U.S.-Japan Trade: Problems and Prospects

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Trade friction between the United States and Japan continues to heighten with emphasis on the issues of market access and import barriers. John F. McDermid examines these in a "nuts-and-bolts" treatment of trade-related issues as they have developed to the present. The problem is approached in terms of the American political scene, with discussion of the importance and depth of each issue as it stands on the agenda between the United States and Japan. Finally, predictions are made as to how the Administration and Congress may act during 1983 concerning relations with Japan.

U.S.-Japan trade relations have consumed an enormous amount of the energy of American bureaucrats, businessmen and academics. The attack against both Japanese exports and Japan's failure to grant U.S. firms reciprocal access to its market has become an almost ritualistic process in Washington. Moreover, threats of U.S. retaliation have arisen as the outlook for resolving the bilateral economic problems between the two countries has grown gloomier each year and particularly as U.S. trade policy continues to be a scapegoat for the country's ills.

THE ECONOMIC AND POLITICAL SETTING

U.S. trade policy towards Japan is heavily influenced by a volatile economic and political domestic setting. Five factors dominate American trade relations with Japan.

First, the United States' discontent over its trade deficit with Japan has become a dominant issue in both countries and is based upon the assumption that the Japanese market is less open to U.S. exports than is the U.S. market to Japanese exports. The figures are difficult for any U.S. public official to defend politically; the United States had a trade deficit with Japan of $10 billion in 1980, more than $16 billion in 1981, and nearly $20 billion in 1982.

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A second and related factor is the strong perception that, in many ways, the U.S. trade deficit with Japan contributes to a multitude of American economic woes, including record unemployment, low capital investment levels and the underutilization of the country's industrial capacity.

Japan's capture of the major market share of some important U.S. industries is another factor contributing to poor trade relations. For example, Japanese firms have captured 22 percent of the U.S. automobile market, 10-15 percent of steel, 20-30 percent of televisions, 90 percent of motorcycles and 50-60 percent of the radio market.

A fourth factor, discussed more fully below, is the conviction that "Uncle Sucker" has been too tolerant of the bilateral trade inequities that are believed to exist between the two countries.[1]

Lastly, an issue only recently introduced to the U.S.-Japan trade debate is one raised by a group of American businessmen, led by executives from Caterpillar and Borg Warner; namely, that the Japanese government is encouraging a weak yen relative to the dollar in order to promote Japanese exports.

These five factors have generally dominated American criticisms of Japanese trade policies, but they can hardly be taken at face value or be a basis for framing trade policy responses. For example, if the trade deficit with Japan is a reflection of a Japanese market less open than America's, does it necessarily follow that the United States' trade surplus with the European Community (amounting to around $10.6 billion in 1981) is a result of a relatively closed U.S. market? Moreover, as recently noted by the President's Council of Economic Advisors, it is not clear that an easing of Japanese trade barriers would reduce the trade deficit. Also, the validity of the charge of currency manipulation can be questioned as there is little, if any, evidence to indicate that the Japanese government has encouraged the depreciation of the yen against the dollar. The yen's weakness is hardly an isolated global phenomenon in as much as all major currencies, including the West German mark, French franc and British pound, have declined in value against the dollar since mid-1980, many by a greater amount than the yen.

There are other reasons why the Japanese trade debate is likely to become more spirited. Protectionist rhetoric has become fashionable and politically expedient, particularly for the new breed of "Atari" Democrats who are determined to protect this country's high technology lead from the Japanese onslaught. Though this rhetoric is perhaps only a form of political posturing, it could represent the basis for an uncanny union between liberal Democrats

1. This is an expression apparently coined by Representative Richard L. Ottinger, the sponsor and leading advocate of legislation to require a high percentage of automobile manufacturing to be done in the United States.

and the New Right — and the latter has already shown signs of adopting a nationalistic, "get tough" protectionist stance.[2]

The U.S.-Japan trade battle could also become more heated due to the increasing dissatisfaction of major U.S. industries over an open American trade policy. Even traditional supporters of free trade — U.S. multinationals and agricultural interests — have begun to feel that their interests no longer lie in an open trading system. Their dissatisfaction is not only with Japanese policies or practices but also with other countries' trade impediments or incentives. Only wavering support for free trade has come from the aircraft industry (due to foreign export credit subsidies), the agricultural sector (due to export subsidies), the auto industry (due to adjustment problems) and the semiconductor industry (due to foreign industrial policies and import surges).

Before turning to what the congressional and Reagan Administration response has been and what it likely may be, a closer look should be taken at the single most important substantive issue affecting current U.S.-Japan trade relations; namely, the Japanese denial of meaningful market access to U.S. firms.

Market Access To Japan

Although all countries, including the United States, maintain barriers to trade and investment, the commonly shared belief is that Japan's market remains far less open to foreign suppliers. For more than a decade, the United States has sought to persuade Japan to open up its economy to more American services and investment. While the Japanese have been generally unresponsive, they have agreed to several significant trade concessions in the past year and a half.[3]

The first concession occurred in November 1981 when Japan agreed to accelerate the implementation of many of the tariff cuts scheduled under the Multilateral Trade Negotiations. On January 30, 1982, the Japanese government announced a second round of concessions including the creation of an Office of Trade Ombudsmen (OTO) to handle complaints about import practices. (This organization is not, however, very credible to U.S. businesses.) Simultaneously, Japan announced the introduction of sixty-seven steps to reduce non-tariff trade barriers, principally in the customs and product standards areas. On May 28, 1982, the Japanese government

2. "News Release" from Senator Jesse Helms, Chairman, Committee on Agriculture, Nutrition and Forestry. Helms stated that "we must be prepared to take unilateral action, if necessary, to induce the Japanese to reduce their trade barriers . . .," 11 January 1983.

3. Office of the U.S. Trade Representative, *Japanese Barriers to U.S. Trade and Recent Japanese Government Trade Initiatives*, November 1982.

announced a third set of initiatives relating to both tariff and non-tariff barriers.

The real hope for increased market access is pinned on the results of the fourth, and latest, round of concessions that Prime Minister Nakasone offered in January 1983. The basis for these concessions was in the announcement stating that a Cabinet level committee would, by the end of March of this year, recommend changes in some forty laws dealing with product testing and standards for imports, an area which affects about 60 percent of U.S. manufactured goods imported into that country.

U.S. pressure on Japan for increased market access has most often been applied in a bilateral context and, by Japanese government choice, on a product-by-product basis. As reflected in the discussion below, there are many misconceptions that prevail as to the extent to which the Japanese market is closed to American exports. At the same time, there continue to be many undisputed real barriers that prevent an increased U.S. commercial presence in Japan.

Tariffs

The common perception is that Japan's principal means for protecting its market is through high tariff barriers. And yet Japan argues that its weighted average tariffs (which include duty free imports) are among the lowest in the world and will be reduced even further as a result of the tariff cuts agreed to during the Tokyo Round of the Multilateral Trade Negotiations. Moreover, Japan notes, there are fewer dutiable manufactured imports in Japan than in the United States. Washington argues that this may indeed be true, but that one must look at the quality rather than the quantity of the tariff levels. In other words, Japan has very high tariffs on many so-called value-added or processed products in which the United States is most competitive but for which Japan believes its industries need protection. For example, tariffs on rawhides and lumber are low but are very high for leather and finished wood products.

Quotas

The United States concedes that Japan has eliminated many of its import quotas. The quotas that remain significantly inhibit American exports to Japan. The Americans have repeatedly argued that the remaining Japanese quotas are in violation of the General Agreement on Tariffs and Trade (GATT) and have sought their removal. Moreover, the United States argues that, in addition to the quotas themselves, it is the way they are established and administered that further hinders U.S. exports. For example, quota sizes are changed arbitrarily, quota changes are announced late or not at all and Japanese domestic competitors are involved in administering many quotas.

Japanese officials, on the other hand, note that although the quotas are mostly on agricultural products (which they find politically difficult to lift, particularly before the July elections), Japan is still the largest and most reliable market for certain American exports. In 1981 the United States exported more agricultural products to Japan than to the Soviet Union, Eastern Europe and West Germany. Moreover, the Japanese government argues that the number of quotas they maintain is below that of most other industrial countries.

Nontariff Barriers

The Japanese government's requirement for elaborate standards, testing, labeling and certification procedures has emerged as the single most important reason for American firms' inability to increase their penetration of the Japanese market. It has taken the U.S. government years just to identify the problems in this area, much less to understand and articulate Japan's internal procedures.

The conflict over the Japanese importation of American metal baseball bats symbolizes the problem U.S. exporters face in dealing with Japanese product standards, inspections and testing procedures. The American bats were subject to costly and time-consuming lot inspections in which a sample number of bats were inspected at the port of entry. If all the samples were approved, the shipment was accepted. If not, it was sent back. The bats were also subject to what U.S. policymakers believed to be a Byzantine nomenclature of Japanese standards and regulations. Only after nearly two years of seemingly endless negotiations and a Japanese Cabinet decree specifically granting concessions to the U.S. bat exporters was the baseball bat issue resolved.

The baseball bat dispute taught Americans much about similar types of nontariff barriers. U.S. exporters have little or no access to the texts of Japanese standards, written in terms of design criteria rather than performance specifications. This can cause an American product which performs as well as a Japanese product to be rejected on grounds of minor differences in design.

As for testing requirements, the U.S. government has found that Japan refuses to accept foreign test data and results — an acceptable practice in the United States — for many products, including pharmaceuticals and medical equipment. Backlogs, including the time required to perform the test in Japan, can cause delays of one to two years before certain products can be approved for importation; this is particularly true for electronic and medical products. Other goods are subject to individual or lot inspection as opposed to type-testing. Finally, U.S. exporters do not apply directly to Japanese government agencies for testing but go through a Japan-based importer or agent. This importer holds the approval rights once they are granted, and an export company cannot change importers without going through the testing process again unless the importer is willing to transfer the approval rights.[4]

Japan's response to American objections to these nontariff barriers is that exporters from any country should expect to have to conform their products to the standards and tests required in foreign markets such as Japan's. The Japanese government has argued that some of the procedures could be avoided for automobiles, for example, if the foreign automakers designed and produced cars specifically to meet the needs of the Japanese market.

Industry Targeting

Another area in Japanese economic policy which has provoked criticism in the United States is industry targeting, involving the designation of a particular industry as essential to the development of the Japanese economy. Targeting gives the firms in that industry a privileged position in the Japanese market, with the firms benefiting from specific government programs.[5] This policy reflects the close cooperation between Japanese industry and government, especially in the setting of long-range goals.

The U.S. government believes such industry targeting can have several consequences for American foreign commerce. It can result in direct trade restrictions within Japan, such as high tariffs, quotas, etc., or indirect restrictions such as cost and/or risk subsidization or government licensing of patents. Another aspect of such support is the government-sponsored creation of so-called Japanese research and development cooperatives. Some of them, the United States believes, are designed to facilitate technology sharing among Japanese firms while others are designed to spread risk. American firms, including Japanese affiliates, have not been able to participate in these cooperatives nor to gain access to the technological advances made by them. The Japanese government's response has been varied. It contends that government-funded research and development projects are open to qualified Japanese subsidiaries of foreign firms. Furthermore, the Japanese contend, the governments of all industrial countries sponsor research and development and the Japanese government actually spends less for this purpose as a percentage of GNP than does the United States.

4. Ibid.
5. Paul W. Tippett, "Put Heat on Japan," *New York Times*, 10 March 1983. Mr. Tippett is Chairman and Chief Executive Officer of American Motors Corporation. *See also* "Meeting Japan's Challenge," a paid advertisement by the Motorola Corporation, *Washington Post*, 16 February 1983.

Private Sector Barriers

The last, and by far the most difficult, barrier for U.S. firms to overcome in Japan is the Byzantine private sector distribution system which is based on a tangled historical web of social and business links.

The *keiretsu*, or large business organizations, are composed of manufacturing and trading companies which revolve around one of Japan's principal banks. Each of the sixteen *keiretsu* is composed of firms in most or all of the major sectors of the economy, and each firm has a tendency to buy and sell only with other members of the group. The Japanese government has argued that the internal corporate and consumer preference for Japanese firms and goods can be bypassed by imaginative marketing on the part of foreign firms and is too fundamental to the Japanese system to be changed rapidly.

THE U.S. RESPONSE TO JAPAN

In formulating a response to the Japanese challenge, the Reagan Administration has, at least publicly, confirmed the historic American commitment to a free trade policy. The Administration's strategy has been to press Japan to open up its markets to foreign products.

The Administration has used two tactics in an attempt to open Japan's markets. First, it has demanded from the Japanese government a time-frame for arriving at a resolution to the problems identified. Second, it has used Congress as the anxious soldier ready to fire protectionist shots at Japan. The Office of the U.S. Trade Representative has, for example, asked the Senate to pass a resolution in support of a controversial petition filed by a U.S. machine tool company accusing the Japanese of using industry targeting, recession cartels, subsidies, etc., and requested the President to deny U.S. purchasers of Japanese machine tools the investment tax credit.[6]

President Reagan has, however, failed to use the vast range of trade laws at his disposal to attack Japanese imports or to press for increased market access. Moreover, the Administration has rarely taken disputes with Japan to the GATT, a tactic which could be considered effective inasmuch as Japan wants to avoid the public exposure and judgment before what is essentially a Western, industrial country forum. The Administration successfully tested this strategy in the baseball bat case when it forced Japan to agree to settle the issue after the United States brought the matter before the GATT. But since there are many reasons why retaliatory action is undesirable, and because the case-by-case bilateral strategy seems

6. Petition by Houdaille Industries, Inc., for Presidential Action under Section 103 (D) of the Revenue Act of 1971, Section 48(a)(7)(D) of the Internal Revenue Code; Senate Resolution 525, *Congressional Record*, 21 December 1982.

to be showing some results, it is probably desirable that the Administration maintain its current course.

While the U.S. Congress has avoided "quick fix" protectionist legislation in the past, recent events have precipitated more anti-Japanese trade rhetoric. Nineteen eighty-two was a major election year with unemployment rising to near-historic highs and the U.S. trade deficit with Japan projected at $20 billion, a figure attributed principally to failure of market access. Former Vice President Mondale and other mainstream Democrats were calling for protectionism, and the Japanese "do not play fair" theme was bolstered by the Hitachi, Mitsubishi and Mitsui scandals.

It was a combination of these and other factors that led the congressional trade debate to be dominated by a call for reciprocity in trade relations, with Japan as the principal target. While reciprocity has historically reflected a policy aimed at achieving an equitable balance of rights and obligations or a balanced exchange in the international trade of goods, in 1982 it took on a new meaning. First, it was used as the rallying cry for a new "get tough" attitude in our trading relations and as a vehicle for prodding others to open up their markets and comply with their international commitments. The call for reciprocity was applied to covering trade barriers for service industries and to reducing or eliminating the trade distorting effects of conditions on foreign investment.

Finally, the concept of reciprocity was applied in a very different context. Previously, it had been used in negotiating forums where concessions were being offered and requested, and all parties involved hoped to benefit from the process. Last year, however, it was used as a threat involving unilateral retaliation rather than multinational consensus.

Congress did little to follow up on its rhetoric. The trade reciprocity legislation that eventually emerged from the Senate Finance Committee, and has been reintroduced this year, has been characterized as being amorphous and ineffective since it does not require the President to retaliate in the event market access fails to be achieved. Also, the highly protectionist automobile local content legislation that passed through the House of Representatives was substantially watered down by an amendment stating, in effect, that it could not be implemented into law if it violated this country's GATT obligations. The bill never even reached the full Senate.

One of the few things Congress did was to endorse the strongest "Buy America" provision ever passed by providing that, with certain exceptions, imported goods could not be used for highway and bridge construction or for any repair funded by the special gasoline tax fund that Congress established.[7] So while the protectionist rhetoric rages on from all sides,

7. Surface Transportation Assistance Act of 1982 (H.R. 6211). *See* 48 *Federal Register* 1946, 17 January 1983, for proposed "Interim Final Rule" of the Federal Highway Administration.

very little — outside of the "Buy America" legislation — has been done by the Administration or Congress in the way of retaliating against Japan.

Although many of the same conditions will prevail in Congress this year, new elements have materialized as well. There are twenty-six new House Democrats, many of whom gained their positions through labor support. There is also increasing congressional concern over high technology imports and the ability of U.S. high technology companies to gain better market access in Japan and elsewhere. Thus, the "Atari Democrats" are likely to gain congressional sympathy, particularly since high technology is viewed as one of this country's last strongholds which simply cannot be lost to the Japanese challenge.

What kind of protectionist legislation can be expected during the 98th Congress? An important consideration is that no major trade legislation has passed Congress in twenty-odd years without Administration support or sponsorship. It is extremely unlikely that the Reagan Administration will support any legislation that requires retaliation against Japan or any other trading partner, or which otherwise severely limits the flow of imported merchandise.

It is possible that the so-called reciprocity bill will pass the Senate and perhaps even the House of Representatives on the grounds that some symbol, however weak, is needed to reflect congressional trade concerns. It is also possible, but much less likely, that some reform of this country's current trade laws — such as the antidumping and countervailing duty laws, as well as the escape clause — will be passed. Such reforms would generally make it easier and less expensive for business to pursue its interests, but would not violate the United States' GATT commitments. Additionally, automobile local content legislation, which has already been reintroduced, will once again be debated but will probably fail to pass. Finally, there will continue to be product or project-specific "Buy America" bills introduced quietly which, like last year, could pass. To avoid appearing weak towards Japan in the upcoming election year, the Reagan Administration could take any number of actions which would be seen as reflecting a tougher and less tolerant trade position. Certainly it will continue to press bilaterally the host of market access issues, particularly regarding reform of Japanese laws relating to testing and licensing procedures. But no major U.S. policy decisions are likely to be made until after Japan's July elections. It is also probable that the Administration will bring several new trade cases under Section 301 of the Trade Act of 1974, which is principally aimed at market access problems considered to be unreasonable, unjustifiable and discriminatory.

In the face of vigorous business and congressional pressure, the Administration may also design and partially implement policies aimed at maintaining this country's high technology edge. How this will be accomplished is still uncertain, but it will probably include challenges to Japan's high technology industry targeting practices. The Administration may also claim that certain high technology imports are jeopardizing this country's national security.

Finally, Japan will in all likelihood face a continuing tide of retaliatory threats depending in large measure upon how well and quickly the U.S. economy recovers. Some new weapons in the trade war arsenal include imposing new health and safety regulations for imported Japanese goods, detailed customs inspections of Japanese goods at U.S. ports, or even unilaterally increased tariffs on goods that Japan is prepared to export in large quantities but which have not yet gained a meaningful market share, such as home computers.

But overall, the Reagan Administration will continue to massage Congress and deal with trade problems on a case-by-case basis for the forseeable future if for no other reason than that the entire international trading system — as reflected and agreed to in the GATT — is in jeopardy. The Administration and, to a lesser extent, Congress understand that if the United States were to step down as the leading advocate of an open international trading system it would further disrupt the already tenuous world economy and spell the end of the GATT as we know it today.