Japan and the Hosokawa Government: a Preliminary Post-Mortem
Parliamentary Research Service

Current Issues Brief Number 5 1994
Japan and the Hosokawa Government: a Preliminary Post-Mortem

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<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
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<tbody>
<tr>
<td>APEC</td>
<td>Asia Pacific Economic Cooperation</td>
</tr>
<tr>
<td>GATT</td>
<td>General Agreement on Tariffs and Trade</td>
</tr>
<tr>
<td>DSP</td>
<td>Democratic Socialist Party</td>
</tr>
<tr>
<td>JCP</td>
<td>Japan Communist Party</td>
</tr>
<tr>
<td>JNP</td>
<td>Japan New Party</td>
</tr>
<tr>
<td>LDP</td>
<td>Liberal Democratic Party</td>
</tr>
<tr>
<td>OECD</td>
<td>Organisation for Economic Cooperation and Development</td>
</tr>
<tr>
<td>SDPJ</td>
<td>Social Democratic Party of Japan</td>
</tr>
<tr>
<td>USDJP</td>
<td>United Social Democrat Party</td>
</tr>
</tbody>
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Y 103 = $US 1.00 Y 75 = $A 1.00
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Executive Summary

This Current Issues Brief examines the main political issues in Japan since the Japanese House of Representatives election on 18 July 1993, in particular the passage of the electoral reform bills, the resignation of Prime Minister Morihiro Hosokawa and the election of his successor.

The ruling coalition formed in the aftermath of the 1993 election was basically held together by a common desire to achieve political reform. Even so, it was not easy for the parties involved to agree on the package of reform measures which were eventually put before the Diet. Not only were there hidden agendas involved - chief of which was Ichiro Ozawa's plan to smash both the LDP and the Socialists - but also ideological and tactical considerations.

The bills required to change the election system and regulate political donations were passed relatively easily in the Lower House but only after significant concessions had been made by the Government in the Upper House, where SDPJ members initially deserted the coalition to vote with the opposition.

The difficulties experienced in obtaining this result showed up the strains within the coalition. The SDPJ, in particular, having suffered a mauling at the polls, faced the constant threat of further isolation and redundancy as a result of Ozawa's efforts to form a new conservative political force.

Nor was the LDP finding it easy to come to terms with being in opposition after so many years as the undisputed ruling party. It continued to suffer defections, although nowhere near on the scale predicted by some political commentators following its election defeat. It still remains by far the largest and best organised party and is likely to profit from any early election.

The more fundamental structural reforms necessary to overcome the longer-term problems of Japanese society, which include a thorough restructuring of the economic system and bureaucracy, are proving more difficult to institute. As opinion polls have consistently suggested, the public is more concerned about the economic situation and efforts to combat corruption in general than with reform of electoral procedures. This is particularly significant as all indicators
secure by the Diet. and to a minority budget for them not weighted towards combine forces in a 'are likely to profit election, which must be fought on the basis of existing electorate boundaries since procedures to implement the reform measures will not be completed for some time. Whether such an outcome will delay Ichiro Ozawa's 'restructuring' of the political system indefinitely remains to be seen. However, the more important casualty is likely to be continuing necessary reform in Japan.

Ironically, it was one of these issues - namely, corruption - which led to the shock resignation of the Prime Minister, revealing once again the difficulty of finding leaders in Japan who have not been tainted by 'money politics.'

The struggle to find a successor to Prime Minister Hosokawa and to craft a coalition policy framework brought out all the tensions between the coalition parties. After making important concessions which ensured the survival of the coalition long enough to secure the election of Tsutomu Hata as the new Prime Minister, the SDPJ finally walked out after discovering that Ozawa had secretly formed a new parliamentary grouping to effectively lock them out of government.

Prime Minister Hata now heads a minority government with its future secure only until the delayed budget for FY 1994/95 has been passed by the Diet. Its platform is heavily weighted towards international trade and other foreign policy issues, in particular the trade dispute with the United States and the question of support for United Nations measures against North Korea, rather than towards the domestic problems which concern the public.

It is widely anticipated that the Government will fall soon, particularly as the LDP and SDPJ may combine forces in a 'marriage of convenience.' Both parties are likely to profit from the ensuing election, which must be fought on the basis of the existing electorate boundaries since procedures to implement the reform measures will not be completed for some time. Whether such an outcome will delay Ichiro Ozawa's 'restructuring' of the political system indefinitely remains to be seen. However, the more important casualty is likely to be continuing necessary reform in Japan.
1. Background

On 18 July 1993 an election was held for the Lower House of the Japanese Diet (Parliament) which resulted in the defeat of the Liberal Democratic Party (LDP), which had ruled Japan continuously since 1955, and its replacement by an eight-party coalition.\(^1\)

The election took place against a background of public anger over links between LDP power brokers and Japanese gangsters - and money politics in general, a feeling of impotence in international affairs, economic depression and a desire (articulated mainly in political circles) for a 'restructuring' of Japanese politics.

The resulting coalition government of former opposition parties and new parties established by defectors from the LDP was established expressly to implement political (chiefly electoral) reforms. This was the only issue uniting the coalition partners.

The reform measures were passed in the Lower House, where the coalition had a majority, on 18 November, but were subsequently defeated in the Upper House, which has a different political complexion. Finally, after protracted wrangling within the coalition and between the coalition and the opposition, and concessions by the Government, the package of bills was adopted on 29 January 1994.

During this confused period the normal consideration of the budget was postponed. The economic problems exacerbated by this state of affairs, combined with the situation of political instability, highlighted the ideological and policy differences between the coalition partners. On top of this, details of financial irregularities involving the Prime Minister re-emerged. Finally, on 8 April Prime Minister Hosokawa stepped down.

For two weeks, the coalition members agonised about future policy, especially the vexed issue of a consumption tax increase, before settling on Foreign Minister Tsutomu Hata as its choice for Prime Minister. On 25 April he was duly elected in the Diet with a clear majority over the rival LDP and JCP candidates, but his triumph was short-lived. A few hours later the Social Democratic Party of Japan (SDPJ), the largest party in the coalition, walked out after they discovered that coalition eminence grise, Ichiro Ozawa, had secretly formed a new

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grouping, *Kaishin* ('Renovation'), to effectively lock them out of the coalition decision making process.

Prime Minister Hata now heads the first minority government for almost 40 years. He also heads a Cabinet composed mainly of defectors from the former ruling party. With the budget for the current fiscal year still not passed and implementation of the political reform measures still to be determined, the Government's future appears very uncertain.

This paper examines these issues and assesses their significance for Japan and the region.

<table>
<thead>
<tr>
<th><strong>Coalition</strong></th>
<th><strong>Political Parties</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>SDPJ Social Democratic Party of Japan</td>
<td>main opposition party from 1955-1993, now largest party in coalition</td>
</tr>
<tr>
<td>Shinseito (Japan Renewal Party)</td>
<td>reform conservative party split from LDP in 1993</td>
</tr>
<tr>
<td>Komeito (Clean Government Party)</td>
<td>political arm of lay Buddhist group Soka Gakkai</td>
</tr>
<tr>
<td>JNP Japan New Party</td>
<td>reform conservative party split from LDP in 1992</td>
</tr>
<tr>
<td>DSP Democratic Socialist Party</td>
<td>supported by right-wing unions</td>
</tr>
<tr>
<td>Sakigake (New Party Harbinger)</td>
<td>reform conservative party split from LDP in 1993</td>
</tr>
<tr>
<td>USDP United Social Democrat Party</td>
<td>centrist reform party</td>
</tr>
<tr>
<td>DRP Democratic Reform Group</td>
<td>Trade Union Confederation-backed party (membership presently confined to Upper House)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th><strong>Opposition Parties</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>LDP Liberal Democratic Party</td>
</tr>
<tr>
<td>JCP Japan Communist Party</td>
</tr>
</tbody>
</table>

*This table reflects the position at the time of the Diet vote in January 1994. Details of the changes which have occurred since then are given below.*
2. Reform Package

When Prime Minister Morihiro Hosokawa was finally forced to step down after only eight months in office, many commentators saw this as a failed opportunity, a return to 'business as usual.' In the end the Prime Minister was brought down by a combination of his failure to live up to his 'clean' image and the strength of the forces ranged against him. Nevertheless, his brief tenure as Prime Minister will be remembered for beginning the process of political change in Japan. The question is, will reform continue? And, linked to this, what future realignments of political forces will occur?

When Prime Minister Hosokawa was elected in July 1993, there was a widespread expectation that his government would finally put an end to the corrupt practices in political funding and electioneering which had long favoured the LDP (and, to a lesser extent, the SDPJ). In order to do this it was necessary to change both the prevailing electoral system based on multi-member constituencies, which forced intra-party rivalry and hindered inter-party competition, and the emphasis on candidates rather than policies, which necessitated spending on local support groups (koenkai).

Although, during the election campaign, the major parties all supported a form of parallel single seat/party list voting system, there was by no means unanimity as to the desirable ratio of seats. More importantly, there was considerable divergence of opinion amongst subsequent coalition members concerning the actual preferred voting method. Shinseito, for example, favoured a single ballot, with the number of votes cast in the single seat constituencies determining the number of proportional representation seats allotted to parties. The Social Democratic Party of Japan [SDPJ], on the other hand, wanted a two-ballot system as, it was argued, this would assist the smaller, less nationally-organised parties. This stance was also endorsed by the Japan New Party [JNP] and Sakigake. Corporate funding of political parties was another divisive issue, with Shinseito arguing for continuing to allow political 'donations'.

In the event, the final political reform package of the coalition - four inter-related bills - represented a compromise. Even 'strongman' Ichiro Ozawa from Shinseito was forced to back down on the voting method and ratio of seats, although he was successful in negotiating the

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2 However, both Komeito and the Democratic Socialist Party [DSP] had previously opposed such a system.

3 Komeito and Shinseito both supported a 300:200 split of electorate and proportional representation seats.
probably more significant continuation of corporate political donations, although this was made subject to review after five years.

In almost all particulars (the exception was the disclosure ceiling) the coalition proposals differed from those of the opposition LDP. The two alternatives finally placed before the Diet can be summarised as follows:4

<table>
<thead>
<tr>
<th>Coalition</th>
<th>LDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>Electoral system</td>
<td>274 single seat electorates + 226 P.R. seats *</td>
</tr>
<tr>
<td>Voting method</td>
<td>2 ballots (electorate + party list)</td>
</tr>
<tr>
<td>Basis of P.R.</td>
<td>nationwide list</td>
</tr>
<tr>
<td>Corporate political donations</td>
<td>no donations to politicians or support groups</td>
</tr>
<tr>
<td></td>
<td>corporate donations to parties to be reviewed after 5 years</td>
</tr>
<tr>
<td>Disclosure rules</td>
<td>disclosure ceiling at Y 50,000</td>
</tr>
<tr>
<td>Public funding</td>
<td>Y 41.4 billion p.a.</td>
</tr>
</tbody>
</table>

* The totals differ because the coalition sought the creation of a 500-seat Lower House, while the LDP urged a return to the historical figure of 471

3. Passage Through the Diet

When the new Diet session started, Prime Minister Morihiro Hosokawa committed his government to giving electoral reforms priority over economic and other pressing issues, and pledged to have the reform package passed by the end of the session on 15 December 1993.

Debate on the bills began on 13 October. From the outset other issues hampered the government’s tight schedule. Apart from Prime Minister Hosokawa’s planned attendance at the APEC summit in Seattle in mid-November, there was also a requirement to prepare a supplementary package of fiscal measures in November, as the three previous stimulus

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There was widespread relief when the government's election reform bills were passed by the House of Representatives on 18 November, but it was not long before they were bogged down in the House of Councillors (Upper House), which has quite a different political configuration from the Lower House.

<table>
<thead>
<tr>
<th>House of Representatives</th>
<th>House of Councillors</th>
</tr>
</thead>
<tbody>
<tr>
<td>LDP</td>
<td>228</td>
</tr>
<tr>
<td>SDPJ</td>
<td>77</td>
</tr>
<tr>
<td>Shinseito</td>
<td>60</td>
</tr>
<tr>
<td>Komeito</td>
<td>52</td>
</tr>
<tr>
<td>S Romantic and NNP</td>
<td>52</td>
</tr>
<tr>
<td>DSP</td>
<td>19</td>
</tr>
<tr>
<td>JCP</td>
<td>15</td>
</tr>
<tr>
<td>Minor parties +</td>
<td>8</td>
</tr>
<tr>
<td>independents</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>511 *</td>
</tr>
</tbody>
</table>

* This is less than the total number of seats because one Member had died. A further Member has since died and another is in gaol.

Even so, the coalition parties nominally controlled 131 of the 252 seats. However, most of the independent members were openly opposed to the package, and a further ten or more members of the SDPJ were unwilling to support all of the proposed measures.

More importantly, as veteran political commentator Eiji Tominomori pointed out at the time, three additional factors combined to produce a hardening of positions in the Upper House. Firstly, the LDP faction of Keizo Obuchi, which is dominant in the House of Councillors, having been disadvantaged by Ichiro Ozawa when he was LDP Secretary-General, wanted to exact some revenge. Secondly, the decision to open the rice market (albeit under pressure to conclude the Uruguay Round) angered many LDP and SDPJ members since the two largest parties rely heavily on rural support. Thirdly, the budget for fiscal year 1994/95 (April-March), which had been scheduled for debate as is customary practice in a week-long session at the end of December after the normal Diet session had ended, had to be delayed due to

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[5] The last Upper House election was held before the push for political restructuring had captured the public mood. The table shows the stand at August 1993. See EIU Country Profile: Japan 1993/94 (London: Economist Intelligence Unit, 1993), p. 4.
differences between the coalition parties. These had arisen over the linking of tax cuts with a rise in the consumption tax rate.\(^6\)

In order to overcome this impasse it was necessary for Prime Minister Hosokawa to seek an extension of the session for a further 40 days. Although the government had the numbers in the House of Representatives to push through the bills, it was necessary to reach some accommodation with the LDP to avoid further disruption to the government's legislative program. A failure to gain the extra time might have led to the dissolution of the Lower House as early as the end of January 1994, leading in turn to a political vacuum without necessary economic decisions having been taken.

On 15 December, the last scheduled sitting day, the LDP - with the exception of four members who later left the party - boycotted the vote on extending the session. LDP Secretary-General Yoshiro Mori called the government's tactic 'a reckless act unprecedented in Japanese democracy'.\(^7\) The LDP also refused to resume debate on the reform bills in the Upper House until the new year and then only following consideration of the budget.

In the event of the House of Councillors voting against the reform measures or delaying them for more than 60 days, the government could still pass them, under Article 59 of the Constitution, by gaining a two-thirds majority in the Lower House or a simple majority in a special joint committee of both Houses. The first of these approaches was extremely unlikely to succeed without LDP cooperation, and the second was entering uncharted waters.

When the bills were put to a vote in the Upper House on 21 January 1994, 17 members of the SDPJ voted with the LDP to ensure their defeat by 130 votes to 118. Opponents of the measures pointed out that public opinion polls suggested less support for radical reform of the electoral system than for efforts to combat corruption, a view endorsed by Nobumichi Izumi, business editor of the influential financial paper \textit{Nihon Keizai Shimbun}.\(^8\)

A flurry of meetings then took place between the Prime Minister's staff and LDP officials to break the impasse. On 25 January it was agreed to refer the matter to a special joint committee of both Houses, a move without any guarantee of success and - as noted above - without precedent. Finally, on 29 January, the last day of the extended


session, Prime Minister Hosokawa announced that he had reached agreement with LDP President Yohei Kono, and the bills were passed. In major concessions to the opposition, the compromise hammered out at the very last minute provided for an electoral system of 300 single seat constituencies and 200 seats to be filled by proportional representation. Further, it permitted politicians to accept corporate donations of up to Y 500,000 from an individual company for the next five years. Finally, the base for the proportional representation was to be eleven regions rather than the entire country. This last concession is likely to be of considerable advantage to the LDP, which still has well-established regional support networks.

4. Political Fallout

The protracted conflict over the passage of the government's political reform measures revealed how fragile the coalition was.

The largest party in the coalition, the SDPJ, was always a reluctant partner. Although long a supporter of electoral reform, its perspective was completely different (due to decades as main opposition party) from that of the new parties formed by breakaway LDP politicians. The debate in the Upper House also revealed how internally divided the SDPJ was as it fought for political survival. Already mauled in the July 1993 election, a public opinion poll conducted on 23 January 1994 showed that support for the SDPJ had subsequently fallen from 15% to 6%, while a computer simulation carried out by Nihon Keizai Shimbun based on last year's election results and the new electoral system would leave the SDPJ with only four House of Representative seats.

Further, as mentioned above, Komeito and Shinseito were both out of step with their coalition partners on the electoral system issue, while Shinseito/Komeito and the SDPJ were split on the question of implementation of the tax cut.

However, opposition to the formation of a 'new' conservative party was revealed in early March when Prime Minister Hosokawa unsuccessfully tried to reshuffle his Cabinet to get rid of Chief Cabinet Secretary, Masayoshi Takemura, President of Sakigake and an outspoken critic of coalition power-broker Ichiro Ozawa's plans.

In the meantime, Ozawa was also known to have held secret talks with former Foreign Minister Michio Watanabe, who in October 1993 launched a supra-party study group with more than 100 members from both the coalition parties and the LDP. This was seen by some observers as a possible precursor to the formation of a party based on Shinseito, Komeito and Watanabe's faction of the LDP.12

On the other side of politics, the powerful Japanese Private Sector Trade Union Confederation (Rengo) came out in support of a three-party 'restructuring' of Japanese politics. Its chairperson, Akira Yamagishi, was initially in favour of a two-party system and had urged the SDPJ to join the coalition. However, he now wanted to break the hold of Ichiro Ozawa and promoted the creation of a new party (New Liberal Party) embracing the SDPJ, Democratic Socialist Party [DSP], Sakigake and some members of the JNP, possibly under the leadership of the popular Governor of Hokkaido, Takahiro Yokomichi.13 Even though Yokomichi indicated that he intended serving out his current third term as governor, he has been courted by the Democrat group of reformists within the SDPJ under former party Secretary-General Hirotaka Akamatsu.14 It is not certain if SDPJ Chairperson Tomiichi Murayama is completely behind the proposal as he has stated publicly that he prefers a 'loosely knit multiparty system,' perhaps even embracing liberal elements from the LDP.15 Nor was it clear which side the Prime Minister would take if such a 'restructuring' took place, since he had been vacillating between reliance on his Chief Cabinet Secretary on the one hand, and Ozawa on the other.

Within the LDP, too, there was a good deal of turmoil, particularly over the disciplining of the thirteen members who voted with the government on the electoral reform package in the Lower House. Although senior party officials were critical of the fact that LDP President Yohe Kono did not expel them but only banned them from holding party office for various periods, former Prime Minister Toshiki Kaifu said that his 187-strong pro-reform faction would support the dissidents.16 Later, following their vote in support of extending the Diet session, four of the group, including former Education Minister and Chairperson of the LDP's Policy Affairs Research Council, Takeo


Nishioka, resigned from the party, intending to form a new party.\textsuperscript{17} However, despite initial fears to the contrary, there has not been a mass exodus to the new grouping and, in a by-election for an Upper House seat in Hiroshima Prefecture on 5 December 1993, former LDP mayor of Hiroshima, Kensei Mizote, easily defeated the rival SDPJ/United Social Democrat Party [USDP] and Japan Communist Party [JCP] candidates.\textsuperscript{18}

Whether the eventual outcome of the 'restructuring' process will be quite as dramatic as depicted in the accompanying cartoon from \textit{Le Monde} remains to be seen. It is unlikely, though, given the way the Japanese public mood has changed.

5. Economic Woes

Prime Minister Hosokawa came to power in July 1993 facing a number of problems which required immediate attention. Overriding them all was the need to maintain a fragile coalition of interests in order to achieve his primary goal of electoral and, more broadly, fundamental political reform. But the struggling Japanese economy also demanded attention, as did such pressing foreign policy issues as Japan's trade relationship with the United States, the North Korea nuclear question and the country's future role in the world.

With the electoral reform package finally passed, the Prime Minister was at last able to turn his attention to these matters.


Public opinion polls had consistently reflected the view that the government should give higher priority to economic measures than to political reform. In a Nikkei poll conducted on 3-5 December 1993, for example, 53.5% of respondents said that priority should be given to economic stimulus measures, while only 21.1% thought political reform more urgent. In the same poll, a two-thirds majority favoured tax cuts, while opinion on a consumption tax increase was evenly divided. Similar views had been repeatedly expressed in the media since the government came to power.

As the Nomura Research Institute suggested, 'the environment surrounding the economy in fiscal 1994 will be rather bleak'. Not only is the gap between supply and demand delaying a recovery in business confidence and corporate profits, but there is a real likelihood that the Japanese economy will experience negative growth (both nominal and real) for the first time since 1945. GDP is contracting and the economy is spiralling into deflation, a problem compounded by the bad loans situation of the Japanese banks.

The government's stimulus package introduced on 16 September 1993 gave priority to the social infrastructure - tax reductions on education and home improvements, investment tax credits for small business, expanded mortgage loans from the Housing Loans Corporation, and so forth. These measures were scarcely likely to achieve the structural reforms necessary for economic recovery. It also proposed action on 94 regulations, but in view of the fact that a recent Management and Coordination Agency report showed a total of 11,402 licenses, ordinances and reporting requirements administered by the government, this represented just the tip of an iceberg.

In the event, the economy continued to falter, and the Prime Minister was eventually forced to pledge on 17 December 1993 to devote 'fifteen unbroken months' to economic revival, using 'every possible measure - financial, fiscal, monetary and legislative'.

On 3 February 1994, Prime Minister Hosokawa announced a fourth economic stimulus package, incorporating a Y 6 trillion cut in personal

and corporate taxes and in property taxes. At the insistence of the Ministry of Finance, this was to be offset by an increase in the rate of the consumption tax - disingenuously called a 'national welfare tax' by the Prime Minister - from 3% to 7%, to come into effect from April 1997. The plan immediately came under fire from the entire SDPJ, which has opposed the consumption tax from the outset because of its regressive nature, Sakigake and USDP. The day after the announcement, the Prime Minister was dramatically forced to back down and apologise to Cabinet for not having consulted them and for having ignored advice from senior coalition officials to postpone his tax program. In a last-ditch effort to get his package through the Diet before the start of the new fiscal year and before leaving to meet US President Bill Clinton in Washington, Prime Minister Hosokawa was forced to bow to SDPJ demands that he scrap the proposed consumption tax increase. Instead, a coalition forum was to examine ways to fund the tax cuts, with a decision expected by December 1994.

Normally the budget is passed by the Lower House before the end of March so that it can take effect from 1 April, but with LDP and JCP deputies boycotting the Lower House Budget Committee session there was no prospect of meeting this timetable. Minister of Finance Hirohisa Fujii therefore proposed a provisional budget for a 50-day period and the Government finally succeeded in passing the necessary bills on the first day of the 1994/95 financial year. This was not an unprecedented move, although one with ominous portent: the government of Noboru Takeshita had been forced to resign in 1989 after adopting a similar provisional budget.

The consequence of this vacillation over how to handle the economy was a dramatic fall in the Prime Minister's popularity, from an unprecedented high of 71% in September 1993 to only 60% at year's end and 52.5% following the tax debacle. The government's approval rating, meanwhile, had plummeted to 49.7% as a result of loss of confidence in Morihiro Hosokawa's ability to lead Japan.

Major structural reforms to the Japanese economy are still needed. Although the government's new advisory panel, the Economic Reform Study Group, chaired by Federation of Economic Organizations (Keidanren) chairperson, Gaishi Hiraiwa, proposed sweeping changes to Japan's economic structure, it is going to take a major effort to


25 Age, 19.3.1994, citing a Jiji News Agency poll.
'undo' Japan's *keiretsu* (affiliated groups)\(^{26}\) or alter the distribution system. However, a start has been made with the agreement reached between the Ministry of Construction and twelve foreign countries in mid-December 1993 on arrangements to open up bidding for public works projects.\(^{27}\)

On the trade front, Japan is once more embroiled in a dispute with the United States. Ultimately, the problem arises from the trade imbalance between the two countries, a surplus in Japan's favour of $US 59.3 billion in 1993 (up 24% from the previous year).\(^{28}\) More than half of the imbalance is due to trade in cars and vehicle parts. There is more than a little irony in this state of affairs considering the US shareholding in Japanese car manufacturing firms:

<table>
<thead>
<tr>
<th>Company</th>
<th>Shareholder</th>
</tr>
</thead>
<tbody>
<tr>
<td>Isuzu</td>
<td>(GM 37.5% - top shareholder)</td>
</tr>
<tr>
<td>Mazda</td>
<td>(Ford 23.9% - top shareholder)</td>
</tr>
<tr>
<td>Mitsubishi</td>
<td>(Chrysler 10.3% - second top shareholder)</td>
</tr>
<tr>
<td>Suzuki</td>
<td>(GM 3.5% - third top shareholder)(^{29})</td>
</tr>
</tbody>
</table>

For the last two decades, both countries have been sniping at each other over the trade imbalance, Japan accurately pointing to the low level of domestic savings in the United States and its chronic budget deficits as major contributing factors. The United States, for its part, blames Japan's closed markets, stifling bureaucracy and lack of 'consumer power.' Of course, the US foreign deficit is really driven by the balance between domestic savings and investment.

On 1 February 1994, President Clinton sent US Trade Representative Micky Kantor and the Deputy Director of the National Economic Council, W. Bowman Cutter, to Tokyo to advise Prime Minister Hosokawa of American determination to achieve 'results.' On 12

\(^{26}\) On the subject of these groupings, which are widely regarded in the West as anti-competitive and hindering the opening of the Japanese market, see Paul Sheard, *Keiretsu and Closedness of the Japanese Market: an Economic Appraisal*, Working Paper Series 93-5 (Sydney: Centre for Japanese Economic Studies, Macquarie University, 1993).


\(^{28}\) On 22 March 1994, the US started including trade in services in its monthly trade report. If trade in services are taken into account (the US had a 2:1 surplus with Japan in 1992), the previously published trade balance figures require revision. See Far Eastern Economic Review, 24.3.1994, 54.

February Prime Minister Hosokawa met the US President in Washington. In response to US demands for an end to accords and a shift to 'numerical benchmarks to measure market openness' (so-called 'objective criteria,' really numerical targets - a trade policy developed by Laura D'Andrea Tyson, head of the White House Council of Economic Advisers), the Japanese Prime Minister said 'No.' The Economic Planning Agency 1994 Report had already examined in considerable detail how anti-competitive and nationalistic numerical targets are. 30 Not only does Japan no longer 'need' the United States as in the past, but this time it occupied the moral high ground.

Three days later the US Administration announced that, as Japan had failed to honour an agreement to open up its cellular phone market, 31 it would begin compiling a list of Japanese high-technology products to become subject to retaliatory tariffs. On 4 March, President Clinton issued an Executive Order reviving the so-called Super 301 (originally Section 301 of the 1974 Trade Act), which requires the President to publish a list of countries using unfair trade practices, which then become subject to mandatory retaliation after 18 months. The Japanese response was predictably to threaten to refer the matter to GATT. It had previously been supported in its stance by the Director-General of GATT, Peter Sutherland, in a speech to the Swedish-American Chamber of Commerce in which he condemned numerical targets. 32 The US Administration's call for managed trade and the threat of invocation of Super 301 had also been condemned previously in a statement by forty leading economists, including four Nobel Laureates [see Appendix].

The upshot of the confrontation between the two countries was that Prime Minister Hosokawa's stance received overwhelming domestic support, although Minister of Finance Hirohise Fujii and Minister of International Trade and Industry Hiroshi Kumagai were asked to draw up plans by the end of March 1994 to cut Japan's trade surplus. Trade and current account surpluses will probably contract in any case over the next two years as a result of cuts in tariff rates (already the lowest in the world for industrial products), increased consumer demand,


31 Actually, the situation is more complicated than the US suggested publicly. Motorola was given a share of the cellular phone bandwidth in the Seoul-Nagoya corridor in 1989 but needed to have its transmitting equipment installed by NTT's private competitor, IDO. Motorola argued that this was taking too long and that they will miss out on business when Japanese are able to own phones, instead of simply renting them, from April 1994. See Time, 28.2.1994, 22.

anticipated expansion of world trade, strength of the yen and expansion of Japanese manufacturing capacity in Asia.\textsuperscript{33}

In the final analysis, US policy will not achieve the desired results:

The Japanese know that U.S. consumers want their Toyotas and Sonys, and that U.S. companies rely on Japanese components. They know that many U.S. companies are making profits in Japan, while Japanese companies employ many Americans at their U.S. plants.\textsuperscript{34}

6. Search for a Role

Japan is still searching for an appropriate role on the world stage. It has increased its financial contributions to peacekeeping operations and despatched Self Defense Force troops overseas in non-combat roles. Although the country's experience in Cambodia was not entirely successful, peacekeepers are to remain in Mozambique and election monitors have been sent to El Salvador. A Japanese official also heads UN operations in former Yugoslavia. It remains unlikely that Japanese troops will be permitted to fulfil other than non-military peacekeeping roles. Indeed, it was promotion of a wider role which led to the forced resignation of Defense Agency Director-General Keisuke Nakanishi in December 1993.

Japan is also the largest donor of Overseas Development Assistance (ODA) in the world, even though total aid in 1992 ($US 11,330 million) represented only 0.3% of GNP, well short of the OECD Development Assistance Committee's recommended target of 0.7% of GNP. However, the government has set a target of $US 70 billion under its 1993-98 aid program, and also intends to increase the proportion of grants as opposed to loans. While new guidelines link aid to demilitarisation, environmental protection and progress towards democracy, Japan has attracted some criticism because it is the largest aid donor to both China and Burma.\textsuperscript{35}

Although there is still some hesitancy about playing a prominent role in Asia, the Japanese Ministry of Foreign Affairs reversed its earlier opposition to the Malaysian-initiated East Asia Economic Caucus, partly out of a realisation that the United States was seeking to play a dominant role in APEC. Nevertheless, there is evidence that the pro-mainland Asia position within the Ministry is once more beginning to assert itself - after a very long hiatus. Ogura Kazuo, Director-


\textsuperscript{34} Business Week, 28.2.1994, 19.

\textsuperscript{35} EIU Country Profile. Japan 1993-94, pp. 41-42.
General of the Economic Affairs Bureau in the Ministry, who has argued cogently for both recognition of a distinctive Asian way of thinking and for closer ties with Australia,\(^{36}\) can be considered representative of this position. So long has Japan's foreign policy, not to mention defence and economic policy, been dominated by its bilateral relations with the United States, that it is not commonly realised that there has always existed a tension in the Ministry of Foreign Affairs between pro-mainland Asia and pro-Western factions, heightened in the early Showa era (1929-1941) by Army-Navy rivalry. However, Japan still has a long way to go to redress the past imbalance in its foreign relations. For example, although some 50,000 foreign students are studying in Japanese universities, only 15 government-sponsored students are studying in other Asian countries, a number which has remained constant for the last 20 years.\(^{37}\)

Relations with Japan's two powerful neighbours, China and Russia, as well as with South Korea, have improved steadily over the last three to four years. Aid to China was resumed in July 1990 after a break due to the Tienanmen Square incident. In October 1993 Russian President Boris Yeltsin finally visited Tokyo after several earlier postponements due to the internal political situation in Russia. Although the 'Northern Territories' dispute was raised in discussions, Japan did not pursue the issue and, in fact, there has been some improvement in local contacts between the Kurile Islands and Hokkaido. Agreements on economic cooperation, trade, cultural exchanges and other bilateral concerns were also concluded, although shortly afterwards the issue of Russian dumping of radioactive waste at sea threatened relations. In November 1993 Prime Minister Hosokawa held successful talks with South Korean President Kim Young-Sam in Seoul.

North Korea's possible development of nuclear weapons and testing of two new medium-range missiles has alarmed neighbouring countries, including Japan.\(^{38}\) Foreign Minister Tsutomu Hata expressed Japan's opposition to the imposition of sanctions against North Korea, preferring instead to pursue the stalled bilateral talks aimed at normalising diplomatic relations with Pyongyang. The reference to the UN Security Council by the International Atomic Energy Agency


\(^{38}\) The two Koreas are themselves concerned about a resurgence of Japanese militarism and her nuclear programme.
(IAEA) of North Korea's non-compliance with the recent inspection of its nuclear facilities will test Japan's policy of openness.

7. More Political Fallout

With a stop-gap budget in place until 20 May, the spotlight in media and political circles once more shifted to the scandal-plagued Prime Minister. It was known before he came to office that, while Governor of Kumamoto Prefecture, Morihiro Hosokawa had accepted a Y 100 million loan from Tokyo Sagawa Kyubin Co, the trucking firm at the centre of last year's political scandal which brought about the downfall of LDP Vice-President Shin Kanemaru. On 15 December 1993 the Prime Minister provided a photocopied receipt for the money to the Diet Budget Committee, claiming that the loan was used to purchase an apartment in the affluent Tokyo suburb of Akasaka and to renovate his home in Kumamoto, and that it had since been repaid. However, both the LDP and JCP questioned this explanation.39

Then the March 1994 issue of the respected journal Bungei Shunju revealed details of a cosy relationship between Prime Minister Hosokawa and Sagawa Kyubin founder, Kiyoshi Sagawa, dating back to 1981, and including not only the previously exposed loan (perhaps, it is suggested, really a political donation), but also financial support for his campaign for election as Governor of Kumamoto Prefecture in 1983 and a Y 1 billion payment for renovations to the family home in Kyoto (twice the amount received by Kanemaru).40 A further scandal involved the part financing (to the tune of Y 100 million) of a holiday house for Prime Minister Hosokawa in the resort town of Karuizawa by the Seibu group within days of his granting 'controversial development approval' to the firm, and a 'cosy relationship' with Yoshiaki Tsutsumi, former head of the Seibu department store empire and Japan's richest person.41

On top of all this, it was alleged that in 1986 he bought 300 shares in the newly privatised Nippon Telegraph and Telephone, later selling 199 of them and making a Y 50 million profit. Prime Minister Hosokawa claimed that he had only arranged a loan to enable his father-in-law to buy the shares but this was disputed by Shuzo Fujiki, the investment consultant who brokered the deal.42

Prime Minister Hosokawa's rejection of demands for additional evidence relating to the first matter led to the boycott of the Diet Budget Committee by LDP and JCP members referred to above, which led in turn to the suspension of further consideration of the budget for fiscal year 1994/95. In the face of the refusal of government agencies to also hand over relevant documents, the Budget Committee took the rare step of moving to subpoena bureaucrats under Article 104 of the Diet Act and threatened to call the Prime Minister's former private secretary, Masatoshi Miyama.43

Speculation began to mount that Prime Minister Hosokawa would have to resign as the price for approval of the budget, with LDP President Yohei Kono ominously citing the 1989 precedent. On 8 April Morihoro Hosokawa informed the stunned leaders of the coalition parties and then Cabinet members of his decision to resign. According to Kyodo News Service, the following conversation took place at the crucial meeting:

Hosokawa: "I have decided to step down because of the parliamentary deadlock and I must clarify my own responsibility over my personal finances."

There followed 10 minutes of silence.

Socialist Party Chairman Tomiichi Murayama and Keigo Ouchi, President of the Democratic Socialist Party (to Hosokawa): "We want to discuss this among ourselves."

Wataru Kubo, Socialist Secretary-General to Ichiro Ozawa, co-leader of Shinseito: "What should we do?"

Ozawa: "Yes, what should we do?"

Kubo to Yuichi Ichikawa, President of Komeito: "What should we do?"

Ichikawa: "It's useless to say 'What should we do?' And it looks like we can't ask him to take back the decision now that the prime minister has made his announcement."

All: "Let's all meet at about 5 pm to decide what to do next." 44

Later that afternoon Morihoro Hosokawa called a news conference to announce his resignation. The news immediately caused a fall in share prices and led Minister of Finance Fujii and Minister of International Trade and Industry Hiroshi Kumagai to voice concerns over the effect

43 Age, 17.3.1994.

44 Reuters Report, Tokyo, 8 April 1994 (1839 AEST).
political instability could have on Japan-United States 'framework' trade talks.\(^4\)

Speculation immediately centred on Minister of Foreign Affairs Tsutomu Hata as the likely successor, although this was by no means a foregone conclusion. He had been a candidate for Prime Minister after the July 1993 election, but it was known that LDP faction leader and former Foreign Minister Michio Watanabe still had prime ministerial ambitions and was, in fact, favoured by some leading members of Shinseito. There was furthermore the distinct possibility that the coalition would split apart.

In accordance with the Constitution, Morihiro Hosokawa would anyway remain as caretaker Prime Minister until his successor could be elected by a clear majority in the Diet and formally confirmed by the Emperor.

On 9 April the coalition leaders (minus Hosokawa) met to discuss the situation. They decided to allocate a week to choosing a successor and to resume debate in the Diet on the 1994/95 budget by 18 April, the LDP having lifted its boycott of proceedings. A serious rift emerged between the SDPJ and Komeito over the need for a policy agreement before choosing a coalition candidate, with Komeito President Yuichi Ichikawa maintaining that two major foreign policy issues faced the Government: resolution of the trade dispute with the United States and the stance to be taken if the United Nations imposed sanctions on North Korea.\(^4\) The implication was that the importance of these matters required a united front.

As Japan's leadership crisis worsened, the previously mentioned split amongst the coalition parties into conservative and liberal wings became accentuated. Urged by Ichiro Ozawa the three right-wing parties - Shinseito, JNP and Komeito - formed a new grouping called Kaikaku ('Reform') which claimed some 150 supporters in the Diet.\(^5\) There was also speculation that LDP faction leader Michio Watanabe would join the coalition if he could persuade enough LDP members to leave the party. Meanwhile, the liberal parties in the coalition nominated SDPJ President Tomiichi Murayama as their prime ministerial candidate. To complicate matters further, Sakigake


\(^5\) Reuters Report, Tokyo, 9 April 1994 (1917 AEST).

\(^5\) This figure included LDP members from Watanabe's faction; the real strength of the parties was around 157.
President (and Ozawa arch-rival) Masayoshi Takemura announced that his party was willing to consider an alliance with the LDP.\textsuperscript{48}

Amid conflicting reports that Watanabe would stand for election as Prime Minister, coalition leaders were endeavouring to paper over their differences. Approval for Minister of Foreign Affairs Hata to leave for the GATT Ministerial Meeting in Marrakesh seemed to indicate that he had emerged as the likely joint candidate, a view confirmed by DSP President Keigo Ouchi, who had previously opposed him.

With the two sides seemingly agreeing in principle to nominate Tsutomu Hata, discussions on a future coalition framework continued. Chief Cabinet Secretary Masayoshi Takemura attempted to lock Ichiro Ozawa out of decision making by pushing for further meetings to be confined to the party leaders. The thrust of his proposal was to prevent a 'dual power structure' with Ozawa pulling the strings.

On 15 April five members of the Mitsuzuka faction of the LDP led by Michihiko Kano, in a move unconnected with the continuing efforts of Michio Watanabe to gather enough supporters for a bid for the prime ministership, left to form a new party (New Party Mirai).\textsuperscript{49} At the same time, Sakigake formally quit the ruling coalition, although promising to continue providing parliamentary support. Meanwhile, a draft policy document drawn up by the JNP was being considered by the rest of the coalition, the key points of which were:

1. Priority would be given to smooth passage of the 1994/95 budget.

2. Bills would be enacted to redraw electoral boundaries following the recommendations of a government panel.


4. The government would maintain the United States-Japan Security Treaty and reinforce participation in UN peacekeeping efforts.

5. Appropriate measures would be taken to reduce the trade surplus with the United States.

\textsuperscript{48} AP Report, Tokyo, 11 April 1994 (1710 AEST).

\textsuperscript{49} Reuters Report, Tokyo, 15 April 1994 (1559 AEST).
6. By the end of 1994 the government would change the tax system to increase the role of indirect taxes.

7. Deregulation of the economy would be hastened.

8. Administrative reform and decentralisation would be promoted.

9. The government would aim for early ratification of the Uruguay Round agreement and promote market reforms in the farm sector.

10. Education and women's rights would be promoted.\(^{50}\)

Three days later a further group of six LDP members resigned, this time from Watanabe's own faction, in a move designed to 'encourage' others to defect to the coalition.\(^{51}\) However, the likelihood of a mass defection appeared remote as opinion polls showed that only some 20 faction members were prepared to leave the LDP and on 19 April Michio Watanabe announced that he was abandoning his bid. To add to the confusion, three JNP members left the party after Morihiko Hosokawa's backed down on a promise to merge with Sakigake and formed the Group Seiun ('Blue Cloud').\(^{52}\)

With a *Yomiuri Shimbun* opinion poll suggesting that a clear majority of people (60.9%) favoured the election of Tsutomu Hata as Prime Minister and leading figures, such as Bank of Japan Governor Yasushi Mieno and President of the Japanese Federation of Employers Takeshi Nagano, warning of the damaging effects of the impasse on the economy,\(^{53}\) the SDPJ was still holding out against its coalition partners on an increase in indirect taxes and on security arrangements. Finally, after midnight on 22 April, SDPJ Secretary-General Wataru Kubo announced that agreement had been reached. The other coalition parties having agreed to obtain 'national consensus' before raising the consumption tax,\(^{54}\) the way was free for the election of Hata to succeed Morihiko Hosokawa.

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\(^{50}\) Reuters Report, Tokyo, 17 April 1994 (1341 AEST).

\(^{51}\) The young deputies in this group are, however, somewhat out of step with other defectors from the LDP since they favour Confucian family values and maintenance of Japanese identity over the increased internationalism pushed by Ozawa. See *Economist*, 23.4.1994, 27.

\(^{52}\) *Australian* 19.4.1994, 8; *Australian Financial Review*, 20.4.1994, 11.


\(^{54}\) Associated Press (AP) Report, Tokyo, 22 April 1994 (0239 AEST).
<table>
<thead>
<tr>
<th>Current Political Groupings</th>
<th>Diet seats</th>
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<td>SDPJ</td>
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<td>Shinseito</td>
<td>62</td>
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<tr>
<td>Komeito</td>
<td>52</td>
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<tr>
<td>Kaikaku (Reform)</td>
<td>37</td>
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<tr>
<td>parliamentary bloc created by JNP</td>
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<tr>
<td>DSP</td>
<td>19</td>
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<tr>
<td>split into pro- and anti-Ozawa factions</td>
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<td>Sakigake</td>
<td>15</td>
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<td>JCP</td>
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<td>Jiyuto (Liberals)</td>
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<tr>
<td>formed by LDP defectors from the Watanabe faction</td>
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<td>New Party Mirai (Future)</td>
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<tr>
<td>formed by LDP defectors from the Mitsuzuka faction</td>
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<td>Kaikaku no kai (Reform Group)</td>
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<td>formed in late 1993 by LDP defectors from the Mitsuzuka faction</td>
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<td>Group Seiun (Blue Cloud)</td>
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<td>formed by JNP defectors</td>
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<td>Independents</td>
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<td>Vacant</td>
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Prime Minister Hosokawa and his Cabinet formally offered their resignations to the Speaker of the House of Representatives on 25 April, paving the way for the election of his successor. In the ballot which followed, Tsutomu Hata received 274 votes in a three-way contest against LDP President Yohei Kono (207 votes) and JCP President Tetsuho Fuwa (15 votes). In the Upper House he gained 127 of the 252 votes.

Early the next day the largest party in the coalition, the SDPJ, walked out after discovering that its partners had secretly formed a parliamentary bloc which excluded it. As has been pointed out by many political observers, Ichiro Ozawa's strategy all along has been to trigger the break-up of both the Socialists and the LDP.\(^{55}\) The SDPJ's departure immediately deprived the coalition of its parliamentary majority and gave rise to renewed speculation about an

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55 Reuters Report, Tokyo, 26 April 1994 (1344 AEST).
early election, but party President Tomiichi Murayama said that the
SDPJ would still support the budget. This shock move led Prime
Minister-designate Hata to delay formation of his Cabinet. Shortly
after his formal swearing-in by Emperor Akihito on 28 April, Tsutomu
Hata made a last effort to persuade the SDPJ to remain in the
coalition, but to no avail. On the contrary, an ‘alliance of convenience’
between the LDP and SDPJ seemed possible following talks between
key parliamentary leaders of the two parties.

The new Government only controls 187 seats in the 511-seat House of
Representatives, making it the first minority government in Japan
since that of Ichiro Hatoyama in 1955. And while Prime Minister Hata
pledged to continue the reformist policies of his predecessor, his
Cabinet is mainly composed of former LDP deputies. Indeed, new
Minister of Foreign Affairs, Koji Kakizawa, who incidentally is a
director of the Japan-Australia Diet Members League, only defected
with his Jiyutu colleagues little over a week earlier.

<table>
<thead>
<tr>
<th>New Japanese Cabinet</th>
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<td>Prime Minister</td>
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<td>Home Affairs</td>
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<td>Chief Cabinet Secretary</td>
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Outlook

While there is no doubt that the 'change of mind (of the Japanese people) is irreversible,' and that reforms will occur, there are serious doubts about whether the present coalition government will preside over future reforms.

Prominent political analysts, such as Professor Rei Shiratori of Tokai University and journalist Masaya Ito, predict that Prime Minister Hata will be forced to call an early election, while the Mainichi Shimbun and Asahi Shimbun even suggested that he should go as soon as the budget was passed. The problem with calling a snap election is that the seven-member panel of academics and lawyers appointed by former Prime Minister Hosokawa to redraw the electorate boundaries is unlikely to complete its task before early October 1994. Any earlier election would therefore have to be based on the existing electorates and would inevitably favour the LDP and SDPJ and their rural constituencies.

While there is still public support for the new Government - varying between 43% and 56.5% in Mainichi Shimbun and Yomiuri Shimbun polls respectively - the overwhelming impression is that this is an administration living on borrowed time.

Whether the prospect of defeat at an early election will bring a temporary halt to Ichiro Ozawa's plans for a restructuring of the Japanese political system remains to be seen, but in the meantime he is universally regarded as the 'puppet master' (kurogo). Even Prime Minister Tsutomu Hata confessed during the last election campaign, 'Ozawa is the scenario writer. I am the actor.'

When the Diet resumes on 10 May and the budget has been passed (with the help of the opposition), attention will inevitably turn to trade friction with the United States and Japan's response to a crisis over North Korea. These are crucial issues for the Government and ones on which it has staked its political survival. If these issues prove not enough to bring down Prime Minister Hata, the expected revelations


57 AP Report, Tokyo, 29 April 1994 (1539 AEST); AFP Report, Tokyo, 30 April 1994 (1844 AEST).

of past financial irregularities almost certainly will. Perhaps, as Moir's cartoon from the *Sydney Morning Herald* suggests, the choice facing Japan is clear.

One is left with the distinct impression that the fundamental reforms of Japanese society anticipated so keenly nine months ago will be a long time coming.

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59 See *Age*, 16.4.1994, 22-23
Statement by Forty Economists on American Trade Policy

IN RESPONSE to calls in the United States for ‘managed trade’ and for actions against ‘unfair trade practices’, forty leading economists issued a statement in April which has received much attention in American newspapers and, therefore, is reprinted here in its entirety. The statement was drafted by Jagdish Bhagwati, of Columbia University, New York.

Signatories to the statement include four Nobel Laureates (Franco Modigliani, Paul Samuelson, Robert Solow and James Tobin), four former Chairmen of the Council of Economic Advisers in the United States Administration (Charles Schultze, Herbert Stein and Murray Weidenbaum, as well as Professor Samuelson), several noted international economists (such as Richard N. Cooper, W.M. Corden, Isaiah Frank, Gottfried Haberler, Peter B. Kenen, Anne O. Krueger, Robert Mundell and Raymond Vernon) and other distinguished economists (among them Robert E. Lucas, Edmund Phelps and Gustav Ranis). Among the signatories are three ‘Japan’ experts (Hugh Patrick, Gary Saxonhouse and Philip Trezise) and leading ‘technology’ experts (Claude Barfield, Richard Eckaus, Kenneth Flamm and Richard Nelson).

The list includes one lawyer, John H. Jackson, of the University of Michigan, one of the foremost experts on GATT law.

STATEMENT

Our trade policy, distinguished by three decades of leadership, is at a perilous turning point.

The possible embrace of managed trade to set up ‘results-oriented’ quantity targets to judge the openness of markets and the current use of retaliatory threats, in bilateral contexts, to open foreign markets are retrograde steps. They are not merely bad policies. They attack at its core, and will bruise fatally, the GATT-focused international trading system that brought the world economy unprecedented economic gains since the Second World War and still serves our interests.

Managed Trade

The proponents of ‘managed trade’ seek to define targets of ‘appropriate’ exports in specific sectors to foreign countries with commitments by these countries then to fulfill these targets.

The 1980s have seen a proliferation of such ‘fix-quantity’ trade arrangements, typically voluntary export restraints (VERs), in regard to our imports. If the managed-trade proponents had their way, we would have ‘voluntary import expansions’ (VIEs) for our exports to match these VERs for our imports.

* This would take us yet further in the direction of politically-determined, ‘quantity-oriented’ bilateral trade arrangements. This would undermine our efforts in the Uruguay Round which are properly focused instead on strengthening the market-focused, ‘rule-oriented’ multilateral trade regime of the GATT.

* Nor is it meaningful to ask countries to ensure target quantities of specific imports from us. They can restrain exports by enforcement. But how are they to ensure imports by their consumers?

* There is also the oft-repeated claim that the targets to be set and enforced for imports of specific items from us, especially by Japan, will reflect our ‘fair’ and ‘appropriate’ share of the (Japanese)
market. But there is generally no plausible way in which such fair shares can be estimated.

'Super-301': Prying Open Foreign Markets

Actions under Section 301 (Trade Act of 1974), now turned into Super-301 under the [Omnibus Trade and Competitiveness Act of 1988], have become an essential part of our arsenal recently. They are used to open foreign markets by alleging unfair trade and threatening retaliation.

Trade barriers have traditionally been reduced by countries trading these reductions. Section 301 actions proceed by unilaterally determining whether foreign trade practices are in violation of contractual obligations and, in cases where new disciplines are being sought by us, by demanding concessions from others without offering one's own. Naturally, only the strong can proceed in this fashion; and we are strong. But might is not right, for the world trading system and for us.

- For, when we so confront the strong, such as the European Community, we are likely to produce strongly spirited reactions, proportionate to our folly. While trade disputes will settle, the battles leave scars. The ethos spreads that the trading system is unfair. Protectionists can only find this to their advantage as they continually seek to manoeuvre the legislative and administrative processes to obtain protection.

- When we so confront the weak, they are likely to buckle under. But the danger now is that the small countries we face in trade will view our Section 301 actions as the way of the bully, reviving the image of the 'ugly American'.

- There is the distinct danger that the targets of our Section 301 efforts will satisfy our demands by diverting trade from other countries (with smaller political clout) to us, satisfying the strong at the expense of the weak. This strikes a body blow to the GATT-type rule of law. We also do not open markets efficiently this way; we divert trade.

- The retaliation that we threaten and utilize is not merely unwise. At times, it has also been GATT-illegal. This is wrong. (i) Contrary to some confusion on this subject, the GATT has the legal force of a treaty. (ii) Consequently, we are not free to raise bound tariffs on manufactured goods at will. We have nonetheless done so.

- The 1988 Act has also greatly expanded the scope of Section 301 actions. The President is urged to 'take all appropriate and feasible action within his power' to obtain the elimination of 'unreasonable' foreign trade practices. But the practices that the 1988 Act lists as objectionable are not agreed to as such by our trading partners in the GATT or in bilateral treaties. The unilateral declaration of such practices as providing us with the excuse for retribution is not calculated to produce an orderly world trading regime.

- Then again, in order for a country to demonstrate that its alleged trade barriers are being removed, it is now expected to show an increase in US imports annually over a three-year period. But trade flows, and balances, are determined (except in the very short-run period) by macro-economic factors and policies, not by changes in trade barriers.

External Payments Deficit

The desired reduction of our balance-of-payments deficit can come only from our correcting the macro-economic situation. If we spend too much, there is no escape from a corresponding payments deficit, no matter what the level of trade barriers abroad. The alleged trade barriers abroad are not the problem; their removal is not the solution.

Given the relative insensitivity of private savings to policy, a reduction of the budget deficit offers a necessary and feasible way of reducing the payments imbalance. It is also likely that, if the budget deficit declines appreciably, the alarm with which any payments deficit is viewed will also diminish, thus producing a doubly favourable effect in regard to our external payments deficit.

Question of Impatience

'But we cannot wait' is the typical refrain. 'We need results' and 'multilateralism is too slow' are variants of this theme. The enemy of a good trade policy, building anew the multilateral trade regime, is this overriding impatience.
It comes from the payments deficit. But it is illogical, as we argued, to blame trade barriers.
It also comes from an inadequate appreciation of what multilateralism has accomplished. Under GATT auspices, we successively lowered tariff barriers among developed countries down to negligible levels, including in Japan. It took over two decades and seven negotiating rounds: but it worked, exceeding all expectations. It is simply wrong to assert that multilateral methods will not work. Admittedly, they are slower, but the broader coverage and the added efficiency of trade it generally implies are well worth the price.

Presidential Leadership and Agenda

The time has come therefore for President Bush to align himself strongly on the side of multilateralism, to strengthen the GATT and to bring US trade policy into conformity with our GATT obligations.

The Presidential efforts need to be directed, not towards accommodating those who would dismantle our traditional trade policies, but rather addressing the underlying sources of concern that fuel such demands. Assault on the budget deficit and policies to raise domestic savings, investment and R & D evidently belong on this agenda. So do policies to prevent our slide into illiteracy, without which we will remain in danger of developing comparative advantage soon in unskilled-labour intensive industries no matter what else we do.

Francis Bator (Harvard)
Alan Blinder (Princeton)
Barry Bosworth (Brookings)
Ralph Bryant (Brookings)
Richard N. Cooper (Harvard)
W. M. Corden (Johns Hopkins)
Robert Crandall (Brookings)
Richard Eckaus (Massachusetts Institute of Technology [MIT])
Ronald Findlay (Columbia)
Kenneth Flamm (Brookings)
Isatah Frank (Johns Hopkins)
Gerfried Haberler (AEI)
John H. Jackson (Michigan)
Peter B. Kenen (Princeton)
Charles P. Kindleberger (MIT)
Anne O. Krueger (Duke)
Robert Z. Lawrence (Brookings)
Robert E. Lucas (Chicago)
Franco Modigliani (MIT)
Robert Mundell (Columbia)
Richard Nelson (Columbia)
Hugh Patrick (Columbia)
Charles Pearson (Johns Hopkins)
Edmund Phelps (Columbia)
Gustav Ranis (Yale)
James Riedel (Johns Hopkins)
Jeffrey Sachs (Harvard)
Paul A. Samuelson (MIT)
Gary Saxonhouse (Michigan)
Charles Schultz (Brookings)
Robert M. Solow (MIT)
T.N. Srinivasan (Yale)
Herbert Stein (AEI)
James Tobin (Yale)
Philip Trezise (Brookings)
Raymond Vernon (Harvard)
Murray Weidenbaum (Washington)