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Discussion

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Discussion After the Speeches of Robert C. Cassidy and Simon V. Potter

QUESTION, *Professor King*: We hear cries that Japan has not opened up her markets; that there are certain markets that are very difficult, very traditionally Japanese; that they do not practice free trade. Should we play a little hardball with Japan? Is the trade surplus, which is on a continuing basis, something we can live with indefinitely?

ANSWER, *Mr. Cassidy*: Before I start, let me declare where I am coming from. I represent Ford, GM and Chrysler as a group who do not like minivans or automobiles from Japan; I represent Sumitomo Metals who exports steel to the United States; I represent DuPont, who does not like many chemicals from Japan; and I represent OKI Electric, who sells semi-conductors and telephones and a lot of other things in the United States. So, I am squarely caught in the middle on this one.

Ignoring all of those client concerns, I have been much involved with Japan now going on almost twenty years because I spent the vast majority of my time in government dealing with Japan issues, a great deal of that time in Japan, and since then, working on both sides of the Japan trade problem.

It is an extremely interesting question and an extremely difficult one for policy makers. Let me tell you very briefly where I think the new administration is going. Then, if I have a moment, I will give you my own views on this. There was an attempt by the Clinton Administration to develop a new Japan policy in time for the meeting of the Prime Minister with the President. That did not succeed for a number of reasons, the most significant of which is that they could not reach any agreement amongst themselves on what the policy towards Japan ought to be. Much to their amazement, but no one else's.

There is a strong argument being made, which is new at least in government at that level, that the traditional approach to U.S.-Japan economic issues in the economic area which has been, to use the term the critics use, a process-oriented approach, does not work. The process approach seeks to manage the disputes and tries to find a resolution to problems as they arise. This approach goes back at least to what was called the Straus-Ushiba Agreement of about 1978. The notion was that disagreements are inevitable. Yes, the Japanese market is closed in many respects, but these are not irrational people and if we have a way in which we can keep talking at them, keep hammering away at them, we can solve these problems one by one. Perhaps over time the problem will alleviate itself. The problem being defined in political terms as the structural bilateral trade deficit.

Now, let me stop there a second. That number is an abstraction. It does not mean anything except that politicians get very excited when they see it. It magnifies the concern that they hear from numerous constituents who say they do not like the fact that the Japanese are buying this factory or they do not like the fact that they lost their job because of competition with the Japanese. So it all becomes focused on the statistical manifestation of this competition which is the trade deficit.

The trouble with the approach, if there is any trouble with the traditional approach, is that the bilateral trade deficit has not changed. It is still there. If anything, it is getting bigger, due, not surprisingly, to a combination of the recession in Japan, the recovery in the United States, and the consequent changes in the exchange rate.

A substantial faction in the Clinton Administration is saying, "Okay, we've tried this approach and it clearly has not worked. We have got to do something else. We have got to stop the business of going in and trying to make the Japanese more like us. We should tell them, in its crudest terms, that we want ten percent of their automobile market. You figure out how to make it happen. And you've got five years to do it. And if you can't do it, well, that's all right. No problem, you just can't sell cars here." That is a proposal which I did not make up. That is a proposal I have heard discussed seriously by a very senior U.S. government official in the new administration.

So, I do not know where this is going to come out. Impasse is certainly a result that is not excluded knowing the depth of the feelings on this issue. However, my guess is that we will have at least some change, certainly a change in tone. We have already had a change in tone in the discussion of Japan, and that was started by the President himself. But it is likely that we will probably find ourselves trying something perhaps a bit less draconian than what I described to you. We will find ourselves trying some variation on the theme of identifying some sectors in Japan where we have a reason to believe that we can succeed because we are competitive and, in essence, asking the Japanese to do whatever they have to do to produce a result.

My guess is also that this approach, if it is adopted, will be accompanied by a continuation of the traditional approach to Japan, which is increasingly, I believe, focused on a fundamental part of the Japanese system: their capital markets. Japanese companies do not have to pay the cost of money that the rest of the world has to pay and it is not entirely attributable to the fact that they have an enormous pool of savings, which is absolutely true. However, it is at least partially due to the fact that there is not any liberal trade in money, if you will, that allows interest rates and stock prices to reach anything near what one would expect to be the market rates for those things. And I believe certainly a Treasury Department working under Mr. Bentsen is likely to focus on that issue increasingly and, in my view, correctly.

Having said that, I think the easy solution to the Japanese problem is for them to reduce their exports of automobiles to something like eighty percent of where they are. If that number was achieved, my clients would be very happy. If you exclude automobiles from U.S.-Japan bilateral trade pattern, and you look over the last thirty years, you have a very normal trading pattern. There are surpluses and there are deficits going both ways. It is a perfectly healthy trading relationship. Therefore, clearly, we have to fix the car problem.

QUESTION, *Mr. Russell*: Can I rise to the bait offered by the two speakers and ask a question of each?

The first question is directed at Robert Cassidy's theory that Section 301 had essentially been successful in citing the semiconductor agreement. As an example of that, I am not sure that the Japanese, somehow inching by the quota in the last month under which the agreement was constructed, qualifies a success of the semiconductor agreement. Whether or not that is the case, does not that sort of managed trade, aggressive unilateralism, have exactly the same sort of problems that Michael Hart identified with industrial policy? That is, you must, in fact, pick winning and losing sectors, decide somewhat arbitrarily what proportion of the market you want, and thereby distort what is, in effect, free trade and what would normally be construed as normal economic efficiency. I would be curious to hear your response to that point of view.

To Simon Potter, briefly, my question is: You raised the issue of the U.S. trading partners being incensed by their position on subsidiaries. It raises the question, I would think logically, of why has somebody not done something about it; i.e. what in your view is the reason that we have not seen a plethora of countervailing duty actions under the Special Import Measures Act or equivalent statutes in other jurisdictions?

ANSWER, *Mr. Potter*: There are two answers to the question: "Why have there not been more CVD cases against the United States?" One easy answer, which is given a little too glibly sometimes, but there is a kernel of truth to it regarding Canada anyway, is that Canadians are simply less litigious and they do not like getting into a fight on these things. They like simply to go to work and do their job and get through the day and go home. There is an element to that. They do not see life as running to the next court battle.

Another element which I think does explain it, besides the fact that many of the people who might complain about it in Canada are actually corporately related to the people against whom they would complain, is that it is the "Defense Department thing." Taking that as an example, you would have a very difficult time showing the "specificness" of the subsidization under the GATT. Showing that the money which came from the government through the Defense Department,

down through its twenty percent ownership of RCA, actually gave to a particular American company a benefit of X. Now, the fact that it is hard to quantify and hard to prove does not mean that it is not there and does not mean that it is not a source of irritation. But it does mean it is more difficult to do something about it. I think that is the main answer.

ANSWER, *Mr. Cassidy*: I have a little trouble with this image of these hard-working Canadian peasants and fitting that in with my dealings with these rapacious Toronto financiers that I usually see. To answer your question about 301, it is worth repeating that I was party to the negotiation on semiconductors for a Japanese company that led to that result so I do not particularly consider it to be a victory. There are those who consider and, indeed, use the example of the semiconductor war as an example of industrial policy itself. It is purely trade related. There is nothing else. That is exactly the kind of thing that I was saying I do not consider to be industrial policy because it was nothing but border measures; that is to say a floor price system for imports, which enriched not only domestic U.S. producers, but even more so, Japanese producers enormously, at the expense of the consumers. That is not you and me, by the way. The consumers are people like IBM and DEC and Compact and Apple who, as a consequence of that, created an entirely new trade association to combat against this ever happening again. But so much for the digression.

Was it a success or not? From the perspective of the people who wanted it, who were the U.S. producers of semiconductors, it was a dramatic success. They received higher prices for their product in their biggest market, which is the United States, and they, as I recall, doubled their market share in the second biggest market for semiconductors in the world, Japan. The fact that the number of twenty percent was just barely met is neither here nor there. The Japanese have never agreed that they agreed to a twenty percent number so that is a debating point. From the perspective of the people who initiated the measures it was a dramatic success.

From an objective point of view I would have to ask you where you are sitting. If you are a producer of computers it was a disaster. One thing that happened is they moved offshore more production so they could get access to less expensive chips that were not subject to the floor price system.

For a consumer, it was a bit of a blip because the price of the chip is such a small overall cost of the machine to us that we did not really see it. As a government policy official, well, that is another seminar.

QUESTION, *Mr. Browne*: I have a question for Mr. Cassidy. In your second intervention you ended by saying we have to solve the automobile problem. I think that is a good illustration of what it is we are looking at here if we are considering industrial policies of governments.

How do we come to grips with the sorts of issues that are raised in the automobile problem? For example, at the largest U.S. auto show, the automobile that was awarded the recognition of the best American car of the year, in fact, came from Canada; the Toyota is now advertised as the best car built in America. There is the example of some U.S. administration that was buying road graders or road-making machinery so they chose an American brand over the Japanese only to find out later that, in fact, the Japanese brand had more American content than the American brand. We keep running into these things.

Also, you referred to the fact that you would like to see more restraints on the sales of minivans from Japan into the United States. Our experience in Canada when we had the VRAs on the exports of automobiles from Japan, after the fact, of course, was that the net effect was to simply transfer economic grants from Canadian consumers to Japanese producers. It seems to me that these sorts of themes or examples suggest that any traditional approach to the industrial or trade policy that says we have an American product or Canadian product or Japanese product and somehow governments have to intervene to isolate a balance is not going to take us very far. How do you come to grips with these sorts of issues?

ANSWER, *Mr. Cassidy*: I was being slightly flip in talking about automobiles given the fact they are my clients. However, let us pursue this for a moment. First of all, you must keep in mind the automobile industry is quite difficult for U.S. and Canadian Government officials to deal with because the industry perceives itself to be North American in a rather profound way which is not too hard to understand when you go south from Detroit over into Windsor and see all those factories sitting there. It is, as you know, the oldest example of U.S.-Canadian free trade under the auto pact.

The border here truly does not exist, insofar as I can make out, in the minds of the people who are making the decisions for the industry. They perceive that they have a problem of competition with Japan in North America, and the fact that it may be in Canada or the U.S. does not seem to register particularly. But because we work in a national system that requires you to use the laws of one country or the other, they have used the dumping laws in Canada and the United States. You still have to deal with the relics of the national system in the automobile sector.

It does appear to me that the industry is tending increasingly to focus its analysis of its competitive problem with the Japanese, first and foremost on its internal problem: its own industrial problem. How do we make ourselves more efficient? If you look at Chrysler and, even more so, at Ford, they have made remarkable steps in becoming more efficient and a great deal more productive in reducing the faults of the vehicle so that for many vehicles today, if you take a look at the

"things gone wrong" surveys, you will find that the American product is at least as good as if not better than the Japanese product. I say American. I mean North America because a lot of these are made in Canada. So that is step one.

Unfortunately, the great big gorilla in this, General Motors, has been rather slow in adapting itself. It has some remarkable success stories to tell, Saturn being the most obvious. But the company overall is at the late stages of the beginning of its reorganization in order to survive, and it is going to be extremely painful. So that is step one, just where they focus.

Step two is that they have established alliances with the Japanese. The purpose of those alliances is to get access to Japanese technology. That has worked reasonably well. At this point there are some new proposals on the table where the Japanese want access to their technology so the question becomes, well, what do we do? Do we give them stuff that they need in exchange or not? It is an interesting strategic question to which they have not yet reached an answer.

Then you have the day-to-day trade problem, so called. First impulse, I think, still is to look at this as an export issue. They would love to get into the Japanese market in a bigger way. They are spending a great deal of money on it and the days when they used to say, "Well, we don't want to make left-hand drive cars" are long behind them. However, it is extremely difficult to get into that market for a variety of reasons all of which are the usual stories one hears about Japan. It will take a long time. Any government assistance they can get from the United States in that regard would be appreciated. Their view strategically is if they can establish themselves effectively in Japan, then a lot of this problem may eliminate itself. But in the meantime, they still have a principal market here in North America, and in order to fund the enormous costs they are incurring to build new facilities and to pay for workers that they have laid off but still have to pay under their union contracts, they see absolutely no harm in talking to the government about the possibility of getting the government doing something to have the Japanese back off a bit. I hasten to say the government has not agreed to do this. The so-called VRAs that the Japanese media announces every March are an illusion. The Japanese government asks car makers how many are they going to ship to the U.S. each year and then add a couple hundred to that. Then they declare that to be their VRA. It is polite. It is reassuring. Exports are not going to shoot up, which is true, so there is some effect to it. But insofar as having a depressing effect on the trade, it is nonsense. There is no simple solution.