

Japan's Trade Frictions: Realities or Misconceptions?

Ali M. El-Agraa
University of Leeds
Leeds, England

As an economist who has devoted a large part of his academic career to date to the problems of West European integration, I have inevitably taken great interest in Japan's relations with the European Community (EC) and the European Free Trade Association (EFTA). I am presently in the process of writing a book on the economies of the Arab League, and Japan's trade relations with the Middle East have attracted my attention. Since my arrival in Japan in August (1984), I have hardly been able to escape the overwhelming publicity given to Japan's trade relations-cum-frictions with the USA. All these considerations have inspired me to undertake research into the global aspects of Japan's trade relations, hence this paper is in the nature of a pilot project: it is intended to suggest directions in which my trends of thought have been drifting. It is therefore a very tentative article which hopes to suggest vital areas for immediate research.

I. The Japanese Economy

(a) The nature of Japan's trade frictions with the EC and USA is rather complicated since there is not a single or simple way of explaining it. At least three "scenarios" can be entertained. However, a meaningful discussion of any of these cannot be contemplated without some understanding of the basic characteristics of the Japanese economy. It is therefore wise to commence this article with a brief review of the basic economic features of the Japanese economy.

Japan comes second in the league of national economies. In the 1960s,

its GNP was only 5% of that of the USA, but in 1982 it amounted to about 35%. Japan has a growth rate which, after the two oil crises, has continued to be higher than the average for the OECD. However, the real rate of growth of GNP was a modest 3% in 1982 and 3.2% in 1983, but it is expected to exceed 4% in 1984. The driving force for the economy seems to be mainly export-led growth rather than domestic demand; the latter is usually the case within the rest of the OECD. Japan's domestic demand actually fell in 1982 and 1983, but it is expected to rise to about 3.5% in 1984.

Japan has a very steady and healthy economy when compared with the rest of the OECD. It has a low rate of inflation of around 2% which has remained stable since 1981. Unemployment is also very low indeed since it has been about 2.5% of the labour force: during the late 1960s, such a low rate was equated with full employment, allowing for structural unemployment.

Japan has a very high savings rate as well as a high rate of investment. Fixed capital formation is presently about 17% of GNP and has been so for a long time. This has been attributed to a tax system which is predominantly direct and whose rate is lower than that in the EC and the USA. It has also been enhanced by the need to take out individual insurance for retirement. However, it has also been argued that there are some fundamental reasons for such a high savings rate which are a manifestation of Japanese society: the savings habit, or rather the mechanism that supports it (poor social security and housing due to a public emphasis on "productive" investment), results in high savings rates which finance further "productive" investment without improving social security or housing, making it necessary for people to save rather than spend their incomes. Freitas¹⁾ gives a good account of this:

Analysis of the need for savings for transactions and precautionary balances readily yields the conclusion that Japanese households require substantially higher savings balances to achieve equivalent patterns of consumption. In the case of transactions balances, the lack of synchronization of personal income and consumption over the life cycle has not been offset by as broad a set of institutional practices in Japan. For example, for many American workers it is no longer important to save for retirement years because of social security and private pension plans. In Japan, not only is social security smaller but private pension plans are still relatively

rare. In their place is a practice of paying a lump-sum retirement allowance. However, compulsory retirement is still commonly around the age of fifty-five, and with a remaining life expectancy of over twenty years the usual levels of retirement allowance . . . are grossly inadequate. There are two ways in which this problem is addressed: greater accumulation of savings during the years of working as a regular employee and a second career as a nonregular worker following retirement. Nonregular worker categories receive substantially lower salaries . . . and receive few or no fringe benefits, causing great reliance on the accumulation of savings . . . Some other spending needs in Japan that require greater savings balances are the costs of education . . . , housing . . . and even the cost of wedding . . .”

Although about 25% of the national budget for 1983 was financed by loans, and the national debt amounted to 40% of GNP, military expenditure is limited to a ceiling of 1% of GNP. This relatively low level of military expenditure is due to both historical and political reasons. Recently, however, there have been some indications to suggest that debate is imminent regarding the raising of this ceiling; a committee has recently been set up to look into it. All this is a reaction to US accusations that Japan is a “free-rider” in the area of defending its national boundaries.

Japan’s official development assistance presently stands at 0.29% of GNP. This compares with 0.53% for the EC, 0.21% for the USA and 0.39% for all developed and advanced nations.

Although about a dozen major companies with very international reputations have become the symbol of Japanese efficiency in trade and industry, they represent only the better known part of the country’s industrial organisation. There is a large number of small firms, which often act as sub-contractors to the major companies. These small businesses, which have a capital of less than 100 million yen (about £320,000) accounted for over 99% of all Japanese firms in 1981, and for two-thirds of their total sales; the total number of firms was 17 million.

The Japanese distribution system is vertically integrated. This is often reflected in the dependence of stockists on domestic producers. This applies particularly to certain sectors such as household electrical appliances and mass-market electrical goods, where over 60% of stockists depend on domestic

producers. The British Prime Minister asserted that the immensely complicated Japanese distribution system is deeply rooted in Japanese culture and in "buy Japanese" tendencies.

Japan has a banking system which is compartmentalised and is more subject to supervision by the monetary and fiscal authorities than its counterparts in the OECD.

Japan has developed a specific system of "standards" and "certification procedures" which has been labelled in the West as a "considerable obstacle for foreign exporters", hence the frequent accusation that Japan's market is relatively uneasy to penetrate by foreign firms. In short, the relative "unopenness" of the Japanese economy has been attributed to: the homogeneous structure of the Japanese domestic market, in which exclusive loyalties unite groups of banks, manufacturers, sub-contractors, distributors and traders in fierce inter-group competition against newcomers and outsiders; the apparent incapacity of the Japanese distribution system to handle foreign manufactures in large volumes; and the lack of interest of some foreign exporters in a market which has long been protected and is apparently unpromising, at a time when other markets have seemed easier and more lucrative.

(b) Given this bird's-eye view of the domestic economy, let us turn to a similar view of the country's external trade position. During the late 1960s and early 1970s, Japan had an overall surplus on the current account including invisibles. However, since 1973 the picture has changed drastically, arguably due mainly to the oil crises and changes in the cyclical trends in the state of the world economy, but the Japanese economy has shown a remarkable capacity to ride this storm. In short, in 1973, after a long period of surpluses, Japan had a deficit of US\$1.4 billion. This increased to US\$6.6 billion in 1974. From 1976 to 1978, Japan had surpluses which rose from US\$2.4 billion to US\$18.4 billion. There followed two years of deficits which came with the second oil crisis: US\$7.5 billion in 1979 and US\$10.9 billion in 1980. Since then, the tendency has been one of increasing surpluses: US\$8.6, US\$6.9 and over US\$21 billion in respectively 1981, 1982 and 1983. All this information is given in Table 1.

However, Japan's balance of transfers and services continues to show

heavy deficits, but it is improving in relative terms all the time. This information is provided in Table 2, both globally and with the EC and the USA. The recent improvement has been attributed to a rapid increase in the income received from Japanese investment abroad.

The inflow and outflow of long-term capital has been on the increase since the late 1970s. This could be attributed mainly to the "liberalisation measures" that were introduced in 1980 by the "foreign exchange law". Japan's capital outflow rose from US\$5 billion in 1972 to US\$27 billion in 1982. Over the same period, inflows of foreign capital rose from US\$0.5 billion to US\$12 billion. The capital outflows were accounted for mainly by purchases of foreign securities and offshore loans, while the bulk of foreign capital inflows stemmed from purchases of Japanese securities and bonds issued abroad by Japanese companies. As Table 2 indicates, the member countries of the

Table 1 Japan's Current Balance (Including Invisible Trade) 1965-82, In Billion US Dollars

Year	Exports	Imports	Current Balance
1965	8.425	8.169	0.283
1966	9.776	9.523	0.253
1967	10.442	11.663	-1.221
1968	12.972	12.987	-0.015
1969	15.990	15.024	0.996
1970	19.318	18.881	0.437
1971	24.121	19.797	4.324
1972	29.088	23.863	5.225
1973	37.017	38.389	-1.372
1974	55.426	61.982	-6.556
1975	55.729	57.842	-2.113
1976	67.321	64.894	2.427
1977	81.083	71.340	9.743
1978	98.353	79.923	18.430
1979	102.299	109.831	-7.532
1980	130.441	141.295	-10.854
1981	151.495	142.866	8.629
1982	138.403	131.516	6.887

Source: *International Financial Statistics*, 1983.

Table 2 Japan's Current Balance (Including Invisibles), 1976-82, Billion US\$

	European Community			USA			Rest of the World		
	T.B.	S./T.	C.B.	T.B.	S./T.	C.B.	T.B.	S./T.	C.B.
1976	3.9	-2.1	1.8	5.5	-2.1	3.4	9.9	-6.2	3.7
1977	4.7	-2.0	2.7	8.7	-1.9	6.8	17.3	-6.4	10.9
1978	5.5	-2.4	3.0	10.6	-1.9	8.7	24.6	-8.1	16.5
1979	4.8	-3.4	1.4	7.6	-2.8	4.9	1.8	-10.6	-8.8
1980	9.3	-4.3	5.0	9.8	-3.6	6.3	2.1	-12.9	-10.8
1981	10.8	-6.9	4.0	16.3	-2.4	13.9	20.0	-15.2	4.8
1982	9.9	-5.1	4.8	15.1	-0.8	14.3	18.1	-11.2	6.9

Note: T.B.=Trade Balance; S./T.=Services and Transfers; C.B.=Current Balance, and the European Community refers to the Nine for the period from 1976 to 1980, but to the EC of Ten thereafter.

Source: EC Delegation in Tokyo and *The Balance of Payments Monthly*, Bank of Japan.

EC accounted for a major part of Japan's capital transactions in the form of portfolio investment. In short, in contrast to the trade balance, Japan's long-term capital balance has been deteriorating steadily since 1965, except in 1980.

An important consideration regarding international trade performance is the fluctuation in a country's exchange rate. The yen has fluctuated against both the US dollar and the European Currency Unit (ECU). Against the ECU, the yen appreciated by about 36% between 1980 and 1983. Over the same period, however, the yen depreciated by about 20% against the US dollar. Of course, there are many parameters involved, but it could be argued that the relative weakness of the yen against the US dollar could be partly due to capital inflows in the form of portfolio investment which were induced by differentials in the two countries' interest rates. In addition, the yen's share in world reserves (about 3-4%) is not in proportion to Japan's relative standing in international trade; for example, the Deutschmark has a share of 12% when West Germany accounts for only 9% of world trade.

Table 2 does not give all the necessary information which is needed to

Table 3 Japan's External Trade Balance, 1976-81,

(a) By "Area" Distribution (US\$ billion)							
	Area	1976	1977	1978	1979	1980	1981
I	Developed Areas	5.6	10.6	12.6	5.7	12.1	22.3
Ia	North America	2.7	6.2	8.8	3.6	4.6	12.3
Ib	USA	3.9	7.3	10.1	6.0	6.9	13.3
Ic	Western Europe	6.0	7.5	6.7	6.3	11.1	12.2
Id	EC	3.6	4.5	5.0	5.1	8.8	10.3
Ie	Australia	-3.1	-3.0	-2.6	-3.7	-3.6	-2.6
If	New Zealand	-0.04	-0.1	-0.2	-0.2	-0.2	0.30
II	Developing Countries	-5.0	-2.4	2.8	15.4	-25.3	-15.4
IIa	SE Asia	0.6	2.1	5.8	-0.1	-0.8	2.5
IIb	Middle East	-11.5	-11.6	-10.0	-18.6	-30.1	-24.9
III	Communist Bloc	1.8	1.6	2.8	2.0	2.5	1.8

Note: figures do not add up due to rounding.

(b) Percentage Distribution												
	1976		1977		1978		1979		1980		1981	
	X	M	X	M	X	M	X	M	X	M	X	M
I	47.1	40.2	47.2	38.9	46.8	33.9	47.3	38.9	47.1	35.0	48.5	35.8
Ia	25.6	22.4	26.6	21.6	27.5	22.7	27.3	22.2	26.0	20.8	27.6	20.8
Ib	23.3	18.2	24.5	17.5	25.5	18.6	25.6	18.5	24.2	17.4	25.4	17.7
Ic	16.3	7.7	16.2	7.9	15.1	10.1	15.9	9.1	16.6	7.4	15.6	8.1
Id	10.8	5.6	10.9	6.9	11.4	7.7	12.3	6.8	12.8	5.6	12.4	6.0
Ie	3.4	8.3	2.9	7.5	2.8	6.7	2.5	5.7	2.6	5.0	3.1	5.2
If	0.6	0.7	0.6	0.7	0.4	0.8	0.6	0.7	0.5	0.6	0.6	0.6
II	46.0	55.4	46.7	56.4	46.4	53.5	45.5	56.2	45.8	60.3	45.3	58.8
IIa	20.9	20.7	21.3	21.3	23.7	21.8	25.4	23.7	23.8	22.6	22.6	22.3
IIb	10.8	2.9	11.0	30.0	11.0	26.2	10.4	26.5	11.1	31.7	11.7	29.8
III	6.9	4.4	6.1	4.7	6.8	4.9	7.2	4.9	7.1	4.7	6.3	5.4

Notes: X means exports and M means imports.

Source: calculated from *Japan: Statistical Survey of Japans' Economy*, various years.

examine Japan's trade balance by "area" distribution. This is given in Table 3, both in terms of absolute values and percentage share. The table shows quite clearly that Japan has a trade surplus with practically every "area"

except for Australia and the Middle East and, until 1981, New Zealand. The table also shows that Japan received over 75% of its imports from the Middle East (29.8%), SE Asia (22.3%), the EC (6.0%) and the USA (17.7%). These "areas" also accounted for a similar proportion of Japan's exports: the Middle East (11.7%), SE Asia (22.6%), the EC (12.4%) and the USA (25.4%).

Most of Japan's exports tend to be manufactured goods, with cars and electrical and electronic commodities at the top of the list. For example, 97% of Japan's total exports to the EC are in this category and in the USA many Japanese imports are seen as "highly visible consumer products, such as automobiles, electronic equipment, and cameras".²⁾ Japan's imports from these two areas are also mainly manufactured products but there are some interesting differences; for example, although 77% of Japan's imports from the EC consist of manufactures, the major items being machinery, transport equipment and chemicals, they cover a wide range of products with lower value-added while Japan's exports tend to be targeted to a few high value-added sectors. It is also interesting to note that about 20% of Japan's imports from the EC are agricultural products. Moreover, the picture is not too different for trade between Japan and the USA, but when it comes to the Middle East, the bulk of trade is imports of petroleum and exports of heavy and light industry products.

The Scenarios

The First Scenario. This is the most straightforward since it depends entirely on the above information. The brief look at the Japanese economy, especially its trade balance, tends to suggest that Japan has had many years of balance of trade surpluses while the EC and the USA have had many years of trade deficits. Hence, it would seem inevitable to conclude that this has been the main cause of the trade frictions between Japan and these countries, particularly given the earlier information about the inherent difficulties associated with a Japanese market which is supposedly relatively difficult for foreign firms. However, it should be apparent that such a scenario would be too simplistic as an explanation of Japan's trade frictions.

The Second Scenario. One needs to make a slight adjustment to Japan's trade balance before presenting the second scenario. Table 1 showed Japan

to have a consistent overall trade surplus except for the five years 1973-75 and 1979-80. However, if one were to look closely at Japan's deficit with the Middle East immediately before those years and contrast this with the overall deficit years, one would be left without doubt that, when due account is taken of the two oil crises, the change in the trade balance with the Middle East is a multiple of Japan's overall deficit. When adjustment is made for this, it becomes clear that one would be justified in asserting that from 1969 to date Japan has been having a *consistent* overall trade surplus with the rest of the world. This would seem to suggest that Japan deems a balance of trade surplus as an indicator of "national wealth". Of course, it could be argued that the trade surplus simply reflects Japan's policy as regards increasing its foreign investment, but there is no clear evidence for this assertion.

The position of the EC and the USA has been the reverse. As Table 4 clearly demonstrates, the EC has been having a consistent deficit in its trade balance since 1973, both with Japan and globally. The table also shows the USA to be in a similar position except for 1973 and 1975 when it had a global trade surplus.

Now, since the world deems it appropriate for countries to correct their trade deficits, it is implicitly assumed that those with trade surpluses must also correct theirs. But things are not so implicit since Lord Keynes spent a great deal of effort trying to establish the principle of equal responsibility as the basis for the creation of the IMF. It is ironic that the White Proposal, which was put forward by the USA, won the day. If this rationale is acceptable, it follows that we have a clear indication of the reason for the trade frictions between the EC and the USA and Japan. This would be consistent with the argument put forward by the United States-Japan Advisory Commission:

The growing trade imbalance is regarded by Americans as the most serious cause of friction between our two countries³⁾ (their italics)

The EC Delegation in Tokyo, speaking on behalf of the EC, put forward a similar argument:

Table 4 The EC, Japan and the USA's Bilateral and Global Trade Imbalances in US\$ Billion

	Japan				USA				EC 10			
	World	US	EC	World	World	Japan	EC	World	World	Japan	US	
1973	- 1.384	179	1.679	1.863	- 1.363	1.140	- 7.344	- 1.570	- 2.497			
1974	- 6.575	117	2.445	- 9.489	- 2.796	1.467	- 22.039	- 2.128	- 5.565			
1975	- 2.110	- 459	2.601	4.207	- 2.773	5.360	- 9.302	- 3.633	- 9.455			
1976	2.427	3.880	4.326	- 14.556	- 6.778	6.780	- 24.646	- 4.825	- 10.435			
1977	9.686	7.321	5.598	- 36.348	- 9.666	3.756	- 14.227	- 6.235	- 6.197			
1978	18.200	10.124	5.890	- 39.430	- 13.606	1.611	- 12.259	- 7.361	- 6.800			
1979	- 7.641	5.972	5.788	- 37.125	- 10.584	7.675	- 41.252	- 7.795	- 12.324			
1980	- 10.721	6.959	9.317	- 32.099	- 12.171	16.397	- 75.299	- 12.140	- 24.820			
1981	8.741	13.321	10.341	- 39.613	- 15.789	10.739	- 41.467	- 11.834	- 13.862			
1982	6.900	12.151	9.504	- 42.610	- 16.778	5.423	- 34.273	- 11.407	- 10.701			

Sources: EC Delegation in Tokyo, Japan Ministry of Finance and US Department of Commerce.

The Community's trade deficit with Japan has been growing steadily since the late 1970s, a source of recurrent, sometimes sharp, tensions.⁴⁾

However, this is a *less superficial* scenario rather than a complete or subtle one. The reason is that if bilateral trade imbalances are the true causes of the trade frictions between Japan and the EC and the USA, then it must follow that a correction of these imbalances would help eliminate the tension. No international trade theorist in his right mind would advocate such a solution: the aim should be to balance the country's *overall* trade account; *bilateral* balancing would be a direct negation of the principle of (dynamic) comparative advantage.⁵⁾ In the case of Japan, the implications of her asking the countries of the Middle East to take measures to correct their bilateral trade surplus would no doubt warrant a whole book, on both the economics and politics of the situation. If overall balancing is all that matters, it would not require much imagination to see that if Japan took measures to correct her overall surplus and distributed this in proportions which were consistent with her trade performance with the EC and the USA, the net effect would be no more than a modest contribution. The picture would not be that much different if Japan were to attain bilateral trade balance with the Middle East and distributed the sum so calculated in accordance with that criterion. (Such calculations would involve a comparison of Tables 1 and 4). Some economists have suggested that Japan and all the other member nations of the OECD should run trade deficits with the Middle East, but it should be clear, no matter what the merit of such a proposal may be, that this will not alter the relative positions of Japan, the EC and the USA.

If one were to concentrate only on the bilateral trade imbalance, one would get a very different picture: the net effect on the USA would be fairly significant but that on the EC would remain small.⁶⁾

One possible less simplistic explanation would be that the EC and the USA have trade deficits with countries, other than Japan, which are themselves in overall trade deficit. Hence, there would be no moral or theoretical justification in asking them to eliminate their imbalances with the EC and the USA. Therefore Japan becomes the obvious target and this would have resulted in

the trade frictions. Well, one does not need any statistics to see that such an argument would not hold much water since the combined deficits of the EC and the USA are of such a magnitude as to render this an impossibility; recall that Japan's trade surplus is far short of the combined deficit of the EC and the USA.

The Third Scenario.

(a) A more convincing argument requires an analysis which digs deeper under the surface. There are many possible avenues here but, due to space limitations, I shall confine myself to only three.

(i) Whether for genuine reasons or not, the Japanese market for manufactures has proved relatively more difficult to penetrate by foreign firms. The question as to whether the reasons are genuine is not clear simply because it could be asserted that in Japan:

- * High tariff barriers persist for some products, particularly those with a high value-added content, despite low average tariff levels.
- * Slow customs procedures, for example, item-by-item inspection of products rather than spot inspections or the holding of air cargo until laborious paperwork is completed, add to import costs.
- * Rigid and discriminatory standards and certification requirements contrast with simpler procedures in the United States. For example, foreign companies are required to pay for overseas travel expenses of Japanese inspectors, implementation of new measures is slow or inconsistent, and clinical testing done outside Japan is not accepted.
- * A relatively small amount of foreign telecommunications equipment is procured by the public Nippon Telephone and Telegraph Corporation, and foreign cigarettes are discriminated against by the Japan Salt and Tobacco Corporation, despite liberalisation in both instances.⁷⁾

The Joint Committee's report does not leave us much the wiser since its recommendations seem to be consistent with the above:

- * It is in Japan's own national interest to make the further opening of the Japanese market a high priority . . . Although Japan has made a series of unilateral trade concessions, there remain specific difficulties

to market entry in Japan which call into question Japan's commitment to free or fair trade. Some of the systematic problems underlying complaints include difficulty in obtaining access to information on Japan's bureaucratic policymaking and implementing processes, a strong bureaucratic tradition conducive to a reactive rather than initiative policy, and a propensity for Japanese to make a distinction between insiders and outsiders.⁸⁾

But it hastens to add:

Positive efforts by Japan to open its markets must be matched by a more positive U.S. export strategy at both governmental and private levels to *take advantage of new opportunities*. The United States also has barriers to market entry which should be reduced, although in view of the generally more open U.S. market, Japan cannot expect full reciprocity for its market-opening measures.⁹⁾

The EC Delegation in Tokyo is more forthcoming since it lists as explanations for the "import imperviousness" (an incorrect term since Japan does have substantial imports) of the Japanese economy, in addition to the item on the homogeneous structure of the Japanese domestic market referred to above, Japan's geographical position (no tradition of trade with neighbouring countries having a comparable level of development), and its recent history (the "export or die" mentality of the early post-war years): growing industries were protected in the 1950s and 1960s through an apparatus of tariff and non-tariff barriers and controls; Japan was a late-comer to GATT and has only gradually taken steps to liberalise its tariffs, quotas and investment restrictions; etc.¹⁰⁾

The point to be stressed is that this is a genuine area for research since all we seem to have at the moment is allegations and counter-allegations. A proper analysis should be conducted to find out whether or not Japan's domestic market is relatively more difficult to penetrate because of hidden barriers or whether it is the foreign firms who do not have the ingenuity and patience to work hard at capturing a share of Japan's market. One must hasten to add that such an analysis must also find out whether any Japanese practices in this respect are more or less protective (effectively) than those practised by other member nations of the OECD. For the immediate purposes of the third

scenario, all one needs to remember is that the Japanese market for manufactures is certainly very "different" from that in the EC or the USA; Table 5 clearly demonstrates this. However, one must add that this "difference" is no more than a reflection of the fact that Japan imports a large amount of raw materials relative to these countries, i.e. Japan has to import less manufactures in order to be able to import those raw materials which are vital for its economy.

(ii) Japan is a member of the OECD, but does not play according to the rules of the game: the OECD is a club whose members ought to have certain characteristics which entitle them to be labelled "advanced nations". Japan is seen as the black sheep of the family due to a discrepancy between her privileged status as a member of the group and her general pattern of behaviour: Japan is recognised as having reached a position of industrial prominence but is still conducting her domestic affairs in ways similar to those of an LDC. It was the norm for a member of the OECD to erode "workaholism" as it became more affluent. Economic advancement was expected to lead to a multiplicity of interests, values and beliefs in a democratic system, but the "Japan Inc." with the one-party system are seen to be in direct contradiction to this. Japan's foreign aid performance is seen as inadequate, her representation at the United Nations and participation in UN projects are considered to be out of proportion with her international status, and she does not allocate what is deemed an

Table 5 A Comparison of the Relative Importance of Manufactures in the Imports of the EC, Japan and the USA

Area	Percentage of imports of manufactures to 1982 GNP*	Percentage of imports of manufactures to 1982 total imports	Percentage of internal consumption of manufactured products covered by imports	Per capita value of imports of manufactures in 1982 in US dollars
EC	7.8	41	9.15	467
USA	8.0	57.7	6.32	629
Japan	3.9	22.9	3.9	223

Note: *The 1960 equivalent percentages were: 3.3, 2 and 2.4 for respectively the EC, USA and Japan.

Source: EC Delegation in Tokyo.

adequate percentage of her economic resources to improving the "quality" of her domestic environment and working conditions. Moreover, Japan does not even contribute to her international defence, hence she is seen as a "free-rider."

With regard to the general economic parameters, Japan is also seen as an outsider. This is because Japan concentrates all her energies on the export sector to the detriment of other important matters. Hence Japan today has congested housing, an inadequate sewage system, cities and towns with very sub-normal park facilities and a work pattern and style which are unpleasant and allow practically no opportunities for recreational and leisure activities. There is a great deal of truth in this; for example, a survey of the average size of a "flat" or apartment showed that Tokyo ranked "startlingly low at 59 square meters, as compared with 200 square meters in New York, 167 square meters in Toronto, 140 square meters in London, and 120 square meters in Dusseldorf".¹¹⁾ Moreover, the lack of public park facilities is acknowledged by all concerned, and even the lack of appropriate protection of the environment is conceded. Finally, the point regarding concentration on exports is substantiated by the published statistics: between 1964 and 1973, Japan's annual average rate of growth of GNP was 10.7% while that for her exports was 15.7%; and between 1973 and 1981, the respective rates were 3.7% and 8.5%.

However, there seem to be some fundamental reasons for the "workaholic" mentality. Ozawa argues, in response to the EC Commission's assertion that the Japanese are "workaholics living in rabbit hutches", that:

the average Japanese work-week is 43 hours, substantially longer than in the United States or Western Europe . . . but . . . the Japanese work long hours not because they are workaholics but because they are poorer than their American and European counterparts. Average hourly earnings in Japan are only \$5.27 per hour, as compared with \$8.73 in the United States and \$7.08 in West Germany. This means that the Japanese must work more hours than Americans or West Germans in order to make ends meet . . . Japan's average of \$5.27 per hour is not very different from Britain's \$5.30 or France's \$5.56. But there is another factor compelling Japanese workers to put in more hours to make more money: the burden of the huge housing loans.¹²⁾

With regard to the last point, the survey mentioned earlier suggested that the average cost per square meter showed Tokyo with US\$2000, New York with US\$660, Toronto with US\$800, London with US\$920 and Dusseldorf with US \$1440.

In short, Japan is seen as an industrial giant which directs all its activities towards its export sector much to the detriment of facilities which are the symbol of Club OECD. Moreover, the totality of Japan's trade relations is conducted with this principle in mind: the voluntary exports restraints (VERs) made by Japan are meant to ease international tension to pave the way for a further round of export onslaught. Well, there is a wealth of food for thought here, hence this is also a genuine area for further research, particularly since, for example, there are indications that the provision of sewage facilities to improve the environment is not lacking; it is the tremors and earthquakes which lead to their disappearance.

(iii) Both the USA and the EC have been having much higher unemployment rates as well as inflation rates relative to Japan—see Table 6. The USA has an overvalued dollar relative to Japan and its present interest rates are much higher too (by 50%). The EC's relative position is more complex since the ECU is a basket of currencies, but it has been known for a long time that, until recently, the Pound Sterling has also been overvalued. These facts when put together seem to suggest that the trade imbalances for the USA and the EC are largely their own doing. In other words, it is the responsibility of the USA to put its own house in order by lowering its interest rates and depreciating the dollar. Given what was stated above regarding the fact that the correction of Japan's trade surplus will not solve the USA's trade deficit, or the EC's, it follows that the reason for the trade frictions must be mainly due to the prevalence of protectionist sentiments at a time of high unemployment coupled with imports from Japan which are highly transparent to the average consumer. What really added fuel to protectionist sentiments was the credibility given to them, albeit in macroeconomic terms, by the Cambridge University (UK) Economic Policy Group, but the misconceptions underlying their theoretical structure have been exposed elsewhere.¹³⁾

If this reasoning is acceptable, it follows that Japan's trade frictions are

Table 6 Inflation Rates and Recorded Unemployment in the EC, Japan and the USA

	Average Annual Rate of Inflation %	Recorded Unemployment
	1970-1981	1981
EC		8
Belgium	7.3	11
Denmark	10.0	9
France	9.9	8
W. Germany	5.0	5
Greece	14.8	
Ireland	14.2	11
Italy	15.7	8
Netherlands	7.6	8
UK	14.4	10
Japan	7.4	2.5
USA	7.2	7.6

Note: Luxembourg is included with Belgium.

Sources: *Statistical Abstract of the United States*, 1983 and *World Development Report*, 1983.

essentially a manifestation of a socio-political rather than an economic phenomenon. "Special Interest" groups find it easier to blame outsiders for their plight, and governments, by not deliberately dispelling this idea tacitly, abet with the result that what started as a misconceived notion became a successful political stance.

(b) When these three elements are considered together, a less unobvious explanation of the Japan/EC/USA trade frictions emerges. The nature of the relatively difficult Japanese market for imports of manufactures, the "abnormality" of Japan as an influential member of Club OECD and the prevalence of protectionist sentiments in times of hardship seem to combine in a way which too easily puts the blame on Japan, particularly when it exports perceptible and popular commodities. However, this does not absolve Japan of all guilt since a country which deems a trade surplus to be a source of national wealth must try to understand that trade surpluses are the mirror image of trade

deficits for other countries. Hence it is the responsibility of all the nations concerned to make efforts to alleviate the situation. It follows that to describe VERs as concessions is both misguided and misleading.

What Needs to be Done?

I have tried to indicate that Japan's trade frictions cannot be attributed to any single factor, indeed it is a reflection of a set of complicated economic, political and social considerations, both of a short and long term nature. But I think I have gone beyond simply suggesting areas for research into some facets of these considerations, since I have tried to imply that, notwithstanding research into one or two urgent areas, what needs to be done is for the rest of the OECD to put its house in order and for Japan to discard the principle that a nation's wealth can be measured in terms of a trade surplus. However, for Japan to do this, she will need a type of international cooperation which takes into consideration her own problem of being dependent on energy imports from the Middle East, an area with which she has been having a consistent trade deficit and which is obviously very susceptible to oil price changes. On the other hand, Japan conducts a major part of her external trade with the Middle East, SE Asia, the EC and the USA. Hence, Japan will need to develop a special type of commercial relationship with these areas.

However, this type of relationship creates certain problems, given the ongoing debate on "Pacific Basin" cooperation-cum-integration.¹⁴⁾ The reason is that this idea does not take into consideration the region in which Japan must have special interest: the Middle East. What is therefore needed is a very involved type of economic integration accompanied by vigorous efforts for promoting international cooperation in general. The theoretical implications as well as the practical problems of such a proposal have been discussed elsewhere,¹⁵⁾ but in this particular context it should be emphasised that one of the implications of such a type of cooperation is that Japan's market cannot remain so difficult to penetrate by foreign exporters for long within such a project. It is therefore of the utmost urgency that proper research should be conducted on this matter.

Conclusions

It would be pointless to list the conclusions that have been reached from this tentative analysis. What remains to stress is that Japan's trade frictions seem to have been a reflection of a very fundamental set of problems which require an appreciation of the socio-political as well as the economic aspects involved. Hence an analysis which concentrated mainly on a single facet of the problem would be completely misguided. In addition, it would be pointless to expend too much energy on the analysis of the causes of the problem since no matter what these may be, it would be more fruitful to conduct research on possible areas of cooperation and integration which would alleviate Japan's fears regarding her dependence on imports of raw materials and "energy", i.e. the "Pacific Basin" idea tackles only some aspects of the Japanese long-term problem.

NOTES

- 1) Lewis P. Freitas, "Views from Abroad: Japan" *Journal of Accounting, Auditing & Finance*, vol. 4. no. 3. Spring 1984, pp. 271-73.
- 2) United States-Japan Advisory Commission, *Challenges and Opportunities in United States-Japan Relations*, a Report submitted to the US President and the Prime Minister of Japan in September, 1984, P. 27.
- 3) *Ibid*, p. 27.
- 4) Commission of the European Communities, EC Delegation in Tokyo, *Japan and the European Community: a Stocktaking*, 1984.
- 5) Of course, There are those who would argue that even *overall* trade balances should not be the goal, only the overall balance of payments. Such an argument would be misguided since it would exhibit no understanding of the mechanisms whereby imbalances can be identified even though the balance of payments is automatically in balance (due to the double-entry accounting system): the distinction between "autonomous" and "accommodating" transactions.
- 6) United States-Japan Advisory Commission, *Ibid.*, pp. 27-31.
- 7) *Ibid*, p. 34.
- 8) *Ibid*, pp. vii and viii.
- 9) *Ibid*, p. ix.
- 10) EC Delegation in Tokyo, *op. cit.*
- 11) Masako Ozawa, "Japan's New Class Society: Consumption Patterns Reveal Growing Class Distinctions" *Monthly Economic Review*, Long-Term Credit Bank

- of Japan, Tokyo.
- 12) Masako Ozawa, *Ibid.*
 - 13) Ali M El-Agraa, "Professor Godley's Protectionism: a Basic Macroeconomic Framework" *Manchester School*, forthcoming.
 - 14) "A regional approach should . . . be regarded as supplementary to and supportive of . . . genuine global solutions . . . [to] the world economic problems. Emphasis [should be] on the progressive nature of any open regionalism, considering that the real alternative to regionalism is not a global free trade . . ., but rather . . . *ad hoc* pressures for bilateral trade restrictions." Hiroshi Kitamura, "Japan and Asian-Pacific Economic Integration," a paper presented to the American Economic Association in December 1984.
 - 15) See Ali M. El-Agraa, *The Economics of the European Community*, Oxford, Philip Allan, 1980, 1985; *International Economic Integration*, London, Macmillan, 1982; *Britain Within the European Community—the Way Forward*. London, Macmillan, 1983; *The Theory of International Trade*, London, Croom Helm; and *Trade Theory and Policy—Some Topical Issues*, London, Macmillan.