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# U.S.-Japan Economic Ties: Status and Outlook

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# U.S.-Japan Economic Ties: Status and Outlook

## SUMMARY

The U.S.-Japan relationship is a long-term one involving mutually accepted principles — regional economic and political stability; market-driven economies; and democratic systems of government. The relationship is also complex, encompassing many factors.

The United States and Japan are closely tied economically. Japan ranks third to Canada and Mexico as the largest single-country market for U.S. exports. Japan is the leading market for U.S. agricultural exports. Japan is also the second largest supplier of U.S. imports. The United States ranks as Japan's number one export market and import supplier. The two economies are also tied by financial capital flows.

Despite, or perhaps because of, the interdependence, U.S.-Japan ties have been burdened by friction for many years. In the late 1960s and the 1970s, these tensions derived from the growth in competition from Japanese imports, first in labor-intensive goods, such as wearing apparel, then later in more capital-intensive goods, such as steel and cars. Since the 1980s, as U.S. competitiveness in these industries improved and/or as Japan's competitiveness lessened, the emphasis of U.S. concerns shifted to market access in Japan for U.S.-made products, such as agricultural products, semiconductors, cars and autoparts, and insurance.

For many on the U.S. side, especially those adversely affected, the trading relationship with Japan was seen as an increasingly unfair one to the advantage of Japan, and the U.S. deficit was considered to be the result of unfair Japanese trade practices. Japan, on the other hand, argued that its growing advantage in trade was the result of the increasing competitiveness of Japanese-made products and the inability of American products to compete in Japanese markets.

In the last few years, U.S.-Japan bilateral economic ties have become less tense, although issues over imports of steel from Japan, high Japanese tariffs on rice, and market access in Japan for insurance, glass, and photo film, have caused friction to increase recently. Moreover, differences have arisen over how Japan should deal with its current economic problems that have led to anemic or even negative economic growth since 1991.

The United States and Japan work together in multilateral fora, such as the World Trade Organization (WTO) and the Asian-Pacific Economic Cooperation (APEC) forum, a fledgling regional organization.

There is a long history of congressional interest in Japan because of Japan's role as a world economic power and an important U.S. ally. Members are concerned about how trade and investment with Japan affects the United States as a whole and their constituencies in particular. These U.S.-Japan ties are frequently the subject of congressional committee oversight hearings.

## Most Recent Developments

On December 20, after meetings with Japanese officials on telecommunications trade, a U.S. negotiator expressed concern over the failure of NTT, the major Japanese telecommunications company, to lower interconnection fees. Japan and several other steel exporting countries continue to pursue a case in the WTO's Dispute Settlement Body against the U.S. decision to impose section 201 (safeguard) remedies against imports of selected steel products. The WTO dispute panel that was established to hear the case held its first hearing on October 29, 2002, a three-day meeting. Japan, the EU, Brazil, China, New Zealand, Norway, South Korea, and Switzerland have argued that the United States did not follow WTO rules in imposing the safeguard actions, a conclusion the United States strongly denies. In an unprecedented move, the Bank of Japan announced on September18 that it would buy shares of stocks held by Japanese commercial banks in an effort to shore up the latter's balance sheets and to halt the slide in the Japanese stock market. Critics charge that the move reduces the banks' incentive to deal with non-performing loans and to undertake fundamental restructuring.

# Overview of Japan-U.S. Economic Ties

The U.S.-Japan relationship is a long-term one involving mutually accepted objectives and principles — regional economic and political stability; market-driven economies; and democratic systems of government. The relationship is also complex encompassing many factors. During the Cold War, national security and defense matters largely defined the relationship. But as the threat of the Soviet Union receded and eventually disappeared and as U.S. and Japanese relations with China have changed, economic matters have become more dominant in U.S.-Japan ties.

The United States and Japan are closely linked economically. Japan is the third largest single-country U.S. export market and is actually the leading market for U.S. agricultural exports, such as corn and wheat; for U.S. crude materials, such as wood; and for U.S.-produced aircraft. Japan is also the second largest supplier of U.S. imports, including cars, consumer electronics, telecommunications equipment, and computers. The United States is Japan's largest export market and import supplier.

The two economies are also tied by financial capital flows. Japan is one of the largest sources of foreign portfolio capital (bank deposits, stocks, bonds, and other securities) and of foreign direct investment (plants and real estate) in the United States. Likewise, the United States is the largest source of foreign portfolio and direct investments in Japan.

Despite or perhaps because of the interdependence, U.S.-Japan ties had been burdened by friction for many years. In the late 1960s and the 1970s, these tensions derived from the growth in competition from Japanese imports, first in labor-intensive goods, such as wearing apparel, then later in more capital-intensive goods, such as steel and cars. Since the 1980s, as U.S. competitiveness in these industries improved and/or as Japan's competitiveness lessened, the emphasis of U.S. concerns shifted to market access in Japan for U.S.-made products, such as agricultural products, semiconductors, cars and autoparts, and insurance.

For many on the U.S. side, especially those adversely affected, the trading relationship with Japan has been seen as increasingly unfair and favoring Japan, symbolized by the imbalance in goods trade. Japan, on the other hand, has argued that its growing advantage in trade has been the result of the increasing competitiveness of Japanese-made products and the inability of American products to compete in Japanese markets.

U.S.-Japan trade friction subsided in the second half of the 1990s but differences over imports of steel from Japan, high Japanese tariffs on rice, and market access in Japan for insurance, and glass have caused friction to increase recently. But it has been Japan's poor economic performance since 1991 that has taken center stage in bilateral relations. The United States and Japan also work together in multilateral fora, such as the World Trade Organization (WTO) and the Asian-Pacific Economic Cooperation (APEC) forum, a fledgling regional organization.

There is a long history of congressional interest in Japan because of its role as a world economic power. Members are concerned about how trade and investment with Japan affect the United States as a whole and their constituencies in particular. They are also concerned about how tensions in economic relations affect the health of the U.S.-Japan alliance. U.S.-Japan economic ties have been the impetus for major trade legislation and are frequently the subject of congressional committee oversight hearings.

## Trends in U.S.-Japan Economic Ties

For many years, the U.S.-Japan economic relationship has been clouded by persistent, large imbalances. As Table 1 below indicates, the U.S. merchandise (exports and imports of goods) trade deficit with Japan was a record $81.3 billion in 2000, but in 2001 the U.S. deficit declined to $69.0 billion, and is continuing to decline in 2002, primarily because the U.S. economic slowdown dampened demand for Japanese imports.

A more inclusive measure of trade balances is the balance on the current account, which includes the balances in merchandise trade, investment income, trade in services, and unilateral transfers. According to Department of Commerce data, the U.S. current account deficit with Japan in 1999 was $87.8 billion and was $97.5 billion in 2000. In 2001, the deficit declined to $78.3 billion.

Economists generally attribute the persistent imbalances in U.S.-Japan trade to domestic savings-investment imbalances in the two countries. Japan has a relatively high savings rate that more than covers domestic (both private and government) investment requirements while the United States has a lower savings rate that does not meet U.S. domestic private and public investments needs. These imbalances are reflected in each country's current account balances with the world and with each other where Japan has consistently run surpluses while the United States has run deficits.

Other factors, such as sudden changes in foreign exchange rates, can cause short-term shifts in the trade balances. The Japanese yen depreciated in 2001 and into the beginning of 2002 in terms of the dollar, making U.S. exports to Japan more expensive and imports from Japan cheaper causing U.S. exporters and import-sensitive producers some competitiveness concerns. On January 2, 2001, the yen/dollar exchange rate was ¥114.75=$1.00. On

February 26, 2002, the rate was ¥133.88 = $1.00, a 14.5% yen depreciation. However, the yen has appreciated since then to ¥119.05 = $1.00 (Jan. 6, 2003) which may eventually cause U.S. imports from Japan to increase. Analysts have attributed the weaker dollar to foreign investors' concerns about the weakened stock market and have reduced their investments in U.S. securities.

**Table 1. U.S. Merchandise Trade with Japan, 1992-2002**

($ billions)

| Year | Exports | Imports | Balances |
|---|---|---|---|
| 1992 | 47.8 | 97.4 | -49.6 |
| 1993 | 47.9 | 107.2 | -59.4 |
| 1994 | 53.5 | 119.2 | -65.7 |
| 1995 | 64.3 | 123.6 | -59.3 |
| 1996 | 67.5 | 115.2 | -47.6 |
| 1997 | 65.5 | 121.7 | -56.1 |
| 1998 | 57.9 | 122.0 | -64.1 |
| 1999 | 57.5 | 131.4 | -73.9 |
| 2000 | 64.9 | 146.5 | -81.6 |
| 2001 | 57.6 | 126.6 | -69.0 |
| 2001* | 53.2 | 117.2 | -64.0 |
| 2002* | 47.3 | 110.3 | -62.9 |

* January-November data.

Source: U.S. Department of Commerce, Bureau of the Census. Exports are total exports valued on a f.a.s. basis. Imports are general imports valued on a customs basis.

## Japan's Economic Problems

Japan's economy has been anemic at best, and at times in decline, for most of the last 10 years. Economists and policymakers in Japan and in the United States have attributed Japan's difficulties to a number of factors. One has been the effects of the "burst" in the economic "bubble," in the early 1990s, which saw the value of land and other assets collapse. The bursting of the bubble led to serious problems for Japan's banking sector as Japanese banks held loans made in the 1980s that had been backed up by inflated real estate. These problems have dampened domestic demand. Furthermore, some analysts point to Japanese fiscal policies that have emphasized budgetary restraint and increased taxes that have also kept a lid on demand. To try to boost demand, the Japanese government has implemented a series of fiscal stimulus packages since 1992.

In the longer term, Japanese and U.S. economists point to rigid government regulations that stifle productivity in a number of sectors. The United States and others have been pressuring Japan to undertake deregulation. (See section below on deregulation.)

Recent data indicate that Japan's economic prospects are not bright.. In 2000, Japanese real gross domestic product (GDP) increased 1.5%. The Japanese Government recently reported that real GDP in January-March 2001 increased 1.0%, but declined 1.2% in the April-June 2001 quarter, 0.5% in the July-September quarter, and 1.2% in the October-December 2001 quarter, meaning that Japan is in recession. During the first quarter 2002, the GDP did not grow but increased slightly at 0.6% (2.4% annualized) during the second quarter. Independent analysts remain skeptical of the long-term prospects for the Japanese economy given other indicators showing weakness including declining business investment, negative consumer spending growth, and an unemployment rate of 5.4% in July 2002. (For more information on Japan's economic problems, see CRS Report RL30176, *Japan's "Economic Miracle": What Happened?*.)

When the Bush Administration assumed power on January 20, 2001, it indicated that, unlike the Clinton Administration, it would not publically confront Japan on its domestic economic policies but would confine its persuasion to private encouragement. It followed this approach during the first year. But continued Japanese economic problems and their possible effects on the United States and other economies have forced Bush Administration economic officials to be more public in their comments. For example, on June 25, 2002, in a speech in Minnesota, then-Treasury Secretary Paul O'Neill warned that Japan had to take action to remedy their economic problems.

# Major Issues

Besides the growing imbalance in bilateral trade, the United States and Japan confront a range of issues, any or all of which could lead to sharpened tensions. The issues include a sudden increase in steel imports from Japan and U.S. concerns over implementation of past agreements. The United States and Japan also hold regular discussions over the latter's efforts at economic deregulation and on foreign investment in Japan.

## U.S.-Japan Economic Partnership for Growth

At their June 30, 2001 summit meeting at Camp David, President Bush and Prime Minister Koizumi announced the formation of a new bilateral framework for addressing economic issues of mutual concern. The "U.S.-Japan Economic Partnership for Growth," (Economic Partnership) follows and draws from bilateral forums that previous U.S. administrations established with their counterpart governments in Japan. In each case the forum was designed to cover a broad range of complex issues.

The Economic Partnership consists of several initiatives or dialogues to include participation from subcabinet level leaders from both governments and participation from members of the business communities and other non-government sectors from both countries. The U.S.-Japan Subcabinet Economic Dialogue will provide overall direction for the Economic Partnership. Other elements of the Economic Partnership include: the

Regulatory Reform and Competition Policy Initiative (with working groups on telecommunications, information technologies, energy, and medical devices and pharmaceuticals, plus a cross-sectoral working group); the Financial Dialogue; the Investment Initiative; and the Trade Forum. Each one of these elements will be responsible for reporting to the president and the prime minister on the progress of their work.

## Steel Imports

In 1998 the United States experienced a sharp increase in imports of various types of steel products. Among the largest sources of the increases were Japan, Brazil, and Russia. U.S. imports of steel from Japan jumped nearly 162% from 1997 to 1998, according to Commerce Department data.

The surge caused the U.S. steel industry to seek remedies from the U.S. government and steel companies and labor unions filed a number of antidumping and countervailing duty cases. In August 5, 1999, the Clinton Administration announced a "steel action plan," to address concerns of the steel industry. Among other things the Administration pledged to enforce U.S. trade laws to remedy problems with antidumping and other practices by foreign steel exporters. In announcing the plan, the Administration labeled Japan as the primary source of the steel import surge in 1998. Subsequently, the United States requested bilateral talks with Japan on the steel situation to which Japan agreed, but the two countries failed to reach an agreement on what was to be done.

A number of Members of the 107$^{th}$ Congress are called for the Bush Administration to take action to curtail steel imports. In addition, Japan has raised concerns over U.S. actions to restrict steel imports from Japan and other countries and to bolster domestic producers. Steel workers and firms have cited a surge in steel imports after 1997 as a reason for financial problems they face. They have claimed that dumping, government subsidies, and general overcapacity in the world steel industry have strained their ability to compete. They pressured the Clinton Administration and now the Bush Administration as well as the Congress to take action.

The 106$^{th}$ Congress passed and President Clinton signed the "Continued Dumping and Subsidy Act of 2000" (P.L. 106-387), the so-called "Byrd Amendment," enacted on October 28, 2000. The Act requires revenues from countervailing duty and antidumping orders to be distributed to firms that have been injured by dumped and subsidized imports. On December 21, 2001, nine countries, including Japan, requested consultations with the United States as the first step in bringing their objections over the "Byrd amendment" to the World Trade Organization (WTO). The countries claim that the law violates U.S. obligations in the WTO.

In the meantime, the Bush Administration on June 22,2001, submitted a request to the U.S. International Trade Commission to investigate whether the surge in imports constitute a substantial cause or threat of "serious injury" to the U.S. industry under the section 201 (escape clause) statute. On December 20, 2001, the Commission issued its determination that domestic steel producers were being seriously injured or are threatened by serious injury from imports of a number of steel products, including some from Japan.

On March 5, 2002, President Bush announced that the United States would impose remedy tariffs on imports of selected steel products. The Administration's decision came after the U.S. International Trade Commission (USITC) determined, under the section 201 (escape clause) statute, that a surge in imports of steel products in 1998 from various countries, including Japan, were a substantial cause or threat of "serious injury" to the U.S. steel industry. In 1998, the total quantity of U.S. imports of steel products increased 35% from the year before. The volume of U.S. imports of steel products from Japan soared 171% in 1998 but has declined substantially since then. In 2001, Japan accounted for about 7% of U.S. imports of steel products.[1]

On March 6, 2002 Prime Minister Koizumi's government called the decision by the Bush Administration to impose the higher tariffs regrettable and stated that the problems of the U.S. steel industry were due to its lack of international competitiveness and not to imports. On March 20, Japan requested formal consultations with the United States through the WTO dispute settlement body, stating that the U.S. action was not in compliance with WTO rules.

On May 17, Japan notified the WTO of its intent to retaliate against U.S. safeguard measures on steel imports by imposing tariffs on imports of U.S. steel worth $4.88 million. In doing so, Japan cited Article 8 of the WTO Safeguard Agreement which allows immediate retaliation if the country imposing the safeguard actions has done so without an absolute increase in imports of the product.

On August 30, the Japanese government announced that it would withdraw its threat to retaliate because, during a review, the United States ended up excluding some steel products from the section 201 decision, including a number of products imported from Japan. Nevertheless, Japan and several other steel exporting countries are pursuing their case in the WTO's Dispute Settlement Body. The WTO dispute panel that was established to hear the case held its first hearing on October 29. Japan, the EU, Brazil, China, New Zealand, Norway, South Korea, and Switzerland have argued that the United States did not follow WTO rules in imposing the safeguard actions, an issue the United States strongly denies.

## Implementation of Agreements

Bilateral, sector-specific agreements or understandings under which Japan agrees to take measures to open its markets to U.S. products or services in various sectors in response to U.S. complaints have been a staple of the U.S.-Japan trade framework for decades. But the agreements themselves are hardly ever the end of the issue. Disputes frequently arise over whether the agreement is being implemented correctly. Recently, U.S. industry and government officials have raised concerns about lack of progress under agreements reached during the last 6 years on access to Japanese markets in several sectors, for example, insurance, flat glass and autos. The Bush Administration has indicated that ensuring compliance with these agreements is one of its trade policy priorities.

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[1] United States International Trade Commission. *U.S. Imports of Steel Products: Overall Trends by Source Country* [http://dataweb.usitc.gov/scripts/steel_monthly/].

In his March 7, 2001, testimony before the House Ways and Means Committee, USTR Zoellick indicated that the United States would continue to press Japan to restructure its economy and take measures to stimulate economic growth. In the 2001 Trade Policy Agenda/2000 Annual report, Zoellick stated that the United States would continue to monitor Japanese compliance with trade agreements.

**Insurance.** Market access in Japan for U.S. financial services has been an issue of growing importance in U.S.-Japanese relations. Financial services are heavily regulated, limiting participation by U.S. and other foreign companies and restricting entry by new domestic firms. Such has been the case with insurance. Specifically, American firms have complained that little public information is available on insurance regulations and on how those regulations are developed, thereby, making it difficult to know how to get approval for doing business in Japan. They also assert that regulations favor insurance companies that are tied to business conglomerates— the keiretsu — making it difficult for foreign companies to enter the market.

Japan is the largest insurance market in the world with the United States closely following, but foreign insurers account for only a small portion of the Japanese market. After years of negotiations, the United States got Japan to agree in October 1994 to take measures to open its market for life insurance and nonlife insurance ( fire and auto insurance). At the same time, Japan agreed to delay deregulation of the so-called third-sector insurance market, which encompasses specialty insurance coverage — such as cancer, hospitalization, nursing care, and personal accident — so as not to reduce the competitive advantages foreign firms, particularly U.S. firms, had built in this market.

At the end of 1995 and early 1996, U.S. officials and the American insurance industry were becoming concerned that Japan was reducing regulations on the third sector as well as the others contrary to the agreement. After many months, U.S. and Japanese negotiators reached agreement on December 15, 1996. Under the agreement, Japan would open life and nonlife insurance market to foreign competition and limit domestic company entry into the third sector until thirty months after it has made "substantial" progress in deregulating the life and nonlife sectors But the United States has protested that Japan has already allowed domestic companies to enter the third sector. Japan has argued that it has already made the "substantial progress" stipulated in the agreement. The two sides have failed to agree to even meet to work out their differences. On February 24 2000, the Japanese government Financial Supervisory Agency announced that it would allow Japanese life and non-life insurance companies to do business in the third sector beginning January 1, 2001.

In late August 2002, the American Council of Life Insurers (ACLI) announced that it would urge the U.S. government to seek consultations with Japan regarding favorable government treatment of Kampo, a government-owned insurance company. According to ACLI, favorable tax and regulatory treatment gives Kampo unfair competitive advantages over foreign and other domestic firms.

**Autos and Autoparts.** On June 28, 1995, the United States and Japan concluded an agreement on the sale of U.S.-made cars and autoparts in Japan. The announcement came hours before a deadline after which the Clinton Administration was prepared to impose sanctions of 100% tariffs on 13 models of Japanese-made luxury cars. The agreement covered Japanese business practices and government regulations that the United States claims prevented U.S. manufacturers from gaining larger shares of the Japanese market in three product areas: autos; original equipment and accessories for autos; and replacement autoparts. On December 3, 2000, the bilateral pact on trade in cars and autoparts expired. The United States pressed Japan to renew, but Japan resisted. On June 26, 2001, a bipartisan group of members of the House and Senate sent a letter to President Bush urging him to push for the pact's renewal during his June 30 meeting with Koizumi. President Bush reportedly raised the issue of the difficulty of U.S. exporters of cars and autoparts to penetrate the Japanese market. On July 19, Assistant USTR Wendy Cutler proposed in a meeting with the Ministry of Economy, Trade and Industry, that the United States and Japan form a bilateral discussion forum on auto trade issues under which both sides would hold regular discussions. Japan is reportedly still considering the proposal. In June 2002, the Office of the USTR indicated its concern over a sharp increase in imports of autos and autoparts from Japan and that it would be monitoring the trends closely.

**Flat Glass.** In 1995 the United States and Japan concluded an agreement to improve access of foreign flat glass producers to the Japanese domestic market. The agreement was in response to complaints by U.S. producers that they were locked out of the Japanese market which has been effectively controlled by three Japanese companies. U.S. manufacturers alleged that a combination of anticompetitive private-sector business practices and Japanese government regulations restricted entry into the market. Under the 1995 agreement the Japanese government pledged to revise building regulations to encourage the use of foreign-produced glass and to more vigorously enforce the Anti-Monopoly Law against anticompetitive practices. Private sector consumers and wholesalers pledged to broaden their source of supplies to include foreign glass. The agreement expired at the end of 1999. Negotiations for an extension of the agreement failed with the United States pressing for an extension and Japan resisting.

## Deregulation

Underlying many of the market access problems U.S. firms have with Japan are the large number of regulations that have been in place on many aspects of Japanese economic activity. Some of these regulations are a product of the immediate post-war era when Japan was rebuilding its economy. Others came later. These regulations have contributed to low productivity in some economic sectors. They have been a factor in the limited choices that Japanese consumers have had in food and other products and also have resulted in the notoriously high prices that Japanese residents must pay for what Americans would consider to be staples.

Japanese policymakers have recognized the adverse economic effects of government regulations but the difficulty has been in implementing reforms. The Economic Planning Agency of Japan released a study in November 1994 indicating the adverse productivity and price effects of regulations and calling for regulatory reform. Recent Japanese governments have promised to undertake deregulation but in many cases they run up against the powerful elements of the permanent bureaucracies of the ministries — Ministry of Finance, Ministry of Agriculture, and Ministry of Construction — that implement the regulations and that would lose authority if extensive deregulation were to take place.

Deregulation is part of bilateral discussions under the U.S.-Japan Economic Partnership for Growth initiative. The deregulation subgroup released its first report on June 26, 2002.

USTR Zoellick indicated that Japan had taken positive steps in deregulating important sectors: telecommunications, pharmaceuticals and medical devices, information technology, financial services, and energy. But he also indicated that the reforms did not quite meet the recommendations that the United States presented to Japan In October 2001.

On December 20, 2002, after meetings with Japanese officials on telecommunications trade, a U.S. negotiator expressed concern over the intention of NTT, the major Japanese telecommunications company, to raise interconnection fees. A deal reached in July 2000 whereby Japan agreed to lower fees expired at the end of 2002. The United States argues that the higher fees inhibit non-NTT telecommunications providers from participating in the Japanese market.

## Foreign Investment in Japan

The level of foreign direct investment in Japan is lower than in other fully industrialized countries. Beginning in the 1950s, the Japanese government severely restricted foreign direct investment to build up Japanese ownership in fledgling industries, such as the automobile sector. Many U.S. companies that have a large presence in Japan, such as IBM and Coca-Cola, originally established themselves before restrictions were put in place.

Although Japan has liberalized controls, foreign direct investment has remained low. Some analysts point to the high costs of establishing business in Japan that results from high price for land, especially in business centers like Tokyo. The yen appreciated sharply against the dollar since 1985, which increased costs for dollar holders. Analysts and companies that want to do business in Japan also cite Japanese government regulations that indirectly inhibit foreign investment. For example, Japan's Large Retail Store Law has protected small retail outlets from competition by imposing burdensome requirements on foreign and domestic entities that wanted to establish large, more efficient retail operations. As a result of pressure from the United States and domestic consumers, the Japanese government revised the Large Retail Store Law to ease entry. As a result, some American-owned chains, such as "Toys R Us," are becoming well-known in Japan. Japan's demand for foreign capital is not as high as the U.S. demand because of the high Japanese savings rate, and this factor probably contributes to the lower level of foreign investment in Japan.

American business officials argue that trade follows foreign investment; that is, once a foreign company has established itself abroad, it imports from the host country increasing the home country's exports. Economists have debated this notion..

The United States and Japan are pursuing talks on foreign investment. U.S. objectives in the discussions are to get Japan to increase financial incentives for foreign investment, change regulations that have made acquisitions and mergers difficult, extend the period in which investors can carryover losses for tax purposes, and change taxation on real estate to reduce the financial burden on investment. Foreign investment in Japan has increased rapidly recently. By the end of the Japanese fiscal year 2000 (Apr. 2000- Mar. 2001) the level of foreign direct investment in Japan had increased 22 % over JFY 1999 which had increased 56% over JFY 1998.

## Regional and Multilateral Negotiations

The United States and Japan have been among the most important architects of the General Agreement on Tariffs and Trade (GATT) and among the most significant members of the World Trade Organization (WTO), the successor organization to and the implementing body of the GATT. Both countries are also founding members of the Asian-Pacific Economic Cooperation (APEC) forum, a fledgling body of 21 member economies of the region.

While the United States and Japan continue to address many issues through bilateral negotiations, both countries are relying to a greater extent than in the past on the multilateral dispute settlement mechanism in the WTO. In part this trend is due to the GATT's broader coverage. As a result of the Uruguay Round agreements, the GATT (and therefore the WTO), covers a broader range of trade practices pertaining to manufactured goods and also some previously uncovered practices affecting agricultural products, services, and foreign investment. In addition, the Uruguay Round agreements helped to address fundamental weaknesses in the GATT dispute settlement mechanism — the ability of a country to veto a judgement rendered against it and the long process leading up to a judgement.

Although Japan and the United States share the WTO goal of trade liberalization, they do not necessarily agree on how the WTO and its members should get there. For example, the two countries disagreed at the November 1999 Seattle Ministerial on an agenda for a new round of multilateral negotiations. Among other things, Japan has argued that member countries' antidumping practices and policies should be reviewed, which the United States has rejected. The United States has called for early elimination of tariffs on products in a number of sectors — a move that Japan has resisted. Their disagreements arguably contributed to the failure of the meeting.

The members of APEC have agreed to the goal of establishing free trade and investment among them by 2010 for the fully industrialized countries and by 2020 for all countries. In the meantime, each member economy has submitted an action plan outlining unilateral measures it will take to liberalize and facilitate trade and investment. All members have agreed on measures to open trade and investment in the region. The United States and Japan have been the most influential economies in shaping and implementing the free trade agenda of APEC. APEC is evolving into a body that supplements, rather than substitutes for, multilateral negotiations. APEC's principles of WTO compatibility and "open regionalism" allow the forum to be a platform on which its members can develop a regional consensus on issues of mutual interest.

## The Outlook for U.S.-Japan Economic Relations

The size of their economies dictates that the United States and Japan will remain significant economic players in the world economy and important partners for one another for the foreseeable future. The scale of that importance might change over time as other countries, especially Mexico and the Asian economies, increase their strength as trading nations. Japan's share of U.S. exports has declined from about l1.0% in the early 1990s to 8.2% in 1999 as Mexico has become a more important market. Also Japan's share of U.S.

imports has dropped from 20.8% in 1987 to 12.8% in 1999 as China has become an increasingly significant source of U.S. imports.

Good indicators of the future climate in U.S.-Japan economic relations and the progress they are making on pending and upcoming issues, include the following:

- the trade imbalance — an increasing U.S. trade deficit with Japan has often led to growing tensions; economic growth and reform in Japan;
- the level of steel imports into the United States from Japan and the status U.S. steel industry antidumping cases against Japanese steel; and
- implementation of the auto and autoparts agreement.

## For Additional Reading

**CRS Products**

CRS Issue Brief IB97004. *Japan-U.S. Relations: Issues for Congress* by Richard Cronin

CRS Report RS20633. *Japan's Telecommunications Deregulation: NTT's Access Fees and Worldwide Expansion*, by Dick K. Nanto.

CRS Report RL30272. *Global Financial Turmoil, the IMF, and the New Financial Architecture*, by Dick K. Nanto.

CRS Report RS20335. *Japan's Landmark Financial Deregulation: What It Means for the United States*, by Dick K. Nanto.

CRS Report RL30176 *Japan's "Economic Miracle": What Happened?*, by William H. Cooper