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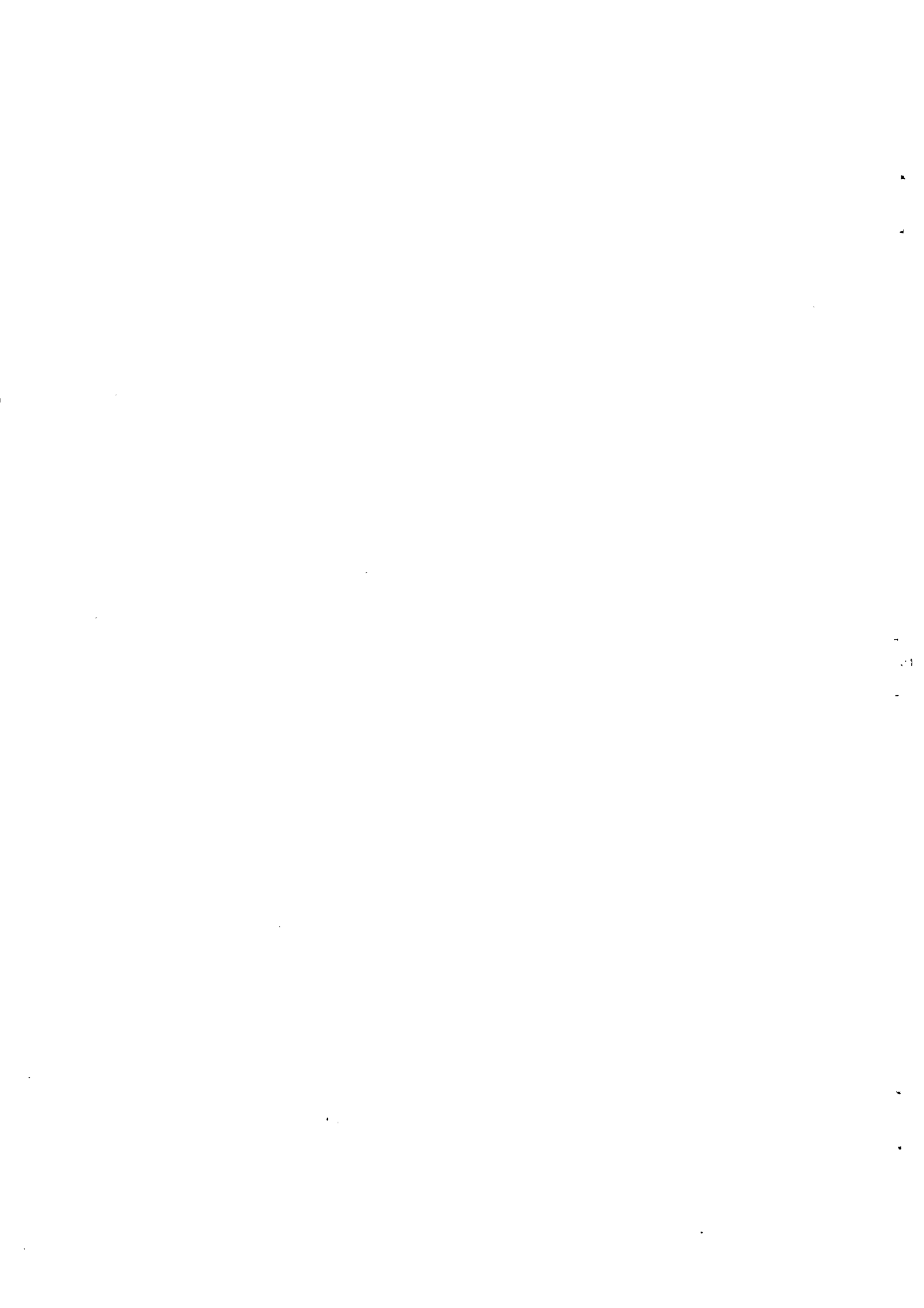
**EAST ASIAN POLITICAL ECONOMIES  
AND THE GATT REGIME**

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## EAST ASIAN POLITICAL ECONOMIES AND THE GATT REGIME

Some scrutators of international trade relations contend that the GATT regime is poorly suited to organizing trade between the political economies of East Asia and the rest of the world. They contend that the East Asian political economies operate fundamentally differently from the national political economies of North America and Europe and that the GATT regime should be replaced with a managed trade regime. I explore in some detail the fit between the East Asian political economies and the GATT regime. I argue that the East Asian political economies are indeed different, but that the differences are of degree, not kind, and that the differences continue to diminish. Hence, since competitive advantage in East Asia today lies more in firm strategy and industrial organization than in state policy and since global interdependence is changing East Asian state policy preferences, I argue that the GATT regime can adequately organize trade relations with Japan, Korea, and Taiwan. Nevertheless, additional rule creation within the GATT regime will be needed for that judgment to be correct in the future.

The norms, rules, and procedures of the GATT regime are guided by six underlying principles: reduction of trade barriers, nondiscrimination, fair trade, multilateralism, reciprocity, and economic development. These principles

guide the rules and operating procedures of the GATT regime. These principles date to the very founding of the regime at the Bretton Woods and Havana conferences of the 1940s. Furthermore, they have afforded the enlargement of the regime to 103 members and growth of the regime rules. The GATT members wrote new rules, especially regarding nontariff barriers, in the Tokyo Round and are writing new rules regarding intellectual property, foreign direct investment, standards harmonization, and trade in services in the Uruguay Round.

Nevertheless, the GATT regime's underlying principles bear the stamp of the original framers: American and British policymakers educated in neo-classical economic theory and steeped in internationalist commercial and diplomatic traditions. They believed that free trade produced greater wealth and resource efficiency and that a minimalist government was best for an economy. The East Asian political economies challenge these assumptions.

I ground the discussion in theory about national political economy, then analyze the Japanese, Korean, and Taiwanese political economy with respect to the principles of GATT--reduction of trade barriers, nondiscrimination, fair trade, multilateralism, reciprocity, and economic development.

East Asia and Types of National Political Economy

A rich literature regarding comparative political economy has been written over the past 15 years, affording this study with theory and empiry. Hence, in a theoretically-grounded way, we can explore the similarities and differences of the political economies of East Asia with those of North America and Europe.

National political economies may be differentiated according to two fundamental dimensions--polity and economy.<sup>1</sup> Polity refers to the structure and process of policymaking. A polity may be pluralist, corporatist, or statist in terms of how policy decisions are made. Economy refers to ownership of production. An economy may be characterized by private ownership, public ownership, or mixed ownership of production. All national political economies may be plotted along these two continua.

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In order to classify polities, we ask three questions:

- (1) Can the state formulate policy goals independent of particular groups within its own society?
- (2) Can the state change the behavior of specific firms?

(3) Can the state directly change the structure of the society in which it operates?<sup>2</sup>

Negative answers suggest a "weak" state (pluralist); positive answers suggest a "strong" state (statist). A pluralist polity (e.g., the United States) is characterized by a de-centralized government and de-centralized, but concentrated, interest groups. Political power is fragmented and dispersed. Specific policy issues bring specialized, powerful interest groups to the policy process. Pluralist states are relatively incapable of formulating policy goals independent of these particular societal groups, thereby earning their "weak" label. A statist polity, on the other hand, (e.g, China) is characterized by a centralized government and de-centralized and unconcentrated interest groups. Interest groups minimally influence policy outcomes; the state acts independently, thereby earning its "strong" label. Of course, policy conflict persists, but it largely occurs within the state government, not within society. In the corporatist political economy (e.g., Germany), interest groups are relatively centralized and concentrated. Policy is the result of continuous bargaining among state and interest group actors; policy is cooperatively achieved.<sup>3</sup>

In order to classify economies, the question: Who owns the means of production? In a private ownership economy (e.g, the United States), private firms own all or most production capability within a state. In a public

ownership economy (e.g., pre-Perestroika Soviet Union), the state owns all production capability. In a mixed economy (e.g., France), production capability is owned by both the state and private firms. Most political economies of the world are of this mixed ownership type.

How should the East Asian states of Japan, Korea, Taiwan be classified? Japan, Korea, and Taiwan are corporatist, mixed ownership political economies. (Though not under study here, China is a statist, public ownership political economy.<sup>4</sup> By this classification, Japan, Korea, and Taiwan are similar to the political economies of western Europe. However, East Asian corporatism differs from European corporatism in important ways. Furthermore, despite broad similarities, the Japanese, Korean, and Taiwanese political economies must be differentiated.

Throughout much of the post-war era, Japanese ownership of productive capabilities was mixed between public and private. The Japanese government owned substantial or all productive capability in energy, transportation, tobacco, and telephone until the 1980s.<sup>5</sup> Japanese private firms owned productive capability in agriculture and manufacturing. Most of the Western European states have had more public ownership of production capability than has Japan.<sup>6</sup> On the economy dimension, then, Japan does not differ from the norm of advanced industrialized countries. However, Japan does differ in interesting and important ways on the polity dimension.

Japan is a corporatist political economy, but it is a distinctly Japanese brand of corporatism. The antecedents of Japanese corporatism emerged during the Meiji Era of 1868-1912. Stunned by the power and technological capability of the West as announced in the person of Admiral Perry, Emperor Mutsuhito and the military *samurai* sought to make Japan a military power which could match Europe and America.<sup>7</sup> The *samurai* sought to learn Western technology and business techniques. They provided leadership, administrative skills, and capital and thereby they, not the petty merchants, became the dominant economic class. The *samurai* led Japan toward phenomenal economic growth and technological advancement during this era.

Japanese corporatism may be explained with reference to Japanese cultural traditions, i.e., the nature of authority in Japanese society. Thomas Roehlen explains that

authority, skillfully wielded, seeks (1) to shift responsibility for control downward to lower level groups where compliance is generated and where control is greater, (2) to maintain a balance among such groups so that they continue to participate in the general political framework, (3) to warn about consequences and seek to publicize potential dangers to efforts to gain general understanding and participation, (4) to avoid public conflict (including legal entanglements and ideological debates), and (5) to the degree possible, to avoid the application of coercive force so that legitimacy is preserved.<sup>8</sup>

Decision-making authority is very diffuse throughout the Japanese polity. Decision-makers discuss and bargain continuously in order to build consensus around a particular



position. Says Karel van Wolferen in his *Enigma of Japanese*

*Power:*

Statecraft in Japan is quite different from in Europe, the Americas and most of contemporary Asia. For centuries it has entailed a balance between semi-autonomous groups that share in power. Today, the most powerful groups include certain ministry officials, some political cliques and clusters of bureaucrat-businessmen. There are many lesser ones, such as the agricultural cooperatives, the police, the press and the gangsters. All are components of what we may call the System in order to distinguish it... from the state. No one is ultimately in charge. The semi-autonomous components, each endowed with discretionary powers that undermine the authority of the state, are not represented by any central body that rules the roost.<sup>9</sup>

According to Katzenstein, a central characteristic of corporatism is as an "ideology of social partnership."<sup>10</sup> The Japanese ideology of social partnership has been defined by Japanese self-perception of the national security vulnerability of their country. An archipelago country with few natural resources, threatened by land powers China and Russia, defeated in war and challenged in peace by the industrial and technological power of the United States, the Japanese nation emerged from the second world war seeking to secure its territory, economy, and people from external threat. The great Meiji Era recalled, a national consensus supported the "developmental state."<sup>11</sup> The Japanese developmental state employed the policy tools of government to help promote the achievement of the national goals of economic growth, technological advance, and natural (especially energy) resource risk management.

The Japanese developmental state, however, was neither statist in polity nor public ownership in economy, neither authoritarian in its politics nor command in its economics. The developmental state accepted the logic of capitalist competition, but sought to shape a national political economic environment which would afford industrial catch-up in the world economy. Government would not be chary to intervene in markets, but would do so in order to promote market behavior.<sup>12</sup> The goal was to shorten the industrialization process, to compress into years what had taken decades in Europe and North America. The mission of the Japanese central government bureaucracy, then, was not only to regulate industry (as did their counterparts in other advanced industrialized countries) but also to promote industry.<sup>13</sup> Because it regulated and promoted the manufacturing industries central to Japanese industrialization, the Ministry of International Trade and Industry (MITI) became the primary institutional arm of the developmental state.

MITI "can bend and shape the market" in Japan by (1) articulating a long-term vision of industries under its jurisdiction, (2) building consensus among political, business, and labor groups, (3) setting sectorial priorities, (4) allocating subsidies and facilitating financial flows to priority sectors, (5) protecting infant industries, (6) encouraging adjustment to industrial change, (7) guiding investment strategies, (8) regulating excessive

competition, (9) promoting exports and mediating trade problems, and (10) reducing firm risks and diffusing costs.<sup>14</sup> MITI had generally succeeded (despite occasional mistakes<sup>15</sup> because Japanese corporatism affords cooperation among business, labor, and government groups through processes of consensus-building and perpetual bargaining which pattern all Japanese political, economic, and social life.<sup>16</sup>

Yet, as Aoki and Friedman emphasize, Japanese competitiveness in international markets and its vigorous national economic growth ultimately rests on the micro-level behavior of its firms.<sup>17</sup> Japanese firms compete so well because of their organizational structures and capabilities--flatter decision-making hierarchies than common in North America and Europe, better integration of production engineering and processes into management, constant product innovation, and tightly linked supply, distribution, and capital networks (*keiretsu* relationships). The structure and process of business in Japan is a key feature of the distinctive Japanese brand of corporatism.

The political economies of Korea and Taiwan are broadly similar to the political economy of Japan.<sup>18</sup> Korea and Taiwan have been shaped by forces similar to those that shaped Japan. Korea and Taiwan are both relatively small geographically and natural resource poor. Both emerged from the second world war with intense territorial and military threats to their national security. Both depended upon

American military and diplomatic protection and foreign aid. Importantly, in both Korea and Taiwan, national security imperatives provided a cohesive military-industrial-governmental nexus. Political processes and structures evolved which were capable of effective (if authoritarian) economic and social policymaking and implementation. Unlike the political economies of Latin America, the Korean and Taiwanese states made public policies which provided stable and predictable environments for business.<sup>19</sup>

Too, Korea and Taiwan have been mightily shaped by Japan itself. Korea and Taiwan were colonial possessions of Japan from late in the nineteenth century until the second world war. The Japanese established political and economic institutions and infrastructures which broke the feudal traditions in each country and which provided the basis for modern development.<sup>20</sup> During the post-war era, Japan has continued to influence Korea and Taiwan: They imitated Japan to become, in Chalmers Johnson's phrase, capitalist developmental states (with government-led industrial policies)<sup>21</sup> or, in Alice Amsden's phrase, late industrializing states (which learned from the developmental experiences of England, the United States, and Germany).<sup>22</sup> Like the Japanese state, the Korean and Taiwanese states sought to compress the period of industrial development.

The economies of Korea and Taiwan, though broadly of the mixed ownership type, nevertheless differ significantly. The Korean economy resembles the Japanese economy: Most

production occurs in the highly concentrated private sector which is dominated by a few *zaibatsu*-like firms called *chaebol*. The Taiwanese economy, on the other hand, was dominated until the 1970s by a small number of publicly-owned corporations. During the past twenty years, however, the private sector has come to dominate the economy and the government has been privatizing the large public corporations.

The Korean and Taiwanese governments have intervened aggressively into markets, especially since the early 1960s. During much of this period, the polities of Korea and Taiwan have been between statist and corporatist, though gradually moving toward corporatist. In the Economic Planning Board and the Ministry of Trade and Industry, Korea has its institutional equivalent to Japan's MITI. In its Council for Economic Planning and Development and Ministry of Economic Affairs, Taiwan has its institutional equivalent to Japan's MITI. The Koreans and Taiwanese also have mirror institutions to Japan's export promotion institution, the Japan External Trade Organization--the Korean Trade Promotion Corporation and the China External Trade Development Council. These institutions have been the powerful institutional arms of state-led industrial policy in Korea and Taiwan. Yet, economic development has led to the rise of powerful business interest groups and the emergence of nascent labor, consumer, and other social interest groups in both countries.<sup>23</sup> Korea and Taiwan are

increasingly looking like the familiar corporatist states of Europe.

#### Reduction of Trade Barriers Principle

A principle underlying the GATT regime is that trade barriers should be reduced in the world economy. Motivated by the gains from free trade which Anglo-American comparative advantage theory postulated, the American and British framers of the GATT committed contracting parties to eliminate (with some exceptions) quotas and to progressively reduce tariff levels. However, the intellectual and policy commitment in East Asia to the reduction of trade barriers in the world economy has been limited. Recalling Meiji Japan, Hunsberger explains that

Japan did not move very far toward theoretical or doctrinal free trade, which was being practiced by Britain, then the world's greatest trading nation and Japan's leading trade partner. A few doctrinaire free traders appeared in Japan, but even some of these later turned protectionist, and the influence of free-trade ideas was minimal. When a Western economic theory did attract a significant following, it was the theory of Friedrich List, the German economist who stressed protection of infant industries during industrialization.<sup>24</sup>

During the late 1800s and due to the unequal treaties which had been forced on Japan by the West, Japanese tariff rates, however, tended to be low. Since the Meiji government lacked the tariff policy tool, it stimulated industry with low interest loans, technical assistance, and government procurement preferences. The antecedents of the modern activist Japanese government thus lie here. Furthermore,

beginning in 1899 and until foreign pressures re-emerged in the 1950s, Japanese tariffs were progressively raised.<sup>25</sup>

Japan acceded to the GATT in 1955. The United States shepherded the Japanese accession through with the 35 members, despite the opposition of many European states. Europeans feared Japanese exports and criticized Japanese import barriers. The one-third tariff cut negotiated as part of the GATT accession was significant, but was the first Japanese tariff cut of the century and left many high tariffs. Despite the Japanese 40% cut in the Kennedy Round, tariffs remained higher than the other advanced industrialized countries until 1972. In that year, the Japanese promulgated a unilateral 20% tariff reduction which made Japanese tariff levels similar to the rest of the OECD countries.<sup>26</sup> By 1987, the overall weighted-average tariff rate was 6.2% in Japan while it was 3.3% in the United States. By sector, manufactures tend to have low tariffs in Japan. The highest Japanese tariff rates are in food products (28.5%), agricultural products (21.8%), footwear (15.7%), and apparel (13.9%).<sup>27</sup> Quotas, too, remain in agriculture markets. Hence, though some tariff barriers and quotas (in important markets) persist, formal market barriers in Japan generally comply with GATT-established norms in the world economy.

The Korean and Taiwanese experiences with trade protection largely parallel the Japanese experience. Korean foreign trade policy has combined export promotion with

import substitution. The Korean government has employed a number of policy tools aimed at protecting domestic industries, including quotas, tariffs, and special customs duties and taxes.<sup>28</sup> Quotas have been imposed on many manufactured and agricultural goods. In 1980, general tariff levels averaged 25% and manufactures averaged 32%. However, by 1989, tariff levels dropped to about 13% generally and about 11% on manufactures.<sup>29</sup> On the other hand, tariffs have tended to be very low on natural resources and other basic inputs for manufacturing. As was the case with Japan, Korea acceded to the GATT under exceedingly generous terms. Until the 1980s, the Ministry of Trade and Industry also demanded that potential importers meet export performance requirements before being granted a license to import. Too, retail distribution by foreign-owned firms were prohibited.<sup>30</sup> Even now, trade protection lingers. Quotas were removed in 1991 on 243 agricultural products, but persist on fruits, grains, beef, pork, and paper.<sup>31</sup>

The Taiwanese government extensively employed import quotas and tariffs in order to protect infant domestic industries. In 1956, about half of import sectors faced tariffs up to 30% and the other half of import sectors faced import tariffs between 31 and 165%.<sup>32</sup> Not a GATT contracting party, Taiwan nevertheless responded to American unilateral pressure beginning in the 1970s. Overall tariff averages have now been gradually reduced to about 10%, but



agricultural commodity tariffs average more than twice that amount.<sup>33</sup>

Hence, overt trade barrier discrimination in Japan, Korea, and Taiwan has been reduced to levels generally consistent with OECD state practice. Barriers persist, especially in agricultural markets, but neither European nor North American policymakers can claim open agricultural markets.

#### Nondiscrimination Principle

The nondiscrimination principle of the GATT regime is established in a number of rules, but most importantly in the Article I most-favored-nation (MFN) commitment and the Article III national treatment commitment. The MFN and national treatment commitments establish that GATT contracting parties will treat each other equally and will treat foreign business enterprises doing business in their markets no less well than they do domestic firms. Yet, these are general commitments which are difficult to implement.

Unlike a commitment to eliminate a quota or lower a tariff, a commitment to offer national treatment runs afoul of national laws, government administrative acts, business norms, and cultural traditions. Nondiscrimination in trade policy is not achieved by the stroke of a pen on a multilateral treaty. The conflict between GATT multilateralism and national political economy is nowhere

greater than in the nondiscrimination principle. Bilateral and multilateral trade conflict in the world economy often centers on issues associated with nondiscrimination principle and rules. Since the Tokyo Round, the GATT contracting parties have attempted rule growth in order to minimize conflict in this area. GATT regime rules regarding import and export licensing procedures, government procurement, health and safety standards and regulations, tax policies, state trading practices, and multiple exchange rate systems begin to address nondiscrimination problems. Nevertheless, GATT members are currently challenged to extend the nondiscrimination principle through new rule-making into trade in services. Furthermore, foreign direct investment (export performance requirements) are being negotiated in the Uruguay Round. We should not be surprised if GATT negotiators take up competition/antitrust policy later in the 1990s. Indeed, efforts regarding nondiscrimination will continue for a very long time: The reconciliation of differences in national political economies challenges policymakers intellectually and politically.

It is regarding health and safety standards and regulations, government procurement, service trade, investment, and competition/antitrust issues that the Japanese political economy poses the greatest challenge to the GATT regime. Health and safety standards and regulations in Japan have become an infamous symbol of

Japan's resistance to imports. American makers of aluminum baseball bats tried without success in 1980 to get the Japanese baseball leagues to approve their bats for use in Japan.<sup>34</sup> The leagues refused, explaining that baseball conditions were unique in Japan and that Japanese players and spectators objected to the sound made by an aluminum bat making contact with a baseball. Negotiations including industry and government representatives from both countries left the dispute unresolved. A more recent US-Japan bilateral dispute--regarding wood products--highlighted similar problems.

Section 1302 of the 1988 Omnibus Trade and Competitiveness Act demanded that, in 1989 and 1990, the Office of the US Trade Representative name priority countries which impose trade barriers which, if eliminated, "are likely to have the most significant potential to increase United States exports...."<sup>35</sup> The legislation, the so-called "Super 301" provision, prompted USTR to name Japan as an unfair trader (along with Brazil and India) with respect to its policies regarding wood products, satellites, and supercomputers.<sup>36</sup> The dispute regarding wood products mainly concerned Japanese Ministry of Construction building codes and product standards, which discouraged the use of wood in Japanese homes and buildings, subsidized Japanese mills, and restricted access to distribution networks.<sup>37</sup> The American wood products industry is perhaps the world's most competitive. Despite the barriers it faced in Japan,

American exporters nevertheless did more than \$4 billion in sales in Japan. The Japanese response emphasized the volume of American wood products exports to the United States, which were described as "robust," "extraordinary," and "a shining star in the bilateral relationship."<sup>38</sup> The Japanese message was clear: The American industry already made a lot of money in Japan. What more did they want? The American response was equally clear: American wood products exporters could and should make much more money in Japan. Nearly a year of negotiations yielded a settlement agreement. The Japanese government agreed to change building codes to permit the use of wood products, to accept US wood grading and product standards, and to change the tariff classifications of wood products from high to low tariff classifications.<sup>39</sup>

Product standards and regulations in Korea have similarly challenged the GATT regime. Yet, again, American unilateralism has pushed Korean government policy toward nondiscriminatory policy. A May 1989 bilateral agreement (which resulted from Korean efforts to stay off of the Super 301 priority unfair trader list) requires Korean government ministries to accept internationally recognized standard and certification marks and to notify GATT of all new or amended trade-related standards and regulations which differ from international norms.<sup>40</sup> American and Korean negotiators have specified in some detail transparency requirements for regulations of the Ministry of Health and Social Affairs.

Discriminatory and/or nontransparent standards and regulations have become apparent in Taiwan as well and have recently been added to the agenda for US-Taiwan bilateral negotiations. Any Taiwanese accession to the GATT will also likely lead to Taiwanese policy change. Nevertheless, discriminatory regulations will likely become increasingly apparent as more foreign companies attempt to do business in Korea and Taiwan. Problems over standards and regulations, however, are not so vexing as to be unmanageable by the GATT regime. GATT rules are simply inadequately developed in this area. The general Article I commitment to provide national treatment is ambiguous; the Article X commitment to make standards, regulations, and administrative procedures transparent is insufficient. Though it will be an ambitious undertaking, the GATT members can write new rules concerning standards and regulations. (In the Uruguay Round, an effort has been underway regarding food standards and regulations). The negotiators may draw lessons from the experience of the European Community states, who have employed a mix of regulatory harmonization with mutual recognition.

Government procurement is similarly a problem area, despite the Tokyo Round code. The Super 301 dispute regarding supercomputers and satellites, however, indicates solutions. USTR complained to the Japanese government that, despite an 80% share of the world supercomputer market and a few sales in the Japanese private sector, American companies had sold only two supercomputers to Japanese government

agencies.<sup>41</sup> Japanese government agencies, contended USTR negotiators, had grown accustomed to receiving deep discounts from Japanese supercomputer makers (as much as 80%). These agencies did not find it in their interests to change the bidding process such that they would be paying full price. The Japanese position in the dispute was predictable: The Japanese market for supercomputers was open and had been since 1975 when computer trade was liberalized.<sup>42</sup> On the other hand, admitted the Japanese, it was "true that government procurement prices, particularly those for universities, are low. This is principally due to budgetary constraints on and special characteristics of universities, whose purposes are education, research, and academic development."<sup>43</sup> The Japanese contradicted USTR's market share figures, claiming that of 37 supercomputer purchases by government organizations (including NTT) and national universities, seven (19%) had been American machines. The Japanese charged that, on the contrary, it was the American market which was closed to Japanese supercomputer makers. They cited government policies which prohibited non-American supercomputer purchases by the Defense Department and government pressure which forced "a private university" [MIT] to cancel an agreement to purchase a Japanese made supercomputer.

Both sides were right: There was no free trade in supercomputers. After much bitter negotiation, a settlement agreement was signed in March 1990.<sup>44</sup> The Japanese

government agreed that its agencies would "throw out excessively low bids." Furthermore, the Japanese government agreed to publish the names of companies which made these low bids. The US government, for its part, made no commitment to change its policies regarding supercomputer procurement.

The satellite dispute was similarly a government procurement dispute. The American negotiators charged that Japanese government agencies and public corporations did not purchase foreign-made satellite equipment. However, there was an important difference from the supercomputer case: The Japanese Ministry of Posts and Telecommunications had publicly announced in April 1984 that it would not permit the purchase of foreign-made satellites.<sup>45</sup> This prohibition included the two largest satellite users in Japan--the quasi-government NTT and NHK, the public radio and television network. Furthermore, MPT would not grant new licenses to foreign firms desiring to sell in the Japanese private market.

Conflict between the American and Japanese industries and governments over the latter's telecommunications policies had become the hardy perennial of the 1980s, just as leather and tobacco had been to the 1970s. The American telecommunications industry complained that NTT compliance with the bilateral agreement signed under the auspices of the MOSS talks was low. In spring 1989, Motorola submitted a Section 301 petition to USTR alleging that MPT had not

complied with the MOSS agreement.<sup>46</sup> The petition resulted in telecommunications being named as a priority practice in the Super 301 announcement of May and in a June concession by MPT to expand access to the mobile telephone market in Japan.<sup>47</sup>

In April 1990, agreement was reached to bring Japanese satellite procurement policy into compliance with the GATT Tokyo Round Government Procurement Code and other GATT provisions.<sup>48</sup> The agreement opened NTT and NHK to American and foreign bidding on satellite procurement and provided for transparency in bidding procedures. The negotiators also agreed to meet annually to review implementation of the agreement. Hence, the satellite case shows that GATT rules merit more credit than they sometimes receive--noncompliance is a manageable problem for the GATT regime. The supercomputer case, on the other hand, illustrates that Japanese business practices differ from North American and European norms. Business practice issues receive more discussion below.

Trade in services is not covered by the GATT, though Uruguay Round negotiators have been working on a General Agreement on Trade in Services (GATS). GATS is a critical need of the GATT regime, for services have become by many measures a significant portion of the world economy. State policies concerning services, however, present substantial barriers to international service businesses. Building on rules and norms extant in bilateral treaties of friendship,



commerce, and navigation and in multilateral OECD and UNCTAD agreements, GATS likely will follow the model of the GATT, including the underlying principles, the rules of behavior, and dispute settlement procedures.<sup>49</sup> GATS negotiators must especially resolve problems regarding national treatment, transparency of regulations, government procurement and public monopolies, market access, and dispute settlement. All this must be done with regard to the different competitive characteristics and policy milieus of the various service sectors--financial, insurance, telecommunications, transportation, construction, etc. It is an ambitious undertaking.

Bilateral US-Japan negotiations have contributed to this process. Legal services markets in Japan, as the result of negotiations with USTR, began being opened in the late 1980s.<sup>50</sup> Too, Congress demanded in Section 1305 of the 1988 Trade Act that USTR initiate an investigation of Japanese government policies regarding American architectural, engineering, and construction services.<sup>51</sup>

In November 1988, USTR formally initiated an investigation and negotiations with the Japanese government regarding construction (as well as architectural and engineering) services.<sup>52</sup> Complaints from the American construction industry, however, were not new and USTR and Commerce Department negotiators had discussed the issue with Japanese Ministries of Construction, Transportation, and Foreign Affairs officials before the November initiation. A

previous round of negotiations had ended in May 1988 with a bilateral agreement, known as the Major Projects Arrangement, aimed at providing greater transparency in bidding procedures for the \$7 billion Kansai International Airport construction project as well as other large projects.<sup>53</sup>

The May 1988 agreement was only a beginning, not an ending, of a process to widen access to public construction projects in Japan. Negotiations in 1989 led to Japanese government commitments to curtail collusive bidding, facilitate the issuance of architectural licenses, as well as other policy changes.<sup>54</sup> Yet, complaints to the Department of Commerce and USTR from American construction, architectural, and engineering firms continued, especially with regard to the airport project.<sup>55</sup> Formal consultations regarding the implementation of previous agreements were due to begin in December 1990. American bargainers came to these meetings with enhanced credibility provided by two pieces of legislation passed by Congress during 1990 which demanded retaliatory sanctions if construction services access problems continued.<sup>56</sup>

In December 1990 and January 1991 negotiators made little progress, but President Bush and Congressional sponsors of the legislation agreed to extend the deadline as a quid pro quo for a Japanese commitment to provide financial support for the Gulf War.<sup>57</sup> Negotiations continued throughout the spring, with a settlement finally

coming shortly before the midnight 1 June 1991 deadline when sanctions would be imposed. Representatives from the Ministries of Foreign Affairs, Construction, and Transportation agreed to open 17 extant and 6 future public construction projects to American company bidding. American negotiators noted that the agreement doubled the number of public projects in Japan upon which American firms could bid.

Many Korean government procurement policies are also inconsistent with GATT rules. Korean negotiators have agreed with representatives of the US Trade Representative's Office to open government procurement to foreign bidders. Negotiations have been coordinated with the June 1990 pledge made by the Korean government to accede to the Tokyo Round Government Procurement Code. Within the context of the GATT negotiations, Korean negotiators have agreed to open some (but not all) telecommunications procurements of the Ministry of Communication and the Korean Telecommunications Authority.<sup>58</sup> Taiwan, on the other hand, overtly contravenes GATT rules: Taiwanese laws require all ministries and public corporations to buy domestically when possible.<sup>59</sup> This policy will be an important issue on the agenda in a GATT accession negotiation.

Concomitant with the Super 301 investigations against Japanese policies regarding supercomputers, satellites, and wood products, USTR announced that it would carry on long-term, wide-ranging bilateral negotiations with the Japanese

government to be called the "Structural Impediments Initiative."<sup>60</sup> The Structural Impediments Initiative (SII) was a sea change in American trade unilateralism and bilateral dispute settlement. It was unprecedented as an attempt to resolve fundamental issues of national political economy. Said the US-Japan Working Group of its mission: "[I]dentify and solve structural problems in both countries which stand as impediments to trade to balance of payments adjustment."<sup>61</sup> SII was an American initiative, but the effort became a forum for both sides to press for policy changes of the other.

Initial meetings in fall 1989 resulted in the identification of two sets of issues for negotiation. The Japanese named a broad array of American policies: savings and investment patterns, corporate investment activities and supply capacity, corporate behavior, government regulations, research and development, export promotion, education and workforce training. The Americans named a broad array of Japanese policies: savings and investment patterns, land use, distribution systems, exclusionary business practices, keiretsu relationships, and pricing mechanisms.<sup>62</sup>

Both sides identified quite specific policies. For example, the Japanese pointed to the benefits to the US economy and business competitiveness of a lower capital gains tax, the reform of certain antitrust laws, the reform of product liability laws, and the adoption of the metric system. The Americans identified suggested reform of the

consumer credit system in order to spur domestic consumption, reform of the land taxation system, rationalization of the official assessment of land values which inflated their values, and deregulation of distribution under the Large-Scale Retail Store Law which preserved the dominance of small, mom-and-pop retailers throughout Japan. Unlike previous bilateral dispute settlement, the negotiators neither alleged that a domestic industry needed protection from foreign competition nor that a foreign government was violating GATT law with protectionist domestic policies of its own. Officials at USTR understood the step that had been taken by the two countries:

We should emphasize at the outset, as we always have, that SII is a unique bilateral undertaking between sovereign governments and is an iterative process. It has, therefore, no set patterns of benchmarks. Many changes will take time to implement; and many changes, when implemented, will take time to show up in the trade balance. The results of these improvements in market access, however, should be felt relatively quickly by US industries.<sup>63</sup>

In summary, the Americans agreed to reduce the size of their government deficit, lower the capital gains tax, liberalize import restrictions on steel and machine tools, encourage private savings and reduce consumer debt, increase spending on education, and maintain liberal FDI policies. The Japanese, in summary, agreed to reform their land policies, make their standards and certification procedures more transparent, increase spending on infrastructure such as housing, roads, airports, and customs processing centers,

modify distribution systems, and ease FDI laws. Each offered to the other an ambitious wish list which, if implemented, would please many people on both sides of the Pacific. The American "commitments" have been urged by many Americans and the Japanese "commitments" have been urged by many Japanese.

SII, then, is about much more than just trade. SII represents an international political institutional invention aimed at economic cooperation which stands alongside the Bretton Woods conference, GATT multilateral trade negotiations, and Group of Seven economic summitry. Whether SII will endure as an institution or even expand as part of OECD, G-7, or GATT cooperative efforts remains to be seen.

Thus, bilateral and multilateral efforts are (slowly) leading the service policies of the East Asian states toward emerging norms of behavior in the world economy. The GATT regime, with the commitment of the GATT membership, appears to be capable of ensuring that service sector policy in East Asia substantially meets the demands of international service business.

Japan was by state policy substantially closed to foreign direct investment before 1980.<sup>64</sup> The 1980 Foreign Exchange and Foreign Trade Control Law, however, liberalized foreign investment to allow wholly owned subsidiaries as well as joint ventures. Before 1980, Japanese law forbade investment unless special, case-by-case governmental approval was offered; after 1980, Japanese law accepts

investment unless case-by-case governmental disapproval. Of course, Japanese ministries, e.g., Ministry of Finance and MITI, possess broad discretion to review, impede, or deny particular foreign direct investment transactions. Yet, thought the horror stories of the 1960s and 1970s chilled the desire of many outsiders to attempt investment into Japan, it appears that investment regulations are not a major barrier to access. A recent study by the American Chamber of Commerce and A.T. Kearney Company [management consultants] indicated that the chief problems confronted by investors doing business in Japan were (1) the high cost of business, (2) staffing problems, (3) business complexity, (4) the time needed to become profitable, and (5) the lack of understanding of Japan.<sup>65</sup> Indeed, some American firms--Avon, Chrysler, General Motors, CBS, Honeywell--have sold Japanese investments not because they were losing money but because their corporate parents needed the cash.<sup>66</sup> Investors, however, do complain about "business complexity" in Japan, which means the *keiretsu* business networks and the arcane, morass of distribution networks.

The *keiretsu* business networks are descendents of the massive, pre-war conglomerate *zaibatsu* business enterprises. The *zaibatsu* were large, privately-owned enterprises which conducted business in many different markets, from banking to all types of manufacturing. This handful of companies dominated the pre-war Japanese economy in collaboration with guidance from the state. General MacArthur and the American

occupiers took steps to break up the *zaibatsu* in order to introduce more competition into Japanese markets.<sup>67</sup> The breakup did introduce more competition, but old relationships persisted in external markets as had in internal markets: The *zaibatsu* became the six major horizontal *keiretsu* networks: Mitsui, Mitsubishi, Sumitomo, Fuyo, Dai-ichi Kangyo, and Sanwa.

Each horizontal *keiretsu* network includes a several dozen company members. The members include a large bank, financial institutions (such as insurance companies), large manufacturing companies, and a big general trading company. The companies are linked with each other through equity ownership, interlocking directorships, capital flows, and firm-to-firm communication and cooperation.<sup>fn</sup> [Yamamura28] Roughly 30-40% of the capital needs of the large manufacturing firms are met by the financial institutions of the *keiretsu*.<sup>68</sup>

Too, the *keiretsu* relationships in Japan are vertical as well as horizontal. The large manufacturing enterprises, such as Toyota, Nissan, Sony, and Hitachi, carryout most of their downstream and upstream business transactions with distributors and suppliers with whom they have long conducted business. Together, horizontal and vertical *keiretsu* still dominate the Japanese economy. Explains Mark Gerlach:

The majority of these firms rank among Japan's largest industrial, financial, and commercial enterprises. While representing only about 10 percent of the



industrial firms listed on the Tokyo Stock Exchange, as of the late 1970s, firms formally affiliated with one of the big-six groups controlled between 43 and 56 percent of total sales in natural resource sectors (oil, coal, and mining), in primary metals (ferrous and non-ferrous metals), and in cement, chemicals, and industrial machinery. Among financial institutions, commercial and trust banks affiliated with these six groups controlled 40 percent of total bank capital, and insurance companies 53-57 percent of total insurance capital. In real estate, 55 percent of total business was controlled by group members, while in distribution 67% of sales was accounted for by formal *keiretsu* member companies, primarily through general trading companies. [Too,] these percentages exclude financial and industrial firms in smaller city-bank groups, such as Daiwa, Kyowa, and Tokai, as well as the many companies affiliated with the Industrial Bank of Japan. In addition, they ignore the share of sales accounted for by the extensive network of satellite and subsidiary firm group companies control that are not consolidated in their own sales figures. Toshiba alone has about 200 related companies in Japan and below those are another 600 "grandchild" companies.<sup>69</sup>

Thus, concludes Gerlach: "The reality of contemporary Japanese industrial organization is neither complete openness nor complete insularity. Rather, it is a complex middle ground based on *preferential* trading patterns which rely on probabilistic rather than deterministic measures and models."<sup>70</sup> The *keiretsu* networks advantage Japanese business enterprises by (1) minimizing the risk of outside takeover (as T. Boone Pickens discovered<sup>71</sup>), (2) affording easier access to capital with less concern for quarterly profits or quick return on investment, (3) promoting intra-group cooperation and coordination regarding R&D, new ventures, marketing, (4) assuring markets, and (5) providing insurance against failure or bankruptcy (such as the recent *defacto* takeover of Suburu by Nissan).<sup>72</sup>

These established relationships, it must be stated, are hard for any business firm--foreign or Japanese--to break into. The barriers to entry in the Japanese market are high. Too, competition amongst the *keiretsu* is vicious. Thus, government policy in the form of competition policy cannot offer an easy, satisfactory fix. Nevertheless, government policy can create more competition in specific ways. In order to determine precisely how, we must delineate the three types of *keiretsu* relationships--horizontal, vertical production supply, vertical consumer distribution.

Antitrust law was unknown in Japan until the American occupying force imposed it in 1947. Cartels and monopoly behavior were until that time not only tolerated but even encouraged. The new law was enforced for about five years, resulting in the breakup of the *zaibatsu* and the fostering of aggressive competition among the horizontal *keiretsu*. Nevertheless, competition among the *keiretsu* remained keen. But, antitrust law lapsed into disuse until the mid-1970s and other competition problems emerged.<sup>73</sup> There was little commitment to free market ideology and to consumer interests, much commitment to the developmental state within global markets and producer interests. Conflict between MITI, the institution of industrial policy, and the Japan Fair Trade Commission, the institution of competition policy, was invariably won by the former.

Vertical control of the consumer distribution networks by the automobile, consumer electronic, cosmetic, pharmaceutical, camera, and newspaper industries assures that all in supply-distribution chain of a *keiretsu* make profits. The arcane laws regarding retail distribution assure that competition for the consumer's yen does not become too intense. Furthermore, distribution system control by the Japanese manufacturers assures that imported consumer goods are introduced only as exotic luxury goods with extraordinarily high markups.<sup>74</sup> "[T]here is little doubt," says Kozo Yamamura, "that the control exerted by large manufacturing firms has been and continues to be an effective means to force Japanese consumers to subsidize the international competitiveness of large manufacturing firms."<sup>75</sup> As a result, firms up and down the vertical supply *keiretsu* are assured of profits.

Enforcement of Japanese competition policy could help promote more competition in both the vertical supply *keiretsu* relationships and the vertical consumer distribution *keiretsu* relationships. De-regulation of consumer distribution would force more price competition on the manufacturers, thus compelling cost reductions throughout the vertical supply networks. Thus, encouraging new competition throughout the chain. Regarding vertical supply *keiretsu*, Article 19 of the Antimonopoly Law prohibits unfair business competition which unjustly discriminates against other entrepreneurs, unreasonably

induces or coerces customers to deal with oneself, unreasonably uses bargaining power in dealing with another firm, or unjustly advantages transactions between firms which share officers or shareholders.<sup>76</sup> The policy tools of change thus do exist, but must be used and must be developed judicially and administratively.

Yet, as Ken-Ichi Imai opines, outsiders can and do break into these vertical production supply *keiretsu* relationships.<sup>77</sup> Masahiko Aoki points out the central logic of supplier relationships: Bargaining power depends upon the control of information, the control of technology. The controller of information can bargain effectively within the *keiretsu*. Foreign firms must understand this logic and act upon it. The solutions to the problems posed by Japanese industrial organization lie more in American industrial organization and corporate strategy than in government policy.

The Korean government has substantially opened its markets to foreign direct investment. By January 1992, about 98% of manufacturing sectors and 62% of service sectors had been opened.<sup>78</sup> Much of this trade policy change came in the 1989 Super 301-motivated bilateral agreement with the United States. Too, since 1989, local content, transfer, and technology licensing performance requirements are no longer a condition of investment. Indeed, the case-by-case FDI investment approval process will be phased out in January 1993 and supplanted with a notification

requirement.<sup>79</sup> Taiwan has similarly removed many FDI barriers and abolished export performance and local content requirements.<sup>80</sup> Some market sectors remain protected, including power generation, petroleum refinery, railroads, trucking, telecommunications, defense, securities, and insurance.

Though not yet an international trade issue, the Korean *chaebol* may come under increasing scrutiny. The *chaebol* are *zaibatsu*-like (i.e., similar to the predecessors of the Japanese *keiretsu*). Foreign companies will increasingly seek to sell to companies within *chaebol* and may find that it is quite difficult to break in. An American inspired Monopoly Regulation and Fair Trade Act exists in Korean law but is not enforced.<sup>81</sup> Despite the lack of *keiretsu*-like business relations in Taiwan, we can expect that the nationalistic business culture in Taiwan will increasingly lead to complaints from foreign companies that marketing in Taiwan is difficult. We can expect, then, that Taiwanese and Korean business practices will challenge international rule writers. However, ultimately, corporate strategy and industrial organization will, as in the case of Japanese *keiretsu*, do more than can government commercial diplomacy.

#### Fair Trade Principle

Fair trade is a principle underlying the GATT regime. The principle is probably rooted in the Anglo-American common law notions of equity, of fair business practices,

and of property rights. Equity is a concept traceable through medieval European law to Aristotle, who said it meant a "correction of legal justice."<sup>82</sup> Aristotle pointed out that the law is not always fair. "The reason is that all law is universal but about some things it is not possible to make universal statement which shall be correct."<sup>83</sup> That is, a legal rule--such as the law of GATT--aims at generalizing for an indefinite number of cases and does not permit the exception. The fair trade principle of GATT offers equity in the form of exceptions to GATT rules such as balance of payments (Article XII), security (Article XXI), emergency safeguard (Article XIX), and general (Article XX). The fair trade principle also encompasses a notion of fair business practices, that it may be (under certain circumstances) unsporting for firms to dump goods in foreign markets at less than normal value and for governments to subsidize their firms. Finally, the fair trade principle affords the writing within the GATT regime of rules regarding intellectual property. Intellectual property rights rules are being negotiated in the Uruguay Round.

Some academic, business, and public policy leaders, however, contend that the East Asian political economies challenge the fair trade principle of the GATT regime. Japan especially, some say, is a mercantilist state which employs a deliberate industrial policy of targeting which

contravenes the spirit and rules of the GATT regime. States Marie Anchordoguy:

Whether it is government subsidization of Japanese firms in the form of financial aid, protectionism, or the encouragement and tolerance of cartels, or it is the transfer of wealth from Japanese citizens to industry in the form of high consumer prices or saver-subsidized low-cost capital, the effect is the same: Japanese producers are given powerful weapons to compete in international competition, weapons that handicap the battle in Japan's favor.<sup>84</sup>

Anchordoguy concludes,

If Japan sees the maintenance of the free-trade system as in its self-interest (and it should as long as the United States and Europe are key markets), it must change some of its policies and institutions. Their comprehensiveness and consistency work in ways that create an uneven playing field. This sense of unfairness makes it increasingly difficult for the United States to get popular support to stave off protectionist sentiment in the country and to support the liberal economic order.<sup>85</sup>

Indeed, Japanese government targeting is not the fiction of a hack writer: The industrial policy of the Japanese developmental state targeted apparel, steel, shipbuilding, automobiles, machine tools, computers, consumer electronics, semiconductors, and telecommunications.<sup>86</sup> This is true even if the targeting of pharmaceuticals, chemicals, and commercial aircraft has (so far, anyway) failed<sup>87</sup> and even if (as I believe) Japanese competitiveness ultimately owes to industrial organization and corporate strategy, not government policy. The Koreans and the Taiwanese have followed the Japanese industrial policy model. They have targeted the same industries using quite similar policy tools.<sup>88</sup>

Yet, it is easier for government policymakers to target for their economies the industries which have historically been shown to be critical to the development of the great industrial powers of the 19th and 20th centuries (apparel, steel, automobiles, machine tools, consumer electronics, computers) than it is to forecast industries critical to continued economic growth in the 21st century. Furthermore, as Okimoto points out, Japanese industrial policy has had much less to do with the commercial success of Japan's new industries of the 1980s than it did in the 1940s through 1970s.<sup>89</sup> Japanese firms simply do not need government help and resist government intervention. Finally, the nature of contemporary commercial competition within global markets makes the nationalism of government targeting anachronistic. Firms must be free to research and develop, design, finance, produce, and market in multiple national markets. Corporate strategy and state strategy are not always congruent any more: It is not always true that "what's good for GM is good for America and vice versa." Hence, an industrial policy of targeting probably is better suited to compressing economic development during the developmental stage of industrialization than accelerating economic growth during the maturity stage of post-industrialism. Nevertheless, whether or not an industrial policy of targeting does or does not<sup>90</sup> make economic or policy sense, states do it. Hence, the question: Can the GATT regime accommodate an industrial policy of targeting?



A government industrial policy of targeting presumes a "smart" state, i.e., one with the bureaucratic structures and processes to pick the key industries which ought to be promoted. The mere intellectual exercise by government bureaucrats of selecting the critical industry which they believe will maximize national development is not incompatible with the GATT regime. The publication of such government "white papers" might seem silly to the Anglo-American architects of the GATT, but ideas and words do not violate GATT rules. Indeed, the GATT regime must accept that it manages trade among more than 100 members now, not the few advanced industrialized societies of Europe and North America. The regime can and must tolerate different conceptions of the proper role of government in economy and society.

However, if words cannot endanger the GATT regime, deeds can. The policy actions of government industrial targeting can be incompatible with the GATT regime. The policy tools of targeting are import trade protection, export trade promotion, inward investment protection, subsidization, and firm dumping. As we have seen, import trade protection as a policy tool has largely been taken away from East Asian policymakers by the GATT regime and by American unilateralism. As we have seen, inward investment protection as a policy tool has also largely been taken away from East Asian policymakers. East Asian policymakers can continue to promote exports through institutions such as the

Japan Export Trade Organization (JETRO), the Korea Export Promotion Corporation, and the China External Trade Development Council without running afoul of GATT rules. Thus, some important policy tools of targeting are not significant problems to the GATT regime.

Government subsidization and firm dumping, however, continue to be problems for the GATT principle of fair trade. Neither government subsidization nor firm dumping violates GATT rule under all circumstances, however. Indeed, government subsidization is a legitimate policy tool of government. Roads, harbors, and schools are all legitimate subsidies. However, GATT rules do specify some government subsidies as unfair advantages for recipient firms in market competition because they injure non-recipient competitors. Unfortunately, GATT rules are inadequately developed regarding subsidies and their remedies, countervailing duties.<sup>91</sup> International rules regarding government subsidization are ambiguous and national policies and practices are contentious because states disagree about what government should and should not do to promote industry. The United States has long maintained a national countervailing duty law, implemented that law most vigorously, and pressed for GATT regime rule creation because the American way of political economy has generally favored minimal government promotion of particular industries. National types of political economy clash in the subsidy/countervailing duty policy area.

Some conclude that as a matter of both national and international policy, subsidy/countervailing duty law should be excised. Some contend that subsidy/countervailing duty policy is just protectionism and that the safeguards policy should be the only remedy available. Others suggest that, at any rate, writing effective subsidy/countervailing duty law is impossible. To the contrary, government subsidies to specific industries or firms do distort markets.<sup>92</sup>

Furthermore, such government subsidies do injure competing firms and ought to be regulated. Furthermore, an effective international subsidy/countervailing duty policy can solve a fundamental problem of interfacing different types of national political economies within the world economy. Within the GATT regime, the elimination of the anachronistic domestic subsidy-export subsidy distinction (i.e., the distinction is meaningless in global markets), the addition of the specificity test, and rule refinement regarding investigation procedures can reduce trade conflict.

Firm dumping, too, is restricted, not prohibited, under GATT rules. Like subsidy policy, antidumping policy is highly contentious, with complaints that it does not make any sense to have such a policy, ought to be completely re-grounded intellectually, and/or that the manner in which states (especially the United States) administer it produces blatant protectionism.<sup>93</sup> By my count, of the 794 active AD and CVD cases investigated by the US Department of Commerce during the 1980s, 203 involved East Asian states (Japan--76,

Korea--40, Taiwan--38, China--19, Macao--1, Malaysia--8, Singapore--11, Thailand--10).<sup>94</sup> Economists may be right that antidumping law as administered is blatant protectionism, but, the market distorted and still-latently protectionist East Asian political economies invite these charges from American business. The political pressure of business demand for remedy must have some outlet. The elimination of the antidumping law would seem to invite only worse trade policy problems. Continued refinement of GATT rules regarding antidumping and use of national antidumping laws, then, even if still imperfect, provide remedy to firm dumping behavior.

In short, East Asian industrial policy need not be a great threat to the GATT regime principle of fair trade. Extant rules, new rule creation, and changes in the world economy largely solve the problems.

East Asian intellectual rights policies have been the source of international trade problems for some time. Korean and Taiwanese IPR laws have until recently been seriously short of OECD state norms. American unilateralism and increasingly knowledge-intensive firm demand have, however, encouraged the writing of IPR laws in both countries. Enforcement of these laws is improving in both countries, though improving more in Korea than in Taiwan.<sup>95</sup> Japanese IPR law, on the other hand, is highly developed and detailed. However, American firms complain often about Japanese IPR law and enforcement. Complaints regarding the

law result primarily from the lack of international consensus regarding IPR law. Japanese IPR differs from American law, but in some ways is similar to European law. Japanese enforcement of IPR law, on the other hand, often makes de facto protection of intellectual property rights less effective than de jure rules would suggest.<sup>96</sup>

Nevertheless, the problems regarding IPR are solvable with new rule creation by the GATT members collectively and individually. The East Asian states have ample domestic motivation to provide effective protection of intellectual property rights, for their firms are increasingly world leaders in the advancement of and use of technology.

Multilateralism, Reciprocity, and  
Economic Development Principles

The principles of multilateralism, reciprocity, and economic development are fundamental to the GATT regime. Multilateralism rests on two assumptions: (1) According to neo-classical economic theory, free trade in an economy maximizes resource use efficiency and increases economic wealth. (2) State interdependence results in mutually dependent economic and political relationships among states. Multilateralism means that the state contracting parties commit themselves to act cooperatively in the management of the world economy. Unfortunately for the GATT regime, neither the Japanese nor the Koreans nor the Taiwanese have been committed to multilateralism. Each state has pursued

the economic development strategy of mercantilist import substitution-export promotion. This state strategy, brilliantly devised and implemented, has compressed into years the industrial development process which took decades in Europe and North America. However, the strategy has been devised and implemented with little regard for either the multilateralism principle of the GATT regime or for the economic, social, and political impacts of their policies on other countries within the regime. In the world trading system, Japan, Korea, and Taiwan have been free riders. The judgment of Stephen Cohen that the Japanese state acted irresponsibly in the world economy in the 1970s and 1980s and indeed endangered the GATT regime by creating protectionist pressures all over the world is, I believe, correct.<sup>97</sup>

Yet, East Asian commitment to multilateralism is growing. It is growing, however, not because of a new-found belief in the logic of comparative advantage but because of a realization about the logic of interdependence. The logic of interdependence operates at two levels of the world economy--firm and state. Firm interdependence, as Helen Milner has shown, leads firms to oppose protectionism.<sup>98</sup> Protectionism leads state policy retaliation and to the raising of firm input costs. Interdependent firms lobby their governments against protectionism and for open markets. State interdependence, as Robert Axelrod and Robert Keohane have argued, lead states to cooperate.<sup>99</sup> It

leads states, as I have shown, to settle trade disputes and comply with international trade regimes because of concern for their international reputations, expectation for reciprocity, and fear of retaliation.<sup>100</sup> It leads states, as Christopher Lenhardt is showing, to reduce barriers to trade.<sup>101</sup> We can expect that first the Japanese and then the Koreans and Taiwanese will become more multilateral over time.

Reciprocity is a fundamental principle of the GATT regime. However, the meaning of "reciprocity" within the GATT regime differs today from the original Havana Conference meaning. Reciprocity then meant "substantially equivalent concessions of trade barrier reduction"; reciprocity now means "substantially equivalent competitive opportunities."<sup>102</sup> As we have seen, the East Asian states have not offered substantially equivalent competitive opportunities. Nevertheless, the direction of policy change in Japan, Korea, and Taiwan is toward such an outcome. By the end of the 1990s, the policy environments of Japan, Korea, and Taiwan will likely closely resemble the environments of North America and Europe. Residual differences likely will be more of firm strategy and industrial organization and likely will not challenge the GATT regime.

The principle of economic development also is fundamental to the GATT regime. Yet, this notion, too, has evolved within the regime over time. The GATT architects

believed strongly in the need for economic development. To them, economic development was the means toward rising standards of living, democracy, and international peace. However, the GATT architects believed that open markets resulted in economic development. Hence, the original rules did not extend preferences to the underdeveloped. After decolonization and through the political mechanism of less developed country unity in the 1970s (such as the Group of 77), the GATT regime added preferences such as the Generalized System of Preferences for less developed countries.

During the 1980s, however, the East Asian states challenged the neo-classical notion of economic development. Rapid industrial development, they showed, is the result of a high level of political development paired with government market intervention through a mercantilist import substitution-export promotion strategy. The success of this strategy has caused both scholars and policymakers of the neo-classical IMF-World Bank school and of the neo-Marxist *dependencia* school to re-think their premises, arguments, and conclusions.

#### Conclusion

Contrary to much conventional wisdom, I have argued that the East Asian political economies do not operate fundamentally differently from the range of normal within the GATT regime. I have argued that the East Asian



political economies are different, but that the differences are of degree, not kind, and are decreasing. Furthermore, since East Asian competitive advantage rests today more on firm strategy and industrial organization than on government policy and since global interdependence is changing East Asian state trade policy preferences, the principles, norms, rules, and procedures are up to the task of managing trade relations. However, I have also specified needs for additional rule creation, without which the regime may ultimately collapse.

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**Figure. Classification of National Political Economies**

