# Japan's Experience in International Trade Frictions and Its Implication for China

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# Japan's Experience in International Trade Frictions and Its Implication for China

Katsuaki Nagaike

## Abstract

After the Second World War, Japan experienced trade frictions with the U.S. and Europe and it settled them on each occasion with various kinds of countermeasures. For example, deregulation of trade control and capital liberalization were carried out step by step over a long period of time with the development of international competitiveness of its industries. In the case of China, however, such frictions might take place in a more compressed form within a shorter period. China may have to face risks of concurrent and multinational frictions with the U.S.A., Europe, Japan and other Asian countries. Fresh in our memory is the trade conflict between China and Japan which boiled up only a few years ago over agricultural products such as Welsh onion, shiitake-mushroom and rush for Japanese "tatami".

In general, industries should develop into higher levels in proportion to the technological advancement and income growth. Products in which a country is no longer competitive may be transferred to lower developed countries so that it can concentrate on more value-added products or sectors. It is, therefore, an important preposition to share the respective market segments each of which has core competence in the global market. Market segregation should also go through constant changes depending on industrial structure and respective competitive strength. At the same time, one may find an approach to minimizing friction in the construction of mutually reliable relationship with other countries and industrial sectors and in reinforcement of strategic collaboration among industries. In order for China to prevent the escalation of trade friction in the future, it had better learn a lesson from the US-Japan trade conflicts in the past.

## Key words

Trade frictions, industrial structure, international competitiveness, mutual relationship, strategic collaboration

## Contents;



## Introduction

China participated in WTO in December 31, 2001. Recent Chinese economic growth is remarkable. Chinese participating in WTO will contribute not only to increase of business opportunities for China and all over the world but also bring business risks for Chinese domestic industries from short term stand point of view. According to the forecast of Brookings Institution, China will reach the same level of nominal GDP as Japan in 2020, if China will be able to continue to grow by 7% and so on year by year. Brooking Institution also forecast that China will be the 2nd largest country in trade exceeding Germany and Japan in terms of the total amount of trade within 10 year after joining WTO. As the same time, trade friction between advanced countries, developing countries such as ASEAN and China will increase in accordance with rapid growth of export from China because China aim to increase export not only value added industries but also labor intensive industries simultaneously. Japan has been transferred industries to Asian NIES , ASEAN countries from low value added industries such as textile to higher value added industries gradually, in other words, that is called "Wild geese flying patterns", but China has every "Wild geese flying patterns" areas in her own countries. China has advanced areas such as Shanghai and seaside industrial area but has many poor areas at the same time.

Therefore, China has possibilities that she has every kind of industries in her countries without transfer to future lower advanced countries in the future. As the result, there will be possibilities that China face to simultaneous trade frictions with many countries in every kind of industries. As a matter of fact, trade conflict between China and Japan has already boiled up in the agricultural field such as Welsh onion, shiitake-mushroom and rush for Japanese "tatami" recent few years ago. These conflict also began to boil up between U.S.A and China, They are making effort to negotiate to minimize problems as much as possible. The more increase market share of Chinese products in foreign market, the more trade conflicts escalate to boil up with foreign countries. Japan has many kind of trade conflicts with U.S.A. and western European countries in the past. In order for China to prevent the escalation of trade friction in the future, China had better to learn the past US-Japan trade conflicts cases.

Generating pattern of trade friction by industry is as follows.

The first stage of trade friction with trading countries develops when the widening gap of trade

imbalance between two countries reaches a level which puts pressure on the enterprises of the other country in the trading of labor-intensive products that focuses on cost competitiveness such as textiles, steel, and electrical appliances. The subjects of friction will then gradually spreads to more significant technology based products such as high-tech products or defense-related products, and software and services that involve intellectual property rights. Once the settlement of friction issues related to high-tech products is reached, then it will extend to a wider and more comprehensive range. It is anticipated, however, that the range of possible negotiation through WTO will eventually increase in this area.

## Ⅰ. Transition and characteristics of international trade and economic conflicts in the postwar period

Since the end of the last war, the Japanese economy has come through the reconstruction period, high economic growth period, stable-growth period, and the long recessive period in the wake of the dissipation of the bubble economy in the '90s.

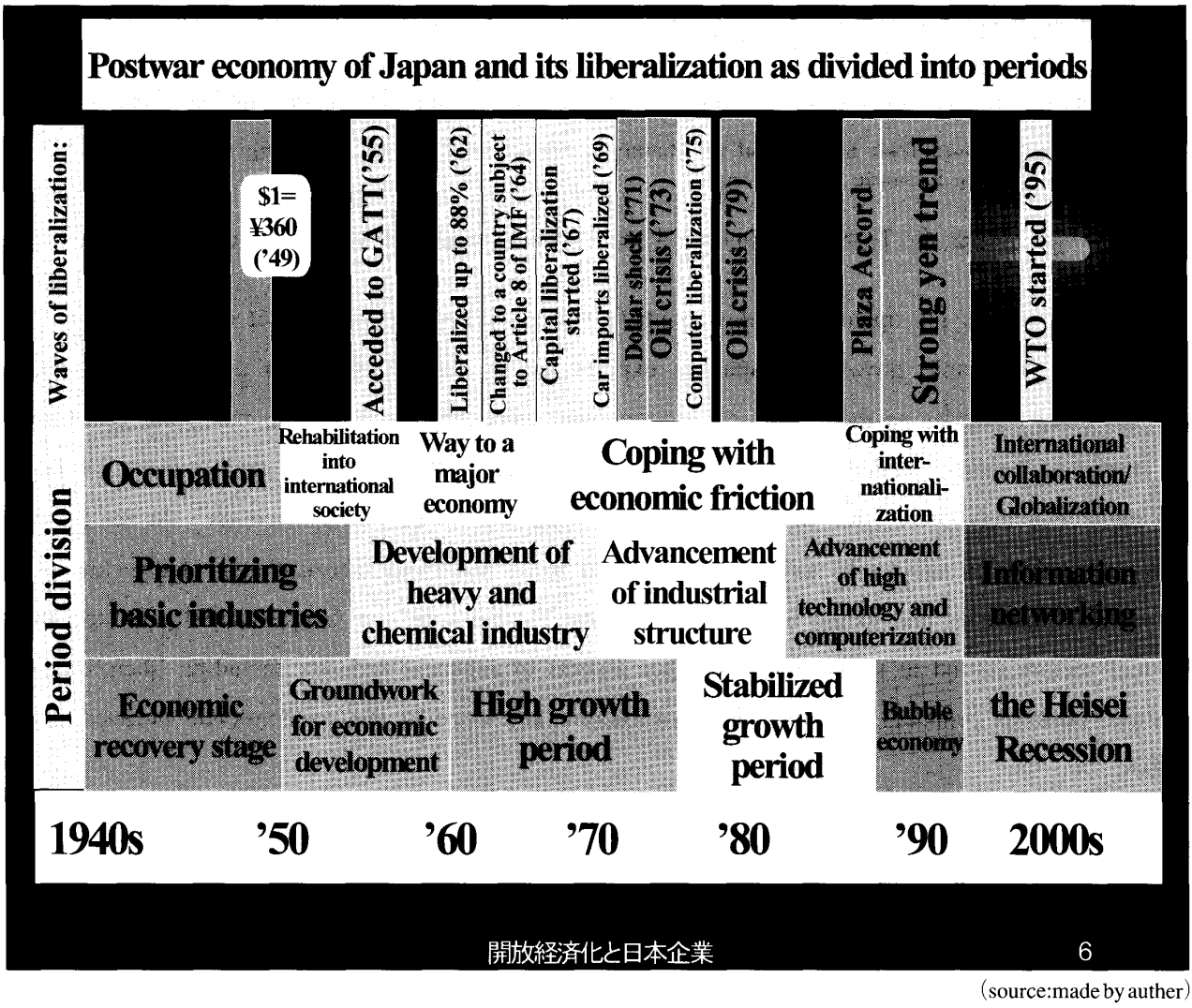


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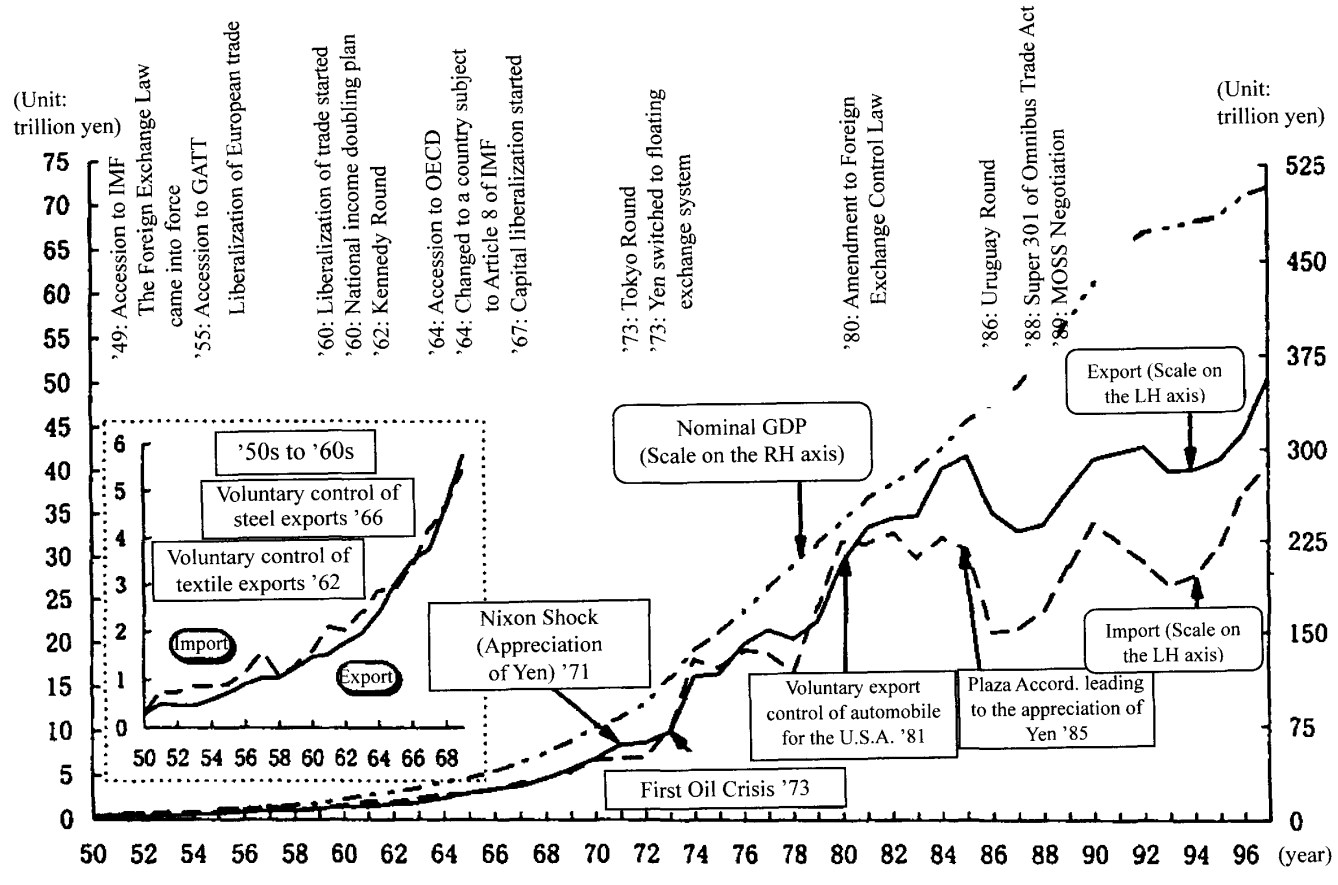
**Fig. 1** : Postwar economy of Japan and its liberalization as divided into periods




Source : "Foreign Trade Statistics" of the Ministry of Finance and "National Accounting Annual Report" of the Economic Planning Agency

Fig. 2 : Transition of imports & exports and nominal GDP in postwar Japan

Meanwhile, waves for opening up the country's economy kept bearing down on it. In the process, the rapid growth in Japanese exports led to trade frictions on different levels between Japan and other countries as the Japanese economy kept increasing its weight in the world economy. The trend started to become particularly noticeable from the late 1960s. Thus, the period from the late '60s to the early '80s may be referred to as the time of "struggle with economic frictions". At the same time, the type of industries subject to such friction started to switch from labor-intensive industries to heavy and chemical industries and to the high-tech industries. Furthermore, the friction initially limited to some individual sectors started to spread out into other aspects of Japanese industry including liberalization, de-regulation, business practices, distribution, infrastructure and even to the governmental policies since the late '80s.

Looking at the history of the trade and capital liberalization of Japan, we can see that the level of liberalization has been stepped up in waves constantly every year from the '60s onward as demonstrated in Fig. 2 above.

| Trade and capital liberalization of Japan (in waves) |
|---|
| · 1949 : Foreign Exchange and Foreign Trade Control Laws came into force (360yen) |
| · 1955 : Accession to GATT |
| · 1960 : Liberalization of foreign exchange and trade |
| · 1962 : 230 items were liberalized by the foreign trade liberalization measure (to the liberalization rate of 88%) |
| · 1963 : Changed to a country subject to Article 11 of GATT |
| · 1964 : Changed to a country subject to Article 8 of IMF (Floating rate system) |
| · 1969 : Initial capital liberalization (Maximum amount eligible for automatic approval was limited to US$200,000) |
| · 1970 : Second capital liberalization (Maximum amount eligible US$1,000,000) |
| · 1971 : Third capital liberalization (Limitation for the automatic approval system abolished) |
| · 1972 : Fourth capital liberalization (Investment and loan activities by the Bank of Japan were to be automatically approved) |
| · 1978 : Fifth capital liberalization (Acquisition of foreign currency securities was liberalized except that it remained notifiable.) |

**Table 1** : Trade and capital liberalization of Japan

## 1. Transition of the U.S.-Japan economic relationship

### 1) Abstract

Overviewing the U.S.-Japan economic relationship in terms of international system, we can come up with two propositions as follows:

(1) The lower the relative position of the U.S.A. in the international economy, the more likely it became for the economic frictions to happen between Japan and the U.S.A.

(2) From the political aspects, the more strained the East-West situation became, the more lenient the political attitude Washington tended to maintain with Japan during the Cold War era, hoping to strengthen the unity of allied countries. As the situation relaxed, however, the U.S. Government tended to take a stricter policy against Japan.

### 2) In the 1960s

The time from the inception of the cold war following the end of WW II until around 1960 was

when the U.S. economy dominantly prevailed over the rest of the world and maintained a relatively friendly attitude toward its allies including Japan. It provided Japan with ample economic and technical supports and kept its domestic markets wide open for Japanese exports, promoting Japan's accession to GATT. Although the U.S.A. started to record losses against Japan in trade after 1965 while the latter overtook Germany in economic performance after 1968 to become the second largest economy of the world. Nonetheless, economic issues had yet developed into such serious political problems as to threaten the U.S.-Japan relationship to its foundation.

### 3) 1970s

The trade friction between the two economic powers started to become noticeable in the earlier half of the 1970s. The Vietnam War was nearing its conclusion and the political tension between East and West started on its way to alleviation as the Moscow Treaty aiming at detent was signed in May 1972. However, the relative position of the U.S.A. in the world economy further backed out, bringing down the value of dollar together with it.

Concurrently, American industries began to lose their relative advantages in many sectors. The so-called Nixon Shock of summer '71 (the announcement of the abolition of the gold conversion system and the imposition of the 10% import surcharge) symbolized the fundamental changes taking place in the international political and economic systems of the postwar era. Incidentally, the U.S. administration started to take a more firm stand against Japan and European countries in this period. Economic issues between Japan and the U.S.A. easily developed into political problems, giving rise to such incidents as the U.S.-Japan textile war and other trade frictions involving steel products and color televisions.

The relative deterioration of economic strength of the U.S. industries continued from the mid-70s to the mid-80s. The Carter Administration used the principle of reciprocity to intensify its demands on Japanese and other governments to open up their domestic markets for American exports, holding up agricultural products such as oranges and beef or electric and communication equipment as the symbols of purported unfair trade practices.

The relatively low wage level of Japanese industry in the 1970s may have caused the trade imbalance and given rise to the international and other trade conflicts.

### 4) 1980s

In the 1980s, the focus of the trade friction started to shift to high-tech products as well as other products, parts, and technologies involved in national defense. With respect to industries, machine tools and automobiles became the source of friction in succession. While the relationship between the U.S.A.

and the Soviet Union was turbulently moving toward a new detent in 1989, America not only recorded the largest twin deficits (trade and federal budget) of all-time but also changed its position from the largest lender to the largest debtor for the first time in the postwar period. Japan then succeeded the U.S.A. as the largest lender.

With the intensifying protectionism of the U.S.A. in the background, the Group of Five (the Conference of Financial Ministers of the Group of Five Countries), with Japan and the U.S.A. in the lead, was held in September 1985 to address the imbalance of the current account. The core intent of the resultant "Plaza Accord" was in the correction of the foreign exchange rates of the respective currencies (by lowering the exchange rate of dollar), that seemed to be quite unmatched to the actual economic performance of the related countries, the appreciation of the Yen and the DM, and the required adjustment and collaboration of the macro economic policies. The U.S.A. seemed to be particularly anxious for the correction of the purported imbalance of the foreign exchanges rates. At the same time, the Reagan Administration set about the application of the Article 301 of the Trade Act, 1974 in earnest.

A significant event of the U.S.-Japan economic affairs was the inception of MOSS (Market Oriented Sector Selective) in order to further accelerate the liberalization of the Japanese Market. The negotiations addressed four critical sectors, namely, telecommunications, electronics, medicines/medical equipment, and forest products.

Irritated by the prescription for correcting the trade imbalance based on the macro economic policy having yielded no noticeable results in the several years after the Plaza Accord, the U.S. government intensified its one-sided demand for recognizable results to the other countries, particularly to Japan. Such irritation caused the U.S. administration to start complaining not only about individual products but also about the economic structures, systems and practices.

Notwithstanding, American manufacturing industries studied in earnest about Japanese production technologies and Japanese business management, digested and put them into practice in their own ways. They gradually started to restrengthen their competitiveness through self-rationalization, the exploitation of IT (information technology), and the improvement of price competitiveness against Japanese industry due to the high Yen in and after the latter half of the '80s.

### 5) 1990s to date

From the 1990s to date, the number of trade friction issues between the U.S.A. and Japan, particularly those of any political significance, decreased relatively from the 1980s levels largely on account of the dissipation of the bubble economy and the relative deterioration of the business competitiveness of Japan and the unprecedented secular boom of the American economy and the recovery of the industry. Today, strategic collaboration is in progress by mutually sharing the respective strengths and conveniently

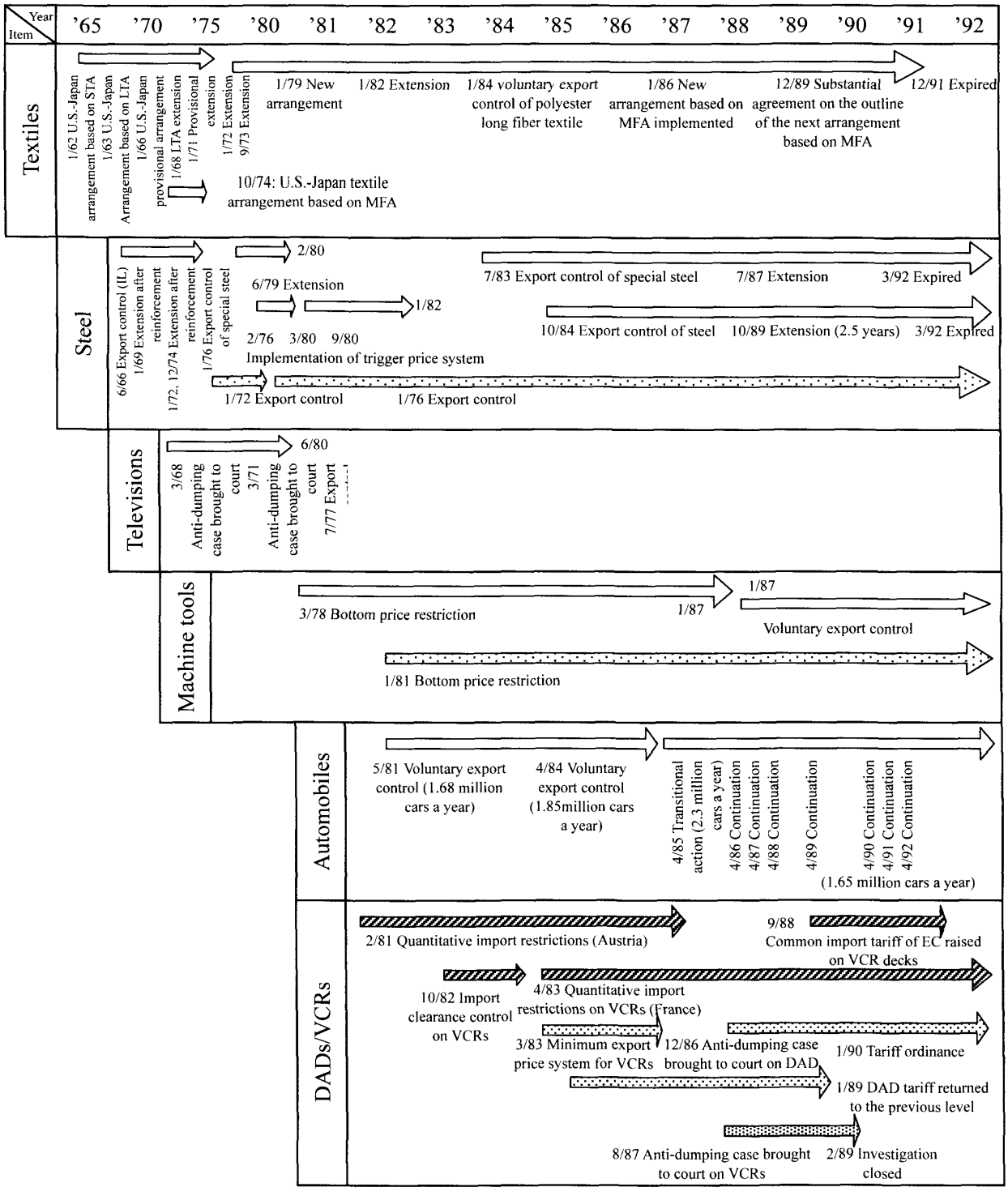
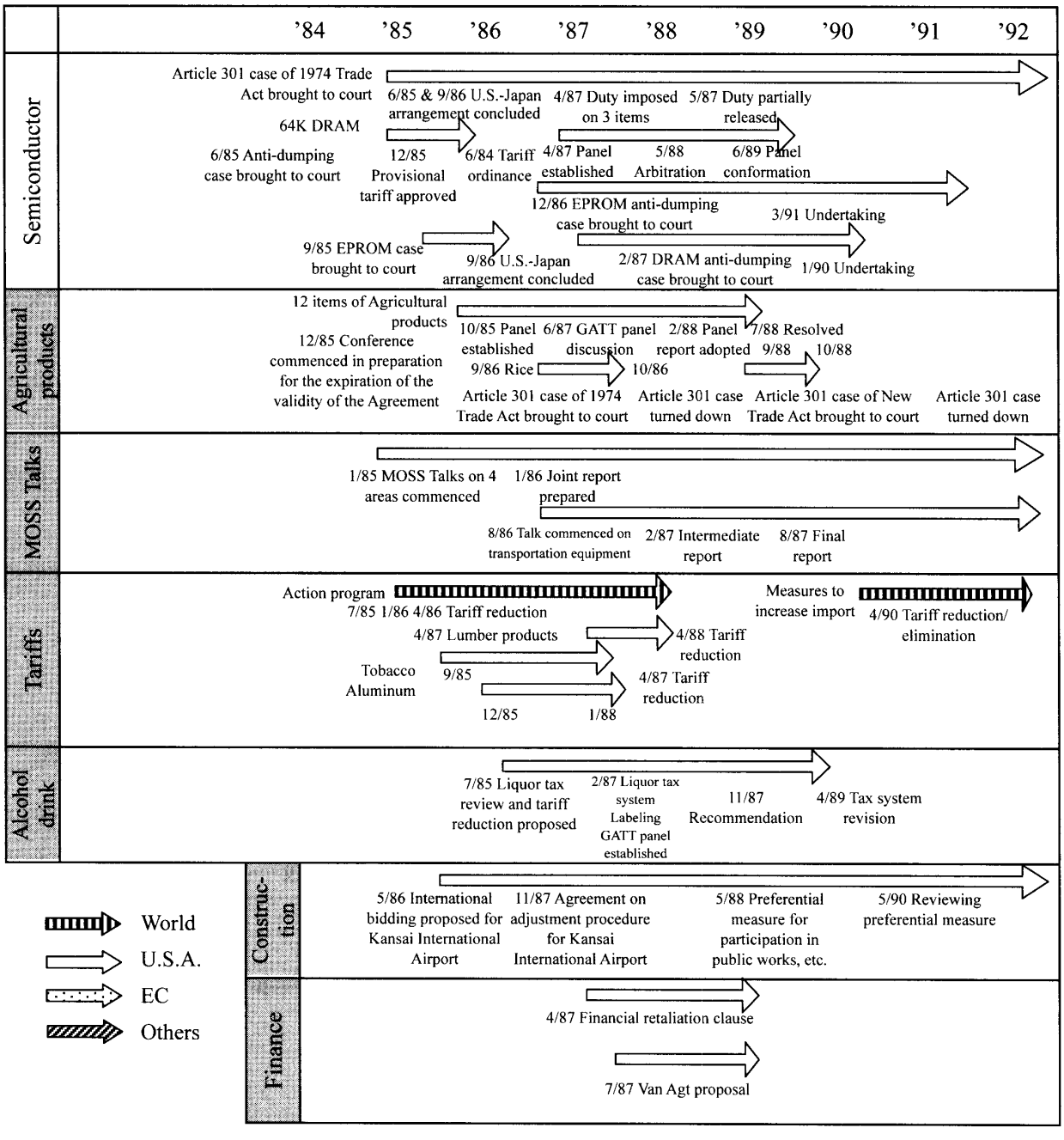



**Table 2** : Transition of major trade issues of Japan

segregating the habitats of each other.

On the other hand, the globalization of IT (Information Technology) and networking has rapidly advanced worldwide since the '90s. In addition, the advancement of the service economy and industry has caused more weight to be placed on the value-added service software surrounding hardware rather than on the hardware itself.




(Remarks)
1. Clause in ▭ refers to trade issues related to export from Japan.
   Clause in ▩ refers to trade issues related to access to market and import to Japan
2. (IL) refers to items based on Export Import Trading Law
3. STA means short-term arrangement related to international trading of cotton products.
   LTA means long-term arrangement related to international trading of cotton products.
   MFA means arrangement related to international trading of textiles

Source: MITI

Under the situation, the world businesses began to build up a new form of global network where businesses look everywhere for management resources for outsourcing and interlink the numerous business bases built around the world with the network. It means that the world businesses have brought the collaborative business strategy into existence to mutually recognize the advantages of the respective

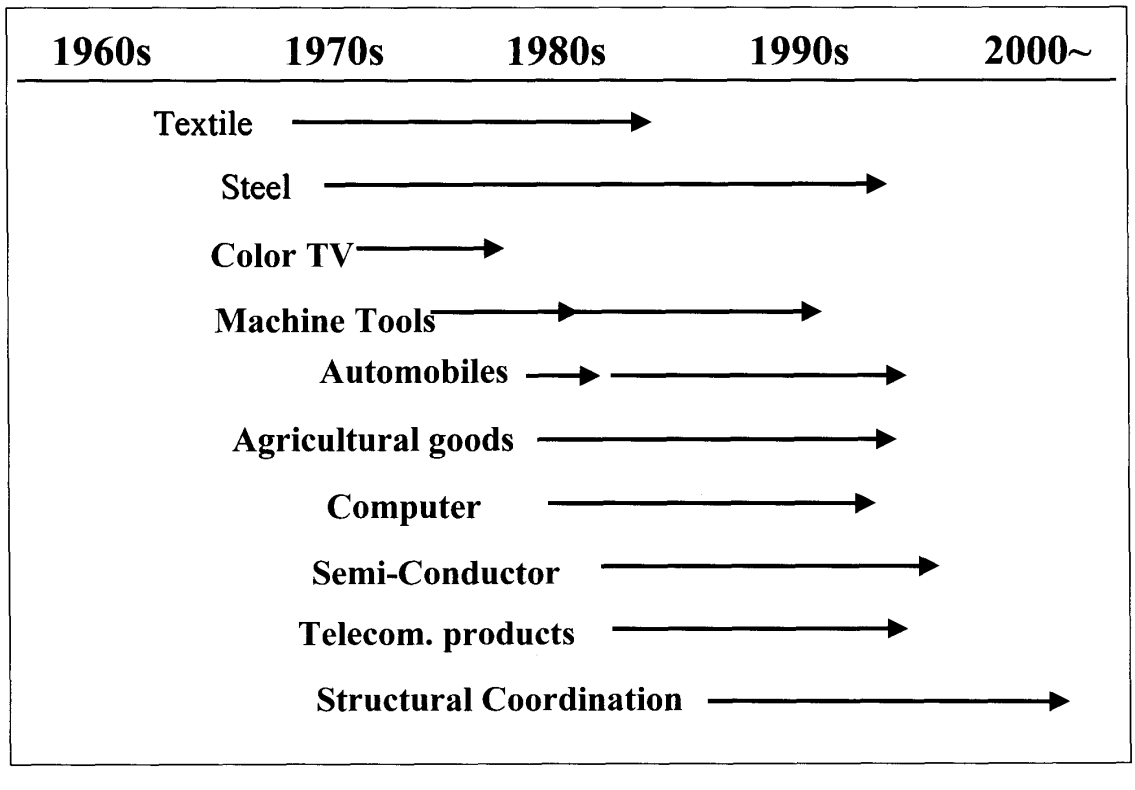
businesses, exploiting them to the best of their benefits. In other words, businesses all over the world started to build up mutually dependent relationship multilaterally across the borders.

It was also a time when the activities of trans-national territorial unity such as NAFTA and EU intensified. Such territorial unity may be considered as a step toward the ultimate globalization, or the formulation of liberalization and rule-making under WTO, although it is not without risk of the blocking of the economy.

Any trade issue is basically the accumulation of bilateral negotiations between countries involved over economic issues, many of which may contain political consideration. Thus, the related countries tend to prefer settling differences and disputes with the help of a multinational organization provided with objective rules and an independent dispute-settlement institution, or WTO. That was the requirement which warranted the establishment of WTO. Products also had to include not only hardware but also hardware integrated with software.

That was the reason why the establishment of WTO, taking the place of GATT, in 1995 was called for.

## 2. Examples and remedy of trade frictions between Japan and the U.S.A.




Source: written by Auther

**Fig. 3** Examples of trade frictions between Japan and the U.S.A

### 1) 1970s

It was in the 1970s that the trade imbalance became prominent and trade friction started to occur in earnest in connection with a number of products.

It ranged from the U.S.-Japan Textile Negotiations under the Nixon Administration to television, steel products, agricultural products negotiations, and the liberalization of Nippon Telegraph and Telephone Public Corporation under the Carter Administration.

They were trade issues between two countries on equal footing in terms of international competition and examples where Japan which had caught up with the U.S.A. in economic strength gave in to the political power of the latter. Agreements were concluded through bilateral negotiations as well as voluntary export control by Japan.

#### (1) Textile

① Characteristics and events

Japanese synthetic textile industry in the 1970s, consisting of manufacturers of nylon and tetoron such as Toray Industries, Teijin and Asahi Chemical Industry, was the active industry of the time that did not easily give in to the pressure of American chemical and synthetic textile industry headed by Du Pont.

② Remedy

A rigid framework was set upon the export of Japanese textiles for the U.S.A. under the U.S.-Japan Textile Agreement between the Nixon and Sato Administrations in 1972. The framework included limitations on the total quantity and annual growth (5%).

Although it was not termed as such, it was practically of the same nature as the OMA (Orderly Marketing Agreement) stipulated under Article 301 of the 1974 Trade Act, and of the same effect as the voluntary export control frequently practiced in the 1980s.

#### (2) Steel

① Characteristics and events

Firmly maintaining the top production volume of steel in the world for a century since the end of 19th Century, the U.S. steel industry dropped this status in and after the '70s. The production of basic steel that peaked in '73 almost halved in the '90s. Particularly the scope of the industry and the number of workers have greatly dwindled as the aftereffects of the recession from '81 to '82 persisted with successive closures of steel mills.

The situation might be attributable to (1) aging facilities and waning productivity due to insufficient investment for modernization; (2) increasing imports from Japan and other Asian countries of improved

competitiveness; and (3) decreased domestic demands as the substitution of steel by plastic advanced.

Steel exports from Japan to the U.S.A. in the '70s and thereafter resulted in an excess of exports on the part of Japan, which led to eventual trade friction between the two countries.

② Remedy

The first and second voluntary export controls were implemented during the period of 1969 to 1974. The U.S.A. enforced a control over Japanese steel exports for the U.S.A. by establishing the trigger price in April 1978. It was a system established by the U.S. Treasury Department where standard prices were stipulated on the basis of the steel production cost of Japanese steel makers that was the lowest in the world so that a dumping investigation would be triggered as soon as any steel exporter undercut the standard price.

The trigger price was established by the U.S. Treasury as the result of a dumping investigation performed by the department in response to a dumping appeal filed by U.S. Steel Corporation in September 1977. Japanese steel makers implemented the voluntary steel export control in '84, which continued until '91.

Meanwhile, American steel makers worked to restructure the industry during the '80s and were on their way to revitalization. Their competitiveness has increased as the investment in plants and equipment increased and corporate income started to improve. Japanese steel imports, on the other hand, have started to increase as led by flat rolls since '87 while the situation of the Asian steel making industry started to transform in recent years with the rapid growth of steel making industries in South Korea and China.

### (3) Color television

① Characteristics and events

The Japanese electric industry has kept increasing their exports to the U.S.A. in succession with transistor radios in the '50s, monochrome televisions and tape recorders in the '60s, and color televisions in the '70s by developing and manufacturing competitive products in the household electronics sector against the background of low labor costs. Having lost competitiveness in the face of increasing imports from Japan, some American manufacturers started outsourcing from overseas to reduce their production costs, some withdrew from production because of failure to cope with the fall in revenue or started to rely on OEM purchases overseas. None of the nearly 20 television manufacturers operating in the U.S.A. in the '70s remains in manufacturing today. As for VCRs, American manufacturers succeeded in the production of VCRs for business use in the '50s but failed in the volume production of VCRs for home use in the '70s and had to pull out from the market.

While American manufacturers kept losing competitiveness in the market, the domestic demands for consumer electronics in the U.S.A. kept rapidly increasing and at a high rate of 16% per annum during

the period from '82 to '86. The U.S. market for high value added products including projection television sets, CD players, and camcorders expanded rapidly in the latter half of the '80s. A dominant part of the domestic demands was fulfilled with imports including OEM or by the local production of American suppliers and products from Japan, NIES, and ASEAN countries, increasing the dependency of American consumer electronics on exports from all over the world from 47% in 1980 to 70% in 1990.

With respect to color televisions, American manufacturers have brought the cases allegedly in breach of trade related laws including the anti-dumping law and the compensating tariff law against Japanese manufacturers to the courts. The tactic called "multiple legal harassment" has become one of the favorite measures used by American industries to fight off Japanese imports since then.

② Remedy

As soon as the Carter Administration took office in 1977, Vice President Mondale was sent to Japan as President Carter's Ambassador at large to request a remedy for the rapid increase of color televisions and steel exports to the U.S.A.

In the London Summit held in May 1977, President Giscard d'Estaing of France proposed the maintenance of order in world trade by using a term "administered trade", to which Prime Minister Takeo Fukuda promised to refrain from torrent-like export. Nevertheless, Japanese exports kept increasing despite the promise, causing Japan to execute OMA with the U.S.A. on color televisions exports to the country, which called for Japan to limit its export of color televisions to not more than 1,750,000 units (finished products × 1,560,000 and semi-finished products × 190,000) for a three year period.

Japanese exports of color television sets for the U.S. market counting 2,530,000 units in '76 (which accounted for 30% of the U.S. demand) dropped immediately to 1,430,000 and 14% respectively in '78. Meanwhile, Japanese manufacturers in an effort to cope with the situation expanded their production of color television sets by subsidiaries in the U.S.A., increasing to 3,350,000 units in '79 and reducing the volume of exports from Japan to 690,000 units to undercut the specified volume under the OMA.

### (4) Beef & Oranges

① Characteristics and events

A consistent complaint from the U.S. side was that the closed nature of the Japanese market prevented American suppliers from exporting internationally competitive American products to Japan. Agricultural products such as beef and oranges, which were subject to quantitative import restrictions by the Japanese government, were the most representative of such products. The U.S. administration was most anxious to remove the import restrictions on these two products, that were not particularly significant among exportable American commodities in terms of value, since the administration, committed itself to remove the Non-Tariff Barrier in the multilateral trade negotiation (Tokyo Round) of GATT, was

looking to secure support from domestic agricultural groups in order to maintain its favorable relationship with the congress and to ensure the congressional approval of the Tokyo Round negotiations. While in Japan, agricultural groups tried to place intense pressure on the government against liberalization, insisting that opening the domestic market to competitive beef and oranges would surely throw Japanese livestock farmers and tangerine growers' business into jeopardy.

② Remedy

Negotiations were held in succession from 1977 to 1978 and concluded in '78 with a tentative agreement on uplifting the import limitations (to 38,000 tons of beef and 82,000 tons of oranges) until fiscal 1983. The issue continued smouldering with negotiations held in 1983-84 and 1987-88 where Japanese Government inched back little by little in compromise until, finally in 1988, agreeing upon the total removal of import restrictions from 1991.

Japanese farmers have been making efforts to improve the quality of domestic beef and tangerines since then.

Japanese consumers have also been trying to adapt themselves to the situation with selective consumption of high class domestic beef such as Kobe and Matsuzaka beef and other imported beef depending on the occasion and with similar segregation of markets between domestic and imported citrus fruits. The resulting effect of the liberalization has not been as grave as everyone thought or insisted to be.

## 2) 1980s

### (1) Machine tools

① Characteristics and events

With the high level of technological standards, the U.S. machine tool industry boasted the world's largest production against the background of the growing user industry including automobile and general machine tool industries for a long time with import dependency being as low as a little over 10% in the earlier half of the '70s. However, the industry started to slow down with notable production delays in the delivery with deteriorating production capacity and, in the 1980s, went through major reorganization where major conglomerates started to reduce in scale or to completely pull out of the industry by selling out their machine tool subsidiaries. The industry at large fell behind Japan in their efforts for product development by economizing prices and producing higher precision products in the area of numerical control or medium to small size machines. It resulted in the increase of machine tool imports, raising the import dependency of domestic demand to 48% by 1989. Major American manufacturers tend to specialize in the production of large high precision machine tools and specialty machines for the aviation, space and defense sectors while utilizing OEM supplies for the provision of small and volume production

machine tools.

Meanwhile, Japanese manufacturers have concentrated on cultivating markets for small and economic type of machine tools and other general purpose machines by generating higher precision and quality products through the most advanced technological innovation such as numerical control, robotic processes, and FMS (Flexible Manufacturing System) based on electronic application technologies. As a result, the Japanese export of machine tools to the U.S. rapidly increased from the late '70s for Japan to record a large excess export.

② Remedy

U.S. industries have strong concern about the excessive dependency on Japan of the machine tool sector which is the most critical of the industrial base. Responding to this atmosphere, Japan has managed to maintain application of voluntary export controls on several items of machine tools since '87 in accordance with the U.S.-Japan Machine Tool Agreement concluded in '86, keeping the U.S. dependency of machine tool demands on Japanese imports at a relatively stable level as compared with that on imports from other countries.

### (2) Automobiles

① Characteristics and events

The shifting demands for compact cars in the U.S. consumers' market as a result of two oil crises has expanded the gap between the U.S. automakers' supply capacities and the emerging demands for compact cars. It resulted in an increased demand for smaller imported cars, particularly energy saving high quality imports from Japan, rapidly increasing the number of Japanese car exports to the U.S.A. It soon led to the implementation of voluntary control on car exports from fiscal '81 as the trade friction was elicited with the expanding share of a Japanese cars in the American market.

Overlapping with the emergence of a recessive trend in the U.S. economy, car sales decreased by 21% in the period from '78 to '80 in general and 29% in American automobiles most of which were large cars. The total deficit of the four major American automobile makers was recorded as 4 billion dollars in '80 with Chrysler Corporation facing a financial crisis. In a situation with 1 out of every 4 workers loosing their job in the automobile industry, Japanese car exports increased by 40% from 1.36 million cars in '78 to 1.91 million cars in '80, enhancing its market share from 12% to 21%. The development forthwith caused car makers' and the UAW's campaign to suppress imports to intensify from around the end of '79, which eventually led to a situation where a succession of import control bills were submitted to the Congress in spite of the adjudication passed upon UAW and Ford Motors by ITC (International Trade Commission) that "the U.S. automobile industry had not been harmed by the increase of imports". Under such circumstances, the Reagan Administration inaugurated in January 1981 requested Japan to

implement a voluntary export control.

② Remedy

The Japanese Government agreed to implement voluntary export controls for the U.S.A. to avoid aggravating the general bilateral relationship in general limiting the quantity of finished car exports to the U.S.A. to 1.68 million cars (against the actual exported quantity of 1.91 million in 1980) in May '81. Since then, Japanese car exports barely increased until '84 and more or less leveled out after that except for some increase recorded in the period between '84 and '86 because of some expansion of the quantity subject to the voluntary control. With respect to the quantity by the size of displacement, while the quantity of cars of 2000cc engine displacement or below started decreasing after it peaked in '86, the number of exports of cars with 2000cc or more displacement has been dramatically increasing since '87. In view of the appreciation of the yen, local production in the U.S.A. by Japanese automakers has gone into full swing since '85 to rapidly increase the production volume. As a result, export in '89 to American markets decreased to 1.95 million cars to undercut the limited volume under the voluntary control.

## (3) Semiconductors

① Characteristics and events

The American semiconductor industry has led the world in both technology and the international market for a quarter of a century since they commercialized transistors in the '50s. However, it started to gradually lose relative competitiveness as Japanese manufacturers started to gain a competitive edge from around the middle of the '70s.

The semiconductor business started to rapidly deteriorate bringing trade friction between the semiconductor industries of both countries from 1984 onward. The Semiconductor Industry Association (SIA) of the U.S.A. brought the case to USTR (Office of the United States Trade Representative) claiming that the protective measures by the Japanese Government were in breach of Article 301 of 1974 Trade Act in June 1985 and USTR commenced its investigation in July of the year. A series of similar dumping investigations were then initiated in response to anti-dumping appeals made by Mikron on 64K DRAM in June 1985, on EPROM by Intel, AMD, and National Semiconductor in September the same year, and by the official authority of the Department of Commerce on DRAM of 256K or above in December the same year. After mutual consultations between the governments of the two counties for a year in an effort to resolve the situation, the U.S.-Japan Semiconductor Agreement was executed in August 1986. The U.S. Administration, however, imposed 100% duty on three items including personal computers on the grounds that Japan failed to achieve market access for foreign invested semiconductor manufacturers guaranteed by the above Semiconductor Agreement in April 1987. As a result, some of the Japanese PC

manufacturers switched to start production in the U.S.A rather than exporting from Japan in view of the excessive duty.

The American semiconductor industry maintains a competitive edge in the high added value sectors over Japan although they have reduced the production level of volume production items such as general-purpose memories.

The American semiconductor industry received a serious blow in the semiconductor recession of '85 as they actively invested in plants and equipment in the booming period in the early 1980s, but have concentrated their efforts in specializing in the sector they are good at in terms of both technology and production. Eventually, American manufacturers were dominating the areas of wiring design technology, MPU and logics where software plays an important role, and the application specific integration circuits (ASIC) with a distinct edge over the others even though many of them may have had to withdraw from the DRAM area where the superiority in the volume production process counts the most.

In the later half of the '80s, American manufacturers were concerned with their late start in building up the technical innovation and volume production capability for the future in the situation where enormous amounts of investment in plants and equipment and research and development are prerequisites to coping with the coming megabit era of the semiconductor industry. The collaborative project "SEMATEC" was commenced in 1988 to develop semiconductor-manufacturing technology in joint a effort between the government and private corporations. The industry has also built up a mutual complementary system to develop and supply products through an international partnership to ensure the provision of technology and products that cannot be effectively covered by each individual corporation. In the aspect of international trade, imports are fast increasing, particularly memories and other products from Japan.

② Remedy

The division of operation based on differentiating products in the IC sector has greatly advanced, reflecting the "segregation of markets" between the U.S. industry which holds the competitive edge in such areas as ASIC and MPU where the design and development technologies count, and Japanese industry which is competitive in the general purpose products such as memories where superiority in the manufacturing technology is indispensable. The cases of bilateral provision of technologies or OEM collaboration are also in progress between the manufacturers of the two countries where the U.S. manufacturer adopts memory-manufacturing technology from Japanese partners while American manufacturer provides the Japanese manufacturer with MPU-manufacturing technology to strengthen their cooperative relationship.

### 3) 1990s

## From friction to structural coordination (U.S.-Japan structural conference)

It is unavoidable to a certain extent that disputes and differences of opinion occur as the trade and capital relationship progresses across borders. The unprecedented sustenance of peace and prosperity in the world economy for over a half century after the World War II, owes a great deal to the steady development of international trade as supported by the GATT (General Agreement on Tariffs and Trade) and IMF (International Monetary Fund).

The real Gross National Product of the 23 members of OECD (Organization for Economic Cooperation and Development) has tripled in the 30 year period from 1960 while real exports (including services) and real imports among OECD countries have developed at a much faster pace and have increased 6 times. As a result, economies heavily depend on each other among these countries and frictions among major stakeholders are increasing in proportion. Irrespective of frictions between Japan and the U.S.A. and Japan and European countries, disputes have never ceased between America and Europe and even between America and Canada.

Among all these incidents, the trade and economic frictions between Japan and the U.S.A. have been particularly remarkable.

| Target country | Description | Action taken |
|---|---|---|
| Japan | Import restriction on leather goods<br>12/77: Investigation commenced<br>01/79: Talks on Article 23-1 and agreement to enlarge limitation<br>04/83: Panel installed 05/84 : Panel recommendation adopted<br>12/85: Japan proposed a compensatory measures related to transition to the tax allocation system and incidental tariff increase.<br>03/86: Sanction exerted as the offer was deemed to be unsatisfactory | Tariff increase by 40% on leather and leather shoes (still in force to date) |
| Japan | Import restriction on leather shoes12/82: Investigation commenced 04/83 : Talks on Article 23-107/85 : brought the case to the panel and requested application of the conclusion of the previous Leather Panel. 12/85 : (T he same path as the above was followed from here on) | |
| Japan | Barrier to accession to the semiconductor market and dumping07/85: Investigation commenced 07/86 : Japan-U.S.A Semiconductor Agreement concluded (Acceleration of market access and prevention of dumping, to be signed in September) 03/87 : U.S.A. decided on implementing sanction for the reason of breaching agreement (Market share not yet improved. Dumping to third countries). 04/87 : Sanction exerted. Japan requested talks under GATT Article 23-1.06/87 : Sanction terminated on color televisions but continued on the rest of items until the New Agreement comes into force in 91. | 100% duty imposed on PC, electric tools and color televisions |

**Table 3** : Major examples of the implementation of Article 301, 1974 Trade Act

Firstly, these frictions intensified almost every few years to develop into major political issues between the two nations.

Secondly, while most of the disputes between the U.S.A. and European countries were limited to agricultural issues, the subject of friction between Japan and the U.S.A. has constantly expanded and elaborated, ranging from textiles, steel, color televisions, and automobiles, to high-tech products including semiconductors and various other items.

Furthermore, countermeasures by the U.S. Government have kept strengthening and becoming more elaborate each time as America's Trade Act has been revised since the 1970s purporting to cope with the so-called "unfair" trade practices of the other country, the most representative of which are Article 301 of 1974 Trade Act and the so-called Articles Super 301 and Special 301 of the 1988 Omnibus Trade Act. Other tactics of the U.S. government include the measures to unilaterally pressure the opposing party by constantly showing off their special tools called "sanctions" outside the framework of GATT/WTO.

Thirdly, the scope of friction kept expanding to include a wide range of problems from disputes related to product export to America, Japanese import restrictions, macroeconomic policies, the closed nature of the Japanese economy, and even economic systems and business practices. It was exemplified by the Japan-US Structural Impediments Initiative (SII) where it has tried to deal with almost every problem including the scope and distribution of Japanese public investments, Large-Scale Retail Stores Law issues, and even the way Japanese corporations' way of running business with their affiliates (KEIRETSU).

In the 1990s, however, corporations increasingly tried to build up more collaborative or interdependent relationships in line with the advancement of globalization, computerization and networking, software utilization, and shift to service industry.

The Japan-US Structural Impediments Initiative is still continuing to date but the focus seems be shifting to both multinational and bilateral coordination while the number of issues developing into significant political disputes is diminishing.

## Ⅱ. Generating causes of trade and economic frictions and settlement patterns

### 1. Generating causes of trade and economic frictions

#### 1) Japan-US trade imbalance

Trade frictions became more frequent as the gap of trade imbalance between Japan and USA widened.

| | Current Account | | Japanese trade balance against US* | | |
|---|---|---|---|---|---|
| | Japan | USA | Export | Import | Balance |
| 1955～59 | 0 | 15 | 7 | 11 | ▲ 4 |
| 1960～64 | ▲ 4 | 43 | 14 | 20 | ▲ 6 |
| 1965～69 | 10 | 24 | 35 | 32 | 3 |
| 1970～74 | 19 | 8 | 89 | 77 | 12 |
| 1975～79 | 43 | ▲ 17 | 196 | 142 | 54 |
| 1980～84 | 138 | ▲ 292 | 419 | 250 | 169 |
| 1985～89 | 718 | ▲ 1,319 | 827 | 353 | 471 |

(Note) *--Customs clearance statistics. ▲indicates deficit
Sources : Ministry of Finance, US Department of Commerce

**Table 4** : Transition of the balance of current account and trade balance
(Annual average : hundred million US dollars)

## 2) Exchange rate issue

The Yen rate has constantly been appreciated against the US dollar through the postwar period to settle the trade imbalance.

## 3) Increase in the U.S. market share of Japanese products vs. occurrence of trade frictions

Trade frictions occurred when the U.S. market share of Japanese products went above a specific level.

| | |
|---|---|
| Semiconductors (Note 1) | 42 |
| Adding machines/Cash registers | 30.8 |
| Automobiles (Note 2) | 16.6 |
| Color televisions | 16.6 |
| Cameras and others | 8.7 |
| Bearings | 7 |
| Computers | 4 |
| Electronic devices | 3.2 |
| Construction machines | 3.1 |
| Valves and pipes | 2.2 |

(Note 1) 1979, 16KB/RAM
(Note 2) 1979
(Source) Prepared from Industrial Outlook '79, U.S. Department of Commerce

**Table 5** : The share of Japanese products in the U.S. Market in 1978

| | | Cotton Prod. | Steel | Color TV | Automobile |
|---|---|---|---|---|---|
| Intensification of campaigns to restrict exports (A) | | 1955 | 1965 | 1970 | 1979 |
| Voluntary export control (B) | | 1957 | 1969 | 1977 | 1981 |
| Volume of Japanese export to U.S. | Year (A) | — | 442 | 88 | 177 |
| | Year (B) | 150 | 729 | 253 | 191 |
| | Following year | 100 | 594 | 143 | 168 |
| Japan's share of US market | Year (A) | — | 4.4 | 16.6 | 16.6 |
| | Year (B) | — | 6.8 | 30.1 | 21.3 |
| | Following year | — | 6.1 | 14.2 | 19.7 |
| U.S. trade deficit on the subject products started | | 1955~ | 1962~ | 1962*~ | 1968~ |
| (Note) Unit: 1 million sq. yard for cotton, 10,000 tons for steel, 10,000 sets for color TVs and cars. *Electrical appliances | | | | | |
| (Source) Akinori Marumo: "U.S. Economy," P. 131, Toyo Keizai, 1982 | | | | | |

(Remarks) Dollar values for the period FY70-FY85 were converted into yen at the interim average of spot central rates of Tokyo Inter-bank market. Exchange rate shown in the figure are calculated on a calendar basis.
(Data) IMF "IFS", the Ministry of Finance "Actual results from the Direct Overseas Investment Report"

**Table 6** : Transition of major products subject to Japan US trade frictions

## 4) Argument of the closed nature of the Japanese market

The "peculiarity" and closed nature of the Japanese market has been frequently discussed in the Japan-US Structural Impediment Initiative in various forms, and their improvement has been often subject

to demands from the U.S. side. Demands brought up included the elimination or mitigation of various regulatory restrictions instituted across the entire system, improvement of KEIRETSU transactions and the complex distribution system, that are collectively called the non-tariff barriers and requested to be brought down to open up the Japanese markets.

## 5) Complaints about the Japanese macro policy

(requirement for domestic demand expansion)

The initiative took such subjects as financial and monetary policy, and the administration of the macro economy for discussion and requested the Japanese government to convert its economic base from the external demand-led system to domestic demand-led system to look for further growth. The "Maekawa Report" was the answer from Japan.

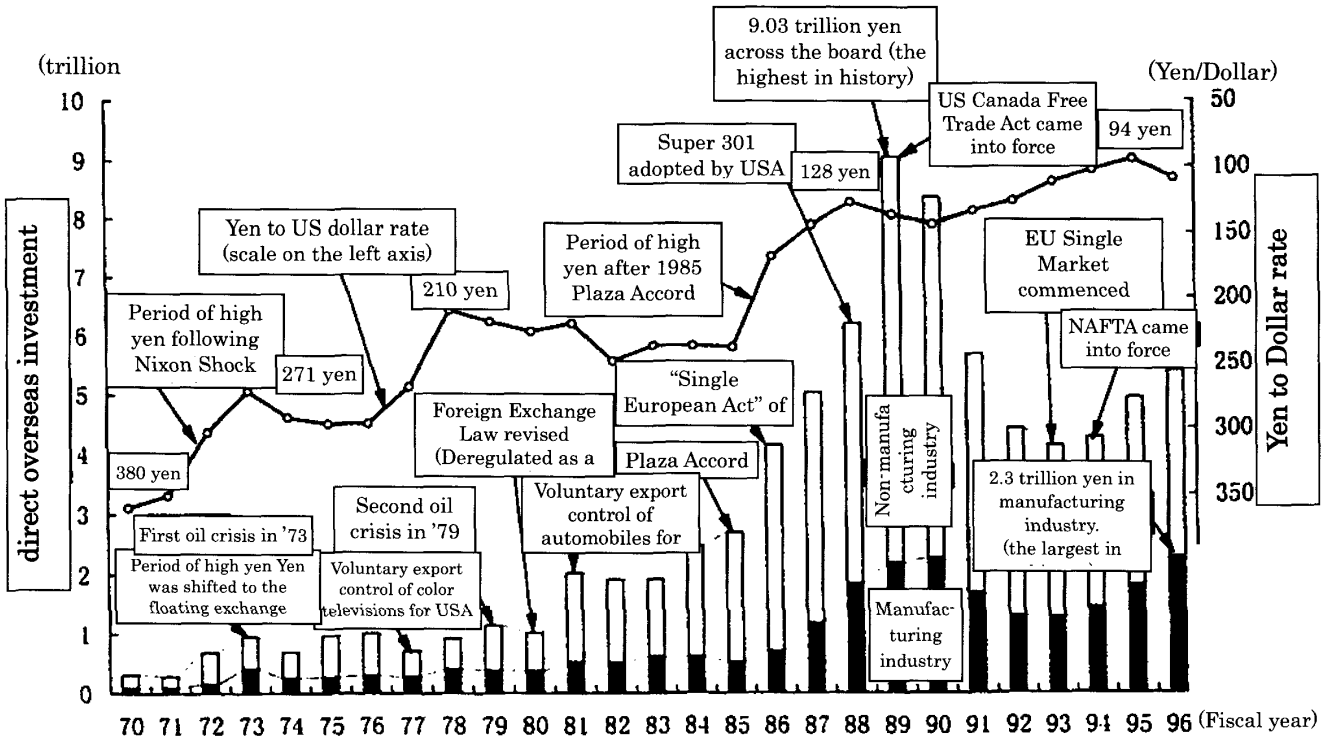



**Fig. 4** : Transition of yen/dollar exchange rates

It is notable as mentioned above that the focus has been switched from the trade negotiation by individual product to all-embracing intergovernmental negotiations since the latter half of the 1980s

## 2. Leading indicators of the emergence of friction between the two countries (empirical rule)

According to "Political Economic Science of the Japan-US Trade Frictions" by Hirotomo Ishikawa, the following empirical rule was found from experience:

### 1) Trade surplus with the U.S. over 20%

Friction may be expected when trade surplus with U.S. exceeds 20% of the total amount of export to the U.S.

20.2% in 1971 → Steel price trigger

22.7% in 1977 → Color television dispute

20.8% in 1981 → Voluntary control of car exports

| Description | Time concluded | Specific results | | |
|---|---|---|---|---|
| Japan-U.S. Textile Agreement | Oct. 1974 | Exported from Japan to U.S.<br>Amount<br>Volume | <1973><br>¥127.699 billion<br>81,132 tons | <1991><br>→ ¥98.951 billion<br>→ 40,374 tons |
| Japan-US Arrangement on NTT's procurement of material | Jan. 1981 | Purchased amount of foreign goods | <1980><br>$ 17 million | <1993><br>$ 1.09 billion |
| Japan-US steel arrangement | May 1985 (retroactively applied to Oct. 1984) | To U.S.A.<br>Exported amount<br>Exported volume | <1983><br>$ 2.49 billion<br>460,000 tons | <1993><br>→ $ 1.92 billion<br>→ 182,000 tons |
| Japan-US semiconductor arrangement | Sep. 1986 | Foreign S/C maker's share<br>Foreign S/C makers' sales in Japan<br>No. of Design-in cases (Index) | <3rd QTR 1991><br>F1 14.3%<br>F2 16.2%<br><1986><br>ca. $ 900million<br>100 | <1st QTR 1994><br>→ 20.7%<br>→ 22.0%<br><1993><br>→ ca.4.1billion<br>→ 670 |
| Tobacco products agreement | Oct. 1986 | Imported U.S cigarettes (amount) | <1986><br>$ 421 million | <1993><br>→ $ 1.811 billion |
| Japan-USmachine toolarrangement | Jan. 1987 | To U.S.A<br>Exported amount<br>Market share of Japanese products | <1986><br>$ 1.18 billion<br>27.6% | <1993><br>→ $ 1.01 billion<br>23.2% |
| Supercomputer installat ionprocedure | Aug. 1987 (Rev.May 1990) | Procurement of foreign made super computer (after 1990 rev.) | <1992><br>0/3 cases | <1993><br>6/15 cases<br><As of Aug. 1994><br>→ 3/7 cases |
| Japan-US Beef and Orange agreement | Jul. 1998 | Imported amount<br>American beef<br>American orange Juice | <1986><br>$ 637 million<br>$ 9 million | <1993><br>→ $ 1.375 billion<br>→ $ 20 million |
| Procurement of computer productsand services | Jan. 1992 | Ratio of foreign products in the government procurement of computers | <FY1991><br>8.8% | <FY1992><br>→ 18.9% |
| Japan-USProvision of paper products | April 1992 | Foreign goods import | <1992><br>10.45 M tons | <1993><br>→ 10.86 M tons |

(Source) MITI

**Table 7 :** Key agreements between Japan and the U.S.A. and specific results

## 2) or when Market share in the U.S. exceeds 10%

January 1980

Japanese cars gained 22% market share in the U.S. → Japan-U.S. automobile war 1976

The market share of Japanese color televisions reached 30.1% (from 15.7% in 1974)

## 3) or the growth of exports to the U.S. is 10% or more

Year on year growth of 10% or more. Rapid growth of export is dangerous.

### 4) or when U.S. jobless rate goes over 7%

1974-75 : 5.6% → 8.5% (Steel and color televisions)
1979-80 : 5.8% → 7.1% (Automobiles)

### 5) or when U.S. business results are poor

1977 : Bethlehem Steel deteriorated in business → Voluntary control of steel exports Zenith had to resort to mass discharge of workers → OMA was concluded on color TVs 1980-81 Chrysler faced clutches of bankruptcy

Ford and GM recorded loss of income → Japan-U.S. trade friction on automobiles

## 3. Remedy

Trade frictions which occurred in the past between the U.S. and Japan were resolved in the following ways :

The above examples can be broken down into patterns as follows:

### 1) Voluntary export control

This is the most popular way of settling trade frictions over major products as experienced so far.

This process has been adopted for → number of products including textiles, steel, color televisions, and machine tools. Many Japanese corporations contrived to shift their production base to the disputing country so as to mitigate frictions. In the disputing countries, there were few industries having successfully strengthened or revived after having settled the trade friction. The U.S. industry has withdrawn from the production of color televisions in view of the lack of justifiable advantage in terms of profit.

American steel-makers have never regained the vigorous position of the past. The automobile industry is one of the few successful examples where the three major U.S. automakers have revived during the period of voluntary export control implemented by Japanese car manufacturers in the 1980s, having developed strategic collaboration between Japanese corporations and actively studied the Japanese way of business management and production systems. Whether industries idle or commit themselves to restructuring during the controlled period may depend on such

elements as the industry's nature, strategy, and self-reliant efforts.

### 2) On-site production in the United States

As described in the section of voluntary export control, Japanese manufacturers actively went out to establish their production bases in the United States. It also reflected the emerging influence of the constant appreciation of the Yen against the U.S. dollars along with import control measures implemented to protect the U.S. industries. The increase of overseas or on-site production was also → part of the strategy practiced as → part of the business globalization measures since the later part of the '80s.

### 3) Segregation of markets

The segregation of markets implemented by Japanese and American manufactures was typically observed in the case of semiconductors, where they segregated the market in accordance with respective advantageous positions to build up the complementary relationship. This move has also proved useful in avoiding frictions.

### 4) Production shift to developing countries

Another measure taken to avoid the trade imbalance between Japan and the U.S.A. and Europe was to move production bases to Southeast Asia and China and to indirectly export Japanese goods from such bases rather than exporting directly from Japan.

### 5) Opening up domestic markets

It has also become popular to reduce trade imbalances with major trading partners by increasing imports from them after removing → number of different restrictions and improving unpopular business practices since the inception of the Japan-U.S. Impediments Initiative.

### 6) Mutual reliance through the globalization of businesses

The mutually reliant relationship began to be established among businesses of the world through the complex network of territorial and corporate collaboration. Take an example of the manufacturing industry that pursues the possibility of outsourcing by locating → series of functions

ranging from R&D to procurement, manufacture, sales, distribution, service and to financing in the respective optimum sites of the world. Multilateral rather than bilateral issues increased as → result of accelerating globalization after the 1985 Plaza Accord.

## 4. Significance of WTO

As described above, the critical issue of the world economy during the period from the latter half of the 1980s was the trade imbalance. Attention began to focus on the existence of structural elements such as productivity, export competitiveness, consumption and investment as the background of the prevailing situation. Such was the time when the Japan-U.S. Impediment Initiative took place. In the meantime, the Uruguay Round commenced under GATT in 1986 to cope with the increasing international trade that could not be effectively dealt with by the existing GATT rule such as the concerns about the emerging move of protectionism and the issue of service trade. As → result, → number of disciplinary stipulations have been established to suppress trade control activities by member countries including the clarification of the operation of the anti-dumping agreement, the subsidy and compensation duty agreement, or the restriction of ambiguous actions such as voluntary export control. In addition, → number of agreements have been formulated in agriculture, service, investment (trade related investment provision), and intellectual property, to take the first step toward the formulation of new rules.

It finally resulted in the establishment of the Word Trade Organization (WTO) in 1995. WTO, as compared to GATT, has such characteristics as:

(1) Comprehensive international trade rules have been established to cover not only the trading of goods but also services and intellectual properties;
(2) The "rule of the law" in the area of trade has been reinforced by the procedural improvement of the settlement of disputes by speeding up and formularizing related processes; and
(3) The same international trade rules shall be applied, as → rule, to advanced countries and developing countries alike after a certain provisional period and with the exception of some special provisions.

In the 1990s, the world economy was going through transformation more drastically and rapidly than ever in the tidal wave of the economic globalization brought about by worldwide corporate activities and the dramatic advancement of information technology. The development of globalization is causing new tasks that all the countries need to solve from an international standpoint. It is increasing in the importance of establishing international rules that can effectively cope with the

diversified forms of economic transactions and avoid risks that are definitely increasing with the enhancement of globalization.

The role of the WTO is to achieve the intended task of international agreements by liberalizing trade and investment, improving the related rules, and facilitating the execution of multilateral trade agreements.

At the same time, the WTO as the core institution of the world trading system, in reality and in name, will further increase its significance as a place for dealing with a wide range of trade issues and for settling disputes through the expansion of the scope of each agreement and the improvement of the organization.

### 5. Accession of China

With respect to the influence of the accession of China to the WTO, while it is accepted as the expansion of business opportunities by most foreign-affiliated firms, it is also anticipated to cause a significant transformation of the economic environment such as intensified competition and the necessity of industrial structural adjustment. The pressure of the structural adjustment of industry within China may increase in the short term, however, the competitiveness of Chinese industry will be reinforced bringing about the growth of the Chinese economy through structural adjustment in the long run.

If China carries out the necessary system reform in accordance with the details of the agreement reached through multilateral and bilateral WTO negotiations, direct investments from Japan and other foreign countries to China are bound to increase accelerating the advancement of the system of division of labor in East Asia and greatly contributing to the prosperity and economic development of East Asia as a whole.

## Ⅲ. Conclusion : Implication from Japanese Experiences

### 1. Generating pattern of trade friction by industry

#### 1) Frictions start with cost-oriented/labor-intensive products

The first stage of trade friction with trading countries develops when the widening gap of trade imbalance between two countries reaches a level which puts pressure on the enterprises of the other country in the trading of labor-intensive products that focuses on cost competitiveness such as textiles, steel, and electrical appliances.

### 2) Spreads to high-tech/defense-related areas

The subjects of friction will then gradually spreads to more significant technology based products such as high-tech products or defense-related products, and software and services that involve intellectual property rights.

### 3) Finally the scope shifts from individual products to comprehensive arrangement of structure

Once the settlement of friction issues related to high-tech products is reached, then it will extend to a wider and more comprehensive range. It is anticipated, however, that the range of possible negotiation through WTO will eventually increase in this area.

## 2. Explosive export drive or export by neglecting rules will invite trade friction

First of all, the explosive increase of exports to a country will provoke the enterprises of the trading partner to intensify trade friction. A country highly dependent on exports, whose economy is in a high growth period, is prone to cause trade friction through an export drive.

Secondly, exports without substantial cost reduction, without thinking of profit, or low price export is not permissible as it ignores the rules of free competition.

Thirdly, a business practice exclusively devoted to export over and above the tolerable capacity of the other country for import, will jeopardize the operation of the domestic industry and upset its employment situation. It will be necessary, therefore, to take necessary precautionary measures in steps such as procuring materials or starting on-site production in the consuming country to increase employment of local population so as to take responsibility as an equitable business enterprise. Suffice to say, the enterprise will have to abide by the rules of the country and try to contribute to the society as a corporate citizen.

## 3. Possibility that China will be required to make multinational adjustment in a shorter period in comparison with Japan

In the case of Japan, adjustments were made step by step in accordance with its own development and with the growing industrial competitiveness over a long time. Frictions occurred but we could settle them as they occur. On the contrary, it may be possible for China to encounter such frictions in a more compressed form within a shorter period.

In the case of Japan, frictions were largely limited to those between the U.S.A. as well as

Europe. Now that the world trade structure is involved in a much more complex way, China may have to risk concurrent and multidirectional frictions with the U.S.A., Europe, Asia, Japan and other countries. Trade frictions may occur concurrently in the labor-intensive sector and high-tech sector as there are territorial differences of industrial development within China. The target of friction may be generated in parallel unlike for Japan where friction occurred in steps initially from the labor-intensive industry, then heavy chemical industry, machine industry and finally in the high-tech industry.

## 4. Segregation of markets and mutual reliance through Core Competence

A country's industry must develop to higher levels in proportion to the technological advancement and income growth. In line with such advancement, industries and products in which the country is internationally competitive may change from one another. Products in which the country is no longer competitive may be transferred to another country so that it can concentrate in more value-added products or sectors. It is, therefore, an important preposition to share the respective market segments each of which has core competence in the global market. Market segregation should also go through constant changes depending on the industrial structure and the respective competitive edges.

At the same time, one may find an approach to minimizing frictional relationships with partners in the construction of mutually reliant relationships with other countries and industrial sectors and in the reinforcement of strategic collaboration among industries.

To this end, China is required to improve legal and taxation systems which make a good basis for inviting aggressive foreign investment.

## 5. Respect for intellectual property rights

As in the case of hardware, software will increase in its importance as business components. The significance of intellectual rights will increase in proportion and must be highly estimated. Rampant counterfeit and pirate editions in the domestic and export markets will jeopardize the trustworthiness and reliability of the country toward its trade partners.

China's accession to the WTO has a great significance to the world as a whole and in consideration of its relationship to the neighboring countries of Asia. We all hope that China will make a substantial contribution to the development of world trade and of Asia as a potent member of WTO.

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