

Speaking of Japan

ISSN 0000-0000
441.2(103)
+ 441.2(326)
+ 382

September 1982
Volume 3 Number 21

The Responsibilities of Success Japan's Role in the World	Sayidiman Suryohadiprojo	1
Free Trade, Fair Trade Prosperity and Economic Freedom	Richard W. Wilcke	8
Three on a Match Japan-E.C. Trade and the U.S.	Leslie Fielding	16
The Changing Military Balance Building up Japan's Capabilities	Charles L. Donnelly, Jr.	23
Sailing to a Brighter Future The Coming of the Pacific Age	Zenko Suzuki	27

Speakers' Bureau
KEIZAI KOHO CENTER
Japan Institute for Social and Economic Affairs

Three on a Match

Japan-E.C. Trade and the U.S.

Leslie Fielding

*Director-General for External Relations
of the Commission of the European Communities*

Delivered to the American Chamber of Commerce in Japan, Tokyo, April 20, 1982.

THE relations between the European Community and Japan, and the triangular relationship of both of them with the U.S., are highly complex. In the economic sphere alone, they embrace not only visible trade, but also financial services and capital movements, cross-investment, industrial and technological tie-ups, a mutual interest in commercially related research and development, and so forth. In addition, there are the political and strategic interests shared in varying degree between the three partners in a shifting and unstable international environment.

Today I want to concentrate on visible trade because this is an aspect of EC-Japan relations which hits the headlines, and which ties in quite closely with your own preoccupations in Japan. Unhappily, it also carries the risk, if it is mishandled, of causing a major international upset. I do not intend to discuss trade in its sectoral, micro-economic details—you know them better than I do; they are your daily bread and butter. Instead, I shall go for the overall picture, by following a more macro-economic approach.

Let me quote at the outset the words of a 17th century English metaphysical poet. His name was John Donne. He wrote: "No man is an Island, entire of itself; everyman is a piece of the Continent, a part of the Main. Any man's death diminishes me, because I am involved in Mankind; and therefore never send to know for whom the bell tolls: it tolls for thee."

These words are curiously apt to the U.S./EC/Japan interrelationship today. The three of us together account for over half the annual gross product of the free world. We conduct 56 percent of free-world trade. Bilateral trade between the three of us is substantial: last year US\$27 billion worth of goods went between the EC and Japan: US\$64 billion between Japan and the U.S.; and US\$95 billion between the U.S. and the Community. A growing proportion of Japan's exports go to the Community (12 percent plus) and to the U.S. (25 percent and more).

Figures like these illustrate clearly why Europe, the U.S. and Japan are the three major pillars of the free world trading system, buttresses of the GATT and dominant partners in the OECD. If trade relations between America and Japan deteriorated seriously, we would feel the shock in Europe and the international system would shudder. If Europe and Japan were to quarrel, it would have the same effect. When Japan's huge trade surplus with the U.S. provokes legislators to table "reciprocity" bills in the U.S. Congress, this brings one degree closer the prospect of restrictive moves in Europe, whose deficit with Japan is of comparable magnitude. Protectionist forces on both sides of the Atlantic tend to feed upon each other—and incidentally in the process render trans-Atlantic trade relations more difficult. In international trade, as John Donne said, no man is an island. We live in an interdependent world.

Which brings me to the Community and Japan.

Vice President Haferkamp of the EC Commission in Brussels put it this way recently to some senior visiting Japanese politicians.

"The regrettable fact is that the EC now has trade problems with Japan of sufficient seriousness to compromise the overall economic and perhaps political relationship between us. If we cannot solve our trade problems, or at any rate render them less acute, then our efforts to restore prosperity and growth to our domestic economies, and to the free world as a whole, will be substantially set back. More than this, the tensions now prevailing in relations with Japan, not only in Europe, but also in the U.S., risk precipitating the end of the free-world trading system as we have known it in the post-war years."

There is in fact now a historically well-established structural trade imbalance between Japan and the Community which gave Europe a trade deficit with Japan of US\$12.2 billion in 1980, and higher still in 1981. Around 80 percent of our exports to Japan are manufactured products. Last year, in real terms, such exports to Japan actually declined. We in

Europe continue, moreover, to be haunted by the prospect of a renewed Japanese export drive to the Community later this year, fueled by as yet sluggish Japanese domestic demand and by the current absurdly low international parity of the yen.

There are three things to remember about all this: the historical background, the wider context, and the current domestic economic situation in Europe.

"...the pressures within the Community are now considerable for a change in the system, notably in regard to Japan."

First, the historical background as far as Europe and Japan are concerned.

This structural imbalance did not emerge yesterday from nowhere and will not disappear into a black hole tomorrow. In 1963, the ten present members of the European Community had a trivial US\$8 million deficit with Japan, and an export/import coverage ratio with Japan of over 98 percent. This ratio fell steadily, to 72 percent in 1970, to 44 percent in 1975 and to 34 percent in 1980. Europe's trade deficit rocketed from US\$8 million in 1963 to US\$500 million in 1970, to US\$3.4 billion in 1975, to over US\$12 billion in 1980. Japan's exports to Europe rose from US\$0.5 billion in 1963 to US\$18.5 billion in 1980. The imbalance has continued to increase and the Community's cover ratio has continued to fall in 1981.

Second, in the wider context, Europe's experience is not unique. It is not due to a strange entrepreneurial decline, or some mysterious collapse of moral fibre peculiar to the EC. Our experience has been shared by most of Japan's trading partners, other than those which supply her almost exclusively with energy and raw materials.

The U.S. deficit has grown in a fashion comparable to our own, although admittedly on double the two-

way volume of trade which we enjoy with Japan. Sometimes Europe, sometimes the U.S., has had the higher nominal bilateral deficit with Japan.

The newly industrialised countries (NICs) of Asia have found it as difficult to conduct balanced two-way trade with Japan as the rest of us, to the point that Taiwan now seems to have thrown in the sponge by resorting to comprehensive import restrictions against Japan.

Taking all developing countries together in 1980, the Community imported four times as much from them as Japan did (US\$69 billion against US\$16 billion). Broken down by category, we gave a market to the less developed countries three times as large for raw materials and food, but six times as large for manufactured products.

The wider trade picture therefore looks to me like this. Japan has exported manufactured goods to the EC, the U.S. and elsewhere on a large and growing scale for the past 15 years. But Japan's imports of manufactured products from all its partners have, by contrast, remained relatively low. This applies to the EC, the U.S., the NICs and the Third World as a whole. Among the OECD countries, only one country imports less manufactured goods per capita than does Japan. The absolute value of Japan's manufactured imports is the same as that of a small advanced country like Switzerland. In 1960, Japanese imports of manufactures were worth 2.4 percent of GNP. In 1980, despite a phenomenal expansion of world trade as the result of successive GATT negotiations, this figure was approximately the same. Over the same period, the EC and the U.S. had doubled this percentage. Thus, the significantly increased penetration of the U.S. and EC markets that accompanied the liberalization of trade as a result of the Dillon, Kennedy and Nixon Rounds of GATT negotiations has not so far been emulated by Japan on a comparable scale. You and we opened our markets, to a degree which Japan has yet to do.

Third, the domestic economic background in the Community. Unemployment has now reached the 11 million mark. Economic growth in the Community was negative last year and is not likely to be much more than 1 percent in 1982. The Community was last year, and is likely to remain this year, substantially in the red, both as to its current account, and as to the visible trade balance with the rest of the world. In many critical sectors of our industry extensive restructuring is required, and is in fact now beginning to take place. But this process is to some degree vulnerable to adverse international economic developments.

Against this background, the pressures within the Community are now considerable for a change in the system, notably in regard to Japan. In a multilateral world, bilateral ups and downs are only to be expected. Swings and roundabouts are inevitably the order of the day. It would be wrong to expect to balance our books neatly with all our partners. But the free trade system can only survive if there is a substantial exchange of goods between the world's major trading partners.

In fact, the conviction within the European Community is growing that Japan, with its relatively prosperous economy and its domestic market of 120 million consumers, makes an inadequate contribution, in terms of imports from other developed and developing countries, to the expansion of world trade. More than this, Japan is perceived as requiring her partners to shoulder a heavier share of the burden of sustaining the international trading system than Japan herself is ready to assume. The impression even exists in some quarters in Europe that Japan still prefers to try to "wait it out"—to take only the minimum absolutely necessary remedial action, at the last moment, to avoid a major showdown. However that may be, much more widespread is an EC perception that Japan is not yet sufficiently international in its approach to world economic problems.

But this does not mean that the authorities in this country are dragging their feet. We Europeans are grateful for the efforts which the government has so far made, particularly in the nontariff area, to bring Japanese practice more into line with generally accepted international practice. The recently decided accelerated MTN tariff cuts, while of only negligible trade impact for us, were at least a symbol of a new and welcome political approach. The EC would like to encourage the Japanese authorities to continue in the same direction. It is surely undesirable that "trade frictions" should constantly dominate the headlines and that our economic relations generally should be in such a continually uncertain and troubled state. I welcome, therefore, the willingness of the Cabinet and of the LDP leadership to take the trade problems of the EC and the U.S. as seriously as they deserve. In this respect, there has been a qualitative change for the better. I hope that not only industrial and business circles, but also the ranks of the bureaucracy, will now follow the new political lead.

"...the conviction within the European Community is growing that Japan...makes an inadequate contribution...to the expansion of world trade."

This said, while Japan has taken steps in the right direction, there is still a very long way to go. What is required is to create the social, economic and commercial conditions in Japan which will enable the cause as well as the symptoms of the current trade problem to be dealt with. Only this will offer a real prospect of a more balanced Japanese trade relationship with the Community and the U.S. Meanwhile, an undeniable gap remains between what it has been possible for the Japanese government to do up to now, and the expectations of the European

Community for an early and substantial improvement in European exports to Japan.

It is not for the Community—or for the U.S., for that matter—to seek to dictate to a friendly and sovereign partner precisely what the latter should or should not do. My Japanese interlocutors frequently invite me to state what Europe's specific requirements are. Japanese attention to detail is, of course, well known. And no doubt both we and you have induced them, through our repeated nitty-gritty complaints, to think in terms of sectors, barriers and the micro-economic dimension.

“The impression even exists in some quarters in Europe that Japan still prefers to...take only the minimum...remedial action.”

But it is today unfortunately no longer a solution for the EC side to continue conscientiously to draw up long lists of requests, and for Japanese officials, as in the past, to go through them laboriously point by point, indicating those few items on which some progress can be achieved and explaining why no progress will be possible on the many remaining items.

Rather, as we see it, it is for the Japanese government itself to demonstrate, in a manner to be autonomously determined, that Japan intends to reciprocate to the Community the trading opportunities which the Community has already given to Japan, and which, as the trade figures indicate, Japan has already substantially exploited. We are not utopian innocents or idle dreamers. We neither expect nor desire revolutionary action instantly to change the whole economic and social structure of Japan. Although it would relieve us, we do not insist on a quantum leap forward by Japan. But we do want an evolutionary approach, with speedy and worthwhile initial results and a clear political commitment to substantive change in the longer term.

Those of us fortunate enough to live here are well placed to appreciate the historical and cultural background of modern Japan, as well as the many admirable, even enviable, features of Japanese life and work. Myself a diplomat and professional observer of mankind for more than a quarter century, and also a friend of Japan, I like to think that I do understand some of the domestic political constraints in Japan. Like Germany and Italy, she is heavily dependent on costly imported energy. Japan is distant from most other developed countries. The Japanese people have remained more homogeneous than most others and it is less than 130 years ago that the period of national seclusion which lasted for over two centuries came to an end. We should not expect that Japan will become more internationally integrated overnight. As I frequently explain to my authorities, there are reasons why things are as they are.

But what is sauce for the goose is naturally also sauce for the gander. *Mutatis mutandis*, we in Europe labor under historical constraints and social and economic difficulties. We have our own farmers, workers, business people, our own unemployed masses, our own electorates to consider. We too need to be understood. The economic pressures on us, and on the international trade system, are great. Governments in Europe can and do fall on issues such as these.

The question therefore is, can the growing trade gap between the EC and Japan be first arrested, and then narrowed? If so, in what manner, and above all, how soon? If not, what policy, how best to manage our mutual relationship in the present difficult circumstances?

The following is what I myself would like to see:

(a) The further opening up of the Japanese market. I would welcome a significant increase in the level of Japan's imports of manufactured and processed goods (currently just under 22 percent of total imports), so that this level more closely approaches that

prevailing in our own economy (44 percent). The questions here are: Can the Japanese government take positive action to achieve this objective—for example, by setting 30 percent as its immediate aim, as the Federal German Minister of Economics, Count Otto von Lambsdorff, suggested in Tokyo two weeks ago? Can the authorities give systematic guidance to the manufacturing industry, public corporations, business associations and so forth, to this effect? Will it be possible for the Japanese government to adopt early and extensive further trade measures, whether as regards tariffs, non-tariff barriers, or other economic and commercial impediments to a more balanced external trade relationship? The social and economic structure in Japan tends to be import-impervious and marked by a “self-sufficiency syndrome”. Can this be progressively modified so as to achieve greater integration and division of labor between this country and her GATT and OECD partners?

(b) Japanese export restraint. Export-led growth by Japan is bound to arouse external resentment at a time when her partners are in economic recession and are in the process of restructuring their industries. For the past two calendar years—at the height of an international recession greater than any the world has known since the Second World War—nearly three-quarters of Japan’s relatively high economic growth has been export-induced. I admit that, as far as the EC is concerned, over the past 12 months Japanese exporters to Europe have on the whole been prudent in sectors of particular sensitivity for us, and I appreciate this. But we need to know—as the U.S. needs to know—whether we can expect continued and effective moderation of Japanese exports to the Community as a whole in certain key sectors, this year and next.

(c) Financial and monetary matters and investment. I will not go into this now, as I want to concentrate on trade. But the trade implications are clear. Can Japan not only reciprocate the financial access

already granted to her in Europe, but also compensate to some degree for her enormous visible trade surplus, by permitting greater European participation in the Japanese capital market and improved access to Japan for our highly competitive financial services? The free trade system cannot work effectively if exchange rates fluctuate wildly. What can the authorities in Japan do, beyond pointing to high U.S. interest rates as the sole source of all evil, to encourage a more realistic exchange rate for the yen? There is also the important related question of investment. Can a climate for foreign investment be created in Japan comparable to that in America and Europe? Will Japan itself make more value-adding, technologically innovative, manufacturing investment of the right kind in the right places in the EC?

“I am confident that Japan is ready to exert her economic strength in the form of more positive international leadership.”

(d) A broader economic relationship. Mr. Edward Heath, the former British Prime Minister, appealed in Tokyo this month for the relationship between Europe and Japan to be broadened beyond the issues of bilateral trade. Among the areas he pointed out were monetary cooperation, energy, technology and investment. The Community has in fact made a start in this direction and a clearer Japanese response is now looked for. Can industrial cooperation be developed? Also cooperation in the field of North/South relations and aid to development, and in regard to long-term, government-sponsored scientific research and development? The agreement of principle reached between M. Jean-Pierre Chevenement, the French Minister for Research and Technology, and his Japanese counterparts last week illustrates the way forward.



LESLIE FIELDING

Born in London, England in 1932. After being educated at Cambridge University and the School of Oriental and African Studies in the University of London, Mr. Fielding entered the diplomatic service in 1956. He served in Tehran and in Singapore before becoming chargé d'affaires in Phnom Penh in 1964. Mr. Fielding then served in Paris from 1967 to 1970. His last assignment was in the Foreign and Commonwealth Office as counsellor and deputy head of the Planning Staff. Mr. Fielding joined the Commission of the European Community in 1973 and, until 1977, was responsible for EC external relations. From 1977 to 1978, he was a visiting fellow at St. Anthony's College, Oxford. Mr. Fielding became head of the Delegation of the Commission of the European Communities in Tokyo in 1978. In August 1982, he was appointed director-general for external relations of the EC.

(e) Japanese leadership. The president of the French Republic, at his press conference last Friday, suggested that Japan should be prepared to make some sacrifices, so as to assume a share of international responsibilities more commensurate with this country's economic might. The U.S. view has also been that the time has come for Japan to assume more fully than hitherto the responsibilities of a world leader. U.S. negotiators have pointed out in recent months that Japan is, economically speaking, no longer an adolescent. It has caught up with, and in some respects surpassed, its Western partners. A former U.S. Secretary of Commerce, Peter Peterson, said in Tokyo last month that "Japan now has the power, and thus the inescapable duty, to help shape and execute tomorrow's agenda for the world economy." Happily, government statements in Japan have echoed this sentiment. At the Western Economic Summit at Versailles this June, and in the years to come, both Europe and America are therefore counting on the imagination and statesmanship that Japan will show.

(f) Warmer hearts and cooler heads. These days, Japan suffers from a "bad press" in Europe and America, and this is regrettable. Emotional thinking is sometimes too much in evidence. Unfortunately, however, Japan too is not immune. There is emotion of the wrong kind in some of the fringe reactions in this country to external trade frictions. Foreigners are not being unfriendly, nor are they seeking to make Japan a scapegoat, when they ask for assistance and redress. Everybody welcomes the fact that Japan is a democratic, stable and prosperous member of the Western comity of nations. No one belittles the efficiency of the more dynamic sections of the Japanese economy, sections which offer international consumers a reliable and innovative product, and help to advance the frontiers of applied technology to the ultimate benefit of all mankind. Japan is not a culprit in these respects. But problems are problems and facts are facts and they have to be

squarely faced between friends and partners. The statistics show that the Europeans in practice hold open their markets more widely to all comers than do the Japanese. Europe devotes more of its GNP than Japan to defence and to overseas aid. Beneficial European industrial investment is largely kept at home. Europe, more than Japan, is bearing the cost of international economic adjustment in terms of dangerously high unemployment. The shoe is on the other foot—or perhaps I should say the scapegoat is on the European side of the fence.

Meanwhile, we in Europe and America need to match our responses to what is done in Japan. A defensive or defeatist approach will not do. Protectionism must be kept in check. It does not solve the problem; it destroys the welfare it is supposed to safeguard; it enfeebles the very international system that is the only alternative to economic nationalism and to the negative consequences of possible trade war.

This applies as much to the U.S. as to the EC. With your automobile limitation agreement, for example, you are no holier than we. Much more important, the reciprocity legislation favored in some quarters in the U.S. Congress is, like all two-edged swords, a dangerous weapon. It can cut down agreed international rules and bleed the GATT to death. Reciprocity in a narrow, bilateral or sectoral sense, as former Trade Representative Bob Strauss was arguing here a week or two back, has no place in any enlightened trade policy. Only reciprocity in its broadest sense—i.e., equality of competitive opportunities across the board between Japan, the EC and the U.S.—is consistent with a liberal trade policy. I am glad that government officials in Washington also hold firmly to this view.

This leads to an important policy decision recently taken in Brussels, one which carries implications for the U.S. The European Community has discussed trade issues with Japan patiently and persistently in Tokyo and Brussels for at least ten years, and with mounting anxiety and discomfort for the past five.

In cooperation with Japan, we will continue this dialogue, patiently and persistently, in the future. But insofar as the EC/Japan trade gap has continued to widen, and the low percentage of manufactures in Japan's imports has remained unchanged, we have so far obtained no satisfactory result. We have therefore opted to have recourse to Article XXIII of the GATT. This Article provides for consultations, initially on a bilateral basis, but, failing a settlement, in a multilateral panel and ultimately, should this be necessary, before all the GATT contracting parties, where it can be shown that benefits which ought to have accrued to one contracting party have been nullified or impaired by another contracting party—in this case Japan.

To quote the text of the EC's written representations in Geneva of April 7, we are indeed now of the view that "the benefits of successive GATT negotiations with Japan have not been realised, owing to a series of factors particular to the Japanese economy which have discouraged imports of products other than raw materials. As a result of this situation, combined with the pattern of growth of Japanese exports to the European Community, the GATT objective of 'reciprocal and mutually advantageous arrangements' has not been adequately achieved between the European Community and Japan."

To spell this out further, the EC view is simply this. Japan is now the most powerful single industrialised country after the U.S., accounting for 10 percent of world GNP. A greater effort is consequently required from Japan in the 1980s than was expected in the 1960s to sustain two-way trade and to move away progressively from the autarkic and self-sufficient economic structure that has characterised the post-war years in this country. The expectations that Japan's partners place upon her in this respect are going to continue to grow as long as the global system holds together and Japan's place in that system remains as important as it now is. It will be increasingly a source of international strain for Japan

to remain an importer chiefly of raw materials, energy resources and certain foodstuffs, self-sufficient in most other respects, yet an exporter of finished goods to her GATT partners along a broad, largely unimpeded one-way street. Sooner rather than later, there has to be more give and take. There has to be what GATT calls "mutually advantageous arrangements."

To conclude, I return to the metaphysical poets and John Donne's view that no man—or for that matter no nation—is an island. Japan and the Community, and Japan and the U.S., cannot choose the path of trade isolation. We have each been there before—in the 1930s—and paid a bitter price for it. Those were the days, remember, of "Buddy, can you spare a dime?" The only acceptable way forward today is multilateral, cooperative and imaginative. We need cooler heads—and, insofar as these can exist in international affairs and matters of state, warmer hearts—in Japan, in the States and in Europe.

I believe that the Japanese leadership has already taken this view for sometime. I am confident that Japan is ready to exert her economic strength in the form of more positive international leadership.

This being so, our mutual problems—which are not shadows but are real—become problems not only of substance, but also of timing. The question is no longer if, or how, Japan can respond to the challenge; it is when? Unfortunately, time is a commodity in short supply. By 1990, other things being equal and barring accidents, a fairer balance will certainly have been struck, a greater degree of interdependence achieved, in the Japan/EC/U.S. trade triangle. But can we get from 1982 to 1990 without an accident?

I think, myself, that the situation is still in hand. If there were such an accident, Japan would not be the only victim. We would all lose something. As John Donne wrote, if the bell tolls, it will toll also for you and for me. □

(This speech was originally titled "The European Community's Trade Relations with Japan—and their Implications for the U.S.")