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APEC as Seen from the Eyes of a Japanese Economist

Ryutaro Komiya

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ABSTRACT

The Japanese trade policy authorities showed great enthusiasm toward the formation and growth of APEC. Viewed from Japan's perspective, since the second half of the 1980s there have been two worrying developments in the world trade system. First, the Uruguay Round did not progress smoothly, and second, regionalism, which included elements running contrary to globalism, was spreading. The ASEAN countries, Australia, Japan, and South Korea hoped for the maintenance and development of a free, multilateral world trade system, as well as for keeping the EU and North America as open as possible. APEC was also expected to strengthen the negotiating power of the West Pacific countries vis-à-vis the U.S. and the EU.

The APEC countries agreed to liberalize trade and investment by 2010 or 2020, but the meaning is not clear. I see difficulties with either of the two approaches to promote the liberalization of trade and investment in APEC: an MFN approach and a reciprocity approach. Most East Asian countries, at least at present, are not in favor of the second approach, which implies the formation of a free trade area. Whereas the U.S. is negative toward an MFN approach, which allows the EU a free ride on the APEC liberalization wagon.

The heat of Japan-U.S. trade "friction" has declined substantially, and this trend will more or less continue. There is widespread acceptance of the concept that Japan has very high trade barriers, but it is a mistaken view.

Will the Japanese government include agricultural products among the targets for free trade? In Japan, "agricultural prefectures" are relatively poor and economically stagnant, but politically influential. Japan's protective agricultural policies will more or less continue for the time being. Because the majority of the Japanese people support free trade, however, Japan's trade barriers relating to agricultural products are unlikely to become higher than at present. Japan is now the world's largest importer of foodstuffs, and the value of its food imports doubled in seven years from 1987 to 1994. Since Japan's agricultural production is expected to stagnate or decrease in the future, its food imports will probably expand steadily in the future.

APEC has so far been a great success. The evaluation of APEC in the next several years will depend on how much progress is made in terms of liberalization and facilitation of trade and investment and economic cooperation among members.

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Ryutaro Komiya

Professor of Economics, Aoyama-Gakuin University
Director General,
Research Institute of International Trade and Industry

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Introduction

The remarkable growth of the Japanese economy after World War II would have been impossible without the GATT (General Agreement on Tariff and Trade)/IMF (International Monetary Fund) regime. Japan has benefited greatly from the GATT regime. For Japan, it is very important to have the multilateral world trade system to grow and function smoothly. Since the 1980s, however, there has been a strengthening tendency toward regionalism in the world trade system, which contain elements running counter to globalism, a tendency which Japan should be greatly concerned about. The trade policy authorities in Japan were profoundly interested in the formation of APEC and are enthusiastic about APEC's development under such recognition.

The purpose of this paper is to discuss the importance of APEC to Japan, its role expected, and relation with Japan from the view point of a Japanese academic economist who has general interest in international trade but little specialist knowledge about APEC.

First, Section I examines the conditions when the Japanese trade policy authorities began discussions with related countries on an economic deliberative group in Asia and Pacific, which was later to develop into APEC, and considers the importance of APEC to Japan.

Section II deals with U.S.-Japan trade friction which has accounted for a large proportion of Japan's trade problems in recent years. One of the factors behind why the Japanese government and governments of several other Asia-Pacific countries have been enthusiastic about APEC's founding and development, relates to their bilateral trade relations with U.S.

In section III, I point out it is not easy for outsider to understand what is APEC. Also, in pushing forward with APEC's trade liberalization there are two conflicting

approaches: (1) an MFN approach and (2) reciprocity approach, the basic problems between these two approaches seem to remain unresolved.

Section IV discusses the problem of the openness and closedness of the Japanese domestic market. I agree that Japan is one of those with the lowest trade barriers among the world's major trading countries, except a few agricultural areas, and that the stereotyped notions that Japan's markets are closed and that Japan has high trade barriers are mistaken.

Section V considers the outlook for Japanese agriculture, agricultural policy and agricultural imports in the near future.

Finally, Section VI evaluates the achievements of APEC since its establishment up to the presents.

1. Importance of APEC to Japan

The trade policy authorities in Japan were profoundly interested in the formation of APEC. I think these authorities, and those concerned with foreign affairs, are currently very enthusiastic about APEC's development. There are, in my general understanding, several reasons for this enthusiasm.

For Japan, it is very important to have the multilateral world trade system to grow and function smoothly. After the Second World War, Japan benefited greatly from the GATT (General Agreement on Tariff and Trade)/IMF (International Monetary Fund) regime. In fact, one of the principal reasons why the Japanese economy came to a dead end in prewar years was the collapse of the multilateral system of world trade, although, of course, the Japanese militarism of the time was also responsible for the collapse. The remarkable postwar growth of the Japanese economy would have been impossible without the GATT/IMF regime. This is the view of most of Japan's well-informed minds today, and they strongly hope that the multilateral,

free world trade system will be maintained and further developed.¹

One thing Japan should be greatly concerned about regarding events related to the world trade system since the 1980s, however, is the development of regionalism, a move that includes elements running contrary to globalism. This regionalism refers to the regional preferential trade agreement (hereafter, "regional agreement") based on GATT Article 24 (and on some other provisions), including customs unions and free-trade areas. It cannot be said, of course, that all such regional agreements are undesirable. When a preferential trade region is formed, the so-called "trade creation" effect could become much greater than the "trade diversion" effect, and the regional agreement could benefit also countries not included in the agreement. There are, however, also instances in which countries outside the agreement suffer disadvantages, especially countries previously having close trade relations with one or more countries in the region.

From the second half of the 1980s, a number of trends emerged in the world trade system that I think Japan and several other countries in situations similar to Japan should be greatly concerned about.

- (1) The tendencies toward closedness seen in two giant regional agreements, EU and NAFTA. These include high tariff and nontariff barriers erected toward countries outside the region, such as the rules of origin issues, antidumping policies, "hub-and-spoke" policies, and so forth.
- (2) The appearance of numerous regional agreements. According to a list published by the GATT Secretariat, it was notified of 109 regional agreements between 1947 and 1994, of which 33 went into effect in the nine years from 1986 to 1994.²
- (3) Many of the regional agreements do not follow the

- "substantially-all-trade" requirement of GATT Article 24.
- (4) Similarly, many of the regional agreements do not follow, or cannot be expected to follow, the requirements of Article 24, that they will complete customs unions or free-trade areas "within a reasonable length of time".
- (5) The "hub-and-spoke" approach, in which a large trade area or large countries (hub), such as the EEC (EC, EU), EFTA, the U.S., and NAFTA, conclude separate free trade area agreements with many small countries (spokes), for which numbers (3) and (4) above apply.³

It was felt that the world's free trade system, based on the principle of "general most-favored nation treatment" of GATT Article 1 was gradually being eroded by numbers (2), (3), (4), and (5) above. I think it is a serious problem for the GATT/WTO regime that erosion has progressed thus far without being checked and continues to progress. If this erosion continues, the effectiveness of GATT's basic principles of nondiscrimination and multilateralism will be weakened, and world trade will become inefficient and unfair because of arbitrary distortions.

Among the present member nations of GATT, only two members, Hong Kong and Japan, do not belong to any GATT Article 24 regional agreement.⁴ The possibility is quite low that Japan will participate in the near future in any regional agreement based upon GATT Article 24.

When Japan's application for accession to GATT was finally accepted in 1955 (Italy was accepted in 1950; West Germany in 1951) after many years of effort in the postwar period, in the period which followed the U.K., France, and many of the European countries, and former British and French colonies, applied GATT Article 35 to Japan, and did not enter into the GATT relationship with Japan. The number of countries applying GATT Article 35 to Japan reached 47 altogether, and for a long period an abnormal situation continued in which Japan could not receive a most-favored-nation treatment from

many members of GATT, even though Japan was a GATT member. A large portion of Japan's commercial diplomacy efforts was spent for many years on negotiations to have application of Article 35 to Japan withdrawn. Today, this is almost entirely a matter of the past, but if the tendency to form a respective trade "bloc" by each of huge trade areas or countries such as the EU, the U.S., and NAFTA continues, and if the "hub-and-spoke" policies of these countries and areas further proceed unchecked, GATT Article 1 will come to lose its substance. There is fear that the position of Japan in the world trade system will then come to resemble the previous situation when many countries applied GATT Article 35 to Japan.

Such a situation is undesirable not only for Japan, but also for many smaller countries -- including the "spoke" countries -- as well as from the viewpoint of the overall efficiency and equity in the world economy.

To halt the reckless establishment of regional agreements under GATT Article 24, and the "hub-and-spoke" policies of large trade areas and countries, and to prevent a loss of the substance of the general principle of most-favored-nation treatment of Article 1, I believe there is a need to clarify the conditions for regional agreements established under Article 24, and to make those conditions strict enough. At the Uruguay Round (UR), among the conditions for establishing regional agreements according to Article 24, agreement was reached to make the "reasonable length of time" condition a period of 10 years in principle. Concerning the "substantially-all-trade" requirement, however, no clarification was made. I think the meaning of the requirement should be made clear regarding the parts of trade in a free-trade area (or a customs union) which are treated as exceptions -- parts that are not subject to complete free trade -- by setting a certain target of percentage of all trade in the area. And, if after the lapse of 10 years, in principle, such a "substantially-all-trade" requirement is not

met, then the regional agreement should become null and void.

It appears to me that the Japanese trade policy authorities often felt anxiety between the end of the 1980s and the early 1990s, and sometimes even a sense of crisis, about the future of the world trade system, regarding the following developments.

- (1) The UR negotiations that began in 1986 did not proceed smoothly, and at times even seemed to become deadlocked.
- (2) The fear, in the context of the "EC 1992" move (Fortress Europe?), that the EC would become more closed.
- (3) The free-trade area agreement (1989) between Canada and the U.S., and the move toward Mexico's participation in it.
- (4) The free-trade agreement between the U.S. and Israel (1985), and the "hub-and-spoke" policy moves thereafter by the U.S., to conclude similar agreements on an individual basis with some Latin American countries, Singapore, South Korea, and others.
- (5) Establishment of NAFTA (1992).

Among these developments, I would suppose, especially the news that the U.S. was beginning to move to conclude bilateral free trade area agreements with Singapore and South Korea was a great shock to the Japanese authorities. If such "hub-and-spoke" policies of the U.S. were to progress, the effect of the "distortions" they would cause in Pacific trade, including trade of Japan, would potentially be enormous.⁵

In this situation:

- (1) The ASEAN countries, Australia, Hong Kong, Japan, New Zealand, South Korea, and Taiwan have important common interests in maintaining and developing a world trade system that is free and open, and especially in keeping the EU and North America as open as possible.
- (2) Given the noticeably high economic (and trade) growth rates in recent years in the countries and areas just

mentioned, and in some other East Asian countries, if they joined together, they would gain a certain degree of negotiating capabilities vis-à-vis the EU, and the U.S.⁶

It can be supposed that such thinking was in the background from around 1987 when the Japanese trade policy authorities began discussions with related countries on an economic cooperative group in Asia and the Pacific -- which later was to develop into APEC -- and began enthusiastically promoting such thinking. Viewed from numbers (1) and (2) above, an Asia-Pacific economic cooperative group like APEC was considered to be very valuable to Japan at the time. It can be said that such thinking, as well as the conditions behind it, has generally not changed today. Because of the successes of APEC to date, it appears that the organization's importance to Japan has increased substantially.⁷

The organizers of this conference asked me, while APEC has been an important issue in Australia, whether it is so in Japan. The foregoing can be considered my answer to that query.

2. U.S.-Japan Trade Friction

Another other factor behind why the Japanese government was enthusiastic about APEC's founding, and why it has also been taking a quite positive attitude toward its development up to now, relates, I think, to Japan's bilateral trade relation with the U.S. In recent years, U.S.-Japan trade friction has accounted for a large proportion of Japan's trade problems.

A number of East Asian nations, starting with Japan, have continuously had difficulties in their economic and trade relations with the U.S. Sometimes they are persistent demands for liberalization, and other times it has been "unilateralism" or whatnot by the U.S., in prolonged bilateral negotiations. It was probably felt that if some kind of multilateral organization could be established in the East Asia/Pacific area, then whether the U.S. was included in the

organization or not -- the Japanese authorities in charge did not even remotely consider a multilateral organization in the East Asia/Pacific area that would not include the U.S. --, it would weaken the pressure somewhat in wearisome bilateral negotiations with the U.S. and alleviate the force of U.S. "unilateralism." The matter of rice imports into Japan, for example, was probably easier to process for Japan because it was handled at the UR rather than bilaterally between Japan and the U.S.

Australia, meanwhile, one of the countries that moved most enthusiastically in the early stages of negotiations for forming and promoting APEC, harbored great dissatisfaction as a result of decisions reached in past bilateral trade negotiations between Japan and the U.S. The two countries did not consider much about the interests of third countries with which they had close trade relationships, and sometimes they agreed on solutions that brought about disadvantages to Australia. Such dissatisfaction was not limited to Australia, but was also seen in South Korea and in other East Asian countries as well as in the EU. Australia and South Korea probably expected the formation of APEC to reduce the number of situations where such dissatisfaction might occur.

To change the subject for a moment, I would like to point out that recently the "heat" of trade or economic "friction" between Japan and the U.S. has substantially decreased, and that, even if there will be some ups and downs along the way, the general downward trend of such friction or its "heat" will continue. In my view, the phenomenon referred to as trade friction is primarily a sociopsychological phenomenon, or a political mass psychology phenomenon. It would not occur if the majority of citizens could understand economic problems properly in rational ways. At least in the case of Japan-U.S. trade friction, I see the main source of trade and economic friction as being based on irrational mass psychology.⁸ I cannot go into detail here, but there are many fallacies concerning trade friction when looked at from

the viewpoint of economics.⁹

One such fallacy is that "a trade deficit is a 'loss' for a country." A country's trade balance (balance of trade in goods and services) is the sum of the balance of trade in goods and services of all the corporations, households, and governments within that country. Because it is a result of the best possible choices made by a countless number of economic entities in the country, it generally cannot be considered a "loss." There are many countries, such as Canada, Australia, and South Korea (and the U.S. in the nineteenth century), whose trade balances have continually been in large deficit while their economies have grown and prospered. In the U.S., however, politicians, the mass media, and the general public have come to view a trade deficit as a "loss," and the superstition is widely believed that the large U.S. trade deficit has occurred because of Japan. This has been a major factor behind the heightened heat of Japan-U.S. trade friction.

Another fallacy is that "the reason why a country has a large trade surplus is because that country's markets are closed." This fallacy is firmly believed by many Americans and others. However, a trade surplus is equivalent to the export of capital, while a trade deficit is equivalent to the import of capital. If this fallacy were true, therefore, countries that export much capital over a long period, such as Great Britain in the second half of the nineteenth century, are to be considered as countries with closed markets and, in reverse, countries that import much capital, such as contemporary China or Latin American countries some time ago, are countries with most open markets. Certainly anyone who has studied a little economics would not believe such absurd propositions.

Another example concerns the trade relationship between Japan and South Korea. Because South Korea's bilateral trade deficit with Japan is persistently quite large, the overwhelming majority of Korean citizens believe that South

Korea is suffering a great "loss." Almost all of South Korea's politicians, government officials, and mass media leaders assert that the greatest problem in the Korea-Japan economic relations is South Korea's chronic trade deficit with Japan. They say that an urgent task for the two countries is to dissolve or eradicate this deficit. They say that the trade surplus, or the foreign currency, earned by Koreans working so hard to export Korean products throughout the world, is all taken away by Japan. As a result, Korea's trade balance almost every year is in deficit, and South Korea's "loss" is immeasurably large. It is said that South Korea and Japan must cooperate to quickly correct the trade imbalance between them. It is amazing how such a fallacy can spread so widely and firmly among a country's citizens.

Because of the trade deficit between Japan and South Korea, funds that are equivalent to the trade deficit are transferred from Korea to Japan, but merchandise equivalent to the trade deficit is moving from Japan to Korea. Korean corporations and individuals are buying that much merchandise from Japan exactly because they decided it is advantageous for them to do so. Japan is located close to Korea, and Korea can buy various types of machinery, equipment, electronic parts, and so on under most favorable conditions from Japan. Benefits to Korea, rather than "losses," from this trade are immeasurably large. Of course, Japan too benefits a great deal from this trade. The bilateral trade balance between Japan and Australia or Japan and Saudi Arabia is chronically in deficit for Japan, but no Japanese doubts that Japan is realizing great benefits from trade with these two countries.

The improvement of a country's trade balance or current account balance should be viewed as a problem of the overall balance vis-à-vis the entire world, not the problem of the bilateral balances vis-à-vis individual countries. The overall current account balance should be the target of macroeconomic management, with fiscal, monetary, and foreign

exchange policies. It is completely wide of the mark to consider as an "urgent task" the correcting of the trade imbalance between two countries.

Whether it is between the U.S. and Japan or between Korea and Japan, one reason why trade issues turn political, giving rise to trade "friction" and why heated debates break out is that the general public, most politicians and government officials in countries concerned do not understand the basic commonsense principles of economics. In other words, trade friction arises because economists in the relevant country have failed to teach proper economics to their countrymen, and the general public has come to believe in fallacies about economic and trade issues. Economics has a concept called "market failures", but I would say that trade friction arises because of an "education failure."

In the present situation, trade issues turn political because of a mass psychology that believes in fallacies. Heated debates emerge, and each government's officials in charge of trade matters end up spending huge amounts of time processing problems, most of which is entirely wasteful. I would like to see the economists in each country -- especially those in the U.S. -- teach their countrymen more about the theory of international trade and standard international macroeconomics having to do with the causes of and measures to overcome the trade deficit.

For years after the Second World War, and even today, the IMF has advised or requested countries which need to reduce their balance of payments deficits to improve their macroeconomics management primarily through fiscal and monetary measures. If a need exists for the U.S. to correct its trade deficit, then it should take the same kinds of measures the IMF, of which the U.S. has the largest voting right, has asked so many countries to take for a long time and even today.

From about 1982 or 1983, several more fallacies became wildly rampant. As a result, U.S.-Japan economic friction

became politicized and quite serious. After the U.S.-Japan auto talks were finally resolved in July 1995, however, the heat of trade issues between Japan and the U.S. began to subside. I believe there were several reasons for the quieting down of discussions:

(1) First, during the 1980s, motor vehicles, machine tools, and other products became increasingly exported from Japan to the U.S., and, moreover, in 1989, Mitsubishi Real Estate bought the Rockefeller Center in New York and Sony Corporation bought Columbia Pictures. A feeling of a threat from Japan spread widely throughout the U.S., and this became a principal source of friction heat. Later, however, in Japan, the financial and real estate "bubbles" burst and a recession ensued for almost five years. Many industries stagnated, the financial structure became widely distrusted, and the Japanese economy continued in the doldrums. Whereas in the U.S., business prospered, especially in leading-edge, high-tech industries and the telecommunications sector. And, above all, Japan's trade surpluses, both overall and bilateral with the U.S., have declined substantially in the last few years. As a result, the threat from Japan as envisaged in the U.S. has almost completely disappeared.

(2) Second, a few years after the Cold War ended, more Americans as well as Japanese have come to realize that the common defense interests of the two countries in Asia and the Pacific are quite large, with the incident of a rape of a school girl by young American military personnel in Okinawa serving as a focal point. The firmly rooted thinking in the U.S. that Japan had been getting a free ride on the coattails of American defense capabilities rapidly faded. More than ever before, recognition has spread more widely among the U.S. public of the great importance to the U.S. of the U.S. bases in Japan and of the defense-related expenses Japan has been bearing. This

was well known among those concerned in the U.S. -- as well as in Japan -- before, but it has now become more widely recognized. It would be unwise to "bash" Japan in such a situation.

- (3) Third, during the many years the Liberal Democratic Party (LDP) held power in Japan, the prime minister, or the leaders of the LDP factions who were possible candidates for the prime ministership, moved to make certain their thinking was attuned to the U.S. president and other influential political leaders. To be on good terms with the U.S. president and other leaders was a necessary condition to be the prime minister elected from the LDP. Thus,-- LDP leaders tended to be compromising on trade issues with the U.S. But that long one-party rule and the faction-based politics within the LDP came to an end.
- (4) Fourth, the generation of the officials responsible for trade negotiations in Japan has changed. The situation has become one in which appeals may be made to the WTO when the U.S. action or request is considered unreasonable. An epoch-making event about this was ratification of the Marrakech Agreement in the U.S. Congress. As a result, the U.S. came to realize that the old strategy of "bashing" Japan until it gave in has become no longer effective.
- (5) Fifth, when in 1995 the U.S. did not recognize the changes in Japan and moved forcefully forward in auto talks to set numerical targets, it failed. The forceful style of U.S. negotiation was viewed unfavorably both internationally and within the U.S. Also, because of the rise of "big emerging markets" (BEMs), the number of countries that are important trade partners for the U.S. has increased, and it has become unwise to concentrate U.S. negotiation efforts on Japan.

For these reasons, the heat of U.S.-Japan economic friction is expected to dissipate, even though it may not entirely disappear. Trade matters between the two countries

will become less politicized and will be resolved more rationally.

3. What is APEC?

No other organization like APEC exists, and it is difficult for those other than persons directly concerned to understand what it is. In its formative stages, one explanation went that APEC was a deliberative council, something like the OECD (Organization for Economic Cooperation and Development). The OECD comprises nations at similar levels of development. It is a group of developed nations that think more or less the same way concerning economic policy. All the OECD's members are also members of GATT and are Article 8 members in the IMF. In contrast, the members of APEC are at widely differing stages of economic development, and include countries and regions that have fundamentally different ways of thinking about economic policy. At the OECD there are exchanges of information, the preparation and publicizing of various statistics and study reports on particular issues, the exchange of opinions concerning macroeconomic and other policies, and a degree of mutual persuasion. The OECD also formulates codes that serve as guidelines to policies in areas such as international capital movements and service trade, and the members must basically observe the codes. It is generally clear what the overall OECD is, what obligations a country assumes when it becomes a member, and what benefits accrue to it.

In contrast to the OECD, it is difficult for outsiders to understand what APEC is, partly because it has only a short history. Existing official documents of APEC are the joint declarations of the seven ministerial meetings and three unofficial summit meetings held up to now. Unlike other international conventions and organizations, moreover, there are no convention rules fundamental to the organization. Most of the members are so far negative concerning the "institutionalization" of APEC, although

members agreed to establish a modest secretariat. Without a rigid legal structure, the members agree in areas where they are able to agree, which allows the wheels of the deliberative body to move little by little. It is understood that such an approach gives APEC an "Asian" touch to its organizational operation that differs somewhat from the Western approach. Concerning the results of the recent APEC Osaka Conference, it was reported that there was no use of words such as "negotiation," "binding," or "reciprocity," and, instead, the words "voluntary", "non-binding" and "unilateral" were heard frequently. Such a difference in the use of words was epochmaking, and it was said that such a style made the meeting more comfortable and congenial for Asians.

The three main pillars of APEC at present are: (1) the liberalization of trade and investment; (2) the facilitation of trade and investment; and (3) economic and technical cooperation. Some of the specific items included in "facilitation" and "economic and technical cooperation," may be truly valuable in terms of the region's growth of trade and investment and economic development. The importance of such items should not be slighted when compared to the liberalization of trade and investment. Concerning facilitation, however, there should be a division of the problems to be handled by APEC and those to be handled by the WTO or other international institutions. And concerning economic cooperation, there is also the problem of the burden to be shared by the World Bank, the Asia Development Bank, and other aid institutions, and what to do about the funds burden.

The issue of greatest interest for an outsider like myself, an academic economist, and the issue that has been of most interest to newspapers and other media, is perhaps number (1) above, the liberalization of trade and investment, especially the liberalization of trade. But for outsiders there are some difficulties in understanding what is meant by trade and investment liberalization within APEC.

In the statement made after the APEC Summit Conference in Bogor, it was said that the objective of "free and open trade and investment" would be achieved by the developed nations of APEC by the year 2010 and the developing nations by 2020.

Concerning the liberalization of investment, at the UR only limited agreement was reached concerning trade-related investment. Up to now, there have been almost no multilateral rules related to international investment (apart from those within the EU) other than the OECD's code on international capital movement. Although it is significant that a basic policy has been recognized in APEC on liberalization of investment, there is a long way to go before agreement is reached concerning specific rules that are effective and before those rules are implemented.

The meaning of free trade or the liberalization of trade differs depending on the country and on the particular period. Taken in its narrowest sense, the liberalization of trade in Japan in the past -- and in a number of other countries -- meant the removal of quantitative restrictions (QR) on imports. In many other instances, it refers to the removal of QR on imports and different kinds of nontariff barriers and tariffs, or the substantial reduction of nontariff barriers and tariff rates, even if it did not mean their complete removal. The "free trade" in a "free-trade area" under GATT Article 24 means the latter. In the original meaning of Article 24, even antidumping duties may not be used within a "free-trade area."

If discussions had been held at the APEC conferences in Jakarta and Bogor in 1994 or at Osaka in 1995 about the meaning of "free and open trade," which was taken as the goal to be reached by the member nations in either 2010 or 2020, the conferences probably would have ended without any agreement being reached. It is exactly because the meaning of the words "free and open trade" is left unclear that APEC is able to move forward.

The meaning of the words "open regionalism" is also unclear. "Open" probably does not mean "anyone who wants to can enter." An amateur like myself cannot understand its exact meaning.

That the meaning of the objectives members of APEC have agreed to achieve is unclear is the first difficult point for outsiders to understand.

In commonsense terms, if "free and open trade" means the removal of QR on imports as well as a substantial reduction (down to what level?) of tariff rates, plus the removal or alleviation of nontariff barriers (such as antidumping and countervailing duties), which are major trade impediments and cannot be rationalized in economic (or social?) terms, the distance APEC member nations will have to travel before they are in a condition to realize that objective vary considerably from country to country. On the one hand, there are (1) members such as Hong Kong and Singapore that are already quite near to that objective, (2) others that are members of the OECD and are relatively close to achieving it. While, on the other hand, among the developing country members, there are (3) IMF Article 8 countries, (4) countries that still have not advanced beyond IMF Article 14 status although they are WTO members, and (5) countries that are still not members of WTO. For countries like China that still have a very long way to go it is difficult to imagine when they will be able to achieve "free and open trade and investment".

Although the countries in category (2) above appear to be close to achieving "free and open trade," if we look back at the history of their trade policies over the past 20 to 30 years we see that great political efforts have been made in each country to reduce tariffs and remove or lower nontariff barriers. Most of the remaining barriers, therefore, are "hard-core." Hence, even though the distance to go appears short, it may not be easy to progress further.

A review of the "initial action" offered by each APEC

member at the Osaka Conference shows that the liberalization measures of countries that played major roles at the UR, such as the U.S., Japan, and a few others, reveals that they were either limited in their actual effects or merely advance implementation of the UR tariff rates. The U.S. included no measures whatsoever related to tariffs. One point to mention by way of background is that the principal negotiating nations at the UR mutually gave in substantially during the UR (or through liberalization measures before the UR) in terms of tariffs, and are now busy absorbing their domestic impact. It is thus difficult for them, viewed from the domestic political situation, to propose new tariff reductions. In comparison with these countries, there were a number of other countries that offered tariff reductions across a wide area that appear to carry with them quite substantial effects. This was a very pleasant development in terms of APEC's growth, but their offers suggest that those countries might not have been serious enough in mutual tariff reductions at the UR.

A second difficult point to understand regarding APEC is the matter of the confrontation of (1) the MFN approach and (2) the reciprocity approach in moving forward with liberalization of trade and investment. According to (1), the liberalization measures decided by the APEC members will be applied unconditionally to countries outside the region. Whereas, according to (2), when the liberalization measures decided on by the APEC members are applied to countries outside the region (with the EU principally in mind), the condition is set that the countries outside APEC will carry out liberalization measures equivalent in value to those of APEC. The reciprocity approach thus means that APEC's reductions in tariffs and nontariff barriers and other liberalization measures apply only to those countries outside APEC which put into effect equivalent liberalization measures. The underlying tone in APEC is said to be that the Asian members support the MFN approach, the U.S. insists on

the reciprocity approach, and Australia is in between. But I see difficulties, however, in either approach.

First of all, to push forward with (2), the reciprocity approach, legally in terms of GATT, APEC will have to become a free-trade area under GATT Article 24. That means APEC must remove the tariffs and other trade regulations for most of the trade among the members "within a reasonable length of time." As pointed out earlier, however, APEC comprises countries and areas which are at quite different stages of economic development and which have different levels of trade liberalization. So many members of APEC would feel it difficult to meet the conditions of the free-trade area. Although the APEC members agree at the present stage to realize "free and open trade and investment" in its unclear format, I would think that many of them could not commit themselves to becoming members of an APEC-wide free trade area under GATT Article 24.

Also, as I mentioned, viewed from Japan's position, or from what I see as being Japan's position, the regional agreement which does not satisfy, or for which there appears to be no outlook for satisfying, GATT Article 24 conditions is harmful and will give birth to distortions in the world's system of multilateral free trade. For Japan, and for the members of APEC that take the same stance regarding the maintenance and growth of the global free trade system, participation in a regional agreement that has an unclear outlook would weaken their contentions. It would not be a wise move.

Next, the MFN approach(1), whereby the APEC members would apply their liberalization measures unconditionally to WTO members outside APEC, would present no special problems for countries that are small in scale in the world trade system, or for countries whose tariff and nontariff barriers are now quite high. For such countries, the promotion of unilateral trade liberalization would promote their national interests.

For countries that are of a larger size, however, first of all, instead of unilaterally reducing trade barriers, it is better for them and their trading partners to reduce trade barriers simultaneously. That usually leads to a larger increase in trade benefits. Therefore, such countries wish to use reduction or removal of trade barriers as levers for negotiation with trading partners.

Second, although trade liberalization measures are generally beneficial for a country as a whole, it is usually disadvantageous for particular groups within the country. As a real-life problem, it is next to impossible to fully compensate for such disadvantages. For this reason, trade liberalization is accompanied domestically by political pain. If most countries carried out liberalization simultaneously and shared the political pain involved, liberalization would be politically easier to accomplish.

Countries like Australia, Canada, Japan, and the U.S. have participated in a number of GATT multilateral trade negotiations on a full scale in the past, and experienced their associated political pain. Their trade barriers have become relatively low, and those that remain are to be considered "hard core." It would be politically difficult for these countries to carry out trade liberalization unilaterally and to offer the results to other countries and the EU unconditionally.

In particular, the U.S. is aggressively conducting trade negotiations with many of its trade partners, including the EU, to push forward with trade policies which are thought to fit its national interests. The U.S. plays trade policy games all the time. For the U.S., the relationship with APEC is little more than another of these trade policy games. With future trade negotiations vis-à-vis the EU in mind, the U.S. will probably not show enthusiasm toward unilateral (nonreciprocal) trade liberalization within APEC based on what is called "concerted unilateral action."

In the early stages of the formation of APEC, the U.S.

did not show much enthusiasm other than indicating that it would participate in it. After President Clinton assumed office, however, since the APEC Seattle Conference in 1993, the U.S. began emphasizing trade liberalization at APEC venues, recognizing the importance of East Asia for its high rate of economic growth. But the U.S. government, at least for the time being, has not put into order the domestic preconditions for an extensive reduction of U.S. tariff and nontariff barriers, and seems to lack the willingness to do so, at least for the time being. When the U.S. representative talks about trade liberalization at APEC, it appears as if what they mean by trade liberalization does not include trade liberalization by the U.S., but means trade liberalization by APEC members other than the U.S. along the lines of U.S. wishes.

Based on the foregoing, it appears that basic problems remain unresolved in pushing forward with APEC's trade liberalization.

4. Openness and Closedness of the Japanese Market

Among the issues related to Japan's trade, one that I wish to mention concerns the openness or closedness of the Japanese domestic market. The stereotyped notions that Japan's markets are closed and that Japan has high trade barriers toward imports are expressed widely in the mass media by politicians, officials, and even economists in many countries, including Japan.¹⁰ But these notions are mistaken. Japan's trade barriers related to certain agricultural products, some services, and a few other sectors are still high, but in most other areas, I think Japan is now -- whatever the situation in the past -- one of those with the lowest trade barriers among the world's major trading countries. Unless this point is well understood, it is not possible to make correct judgments concerning many policy issues related to Japan's trade.

If evidence is asked from persons who assert that Japan's

markets are very much closed or that Japan has very high trade barriers, the usual answer is Japan's large trade surplus. But linking trade barriers with a trade surplus is a typical example of what is called "the fallacy of composition" in economics. In macroeconomic terms, it is obvious that there is no relationship between a trade surplus and the matter of whether trade barriers are high or low. It is also clear by looking at historical examples of a number of countries and the recent experience of various countries that, although there may be a relationship between trade barriers and trade surpluses and deficits over a short run, macroeconomic factors are crucial in accounting for the size of trade surpluses and deficits over periods longer than two or three years. In other words, the height of trade barriers or changes in them have nothing to do with the size of trade surpluses or deficits over a long run, especially under floating exchange rates.

After persons who say Japan's markets are closed are persuaded that there is no relationship between trade surpluses and trade barriers, the next piece of evidence they present as proof of Japan's closed nature is anecdotes on how difficult it is to export to Japan or how difficult it is for foreign businessmen to do business in Japan. I frequently hear such stories from foreigners, especially from Americans, and I see them written in publications. But many of them are clearly mistaken or lack credibility. Concerning most countries, there are many such anecdotes related to import barriers. The "anecdote approach" to proving that a given country's import barriers are high by using a few such examples cannot be considered scientific.

There are also persons who present as a proof the degree of penetration of imports in the Japanese market, i.e., the ratio of import volumes compared to total domestic consumption or the ratio of imports to GDP. Some say that the low level of manufactured product imports in Japan is proof that the Japanese market is closed. But that approach,

working backward from "results," also cannot be considered a scientific argument.

There are many American baseball players in professional Japanese baseball teams, but there has been only one Japanese baseball player in the past on an American major-league baseball team before Hideo Nomo, who is now well known. As a man-made restriction, the Japanese professional baseball teams can register only up to three foreign ballplayers. There is no such restriction in the U.S. Which of American and Japanese professional baseball is more closed to foreigners?

It is extremely difficult to enter universities such as Oxford and Cambridge in England, Harvard in the U.S., Beijing in China, and the University of Tokyo in Japan, especially for foreign nationals, but it does not mean that these universities are "closed." A person who masters the particular country's language and has excellent academic capabilities can enter these universities. In short, there is no close relationship between the level of import penetration and the matter of whether a country's markets are open or closed.

It is possible to make clear international comparisons with regard to some trade barriers, such as tariff rates, the number of items under quantitative restrictions on imports to protect domestic industries, gray-area measures restricting imports, import items under antidumping and countervailing duties, and safeguards. As far as these straightforward trade barriers are concerned, trade barriers in Japan are clearly lower than in either the U.S. or the EU.¹¹ This is particularly true of sectors other than agriculture. Unless there is irrefutable evidence that proves otherwise, therefore, we can say that among the world's major trading nations, Japan is one of those with the lowest trade barriers. Once matters are explained this way, those who still assert Japan's markets are closed turn to trade barriers other than those for which international comparisons can be

readily made. They often say that various other nontariff barriers, as well as Japanese business practices, make it difficult for foreigners to participate in Japan's markets, and for those reasons the country is closed. But there are almost no attempts at international comparisons of "various other nontariff barriers" that are worth respect. Also, even if one country is strict and another is not all that strict concerning, say, animal and vegetable quarantine inspections, regulations concerning pharmaceuticals, or various kinds of safety standards, if such restrictions -- looked at from a certain viewpoint -- have a certain degree of rationality, it is not proper to criticize a country with strict regulations as "closed." Also, private business practices are like the languages, customs, manners, and religions of different countries, and they cannot be included among nontariff barriers.¹²

There are also many persons who argue that the large difference between prices of goods in Japan and in foreign countries is proof of the existence of trade barriers in Japan. The price difference reflects perhaps trade barriers concerning some food products, such as rice, beef, and dairy products, and also concerning leather products, footwear and medical/pharmaceutical products. But a general impression I get from data on price differences and from information on trade barriers is that the items of which price differences are caused by identifiable trade barriers are relatively few. Even among agricultural products, imports of fruits, vegetables, and flowers are now increasing rapidly. Tariff rates on these products are low but transportation costs are very high: much of these products are imported into Japan by air. It is only natural that, compared to countries blessed with favorable climatic conditions and ample land, the prices of these products in Japan are very high.

I think the principal cause of the price disparity inside and outside Japan is that labor and land prices in Japan are extraordinarily high. The wages (and other labor

costs) for unskilled workers in Japan are 2 to 2.5 times higher than for their counterparts in the U.S. Other major causes are the high cost of electricity -- more than double the cost in South Korea -- and high costs of retailing. Much of the reason for these high costs reflect the high costs of labor and land in Japan. If wages and the price of land in Japan were as low as those in other countries, many of the high prices at the retail level in Japan could be substantially reduced.

Another factor which may be mentioned is high levels of consumer quality demands related to products and incidental services. Most surveys of price differences of products between Japan and other countries do not carefully compare prices for the same quality, specifications, and incidental services. The policy of price discrimination by foreign manufacturers of famous brand products may also be mentioned. Apparently they consider the price elasticity of demand by Japanese consumers quite low.

There are econometric studies that purport to prove that Japan's level of imports is extremely low because Japan's markets are closed. There are also quantitative studies which are said to have shown extremely high trade barriers in Japan. As far as I can see, however, the hypotheses and measuring methods these studies base their conclusions on are unrealistic and unscientific, and I find the results unconvincing.¹³

An example is a study by Robert Lawrence, which has been quoted widely as having proved by an econometric method that Japan's imports are too small and its domestic markets are closed.¹⁴ It was influential in the U.S., but the hypotheses it depended on were utterly unrealistic. One hypothesis said that the utility indifference curves of consumers (as well as producers) in all countries are identical and homothetic, and that consumers in every country consume products of various countries in a particular product group in the same proportion. To explain this in simple

terms, imagine books and magazines being produced in English, Chinese, and Japanese languages at the ratio of 7:2:1 in the world as a whole. The hypothesis is that anyone, whether in the U.S., the U.K., China, or Japan would consume (read) the English, Chinese, and Japanese books at the ratio of 7:2:1. If the value of imports calculated according to this hypothesis is lower than the actual value of imports, it is concluded that the country's markets are closed.

Looking at just passenger cars, we see that in real life people in the Scandinavian countries often use cars made by Volvo and Saab that are most suitable for the cold climatic conditions, and in the U.S. we see that large cars are preferred because they are suitable for driving long distances at high speeds through the network of wide roads. In Italy and Japan, however, where there are many hills and slopes, and where crowded conditions prevail in urban areas and roads are narrow, minicars are widely used. Because kimonos and Japanese tableware are produced only in Japan, Japanese must be self-sufficient in them.

Concerning passenger cars, moreover, there have been quantitative restrictions and/or gray measures in addition to tariffs on imports from Japan by the U.S., the U.K., France, and Italy. Domestic auto industries in these countries could not compete evenly with Japanese cars, despite fairly high transportation costs plus tariffs, and could not have held down the increase in imports of Japanese cars without quantitative restrictions on imports. This happened because the passenger cars produced in those countries were generally inferior to Japanese passenger cars in terms of price and quality. So it is only natural that foreign cars did not sell well in Japan until recently.

The above would indicate how unrealistic Lawrence's hypothesis is. I cannot help being surprised that the results of research based on such unrealistic hypotheses would have a powerful influence in the U.S. I believe whether or not a country's trade barriers are high cannot be

determined by econometric studies which depend on highly simplified models with unrealistic assumptions.

Another example I might mention is a quantitative study by Yoko Sazanami, Hidejiro Urata, and Hiroki Kawai.¹⁵ On the one hand, based on (a) import (customs) statistics, they calculated the average price by dividing the total value (CIF) by the volume of imports under a certain item in an import classification. On the other hand, based on (b) Japan's production statistics (on which the Input-Output Table is based), they similarly calculated the average price from the value and the volume of shipment for more or less the same items. They called the difference between the two average prices the price disparity between Japan and overseas, and they claimed that this price disparity showed the height of Japan's tariff and nontariff barriers. For cosmetics, for example, they found the average price of products produced in Japan (b) was about 660% higher than imported products (a). They considered that this 660% as the height of Japan's trade barriers (total of tariff and nontariff barriers) converted to a tariff rate. They concluded that the Japanese government was protecting the domestic cosmetics industry with these high trade barriers, and Japan's consumers were suffering great losses. But this conclusion is entirely wrong.

It is wrong because one cannot derive, by the above procedures, comparable prices of imports and domestically produced goods of more or less the same specifications, quality, form of packaging, etc. There are various items included under cosmetics, such as lipsticks, creams, lotions, perfumes, and hair conditioners. No matter which one of these is taken, say lipstick or cream, there are products, that are expensive as well as products that are inexpensive, within the category. The average price per kilogram has almost no significance. The principal reason for the 660% price disparity mentioned above is the difference in the product mix and in quality between imported and domestic

products.

Sazanami et al. admit that readers who believe the difference in unit price between imports and domestic products is due to the difference in quality would not agree with their analysis.¹⁶ It is not just the difference in quality which matters here. More important is the difference in the types of products and in specifications: that is, the difference in product mix.

Let me use an example to illustrate how absurd the contention made by Sazanami et al. is. When the average price is computed from U.S. customs statistics for airplanes imported in the U.S. (about 700 planes) in 1992, it was about \$5.7 million. When the average price of domestically produced airplanes (about 2,500 airplanes) is calculated from U.S. production statistics, it was about \$12.6 million in 1992. The average price of one airplane produced in the U.S. was about 120% more expensive than the average price of one imported airplane (in 1991, one domestically made airplane was 530% more expensive than one imported airplane, on average). Based on such results, Sazanami et al. would conclude that the difference in prices between domestically produced and imported products, i.e., the 120% difference, is due to tariff and nontariff barriers set up by the U.S. government to protect the U.S. domestic aircraft industry! I think anyone can see that this type of argument is totally absurd. The 120% difference in price has little to do with trade barriers, and reflects the fact that while domestic U.S. aircraft production includes many expensive aircraft, such as jumbo jets, imported aircraft include many smaller planes. The difference in price is nothing but a reflection of the different product-mix --not the difference in "quality"!-- of domestic and imported products.¹⁷

Tadahiro Sekimoto, chairman of NEC, was angered by the conclusion of Sazanami et al., which says that, concerning semiconductors, Japan has 106% tariff and nontariff barriers. He severely criticized Sazanami et al. that the price difference

between domestic-made and imported products Sazanami et al. computed simply reflected the fact that domestically produced semiconductors are relatively expensive, while imports include many inexpensive, standard products. Concerning semiconductors, he said, there are no tariff or nontariff barriers whatsoever in Japan.¹⁸

In short, no useful information on trade barriers can be derived from quantity and value statistics on imports and domestic production. To investigate the restrictive effects of tariff and nontariff barriers, one must first identify what barriers exist in individual categories, and then evaluate their restrictive effects.

5. Agricultural Imports into Japan

It was agreed in APEC that the developed nation members of APEC will achieve the objective of free and open trade by the year 2010. I was asked whether the Japanese government would include agricultural products as targets of free trade. I lack the imagination to foresee what changes will occur by 2010 regarding Japanese agriculture and agricultural policy. Concerning the next five years, or maybe seven or eight years, if asked, I would guess roughly as follows, however.

- (1) The agricultural labor force in Japan consists of small farmers and their families, working to cultivate the small pieces of land they own. There are very few workers employed in Japan's agricultural sector. It now forms only a small portion of the total labor force, and perhaps 60% or more of those who work in agriculture (farmers) are 55 years of age or older and thus have nearly no mobility for moving into other industries. While some workers in their 40s and 50s enter the agricultural industry, very few who are 30 or younger do so. This trend of a decreasing agricultural labor force and its aging will continue.¹⁹ Japanese agricultural output is expected to stagnate or decline from now on, and may decline fairly

rapidly beyond a certain time in the future. Japanese agriculture is now mainly food production, with very little nonfood items produced.²⁰

(2) In Japan, the Tokyo, Osaka, and Fukuoka axis ("center"; Sendai is being added) are relatively rich and well developed, but prefectures distant from the "center" ("periphery") have been stagnant and relatively poor. They are mostly "agricultural prefectures." From the second half of the 1960s to the early 1980s, many industrial factories were built in the "periphery" because of the abundant labor force there. Recently, however, Japanese enterprises have begun shifting production offshore to Southeast Asia and China, causing concern about employment at the factories in the agricultural prefectures. Light-industry manufactures and agricultural and fishery "specialty" products which have been produced by the "periphery" are now also facing keen competition with imports, especially those from East Asia. Hence, maintenance of agricultural income is a matter of great importance for the economy of these prefectures.

(3) The agricultural sector has powerful influence in Japanese domestic politics. The nonagriculture population has so far been sympathetic to this sector and has not shown much opposition to agricultural protection policies. Such policies are therefore expected to continue for the time being, with no major changes occurring in the near future. On the other hand, since the majority of the Japanese populace supports the maintenance of free trade, however, the strengthening of barriers against agricultural imports is unlikely.

(4) If the Japanese economy recovers from the current recession and grows at a steady rate afterward, agricultural imports will steadily increase. Japan is now

the world's largest food importing country, and the value of its food imports doubled in dollar terms from \$23.7 billion to \$47.6 billion during the seven years from 1987 to 1994. No other country among the world's major trading nations has increased its food imports so rapidly.

If the APEC objective of "free and open trade" is interpreted as the "complete removal of quantitative restrictions on imports as well as tariffs," Japan's chances of achieving that objective with respect to agricultural products over the next five to eight years are slim. Future Japanese trade policy, however, will be directed toward "freer and more open trade" including agricultural products, and food imports into Japan are likely to increase steadily in the future.

6. Success of APEC

Perhaps one could not say that APEC itself has achieved a substantial increase in trade volumes or direct investment in the seven or so years since its establishment. Yet I think between 1987~88, when APEC was first being formulated, and the present, it has achieved substantial successes in ways that cannot be readily measured.

Stated succinctly, as a multilateral deliberative "forum" targeting cooperation for development and the liberalization of trade and investment in the Asia Pacific area, APEC has also become a powerful group in promoting multilateral free trade throughout the entire world. The countries that played a key role in establishing this deliberative council are the countries of the West Pacific rim, such as the ASEAN countries, Australia, Japan, and Korea. These countries form the "core" of APEC.

The United States, though hesitant at first, from a certain point in time came to participate actively in APEC. Because of the high rate of economic growth in East Asia, and because the size of U.S. Pacific trade has now surpassed that

of Atlantic trade, it was impossible for the U.S. not to join an economic deliberative body that contained the word "Pacific" -- the name of a deliberative body that includes the countries of the western Pacific, Australia, and New Zealand naturally contain the word "Pacific." Almost the same can be said about Canada. China, meanwhile, whose participation in the WTO was not yet accepted and had little chance to play a positive role in important multilateral conferences, also enthusiastically requested to join APEC. The "three Chinas" -- China, Taiwan, and Hong Kong -- joined APEC from the Third Ministerial meeting in Seoul, the first time for all three to participate at the same time in an international conference. This was a remarkable achievement of fine Korean diplomacy, South Korea being the host country at the time.

On the initiative of U.S. President Clinton, during APEC's fifth meeting, held in Seattle in 1993, a Summit Conference --although termed "unofficial"-- was held simultaneously with the ministerial meeting. Although I know little about diplomacy, I suppose there must have been a very great significance in having the heads of state meet directly.

I remember being greatly impressed by the imaginative diplomatic conceptual capabilities of French President Giscard d'Estaing's proposal and the realization of the first "Summit" meeting at Lambouille of the heads of the leading industrial democracies in 1975. In the same year, shortly before the Lambouille Summit, the Conference on Security and Cooperation in Europe (CSCE) was held in Helsinki, attended by 32 European countries, the U.S., and Canada. The results of that conference seemed to be more advantageous for the USSR and its allies than the West. In such a situation, President d'Estaing called for a major world-scale conference on economic problems, inviting faraway Japan as well, a non-CSCE member. This meeting contributed much to information exchange and greater mutual understanding among the heads of state of the largest European countries, the U.S., and Japan, and enhanced the coherence and prestige of the West. This

was the beginning of the important "G7" meetings (G6 at first) of the leading industrial democracies. In recent years the Summits have at times been criticized as having become stereotyped, but they remain quite significant in that they allow the leaders of the principal industrial democracies to meet and discuss global economic problems.

APEC was not formulated or established in as short a period of time as the G7 Summits. It took several years to assume its current form, and its organization and functions are still undergoing change. Moreover, APEC was not the idea of a single politician but the product of participation by many statesmen and senior officials of several countries. Yet, it is the result of superb diplomatic conception. The success of APEC can be measured by the fact that many countries in the Asia-Pacific region eagerly participate in it, and that many more wish to become members, as it provides an important opportunity to exchange information and to discuss problems of common interest. The Asia and Europe Summit Meeting (ASEM) held in Bangkok in March 1996 may be taken to reflect the rising negotiation power of East Asian countries which have been promoted through APEC.

The above evaluation of the successes of APEC applies to its development during the few years to the present. But if it will remain simply a "forum" in the coming years, it will not be evaluated as being successful. The future evaluation of APEC will depend crucially on the progress made over the next few years in liberalization, facilitation, and the economic cooperation among its members.

Notes

* This paper was written for the Conference on the International Trade Policy and the Pacific Rim held under the auspices of the International Economic Association (IEA) in Sydney, Australia, from July 15 to 17, 1996. The author is Professor of Economics at Aoyama Gakuin University, and Director General, Research Institute of International Trade and Industry, MITI. He wishes to express his thanks to those concerned with trade policies and foreign affairs in the Japanese government and a number of colleagues at Aoyama Gakuin University for their kindly providing information and making comments on an earlier draft. The views stated in this paper are his personal views, however, and should not be taken as reflecting those of the Japanese government.

1. Even after the end of the Second World War, free trade was not universally favored in Japan. In the past, the left wing (Socialist Party, Communist Party, and Marxists) was always ideologically against trade (and foreign direct investment) liberalization. The influence of the left-wingers gradually declined with the growth of the Japanese economy and the development of its trade, but it was only after the collapse of the USSR that the left wing finally lost much influence. Even now, however, those related to agriculture, some politicians, and some of those in citizens' movement groups adopt a posture of basic opposition to trade liberalization.

2. Regionalism and the World Trading System, Geneva: WTO, 1995, pp. 77-91.

3. For the negative effects on world trade caused by the "hub-and-spoke" approach, see Kym Anderson and Richard Snape, "European and American Regionalism: Effects on and Options for Asia," Journal of the Japanese and International Economies, Vol. 8, 1994 (also CEPR Discussion Paper, No. 983).

4. "Regionalism and the World Trading System," op. cit., p. 1. Earlier, I thought that South Korea, as Japan, did not belong to any regional agreement, but this was wrong. It was a member of a preferential trade arrangement with six other countries of South and Southeast Asia established in 1976, which was reported to GATT under the "1979 Enabling Clause." In reality, South Korea is in a "nonpainted" part of the world, as is Japan.

5. I feel that the Japanese trade policy authorities did not pay much attention until recently to the negative effects on the world trade system caused by the "hub-and-spoke" policy of the U.S. and EU. When NAFTA was formed, it might have been felt that the new organization would promote the Uruguay Round, but I was surprised at the welcome given it by the Japanese authorities. Under the Canada-U.S. Free Trade Area Agreement reached before NAFTA, passenger cars which were produced at Honda's plant in Canada with engines made in the U.S. and exported to the U.S. were treated by U.S. customs as passenger cars produced outside of the free-trade area because of a certain interpretation of the country of origin rule. This decision was very unpleasant news to Japan. At the time NAFTA was created, therefore, I felt that the Japanese government should not have expressed its welcome, but should have requested that NAFTA be kept as open as possible to countries outside it, and said that Japan would be closely watching NAFTA's future development.

Although existing as regional agreements within APEC, the Australia and New Zealand Closer Economic Relationship Agreement (ANZCER) and ASEAN Free Trade Area Agreement (AFTA) perhaps differ from NAFTA, in that they do not appear to have significant trade diversion effects, although it is difficult to predict what will happen in the future regarding the latter agreement.

I think the Japanese trade policy authorities have not been vigilant enough to the negative effect on the world

trade system caused by the hub-and-spoke policies of the EU and the U.S.

6. The Japanese government thought from the beginning that an Asia Pacific economic deliberative body without the U.S. was out of the question, and that the effect of (2) in the text would be produced even when the U.S. is included in the organization. Viewed from the eyes of Australia during the earliest period of formulating APEC's establishment, there was the possibility, quite undesirable for Australia, that Japan and the U.S. would agree on a free-trade area.

7. My knowledge about the process of APEC's formation and its development afterward is mainly from Yoichi Funabashi, Asia Pacific Fusion: Japan's Role in APEC, Washington, D.C.: Institute for International Economics, 1995: Japanese version published by Chuo Koron-sha, 1995; and Tsutomu Kikuchi, APEC: Groping for a New Asia Pacific Order, (in Japanese) Japan Institute for International Affairs (Nihon Kokusai Mondai Kenkyujo), 1995.

8. It is perhaps needless to say that there are interest groups (protected industries, industries which can expand exports, etc.) that take advantage of this irrational mass psychology.

9. For details of this point and points hereafter, see Ryutaro Komiya, The Economics of Trade Surplus and Deficit, (in Japanese), Toyo Keizai Shinpo-sha, 1994.

10. Y. Funabashi, Asia Pacific Fusion: Japan's Role in APEC, op. cit., also contains this misunderstanding.

11. Especially high trade barriers in the U.S. and the EU are their antidumping policies. See, for example, Patrick A. Messerlin and Geoffrey Reed, "Antidumping Policies in the

United States and the European Community", Economic Journal, No.105, November 1995: Industrial Structure Council (Japan), 1996 Report on the GATT Consistency of Trade Policies by Major Trading Partners, Tokyo: Ministry of International Trade and Industry, 1996, pp.98-128.

12. Standards, approvals, quarantine systems, and other regulations often have the side effects of protecting domestic industries, and sometimes function as nontariff barriers, as they are maintained even when they have become unnecessary, or when there are other methods of accomplishing their objectives without obstructing trade. In private business, there are practices which are illegal or undesirable from the viewpoint of competition (antitrust) policy. These issues should be the subject of "facilitation" in APEC. However, competition policy differs from country to country, and it would be quite difficult to harmonize competition policy internationally.

13. For a recent survey of studies on whether or not Japan imports too little, see Yoshinobu Nakamura and Minoru Shibuya, The Closedness of the Japanese Market: A Critical Review of Econometric Studies, Studies in International Trade and Industry No. 20, Tokyo: MITI Research Institute, 1995. See also Robert Z. Lawrence, "Japan's Different Trade Regime: An Analysis with Particular Reference to Keiretsu", and Gary R. Saxonhouse, "What Does Japanese Trade Structure Tell Us about Japanese Trade Policy?" both in Journal of Economic Perspectives, Summer 1993.

14. Robert Lawrence, "Imports in Japan: Closed Markets or Minds?" Brookings Papers on Economic Activity, 1987, No. 2.

15. Y. Sazanami, S. Urata and H. Kawai, Measuring the Cost of Protection in Japan. Washington D.C.: Institute for International Economics, 1995; Japanese version: Economics of

Price Differences Inside and Outside Japan (in Japanese),
Toyo Keizai Shinpo-sha, 1996.

16. Y. Sazanami et al., op. cit., Japanese version, p.22.

17. Sazanami et al. claim that they derived large price differences between imports and domestic products under such categories as chemical machinery, computers, telecommunications equipment, and medical equipment and apparatuses. To my knowledge, however, no meaningful unit price information for these categories can be obtained from customs statistics nor from production statistics, since the types of machines and equipment, specifications, etc., are likely to differ from unit to unit.

Sazanami et al. are extremely naive at price comparison, to say the least. Agricultural products are generally thought of as more homogenous than various types of machinery just mentioned. According to a market report column in a recent newspaper, however, the price of polished rice traded on the wholesale market varies a great deal, not only by variety but also by where it is produced: the price of well-known Sasanishiki rice, widely cultivated in Japan, ranges from 29,000 yen per 60 kilograms for the product of vonuma Country, Niigata Prefecture, to 19,000 yen for the product of Kumamoto Prefecture -- how expensive, in any case! Also, in Japanese supermarkets, more delicious Taiwan bananas sell for more than twice that of bananas from the Philippines.

Obviously, these price differences have nothing to do with trade barriers, and the average price would mean little in either case.

18. Sankei Shimbun, February 22, 1995. To the best of my knowledge, Sazanami et al. have made no counter argument to this criticism.

19. There are difficulties in measuring the ratio of the

agricultural labor force to the total labor force in Japan, because an overwhelming majority of those who work in agricultural are engaged in other jobs also. The same difficulties exist in defining a concept of or measuring the mobility of labor between agriculture and other industries.

20. A noteworthy exception may be the cultivation of flower plants used for visual enjoyment. The income elasticity of demand for these products is quite high, and both domestic production and imports are increasing every year.