, the United States economy is a manufacturing economy. There is no such thing as a service economy. The fundamental issue for the United States is to get and stay competitive.

As to the U.S.-Japan partnership, this kind of a dialogue cannot take place unless the relationship is fundamentally strong. Can representatives be as frank with one another if

they are not friends? It is a very good, solid, strong relationship, not unlike the personal relationship between Akao and Massey. We have been friends for twenty-seven years. The United States and Japan have a good and solid relationship, but in some respects it is troubled. Partners often have troubles, but good partners can overcome them.

Akao: Many of the trade issues that have been raised today are very small issues from the perspective of the importance of overall bilateral relations. We, Japan and the U.S., have much more important roles and responsibilities in the global context and so political rhetoric should be avoided. Unfortunately at the beginning of a new administration issues tend to become inflated and more politicalized. Care must be exercised in dealing with that.

The U.S. and Japan need to cooperate in many different dimensions. One of these is macroeconomic policy. A second is the Uruguay Round. The United States has played a very important role in the past rounds of trade negotiations, but Japan should be playing as important or an even more important role than the United States in the current round of multilateral negotiations.

Another area in need of greater cooperation is the accumulated debt issue and economic development in the third world. Japan is the only country which provides money to support the Brady plan. Japan is now becoming the number one ODA provider, surpassing the United States in 1989. Japan not only provides aid, but is trying to enable other countries to procure products under Japanese ODA. American companies are not interested in using Japanese ODA money for export of their own products, so Japan is now organizing, in cooperation with the U.S. Government, a series of seminars in the United States to teach American manufacturers how to utilize Japanese ODA for the export of their own products.

The global environment is another very important issue, and Japan wants to

cooperate with the United States and other countries in playing a positive role. There must be positive cooperation between the two countries in many other areas. We should not aggravate U.S.-Japan bilateral relations by overemphasizing small trade issues.

Patrick: I want to thank our speakers, both for their frankness and for their good humor in dealing with issues that they obviously discuss with each other all the time. We have all benefitted. Thank you very much.