Jean Monnet Chair Papers

Europe and the East Asian Agenda

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Jean Monnet Chair Papers

Andersson and Linder, *Europe and the East Asian Agenda*

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Foreword

About the Authorship of this Jean Monnet Chair Paper

This Jean Monnet Chair Paper has grown out of three seminars which I gave as a Jean Monnet Visiting Professor at the European University Institute in Florence in the winter of 1990. The texts for these presentations are based on a number of discussions I had with Dr Thomas Andersson.

Dr Andersson, at a later stage, reworked the original manuscript and brought in research results and ideas of his own. He has thus made substantial and independent contributions.

Staffan Burenstam Linder

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Staffan Burenstam Linder Thomas Andersson

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Abstract

This paper presents the need of a European agenda for East Asia. The root of East Asian dynamism lies in an actively pursued export-oriented development strategy. The consequences embrace new opportunities as well as risks. Security issues have been replaced by economic development at the core of the international agenda, and the categorization of a first, a second and a third world has become outmoded.
East Asian dynamism spurs influences towards protectionism as well as liberalization. The United States is giving up its position as champion of free trade and there is a fear of growing non-tariff barriers and domestic trade barriers in developed countries. On the other hand, there has been a demonstration of super-gains from trade. Previously planned economies open up and seek a change of their systems, and there are strong tendencies towards regional integration, particularly in the EC.

The underexploited economic relationship between the EC and East Asia is very much at the core of which way the world economy is to go. The Japanese and other East Asians are now taking major steps to increase their activities in Europe, while the Europeans are preoccupied with their own restructuring. There is a great need of a European policy vis-à-vis East Asia which can serve as a pillar in a future liberal trade and investment regime worldwide, promoting the social welfare of all nations.

1. Introduction: A New World

The last decades have seen sweeping changes in our economic and social landscape. The first world, the industrialized and market-oriented economies of the west, has lost its dominant position. The second world, i.e. the state planned socialist economies, has virtually ceased to exist as we know it. The third world of developing countries, finally, has split in subcategories which display very divergent economic trends. While Latin America and Africa are lagging behind, the phenomenal dynamism of East Asia stands out as a remarkable and continuing success story. Japan has, of course, already been transformed not only to a leading industrialized economy, but to an eminent power in services and finance as well. A number of countries in the region are now about to follow suit.

These conspicuous developments are the result of a long process, the impact of which has merely become visible during the 1980s. The turbulent changes in different regions have had repercussions on each other. For example, Asian Pacific dynamism has made a lagging Soviet Union more exposed to unfavourable comparisons. More significantly, a set of successful economic policies provided an alternative model to those wanting to develop and grow. A dynamic Far East, and not just a growing West, further undermined the relative strength of the economic base provided by the old Soviet system for military security.

The United States and the Soviet Union used to assume special roles on the basis of their military might. The United States has further strengthened its muscle in the last decades, which has contributed to forcing the Soviet Union to reappraise its policies. At the same time, both these powers have lost in importance due to domestic social and economic weaknesses as well as an intensified pursuit of economic goals rather than ideological struggles across the world. Centrifugal forces are now turning the Soviet Union into a source of destabilization for itself and others. Meanwhile, the previously undisputed leadership of the U.S. has been reduced by the country's inability to 'keep its own house in order' and to correct its deficits, combined with the unavoidable relative decline as other economies grow.

The first world encounters the ongoing challenge of adjusting to East Asian competition and the new opportunities arising there. As a result, the West is no longer the undisputed champion of free trade and capital movements. In particular, the international trade policy of the U.S. has become less constructive and more quarrelsome. 'Super 301' and 'Regular 301' have emerged as powerful bilateral instruments to by-pass the General Agreement on Tariffs and Trade (GATT). This trend towards new protectionist policies is followed by a number of other developed countries.

Broadly speaking, national size in itself seems less an advantage as a basis for growth at the present time. While 'bigness' can effectively be managed over the strategic or military dimension, it is not so easy over the social or economic one. The Soviet Union may have more trouble than the other communist countries in getting its economy to work, and the U.S. is having trouble with its long term vitality. Meanwhile, the countries that are the most successful in economic terms are relatively small. What matters is not a comfortable home market but the competitive pressure that follows from international exposure. Rewards do not first and foremost emanate from dominance in the domestic market or richness in natural resources, but rather from economic incentives, high quality of human capital, and emphasis on world markets.

In the Third World, the image of a 'bloc' of poverty-stricken and exploited countries has started to fade. The doctrines upon which the Third World based itself have become less relevant and less realistic. Of course, this is not to say that there are not many countries in a deplorable state, and some will continue to be poor because of gravely inhospitable conditions. Still, it is increasingly accepted that many contribute to their economic and social debacle by inept, not to say disastrous, economic policies. More and more of them are looking to East Asia to acquire some kind of model for development.

As the Cold War seems to be over, and the ideological cleft between rich and poor countries diminishes, foreign policies of appeasement and coexistence can be applied at less risk. The security problems have not disappeared, but 'new' sources of conflict may abide around the corner. History makes it necessary to remember that, unfortunately, there is a tradition here. Worries now increasingly concentrate on what Berlin and Tokyo eventually may come to wish. Unable to pursue an independent foreign policy into military might, these players have concentrated their energies on economic pursuits. This has again provided them with the means to widen, should they wish to, their foreign policy into military might. Or have they found that the goals of foreign policy are better achieved through international trade and investments than through diplomacy and the power to pursue the ultimate stage of diplomacy?

The fact is that Japan and a reunited Germany are centers of the two regions that now attract everyone's attention. Japan's growth-miracle is being followed by that of the Asian Newly Industrialized Economies (NIEs), and behind them the countries in the Association of South-East Asian Nations (ASEAN) are following a similar path. Germany is temporarily burdened by the reconstruction and assimilation of its Eastern part, but is no doubt the heavy-weight of the European Community (EC). Along with the Single Market, which is to be completed in the EC by 1992, changes are sweeping across Eastern Europe as planned economies turn market oriented. As the largest capital-goods exporter in Europe, and also due to cultural and structural ties, Germany will probably benefit the most from the expected economic revitalization of Eastern Europe .

With a diminished role for the U.S. in the world economy, and the lack of a single champion of free trade, the major question is now what paths will be followed by Europe and East Asia. To some extent, this is a matter of how these regions will behave with regard to each other. Looking at simple comparisons of trade and investment figures, the potential relationship between Europe and East Asia must be viewed as underexploited. With the appearance of the EC as the world's largest single market by 1992, East Asia is pushing for a change of this state of affairs. But the EC is preoccupied with its own restructuring, and it is still unclear what its external policy will look like.

As we are witnessing the formation of a free-trade area in North America, and a 'non-treaty' organization in the Pacific, there is a fear of a segmentation of the world economy into 'blocs' of countries which would liberalize trade amongst themselves, but pursue protectionist policies vis-à-vis each other. In 1986, 34.4 per cent of the world's total trade was of the intra-area kind (IMF, 1988). Moreover, tariff preferences granted under preferential trading arrangements affected more of world exports than preferences granted under the Generalized System of Preferences (GSP).

Some observers have believed that the European Economic Space (EES) would be a possible means for the West European outsiders to participate in the momentum that is hoped to be established by 1992. Meanwhile, 1990 and 1991 may in retrospect turn out as revolutionary as 1992 promises to be, as Eastern Europe enters the world economic stage in an unscheduled way. In that case, the EES could serve to accommodate the reforming countries of Eastern Europe. The negotiations between the EC and the European Free Trade Association (EFTA) indicate, however, that countries which harmonize their policies with the EC but remain outside will have little chance to influence its policies. Countries like Austria and Sweden consequently seem to be heading for membership, and others may follow.

All in all, we are entering an era of new challenges, opportunities and risks. There are more favourable opportunities for peaceful coexistence, and there is a more general acceptance of the usefulness of functioning market systems. At the same time, there is no clear leadership defending openness in trade and investment as old champions for free trade change clothes, and new ones have not yet fully dressed. In this situation, new protectionist tendencies grow stronger, and it may become more important to be part of an economic 'bloc'.

The interaction between Europe and East Asia is very much at the heart of which way the world economy is to go. This, in turn, will have a profound influence on the welfare of future generations world wide. Of course, there are many other issues which are acutely pressing. Poverty forces many people to live on the edge of survival in countries where population growth rates remain high. Expanding industrial activities increasingly threaten our global 'commons', such as the oceans and the atmosphere. Handling such matters will require an improved allocation of resources, and favourable conditions for cooperation between nations.

There can be no doubt that this will be greatly facilitated by an open trade and investment regime.

Focusing on the relationship between Europe and East Asia, this paper is organized as follows. Chapter 2 establishes the gravity shift that has taken place between the Atlantic and the Pacific, and surveys causes as well as consequences of East Asian dynamism. Chapter 3 analyses the impact of East Asian dynamism on trade policies, towards protectionism as well as liberalization. Chapter 4 investigates the third leg of the world triangle in trade and investments, which is the not fully developed relationship between Europe and East Asia, and how this might be affected by EC 1992. Chapter 5 presents an agenda for a European policy vis-à-vis East Asia. Chapter 6 summarizes.

2. Economic and Political Consequences of East Asian Dynamism

2.1 The Gravity Shift

There has been a gradual increase in the economic importance of the Pacific for over three decades now. This follows from a simple comparison of the statistics concerning income, trade and international investments. The unprecedented rise of Japan is also evident in the value of stock exchange, the market share of industrial corporations, technological progress, international assets of banks, and so on.

The term 'East Asia' is here understood to be Japan, the four Newly Industrialized Economies (NIEs), and the Association of Southeast Asian Nations (ASEAN).[1] The 'Asian Pacific region' also includes Australia, New Zealand, Papua New Guinea, and the island states of the South Pacific. To get the whole 'Pacific Basin' we also include China, the Canadian and the U.S. western seaboard states. Of course, Indochina, Burma, and the Democratic Republic of Korea are also part of the region, but have here been left out of the statistics.

Table 1 presents basic data on population, area, GDP and GDP per capita for the countries in the Pacific basin which are the most important from an economic viewpoint. Table 2 shows the shares of various Asian-Pacific countries in world population, area and income (USSR and Eastern Europe excluded) as of 1987. It can be seen, among other things, that the Asian-Pacific region holds 11.1 per cent of the world's population, 12.4 per cent of its area and 20.5 per cent of GDP.

From Table 3 it is evident that there has been a significant increase in the weight of the Asian Pacific region, as well as of the Asian Pacific

[1] The four East Asian Newly Industrialized Economies are; The Republic of Korea, The Republic of China (Taiwan), Hong Kong and Singapore. Singapore also belongs to ASEAN, whose other members are; Brunei, Indonesia, Malaysia, the Philippines and Thailand.

Basin, in terms of income. For example, the Asian-Pacific share of world GDP increased from 7.8 per cent in 1960 to 20 per cent in 1987. The Pacific Basin GDP increased from 38.5 per cent of the Atlantic Basin GDP in 1960 to 62.9 per cent in 1987. Finally, comparing the Asian-Pacific GDP with that of Europe, there was an increase from 27.5 per cent in 1960 to 63.7 per cent in 1987.

The increased Asian-Pacific weight is equally visible in trade statistics. As reported in Table 4, Asian-Pacific exports increased from 9 per cent of World exports in 1960 to 22 per cent in 1988. Compared to U.S. trade, the Asian-Pacific is considerably larger. Compared to European trade, the Asian-Pacific is not much behind if we exclude the intra-regional trade. U.S. trade with the Asia-Pacific had surpassed U.S. trade with Europe in 1980, and was 40 per cent larger in 1988. Meanwhile, EC trade with the Asia-Pacific has grown to about the same size as EC trade with the U.S.

It is also worth noting that the four small East Asian NIEs, which have about 70 million inhabitants altogether, now account for about 70 per cent of all exports of manufactures from developing countries. In the mid 1980s, the small Asian NIEs accounted for a larger import penetration ratio[2] than did the Latin American NIEs Mexico and Brazil in all OECD countries except Italy (OECD, 1985).

In many dimensions, the Pacific Basin will no doubt have overtaken the Atlantic Basin by the year 2000. In some respects, this gravity shift has already taken place. For further comparisons, see Burenstam Linder (1986).

2.2 Causes of Growth

To discuss the consequences of East Asian dynamism it is important to have some understanding of its fundamental causes. Of course, there have been many disparate efforts to explain East Asian growth. Many of them have focused on factors that are unique to the region. Such *ad hoc* explanations include references to Confucian values, the economic skills of the Chinese and Chinese minorities, the Japanese ethos, the industriousness and high level of education in the region, lack of raw materials, abundant U.S. aid, political stability, and so forth.

A basic problem with these explanations is their *ad hoc* nature. The region is heterogeneous in every way, with countries differing in history, constitution, race, size, resource endowments, and climate. Yet, high growth is the typical pattern in the countries here referred to as East Asia. The countries in Indochina, Burma, and North Korea, on the other hand, display a very different record. China itself made impressive progress from 1979 onwards, but seems to have set itself back with the retreat from economic reforms after last year's events in Tiananmen Square.

[2] By import penetration ratio is meant the share of apparent domestic consumption, i.e. domestic production plus imports less exports.

These differences in performance point towards a major influence of economic policies. Needless to say, this does not leave out the importance of exogenous factors. Little (1981) concluded that the success of the Asian NIEs is entirely due to 'good policies and the people'. These are not really separate explanations, rather 'good people' have pursued good policies, and good polices have been facilitated by 'good people'.

While the specific design of policies differs across countries, those that have succeeded share certain basic characteristics. The most clear-cut and general difference from other developing countries is that East Asia has pursued relatively more export-oriented policies. While East Asia has promoted sales on world markets, exposure to competition and utilization of scale advantages, other developing countries have tended rather to bias their incentive systems away from world markets and comparative advantage. Using indices for price distortions, it has been shown that the developing countries in East Asia have had considerably less distorted prices than most other developing countries (The World Bank, 1983).

This is not to say that the East Asian countries, with the exception of Hong Kong, have practiced *laissez faire*. Export promotion has not taken place through a general liberalization of imports, but there has been a combination of exchange rate management and fiscal incentives for exports. In addition to the provision of infrastructure and other minimal functions, the governments can be said to have intervened in four broad areas:

i) they have actively engaged in industrial development through industrial incentives,
ii) they have claimed responsibility for macroeconomic stability,
iii) they have, in some cases, intervened in the distribution of ownership through land reform, and
iv) they have set up some public enterprises to produce private goods.

Of these four functions, it is clear that the fourth one has been a relatively unimportant factor in the growth of the region. The state-owned companies in East Asia are not particularly 'small' e.g. compared to Latin America, but their share of industry is still small relative to that of the private sector, and their growth has been low throughout, with the exception of the oil sector in Indonesia (Riedel, 1988).

The importance of the second and third factors has been emphasized for Japan, Taiwan and Korea (Sachs, 1986). Regarding macro-economic policy, government budgets have been kept in balance a fact, which has contributed to high savings and low inflation rates among other things. Nominal exchange rates have been adjusted so as to keep real exchange rates at reasonable levels. The good public finances have allowed governments not to promote industrial growth at the cost of taxing agriculture which, rather, has been protected compared to industry. At the same time, the land reforms in Japan, South Korea and Taiwan created a conservative peasantry of independent proprietary farmers which has lent support to the national governments.[3]

The involvement of governments in the management of private industries is the hardest to evaluate. Korea, for example, has supplemented moderate protectionism with selective export promotion, achieving neutrality on the whole. Whether the economic performance would have been even better without this kind of interference we do not know. It is clear, however, that the measures used have generally aimed at stimulating the efficiency of markets. Incentives have promoted activities in line with comparative advantage; at one point labour-intensity, at another capital-intensity. Input and output prices have been carefully maintained at the level of the world market, so as to encourage competition. Concerning technology, governments have intervened to promote the bargaining position of domestic firms relative to foreign ones, and facilitated the exploitation of static and dynamic scale economies (Hong, 1990).

Moreover, East Asia has not used policy interventions to make life easy for business. Rather, there is a joint and continuous effort on the part of government and private firms to foster the development of the latter, spurring them to adapt to changing circumstances and achieving success in world markets. For Japan, Johnson (1982) characterizes the state as developmentally oriented, in contrast to the regulatory state of the West. Interventions have been promotional rather than restrictive. Private initiatives and ownership have been at the core of the process.

Another factor to take note of is foreign capital. Commercial borrowing has been less extensive than in most of Latin America, even considering that South Korea borrowed heavily in the late 1970s, and the Philippines and Indonesia continue to suffer from considerable and troublesome debt burdens. A great deal of foreign development assistance from the United States no doubt contributed to setting growth off in countries such as Japan, South Korea, Taiwan and Indonesia. Compared to other developing regions, however, only direct investment – undertaken by private corporations – is more prominent in East Asia.

Direct investment has played a conspicuous role in East Asia for a long time. In the wake of colonization there were at first substantial European investments for extraction and distribution of natural resources, especially in Singapore, Malaysia and Indonesia. Before long, the U.S. became the predominant source of direct investment, focusing on the Philippines and Taiwan in addition to those countries just mentioned. However, Japan and South Korea were not particularly welcoming to foreign direct investment, while China was an entirely closed country.

[3] These land reforms were facilitated by historical incidents, notably the defeat of the Japanese in the second World War, and the takeover by the mainlanders in Taiwan. As is well-known, no such incidents have occurred in the Philippines, which has not been able to carry out any real reform of the extremely unequal land distribution. This contributes to the political turmoil and relatively poor economic record of this country.

In the 1980s, Japanese financial institutions have became major players in the Euro-dollar markets. Low capital standards and dividend pressure made it possible for them to focus on size and market share, and interest rate regulations at home allowed them to arbitrage on price or with respect to risk (Dufey, 1990). Further supported by high savings at home, the current account surplus and the appreciation of the yen from 1985, the total international asets of Japanese banks grew from less than those of US banks in 1983 to more than three times as much in 1990. During these years Japanese banks and industrial firms have also evolved as major sources of direct investment world wide, and they have overtaken the West as the dominant investor in most of East Asia.

At present, Japanese direct investment seems to serve as a locomotive for growth in East Asia as a whole. At the same time, there is a fear of dependence on Japan in many countries, and a resentment of the cultural influence it may inflict. The Japanese are sensitive to these fears, and actively work on making their activities stand out as a positive contribution to social welfare in the host countries. In recent years, there has also been a great deal of direct investment from Korea, Taiwan, Hong Kong and Singapore in other countries in East Asia. This can be expected to continue as the Asian NIEs often have the technology that is the most suitable for effective operations in developing countries.

There is little doubt that the internationalization of business within East Asia constitutes a major factor for the spread of growth and exploitation of differences in factor costs as well as natural resources. A popular illustration of the development of the region is that of 'the flying wild geese'. Following the 'leading goose' in a wide formation, the individual countries move up the industrial ladder after each other, chasing those ahead as changing factor price relations alter comparative advantages. In this process, the mobility and flexibility of private business is a key factor.

Finally, it can be noted that the growth in East Asia defies the traditional wisdom that there would be a conflict between growth policies and policies for greater equity (Kuznets, 1965). In East Asia, a more equal income distribution has been achieved by land reforms and large investments in human capital, for example, through educational reforms. As pointed out by Stiglitz (1990), there may well be a positive relationship between equity and efficiency in a world of imperfect information.[4]

The spectacular growth performance in East Asia has strongly affected the rest of the world. In the following sections, we will distinguish between three different external effects: a) the demonstration effect, b) the opportunity of a bigger world, and c) the threat to established interests.

[4] From the Wicksell Lecture of May 15th 1990, 'Whither Socialism? Perspectives from the Economics of Information', the Stockholm School of Economics.

2.3 The Demonstration Effect

Growth explained by reference to a set of economic policies may be possible to duplicate by other countries. The image of a growth 'miracle' is displaced by that of a growth 'model'. The fact that the East-Asian countries are so different lends support to the idea that others can replicate their performance. A resemblance to the policies originally favoured by the West in the early phases of its industrialization lends further support to this reasoning: It can be repeated – you can do it too!

The demonstration effect has already had considerable influence on the policies of other developing countries. Spurred by the striking differences in economic performance, China pursued economic reform for ten years, until the surge for political freedom resulted in crude violence and a setback of policies. Vietnam and Laos, on the other hand, are now relaxing their planned economies at a much greater pace. They seem likely to continue to do so together with Cambodia, if only the unfortunate conflict in that country can be solved.

The emulation of the East Asian example in practice encompasses attempts both to let markets determine prices in previously planned economies, and to expose protected economies to competition from world markets. The pace of change is still low in Africa and Latin America, however. Similarly, governments seldom assume a constructive role regarding equity issues, which could be conducive to economic growth. The Philippines and most Latin American countries, for example, are marked by extreme inequality in the distribution of land and human capital. As the development of Japan and the Asian NIEs continues, however, the eyes of politicians elsewhere are bound to focus more and more on the possibilities underscored by their examples.

The demonstration effect has influenced development theory as well. Neo-marxism and the 'dependency' school of 'unequal exchange' have expired. While the traditional import substitution school[5] argued that secularly falling terms of trade and limited export markets would make it impossible for developing countries to rely on world markets, precisely those countries that have gone for the world market have succeeded in achieving development. Likewise, planning has been discredited and few countries now prepare much advertised 'Five Year Plans' of the sort that used to prevail in the past. Similarly, there is considerably less call for a New World Economic Order – with regulated international trade and prices, and 'massive resource transfers'.

East Asian dynamism has, of course, had a profound impact on Marxian and neo-Marxian theory. It can be seen in writings such as the Communist manifesto that Marx looked upon capitalism as a powerful engine of growth which would spread to the poor countries and set up a process of growth there, too. The breakdown of capitalism would come later because

[5] See e.g. Prebish (1962) and Nurkse (1952).

of the inner contradictions of strong capitalist growth. It was neo-Marxists, impatient with the downfall of capitalism, and unwilling to experience capitalism in developing countries, who formed the arguments of exploitation of poor countries.

The demonstration effect has also had some implications for neoclassical economics. As already commented on, the development in East Asia does indicate a role for government. This, however, is the role of supporting and spurring activities in private firms, correcting for market imperfections and thereby facilitating the functioning of markets. The arguments concern mainly what scope and kind of government intervention is desirable.

Concerning the virtues of an export-oriented growth strategy, there is now little disagreement in regard to East Asia. As for other countries, objections are still raised about its viability. It has been argued, for example, that export-orientation makes developing countries dependent on growth in the industrialized countries, so that the former do well only when the latter do. This argument is effectively countered by the rapid growth of the market shares of the NIEs in the industrialized countries (see Table 8).

Another, more biting, counter-argument to export-orientation can be referred to as the 'adding-up problem'. The Asian NIEs have already penetrated the markets of the industrialized countries with such fierceness that they are accused of unfair trade behaviour. As a consequence, the rich countries have increasingly used quantitative restrictions to protect their industries. Since 1977, many of the developed countries have assigned a global market share to the developing countries in general, and then distributed quotas for individual countries within that global quota. With more and more developing countries competing for industrial exports, the protectionist pressure would finally become irresistable. Thus, the traditional elasticity pessimism of those in favour of import substitution has been replaced by a new one, based on the protectionist measures applied against new producers in the Third World.

For a number of reasons, the new elasticity pessimism may exaggerate the difficulties of other developing countries to follow East Asia on the track of export orientation. Greater exports from developing countries also mean increased purchasing capacity and larger imports. Hence, there will not necessarily be any larger deficits for the developed countries, but simply more trade. Moreover, there are improved possibilities for trade between developing countries. This becomes increasingly so as they develop at different pace, and turn more complementary in nature.

Another counter-argument against the rise of protectionism has been brought forward by Bhagwati (1988), who stresses the paramount role of multinational corporations in international trade. Because such a great part of world trade takes place within these firms, they have a lot to gain from preventing protectionism from spreading. As firms become increasingly international, they are likely to set up more and more resistance against protectionist measures.

Still, there is certainly some merit to the worrying about trade policies in developed countries. There can be no doubt that they have held the growth rates of exports e.g. in clothing and textiles below potential. This reduces the strength of the demonstration effect among policy makers in the Third World. The future significance of this factor is not yet clear, however. The matter will be returned to in Chapters 3 and 4.

2.4 The Opportunity of a Bigger World

The Asian-Pacific region has not only greatly expanded its exports. As can be seen from Table 5, imports have increased dramatically as well. For example, the region's imports from the U.S.went from US $3 billion in 1960 to US $98 billion in 1988. In the same period, imports from Europe went from US $3 billion to US $83 billion. Nonetheless, the American and European market shares in the Asia-Pacific have declined, as can be seen in the lower part of the table. The reason is that intra-regional trade has expanded fast enough for all market shares of external regions to diminish. East Asia contains without comparison the world's most rapidly expanding markets.

Consider, instead, the share of countries' exports going to East Asia. Table 6 reports that the share of U.S. exports going to this region expanded rapidly from 13 per cent in 1960 to 27 per cent in 1988. Because of the great increase in intra-regional trade in Europe, the share of European exports going to East Asia remained stagnant over the period as a whole. Still, it rose from 3.7 per cent to 5.6 per cent between 1980 and 1988. And, if we exclude European intraregional trade, we see a marked increase in the share of European exports going to East Asia between 1960 and 1988. In fact, it almost doubled in the 1980s, reaching 19 per cent of EC's total external exports today.

The benefits of expanding export opportunities due to increasing markets elsewhere usually do not need much arguing to establish. However, a country exports basically to be able to pay for its imports. As long as it does not want to donate means to foreigners, or build up credits abroad purely for their own sake, this is the only reason to export. So, if newcomers on the world's economic scene provide new opportunities for imports, this should be seen as an advantage.

Without doubt, consumers everywhere are quite willing to turn to goods provided by East Asian producers. Importers of capital goods and intermediate goods are similarly interested in imports from East Asia. Table 7 shows that U.S. imports from East Asia rose from some US $2 billion in 1960 to US $180 billion in 1988. Europe (OECD) imported for just over US $3 billion in 1960, and for US $120 billion in 1988. As a percentage of total imports, the U.S. imported 15 per cent from the Asia Pacific in 1960 and almost 40 per cent in 1988. During this period, the

European share of imports from East Asia rose from only 6 per cent to 9 per cent. The increase was larger in the case of Sweden, for which the share coming from the Asia-Pacific rose from about 3 per cent to 10 per cent.

The growth in East Asia has yielded advantages beyond the increased scope for trade. The competitive pressure has increased in most branches, which should enhance the economic performance of all countries. Furthermore, there are new opportunities for investments nationally and internationally because of larger markets as well as faster growth of technology. This has particularly been the case as Japanese R&D has caught up and passed from copying to leading in a number of fields. This change has intensified the 'high tech' race; policy makers and executives in the U.S. and Europe have been forced to try harder in order not to be outcompeted, and other countries have been able to import new technologies. At the same time, the West has learnt what licensing arrangements can do in the hands of an innovative imitator, which has made the U.S. and the EC considerably more reluctant to provide NIEs with advanced technology. Although the individual firms and governments in developed countries have not been able to coordinate any effective blockade in technology, it has become increasingly important for the NIEs to invest in R&D themselves.

Not only is there a race for 'high tech' leadership, but also what might be referred to as a 'high ec' competition, i.e. a competition between economic systems. As we have already argued, East Asian dynamism has added new insights into the importance of markets. At the same time, it has demonstrated that governments can play a positive role in relation to markets.

On a less elevated plane, Japanese corporate management is the object of much study, not least in regard to ongoing technological progress. Methods for organizing the labour force, such as seniority wages, lifetime employment and job rotation have been investigated by a great number of researchers (see e.g. Okimoto and Rohlen, 1988). Abegglen and Stalk (1985) describe the competitive drive of Japanese companies, their growth bias and aggressive way of dealing with competitors. Aoki (1988) models the development of communication and incentive systems in Japanese firms which, he argues, are superior to those in the West in some respects.

2.5 The Threat to Established Interests

East Asian competition is not just experienced by the outside world as a source of benefits. On the contrary, the producers exposed to it are seldom thankful. The U.S. as well as Europe have had much to say about the competitive practices of East Asian firms and the export surpluses which East Asian countries have been running from the 1980s. Most accusations of unfair competition focus on Japan. 'Japan-bashing' has increased in intensity in Washington through the 1980s, and the U.S. exerts pressure on Japan to reduce its protection at home. The fact is that Japan has reduced both its tariffs and its non-tariff barriers. Traditional trade obstacles – which are covered by GATT rules – are lower than, or as low, as in other industrial countries, cf. IMF (1988). In any case, they are certainly lower than in the U.S. Intensive criticism continues against those import restrictions which continue to exist – notably on agricultural products – and against 'structural impediments'. The so-called 'Structural Impediments Initiative' is trying to force Japan to reduce its domestic savings rate and change the multi-layer domestic distribution system which complicates the introduction of new products.

It can only be stated that there are strongly varying views on whether the Japanese market actually is closed or not. Leaving aside the favorite anecdotes and looking at some simple comparisons on the import behaviour of Japan and other countries, it seems difficult to argue that Japan imports 'too little' from the U.S. For example, West Germany, France and Italy have a combined GDP which surpasses that of Japan. Still, the U.S. exported only US $31.2 billion to these countries in 1988, compared to US $37.7 billion to Japan.

Criticism about protectionism at home has increasingly targeted the Asian NIEs as well. The background is, of course, their success throughout a wide industrial spectrum. Table 8 reports the import penetration ratios (see note 3) of NIEs in the major EC markets, the U.S., Australia, Japan and Sweden in 1970 and 1985. Figures are given for total manufacturing, textiles, electrical machines and appliances, and communication. As can be seen, the NIEs recorded a significant increase in all the EC countries in every product group included in the table, as well as in total manufacturing. In the U.S., Australia and Sweden it was even higher, while it was lower in Japan. Broadly speaking, the highest ratios were recorded in textiles and radio & TV. The Asian NIEs were responsible for most of the increase throughout.

In terms of protectionist policy, the Asian NIEs leave room for criticism to a varying degree. Taiwan and, especially, Korea operate a number of import obstacles, but less so than comparable LDCs. Export promotion also means that resources are not biased into import substitution, which makes the market mechanisms less distorted and, in effect, the domestic markets less protected. Tariffs have also been reduced and many other obstacles to imports dismantled during the last few years. Singapore has relatively few trade obstacles, and Hong Kong is undoubtedly the freest trader that exists. The developing countries in ASEAN, followers of the NIEs in industrialization, are more protected, especially Indonesia. Still, their trade policies are considerably more liberal than those of other developing countries on average.

3. Conflicting Trade Policies: Protectionism and Super-Gains from Trade

3.1 Trade Policy Impact of East Asian Dynamism

Many forces contribute to the shaping of the trade policies pursued by countries, groups of countries, or international bodies. Presently, one of the most important – probably the most important one – is East Asian dynamism. Other countries have generally found it necessary to design their policies in such a way as to deal with the new situation and, possibly, learn from the successful entrance of East Asia on the international economic stage.

The various East Asian influences on trade policies can be divided in five different categories:

i) Protectionist measures, in the U.S. as well as in Europe, to reduce competitive pressures.
ii) Protectionist threats, primarily in the U.S., aimed at 'opening up' the East Asian market.
iii) Trade liberalization, undertaken by LDCs in and out of the region, in order to improve competitive positions.
iv) Trade liberalization in the form of economic integration, in Europe, North America, and to some extent in the Pacific Basin, in order to organize oneself so as to duplicate and/or continue East Asian growth.
v) Deregulation of domestic economies, mostly by previously state-planned countries but also in the West, in order to create or improve the functioning of markets. This includes institutional changes that facilitate countries' engagement in international trade.

Some of these developments in international trade policy are contradictory. Protectionist pressures and policies are spreading, especially in the U.S. The EC has also instituted an increasing amount of trade obstacles, not least in their relations with East Asia. As regularly calculated by GATT, a high percentage of international trade is subjected to protectionist measures other than tariffs. The current debate is dominated by protectionist pronouncements and there is much talk about the risk of 'trade wars'.

As far as protectionism is concerned, we are mostly concerned with the U.S. in this chapter. Of course, there have always been isolationist forces at work within this country. Still, the U.S. can be regarded as the prime champion of free trade since the end of World War II. For this reason, its gradual 'drop-out' of that camp represents the most fundamental change in attitudes taking place in this field today. In Chapter 4, we will look more closely at the European development.

3.2 U.S. Protectionism

During the 1980s, the U.S. negotiated, or increasingly often imposed, a number of import restrictions. These were particularly imposed against East Asia. Aggressive anti-dumping and countervailing duties, rather than voluntary export restraints (VERs) and orderly market agreements (OMAs), became the preferred instruments. The tendency is a weakened commitment to multilateralism, and steps being taken towards bilateralism as well as unilateralism. This is most ominous in the form of arbitrary 'fair trade' provisions like the 'Regular 301' and 'Super 301'. There are also vociferous calls for 'managed trade' with demands for reciprocity, not in opportunities but in 'results'. These 'results' should come from sweeping East Asian structural reforms to accommodate U.S. exporters. More concretely, there are now two parallel trade policy 'discussions' going on between Washington and Tokyo. These are the Super 301 negotiations and the Structural Impediments Initiative.

Under the 'Super 301' provision, the Administration must report to Congress in the spring of each year and identify countries for bilateral negotiations aimed at removing specific trade barriers that damage U.S. exports. Japan, together with India and Brazil, was cited under 301 in 1989. Bilateral discussions with Japan deal with import barriers to foreign satellites, super computers, semiconductors, and forest and agricultural products.

Of course, the U.S. does not speak only with one voice, and the Administration is less protectionist than Congress. The Administration takes total interests – and not just vested interests – into account. It therefore has strong incentives to avoid confrontation with Japan, being a major power with considerable influence on macro policy conditions. The Administration has – both under Reagan and Bush – emphasized efforts to open East Asian markets rather than close the U.S., thus threatening protection to avoid protection. Carla Hills, the US Trade Representative, defends Super 301 as a market opening, non-protectionist device.

In practice, it may be that both the 'Regular 301' and 'Super 301' represent dangerous interventions in trade not because of what they do to U.S. export policy, but because of what they do to import policy. Their effect is to disarm the old option of a president to call for 'export policies' as a way of doing away with protectionist pressure in the U.S. '301' arms a president not with the authority to remove U.S. import restrictions, but with the authority to impose new ones. It provides the vehicle to press for export expansion without paying the price of removing U.S. import restrictions.

The fact is that, although they certainly have trade barriers, the Asian NIEs as well as Japan have gradually liberalized their trade regimes. As already commented on, Japan probably has fewer government controlled trade obstacles than most other countries. Much attention has consequently been focused on the Structural Impediments Initiative, i.e. on various structural impediments in Japan, and 'differences' which make exporting to this country more difficult.

Above all, Washington wants Japan to reform its multi-layer distribution system in order to facilitate new imports, rationalize land use to make more land available for construction purposes, increase infrastructure investment, loosen up company groupings ('keiretsu') to discourage excluding business practices (such as bid rigging, price fixing, group boycott, and market allocation), and to improve protection of intellectual property rights (for instance by speeding up processes for granting foreigners patent protection). Tokyo retorts by asking the U.S. to tackle at long last the problems of its budget deficit, reduce excessive consumption and promote savings, increase the availability of low cost capital, and improve the educational system to enhance competitiveness. Still, the International Herald Tribune (1990a) reported that Kaifu, after the Bush-Kaifu meeting in California, promised to undertake the task to 'firmly tackle structural reforms of Japan as one of the top priorities of my cabinet, with a view to improving the quality of Japanese life with further stress on the consumer-oriented society'. In spite of these reports, U.S. officials have expressed doubts that Kaifu, because of domestic political obstacles, will be able to deliver on his promises.

The structural reforms that have been requested are really outside the control of the usual expenditure switches and adjustments which make up the ordinary macro-economic kit. Their undertaking involves fundamental alterations of Japanese life, and will generate almost by definition a great deal of political resistance. Again according to the IHT (1990b), 'harsh criticism greets Kaifu on return from Bush talks'. It can be noted that the U.S. itself has been unable to deliver on numerous international undertakings, also within the Structural Impediments Initiative discussions with Japan. Still, redressing the U.S. economic imbalances requires much less disconcerting measures, and can be managed through the conventional method of adequate macro-economic policies.

If Japan manage the internal political problems of freeing agricultural imports and undertaking a number of the structural reforms which have been requested, the difficulties of entering its market should diminish. At the same time, Japanese exporters would become more efficient and competitive. Capital and labour would be reallocated from inefficient uses in agriculture and in the distribution system to efficient export industries. For this reason, outside pressures are welcome by many policy makers in Japan, intent on undertaking what they find to be to their advantage under any circumstances, namely structural reform. The U.S. pressures to 'open up' Japan may remind us of Commodore Perry's opening up of Japan in 1868, and the subsequent enormous increase in Japanese competitiveness.

Protectionist measures may have been provided with a rationale by the 'strategic trade theory' (see e.g. Krugman, 1986). When trade takes place under increasing returns to scale, product differentiation and imperfect competition, the simplicity of the free trade conclusions of models of perfectly competitive markets disappears. However, similar to the arguments for optimum tariffs, it is not easy in practice to apply interventions to capture gains through strategic trade policy. Strategic trade theory does not tell us under what circumstances interventionist policies can be effective, how large the gains may be, or whether policy-makers possess the information to design them. This is, for example, the conclusion from a conference arranged by the NBER (National Bureau of Economic Research) and CEPR (Centre for Economic Policy Research) to explore the empirical aspects of strategic trade policy (CEPR Bulletin, 1989).

Protectionist policies will not cure the deficits. As long as the U.S. uses more resources through consumption and investment than it produces, the balance must ultimately be achieved through an influx of capital from abroad, and show up as a deficit on the current account. Of course, the natural supplier in the 1980s has been high-saving Japan, which provides such a great proportion of the imports that the U.S. is asking for.

3.3 The Diminished Giant Syndrome

One might, then, ask for the real reason behind U.S. protectionism. The fact is that balance-of-payments difficulties very often give rise to protectionist activities. National interest groups centering on the necessity of retaining this or that industry, or nurturing new industries, play their role. The balance-of-payments deficits recorded by the U.S. in the bilateral trade, and the continuing takeover of new and fashionable industries, makes it easy to see why 'Japan-bashing' has become attractive in Washington. The de-industrialization that took place during the years of an exaggerated dollar rate now aggravates these sentiments.

What Bhagwati (1989) calls 'the diminished giant syndrome' probably best explains the ongoing change in U.S. trade policies. The U.S. has lost its previous economic dominance, partly through the rise of Japan and the Asian NIEs. The concomitant change in U.S. trade policy comes as no surprise when viewed from a historical perspective.

Comparing with earlier periods, Great Britain held a secure economic superiority in the nineteenth century. At that time, 'its policy of fair field and no favour was also a minimal restatement of the political conditions for economic hegemony.'[6] By the time of the Great Depression (1873-1894), the diminution in Britain's pre-eminence in the world economy had begun. This led to a rise in protectionist sentiments and demands for an end to Britain's unilateral embrace of free-trade principles. 'Fair trade' and 'reciprocity' became promoted by the National Fair Trade League, the National Society for the Defence of British Industry, and the Reciprocity Fair Trade Association. Today, the U.S. follows the same path as Great Britain once did. The U.S. and Germany were to Britain what the Pacific nations – and Japan in particular – are now to the U.S.

[6] Lipson (1985), p. 39.

To the extent that the US still sets patterns, this development is threatening. Agricultural policies in violation of GATT rules, which do not make an exception for agriculture, is nowadays generally wide-spread in developed countries. It has been estimated by the Secretariat that the costs to the OECD countries are about 1 per cent of real income (OECD, 1990). Still, there is much resistance to cope with the problems, and the conflicts in interests involved have led to substantial difficulties for the Uruguay round. The mess can be traced back to U.S. unilateral action to introduce quotas on dairy products in 1950, and on other products in 1951. These policies, legalized by the U.S., were happily copied by others with unhappy results. Similarly, the U.S. legalized protectionism in textiles through a VER with Japan in 1957. An instrument was thereby created which has been used over and over again by the U.S. itself as well as others across a wide range of goods, in spite of its highly detrimental effects on social welfare.

In the post-war period, U.S. support for free trade and an orderly investment regime has been much more important than its deviations. As the U.S. no longer exercises this important leadership, but instead sets new destructive examples, the consequences will be far-reaching. This has, for instance, been pointed out in a statement by forty leading U.S. economists, among them four Nobel Laureates and four former Chairmen of the Council of Economic Advisers in the U.S. Administration (The World Economy, 1989).

The arbitrariness of a major power, seeking not rules – the application of which it would be willing to reciprocate when tables turn – but its own ad hoc advantage, has always created deep international animosities. Kindleberger (1969) claimed that international order is a public good which must emanate from a single leading nation. Likewise, Gilpin (1965) maintained that a stable, liberal order historically has been the creation of a succession of hegemonial powers. He predicted the decline in U.S. hegemony to cause general instability and uncertainty in the world economy.

Such views have not been undisputed. Keohane and Nye (1977) noted that shifts in hegemonial power cannot account for variations in the international structure of issues. A similar controversy has evolved over the exposure of foreign investments to political risk in developing countries. Allegations that political/ideological motives (related e.g. to U.S. hegemony and preparedness to defend foreign investments) would explain the variations in nationalizations of foreign-owned firms across countries and over time, have largely been discarded (Minor, 1988). Andersson (1991) similarly explains the occurrence and distribution of nationalizations based on their economic costs and benefits when countries compete for gains from foreign investments. The issue at stake in the present context is rather under what circumstances the Europeans and others will follow the Americans on a possible protectionist trail, and what can be done to reduce the risk that this happens.

3.4 Super-gains from Trade

In the best of all possible worlds, the model of free trade assures us that open competition is in everyone's interest. For this reason, and to prevent large countries from discriminating against small ones, there is nowadays a more or less universal adherence to the principle of 'multilateralism', at least in theory. With this is understood that a large power must do to another large power what it does to a small one. Within the framework of GATT, there have been substantial reductions in tariff rates in the last decades. After successive rounds of multilateral negotiations, the average most-favoured-nation (MFN) rates have come down to 5-6 per cent on industrial products in most developed countries.[7]

Efforts to estimate the size of the gains from trade through an elimination of tariffs, for instance in a European customs union, have shown these gains to be fairly modest. As indicated above, however, the tendency towards protectionism in our time concerns not tariffs but non-tariff barriers (NTBs). This is so even though NTBs generally are considerably more detrimental to social welfare in the country which adopts them. As has been calculated, e.g. in the Cecchini report (1988) for the European Community, the abolishment of NTBs is likely to be associated with major economic gains.

NTBs take the form of border as well as non-border measures. They include controls for the imposition of domestic taxes and all sorts of inspections, protectionist rules for public procurement, transports, telecommunications, market access and so on. The costs of NTBs in terms of reduced welfare and growth come through an inferior allocation of resources, lower economies to scale, reduced competition, and more cumbersome macro-economic problems. The reason that they are still instituted is that a small group of well organized producers often are in the position to capture large profits thanks to them, while the losses are spread among the large number of consumers. Hence, they tend to be detrimental from an equity viewpoint as well.

The East Asian success with an outward oriented development strategy has focused attention on gains from trade which go beyond the gains of the basic free trade models. In addition, trade can be expected to exert an influence on policies, which generates further gains. The following *super-gains* from trade can be added to those normally put forward in the literature;

- Competition stimulates *search processes* which are vital for growth. International trade enables a larger scale of production, which makes fixed costs for improvements in technologies, production methods, marketing and investments easier to carry, and improvements more profitable. Moreover, international trade makes it more costly not to

[7] IMF (1988). Of course, tariffs are considerably higher on agricultural products.

search. With a greater number of competitors there is a bigger risk of being outcompeted by others engaged in more intensive search.

- A close contact with foreign markets facilitates and necessitates a *feedback of information*. In this way, trade stimulates innovation and invention, faster diffusion of new technologies and new production and marketing methods.
- Trade, by allowing a greater number of countries to develop, increases the net pool of *R&D resources* (e.g. money and researchers). To the extent that countries such as Taiwan and Korea advance to the technological frontiers, there will be more and more noticeable competition for leadership in 'high tech'. Japan's advancement has already released such efforts on a large scale in both the U.S. and Europe.
- A commitment to increased trade in a growing number of countries reduces uncertainty in investment which is oriented towards the world market, and facilitates an efficient allocation of resources internationally.
- There are positive employment effects in less developed countries when the factor markets are not distorted so that it pays to use labour-intensive production methods rather than the high capital intensity of import substitution. Together with the realization of more efficient markets this makes it possible to achieve a more *equitable income distribution* without compromising incentives.
- Both management and work forces get used to adjustment needs and try to handle them by *acting rather than reacting*. They do not engage so quickly and so much in what has been referred to as 'directly-unproductive activities', i.e. the spending of resources on persuading governments to provide protection and privilege.
- When gains from trade are clearly recognized, *governments* are more likely to *accept change* and to weather whatever domestic pressures there are to protect against adjustment.[8]
- An open economy is more exposed to international economic disturbances, but is also *better equipped to handle shocks*. A large export sector can more easily be expanded and imports more easily be contracted. At the same time, the government is better prepared to apply macro-economic adjustment tools. In an import substituting country, by contrast, income levels are often too low to compress. This means that mainly essentials are imported, i.e. costly input goods which are necessary to keep the expensive and inefficient production going. These differences were highlighted by the differing performances of countries during the oil crises of the 1970s.
- If one can conduct business without constant contacts with the government, it is easier to survive in the provinces. This has a positive effect

[8] Treaty obligations in the form of GATT rules make it still easier to stand up against pressures for protectionism. International agreements can be said to give the advantage of 'tying one's hands'.

on the *regional distribution* of activities, which contributes to a more equitable income distribution overall.

Concerning policies, countries pursue not only tariffs and non-tariff trade barriers, but also what we may call 'domestic trade obstacles' (DTBs). These come in many forms, e.g. subsidies, zoning laws, government production, economic planning in general, restrictive practices by unions and corporations, limitations on the right of establishment, and so on. They could be put into effect by governments or by firms, groups of firms, or unions (see further Olson, 1982).

Neither the aim nor the immediate consequence of DTBs is to regulate trade. Their effects on international trade appear *indirectly*, and they are often such that it is difficult to classify a regulation as an NTB or a DTB. Yet the distinction can usually be made. For example, a rule preventing the establishment of foreign banks is an NTB, while a regulation prohibiting banks from owning an insurance company is a DTB.

Tariffs and NTBs give rise to smuggling across national borders. DTBs set up similar forces. There is 'smuggling' in the form of tax evasion and the development of an underground economy. And the more difficult this 'smuggling' is, the more 'home' production there will be. The theoretical trade models usually assume free domestic trade and then explore the consequences of an opening up of international trade, i.e. a removal of tariffs and NTBs. This may obscure important relationships, however. There is often a substantial mileage of high domestic trade obstacles and this can be the case even in countries with strong support of the ideals of free trade.

As domestic trade obstacles ultimately will have foreign trade effects, international trade could have an impact on domestic trade obstacles as well. Tariffs and NTBs are eliminated through unilateral decisions, negotiations, cross-country agreements, or some sort of foreign pressure. The domestic bank market, for example, may be opened to foreign banks because it is necessary for the national banks to be permitted to establish branches abroad. DTBs may, similarly, be exposed to foreign pressures. Typically, however, other countries are likely to accept 'national treatment', i.e. they accept domestic obstacles to trade which do not discriminate against foreigners. DTBs which are the result of private operations are also relatively difficult to combat by government decisions. Hence, DTBs must often be removed through other mechanisms.

Some DTBs are eliminated through *foreign competition* as a direct result of an opening up to international trade. Some domestic monopolies and some private restrictive practices may be broken up in this way. Olson (1982) sets out reasons why 'distributional alliances' may be harder to operate in a wider market. Still, most DTBs are not undone in this direct way.

A number of government DTBs could be eradicated through *unilateral decision (deregulation)* in order to increase the international competitiveness of the economic system as a whole or to put certain branches in a better position in relation to their international competitors. A country may, for instance, have negotiated the elimination of NTBs preventing the establishment of foreign insurance companies. Not to put national insurance corporations at an impossible competitive disadvantage it may be necessary as the next step to eliminate domestic trade obstacles in the insurance business. A country which eliminates its foreign exchange restrictions may similarly find it advantageous to reduce taxes on capital market transactions. The more mobile factors, establishments and activities are across borders, the greater the likelihood that domestic pressures will keep obstacles to domestic trade down in an effort to remain internationally competitive.

The 'Structural Impediments Initiative', already discussed in the previous chapter represents an interesting example of strong international pressure on DTBs, in this case on Japan. The removal of the DTBs targeted would mean an elimination of domestic trade obstacles. Foreigners would benefit less than the Japanese themselves. Entry would be made easier, particularly for new Japanese goods and firms on the domestic market. It is also for this reason that some Japanese hope that American pressures will help them solve a number of serious domestic problems and eliminate DTBs which the government by itself is not strong enough to abolish. Openness to trade brings pressures that can help to identify where the obstacles to efficiency are, and furthermore, to generate the political power to combat the groups that gain from them. This way, trade can help to remove internal obstacles so as to revitalize an economy from within. The financial sector is probably as good an example as any merchandise sector.

The effects of removing DTBs will be positive when they break up obstacles which are undesirable from a social point of view. Domestic trade is as important as international trade, and gains from domestic trade are basically the same as the gains from international trade. It should be noted, however, that some DTBs may be useful regulations of trade. It is not in the interest of a society to import all goods. There are, for example, goods and services whose consumption is associated with negative externalities, such as pollution.

3.5 International Movements towards Trade Liberalization

Parallel to the pressure for protectionism, there are continuous and successful movements in favour of liberalization as well. The new protectionism sometimes appear to dominate only because, on the whole, trade liberalization efforts are pursued under other headings. One is the Uruguay Round, which *may* eventually lead to further reductions in conventional trade obstacles as well as NTBs. The success which the East Asian countries have recorded with outward-oriented strategies has increased the LDC interest in the Round.

Still, the Third World favors the right of each country to maintain whatever policies it likes, and the multilateral negotiations clearly encounter substantial difficulties. For LDCs, the Uruguay Round – except for agricultural products – is actually of limited interest. The East Asian demonstration effect, to the extent that it works at all, rather makes LDCs look for *unilateral* reductions, insisting that they be exempted from the normal standards of the GATT discipline. The demands concern unilateral removal of developed country tariffs, NTBs, and most notably, DTBs. Other examples of unilateral reductions include:

- A number of industrial countries have made unilateral reductions in DTBs for domestic profit, but also in order to increase their international competitiveness, especially in services.
- The East European countries are moving unilaterally towards liberalization, particularly in their DTBs. The elimination of DTBs is likely to be followed by reductions in tariffs and NTBs, probably with concessions by other countries to begin with. For example, the East European countries will most likely be accorded MFN treatment and be permitted to become members of GATT (which some already are, but only in name).
- East Asian countries are reducing tariffs and NTBs partly as a result of foreign pressures, partly to give a sharper edge to their already successful trade strategies.
- The most important efforts to sweep away NTBs, however, are part of the greater efforts to achieve the economic integration of countries. By far the most pervasive example is that of turning the 'Common Market' in Europe into the Single Market. This has been paralleled by, and facilitated by, unilateral reductions in DTBs. Intentionally or unintentionally, however, the EC may assume rights to introduce DTBs. Mrs. Thatcher's misgivings about yielding authority to Brussels are probably not primarily that the EC might become protectionist in the sense that it will develop high tariffs or even NTBs, but rather that the central authorities will issue increasingly ambitious – that is, restrictive – European-wide DTBs.

In connection to the 1992 program, there are also negotiations over a European Economic Space (EES). The idea has been to cater for free trade arrangements between the EC and individual EFTA countries which could be tied to the Single Market. The four freedoms – of goods, services, people and capital – would be extended to the EFTA countries, although border controls would remain as the EES is not a customs union. In addition to certain specific issues, such as fishing in Nordic waters and environmentally sensitive transit traffic in Austria and Switzerland, the decision-making process presents complications. The EFTA countries want to avoid the humiliation of just having to put into effect decisions already taken by EC authorities. The EC, on the other hand, does not want to throw any doubt upon the Community's institutional system and the autonomy of its decision-making. For the time being, there seems to be a reasonable chance of a satisfactory agreement. Still, as the tide is moving and the EC has the momentum of change in its hand, full or no liberalization with regard to the Single Market may turn out to be the only viable option for the EFTA countries, unless they are merely to implement the decisions already taken by the EC.

There are also efforts towards integration within the Pacific region. The Southeast Asian Nations (ASEAN) had already grouped themselves together in ASEAN in 1965. Their cooperation has been successful in political terms, which perhaps was the primary objective, but the economic integration has been meagre. The countries' heterogeneity and, at the same time, competition in trade and investment has prevented any great success.[9] For very much the same reason, efforts to cooperate in the Pacific region as a whole have yielded only a number of forums for general political and economic discussions. Being on the periphery, Australia has over the years had a special interest in Pacific integration. The efforts of the Prime Minister, Mr. Hawke, have resulted in the formation of a 'non-treaty organization'. It is unlikely that the foreseeable future will offer anything more ambitious than an OECD-type of organization for the Pacific countries.

4. The Third Leg of the Triangle

4.1 Introduction

To sum up some points made in the previous chapters, there is an ongoing gravity shift in the importance of economic relationships from the Atlantic to the Pacific. A key factor behind East Asian dynamism is the outward orientation of the region. Its example has exerted a demonstration effect on the rest of the world and created new opportunities, but also set up new risks.

There have been partly contradictory influences on trade policies in developed as well as developing economies. Above all, the U.S. has stepped down from its position as champion of free trade and capital movements. Under the umbrella of GATT, tariffs have been stabilized at a low level, and many countries take decisive steps towards an opening up of their trade regimes. This has partly been motivated by the costs of the new protectionism, and the existence of super gains from trade, some of which are conspicuous in East Asia. Openness brings increased competition, communication, and stimulates not only industrial efficiency but also

[9] The differences in national policies have contributed to preventing not only a free trade area, but also agreements on 'planned specialization'. Why would the Singaporeans wish to pay high prices for diesel engines from Malaysia when they can get them inexpensively from Taiwan?

human skills. In addition, trade serves to break up domestic trade barriers which politicians may not be able to deal with directly.

At the same time there is a tendency towards protectionism in the form of NTBs and DTBs, although such measures tend to be much more detrimental to social welfare than tariffs. We have noted the argument that a liberal world order would require the leadership of a single hegemonial power, such as Great Britain in the nineteenth century and the United States in part of the twentieth century. The question in our time is whether other countries will follow on a trail towards protectionism as the U.S. has lost the economic leadership. While the potential advantages of going for world markets have been powerfully demonstrated, the prospects of new barriers to trade diminish the belief of other developing countries that they can emulate the achievements of East Asia.

Thus, some factors point towards liberalization, while others seem to favor a protectionist tendency. Which way are we to go? As pointed out in Chapter 1, the decline of 'big' powers is accompanied by the rise of relatively small and more flexible countries which emphasize human skills, high specialization and advanced technology. At the heart of these developments lies, on the one hand, Japan which is followed by the surrounding East Asian countries and, on the other hand, Germany accompanied by the rest of the European Community.

This chapter focuses on the relationship between Europe and East Asia, particularly on whether Europe has taken advantage of the opportunities and faced up to the risks that emanate from East Asian dynamism. Initially, we will consider some trade and investment figures. The process of integration in the EC is thereafter reviewed, as well as the expected effects of the 1992 program. This is followed by an analysis of the risk for external protectionism in the EC.

4.2 A Triangle of Economic Relations

The bulk of world trade in goods and factors as of today can be characterized as a triangular flow. This triangle consists of the U.S., Europe, and East Asia. Broadly speaking, the economic activities along the three sides show the following intensities:

- Between the U.S. and Europe, there are intensive trade and investment relations.
- The U.S.- East Asia side of the triangle shows a high trade and investment activity.
- Trade and investment relations between East Asia and Europe are relatively undeveloped.

To look more closely at the figures behind these broad arguments, we consider some alternative measures of trade intensities. Studying the U.S. export penetration of Japan, we either compare U.S. exports to Japan with U.S. exports to the EC, or we compare U.S. exports to Japan with

EC exports to Japan. Because we compare exports from different countries to one and the same market, the disputed degree of Japanese 'openness' to imports does not affect the comparison.

To make figures from different countries comparable, Table 9 eliminates the difference in size between markets by dividing export figures by market GDP in the exporting country. In Table 10, on the other hand, the export figures are divided by the total exports of the exporting country. In this case, intra-EC trade has been excluded in order to facilitate a comparison between the US and the EC. In Table 11, these comparisons are replicated for exports to Japan in manufacturing alone. Table 12, finally, calculates the imports from East Asian countries divided by the GDP of the importing country.

4.3 Exports, Imports and Direct Investments

In Table 9, it can be seen that the U.S. has had a considerably higher export intensity to Japan than the EC or Sweden since 1970. Only in 1987 did the figure for the EC or Sweden surpass 50 per cent of that of the U.S. A comparison of the export intensities to South Korea, Taiwan, or the Asian NIEs as a whole similarly shows larger figures for the U.S. than for the EC or Sweden. Broadly speaking, however, the differences were the largest in 1980, and they shrank somewhat up to 1987. In fact, the EC-Japan export intensity almost doubled between 1975 and 1987, while that of the U.S.-Japan remained stagnant.

In Southeast Asia, on the other hand, Table 9 shows that the U.S. and the EC did about equally well. In the 1980s, Sweden was consistently ahead of both the U.S. and the EC in Thailand as well as in ASEAN as a whole. Compared to the record of Japan, however, all Western countries were significantly behind. This applies particularly to the NIEs, where Japan recorded an export intensity three times as high as the U.S. or the EC in 1987. In ASEAN, Japan's export intensity was about twice as high as those of its competitors in the West.

As can be seen from Table 10, the general patterns in export intensities are largely unchanged when exports are divided by total exports instead of GDP. However, the U.S. emphasis on Japan and the Asian NIEs relative to that of the EC is magnified. While the U.S. exported 11 per cent of its total exports to Japan, the corresponding figure for the EC was just above 5 per cent. Still, the difference has declined significantly over the 1980s. In ASEAN, the U.S. was marginally ahead of Europe. Furthermore, the substantial Japanese lead recorded in Table 9 is here much diminished. The share of Japan's total exports going to ASEAN in 1987, for example, is less than twice as high as that of the U.S. (6.8 per cent compared to 3.9 per cent).

As shown by Smith and Venables (1989) among others, the present segmentation of the European Community has led to an over-emphasis on trade between the individual member countries. Compared to the EC's total external trade, Table 13 shows that the EC's internal trade increased from 108 per cent in 1982 to 142 per cent in 1988. The swamping effect of EC's internal trade is not captured in Table 10 since intra-European trade has been excluded. The falling behind of the export intensity of the European countries in East Asia that is recorded in Table 10, as compared to Table 9, would consequently have been further magnified had the intra-European trade been included.

Considering only manufactured exports, Table 11 shows that the general picture for Japan changes somewhat. As can be seen at the bottom of the table, more than 80 per cent of the EC's exports to Japan consist of manufactures, compared to only 50 per cent for the U.S., as of 1985. In relation to GDP, the intensity of the EC's manufacturing exports to Japan was much behind that of the U.S. in 1980, but it had almost caught up by 1985. As a share of total exports, however, the EC exported less than 1 per cent to Japan when the internal trade of the EC is included. Excluding *all* West European trade, the EC still exported only 2.7 per cent to Japan in 1985. For the U.S., the corresponding figure was 5.2 per cent. This impression of a greater emphasis on Japan by U.S. manufactured exports compared to EC manufactured exports is magnified by a comparison with total manufacturing exports. Excluding EC's internal trade, the EC exported only 2.6 per cent of its total *manufacturing* exports to Japan in 1985. The corresponding figure for the U.S. was 7.7 per cent – or about three times as much as the EC!

Turning to import intensities, Table 12 shows a consistently larger share of imports from countries in East Asia for the U.S. compared to the EC or Sweden. In 1980, the U.S. imported almost twice as much of its total imports from Japan as did the EC. While this difference diminished up to 1987, the gap instead widened in imports from the Asian NIEs. In 1987, the US imported 13.1 per cent of its total imports from these countries, while the corresponding figure for the EC was only 5.7 per cent. In the case of the ASEAN countries, the difference was smaller. It can be noted that Japan in 1987 imported a smaller share of its total imports from the Asian NIEs than did the U.S.

Comparing the stock of direct investments, finally, Tables 14 and 15 indicate a highly skewed pattern. According to the home countries, West Germany held 20 times as much investment in the U.S. as in Japan in 1986, and the United Kingdom 40 times as much in 1984. The stock of Japanese direct investment in the U.S. is about 2.5 times as large as that in Western Europe. The data reported by the host countries show that Japan has attracted almost three times as much direct investment from the U.S. as from Western Europe. The relatively small numbers recorded for Japanese investments in the U.S. as well as in Western Europe have been much magnified in the most recent years.

To sum up, the comparisons of intensities in exports, imports and the pattern of direct investments point towards an imbalanced triangular flow in world trade and investments. The European-East Asian side is underdeveloped. Europe has done well in increasing its exports in manufacturing goods to Japan which, among other things, shows that success can be achieved. In terms of its overall manufacturing exports, however, the EC sells a much smaller share in Japan than does the U.S. The small amount of EC direct investment in Japan, compared to that of the U.S., also indicates that the EC has not put much effort into exploiting East Asian markets.

4.4 The Imbalances – Missed Opportunities and Looming Risks

Not only are the economic relations between Europe and East Asia underexploited, but they are also severely imbalanced, and threaten to become even more so in the future. Consider Figure 1, which depicts the EC's trade balance with external countries in relation to the EC's exports to these countries (1a), and in percentage of the EC's total external exports respectively (1b). The EC had a deficit with the U.S./Canada in 1982, but this turned into a surplus in 1987 and 1988. With EFTA, the EC had a fairly stable trade surplus, amounting to 1-2 per cent of EC's total exports over the period studied. Japan and the other export-oriented countries in East Asia, on the other hand, account for large and growing deficits.

Figure 1a: EC'S EXTERNAL TRADE BALANCES IN PERCENTAGE OF EXPORTS TO REGIONS

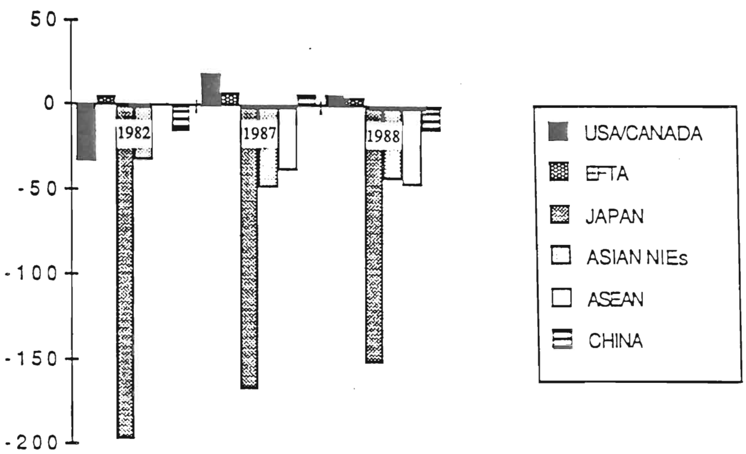
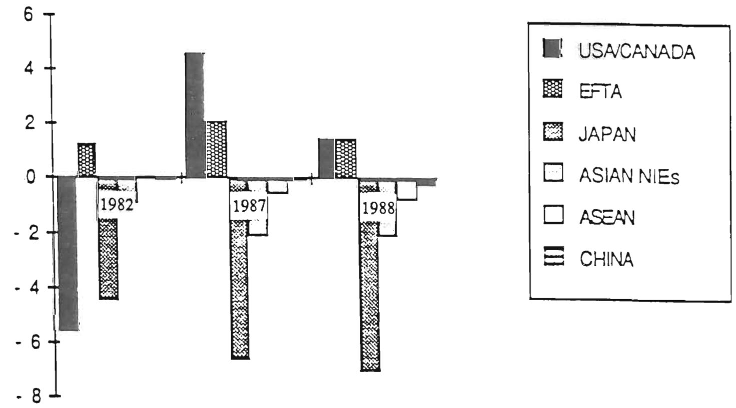


Figure 1b: EC'S EXTERNAL TRADE BALANCES IN PERCENTAGE OF TOTAL EC EXPORTS



Source: IMF, Direction of Trade Statistics.

Figure 2a: EC EXPORTS TO DEVELOPING COUNTRIES *

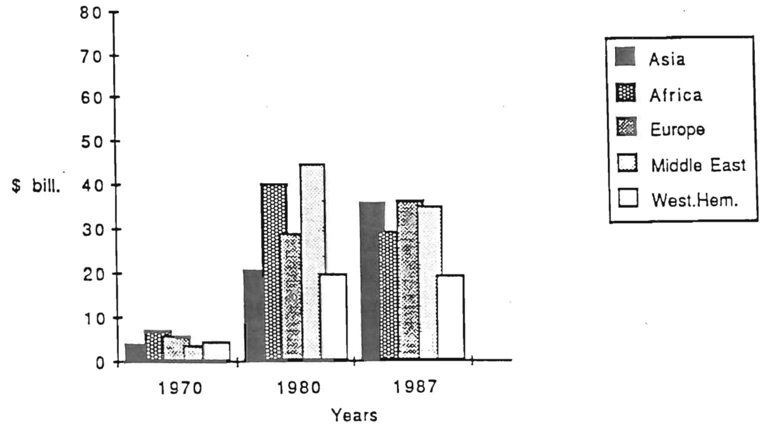
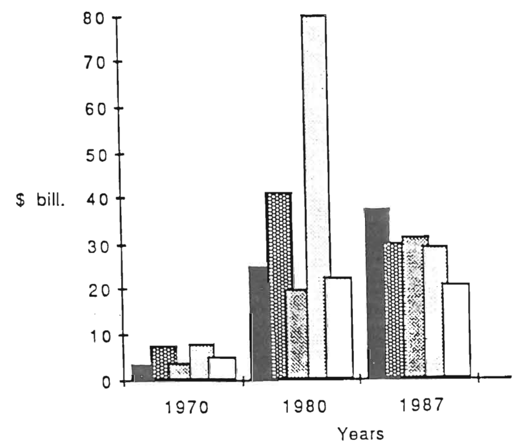


Figure 2b: EC IMPORTS FROM DEVELOPING COUNTRIES



Source: International Monetary Fund, Direction of Trade Statistics, various issues.

* The figure includes only the six original EC members plus Denmark, Ireland and the U.K. in order to enable comparisons over time.

In relation to EC exports to respective country/region, Figure 1a shows that the deficit with Japan shrank from 200 per cent to about 150 per cent in 1988. In relation to the total exports of the EC, however, it can be seen from Figure 1b that the deficit with Japan increased from about 4 per cent in 1982 to about 7 per cent in 1988. The deficit with the Asian NIEs has also grown steadily to about 2 per cent of total EC exports. Trade with the other ASEAN countries (excluding Singapore) displays a similar trend.

In the EC's trade with developing countries in general, Asia has become more and more dominant. Figure 2a and 2b depict the composition of the EC's trade with five regions of developing countries in 1970, 1980 and 1987. As is illustrated in Figure 2a, the Asian countries increased their share of EC exports from 15 to 23 per cent. Figure 2b displays an even greater increase in the Asian share of EC imports from developing countries, up from 11 to 25 per cent in 1987. As for other developing countries, those in Europe also increased their share of EC exports, but they recorded only a marginal increase on the EC's import side. The 'losers' in trade with the EC were Africa, the Western Hemisphere and, on the import side in the 1980s, the Middle East. At the same time, the EC's trade with developing countries was reduced from over 20 per cent of total EC trade in the 1970s to only 17 per cent in 1987.

Thus, East Asian dynamism makes itself felt in large deficits for Europe in the regional trade between the regions. Trade increases in both directions, but the deficits are widening relative to EC's total trade. This is not least the case as East Asia now pays much more attention to Europe than it used to do. To provide some anecdotal evidence, Newsweek (1989) reported that, according to a Marubeni Corporation employee, there is now only standing room on seminars focusing on the EC market. Sumitomo Bank is said to devote as much attention to the European market as to the U.S. market. Sony has, according to the same article, appointed its senior European manager to its board of directors.

In the case of the U.S., the trade imbalances reflect severe macro-economic problems, which lays the foundation for additional frictions. A macro-economic correction in the U.S., or additional protectionist measures there, will eventually mean a reduction of U.S. imports of trade and investment from East Asia. As the EC propensity to import from East Asia is relatively low, there is more room for East Asian efforts to raise it. U.S. corrections would further intensify East Asian efforts to sell in Europe. Such a re-orientation of East Asian exports and investments might, because of the present trade and investment imbalances, stir considerable friction, unless there is a shape-up of EC export and investment activities in East Asia.

Of course, there may be nothing wrong or abnormal about bilateral deficits in trade and investments. In the present context, however, we will see that the business relationship between Asia and Europe is generally hampered by a lack of knowledge. While the Asians are now moving to change this state of affairs, the Europeans have become preoccupied with their own restructuring. The imbalances that prevail in trade and investments consequently indicate missed opportunities, particularly on the part of Europeans in East Asia.

Firstly, the fact that the U.S. intensities in exports and investments across the Pacific are higher than those of the EC in East Asia might suggest that there are missed opportunities on behalf of the EC in East Asia. Second, higher export and investment incentives across the Atlantic than those Japan has achieved within Europe indicate that there are still missed Japanese opportunities in Europe. Third, the greater export and investment figures accounted for by the Japanese in both the U.S. and the EC might indicate missed opportunities in East Asia on behalf of both these regions.

Moreover, U.S. exports to Japan and the NIEs, as well as the size of American investments there, out-perform those achieved by Europe. This is so in spite of the fundamental imbalances in the U.S. macro-economy. While Europeans supposedly have more internationally oriented companies and management than the Americans, who for long could rely on their large domestic market, the U.S. has been more active in East Asia. The impression of missed European opportunities is underscored by the worries in many East Asian countries of being economically dominated by the Japanese, as well as politically dominated by the Americans. Some countries, e.g. in ASEAN, are involved in outright efforts to increase the European investments.

4.5 Stages of European Integration

From the early 1970s, the EC's economic record has deteriorated in absolute as well as relative terms. As can be seen from Table 16, the EC countries accounted for about 2-4 per cent annual growth in the period 1965-1980. Between 1980-86, average annual growth was about one per cent (except for the United Kingdom), and in industry it was even less. Other regions had lower growth too, but the decline was generally less drastic than in the EC. As can further be seen from Table 16, many EC countries have above 10 per cent unemployment, which is more than in the U.S., Japan or Sweden. The figures for developing countries are not directly comparable.

With this kind of economic record, it is no surprise that Europe was widely viewed as the 'tired continent' up to a few years ago. Eurosclerosis became a term for stagnation in old age, in economic terms. In the research project *Costs of non-Europe*, the EC Commission partly blamed the economic problems on the limited integration of the member economies. European firms tend to be too small to fully exploit advantages of scale, resulting in inefficient resource utilization, while they are too large for their domestic markets, resulting in monopolistic pricing.

The economic problems, as well as the necessity to handle the new competition from the Asian NIEs, have gradually intensified the quest for European integration. Broadly speaking, this can be said to have passed through three stages:

- The first period was driven primarily by *visions*. The Treaty of Rome was signed and the great plans laid down to prevent future wars between France and Germany. A new Europe was to be constructed which could compete economically with the U.S. and the Soviet Union, both of which were viewed as formidable competitors at the time. By creating an economically stronger Europe, it was hoped that electorates would not be attracted to give up political and economic freedoms for economic growth. After some years, the political goal to establish a close relationship between France and Germany seemed to have been reached. The Americans no longer appeared as impossible to beat and most people forgot that there had ever been any competitive threat from the economy of the Soviet Union.
- The second phase was initiated as these pressures from the outside disappeared, and the EC became characterized by growing *bureaucracy* rather than further liberalization. Brussels increasingly regulated production and trade in agriculture, and also in industries such as steel, ship-building, and textiles. The ideals had lost their power, and Europessimism grew instead.
- The third stage is that of the *Renaissance*. New pressures on Europe have developed, at this time in the form of competition from Japan and East Asia. The creation of the Single Market is basically the response to these new pressures.

4.6 The Effects of the Single Market

Today, the EC serves as a customs union with a common external tariff. Apart from this, there is no clear definition of common rules for the external policy. In particular, the EC countries maintain different quantitative restrictions on imports from third countries. In addition, there are exceptions from free trade in goods as well as factors within the EC, due to e.g. differing technical, hygienic and veterinary standards, and restrictions in the right to import services. By 1992, the interior barriers to trade are to disappear, public procurement is to be opened up, and the factor markets deregulated. An increased budget will support European research and development programs, and enable greater common responsibility for environmental, regional and social issues.

The legislative program for 1992 was set out in the 1985 White Paper *Completing the Internal Market*. Its message was reinforced in mid-1987 by the passing of the Single European Act, which instituted a weighted form of majority voting as the norm in the council for its 1992 directive-passing. This amounts to a binding commitment to fulfill the internal market. In June 1988, there was an agreement to remove exchange controls, and in February 1989 a settlement on budget and farm policies. By the summer of that year, about half of the roughly 300 European laws of the White Paper had been passed. The project can be said to be developing at a satisfactory pace for completion in 1992.

There is little doubt that the 1992 program actually will result in increased integration. A company located in one member country will be able to compete more effectively in the others. Meanwhile, competition will increase in its own country. The result will be an improved utilization of scale advantages and higher efficiency due to more competition. From simulation models it has been concluded that prices will be reduced and production will increase in the many industries characterized by scale advantages and imperfect competition. Sectors will be affected differently, however, due to factors such as different transport and communication costs, and because the present level of competition differs. The welfare effects of the resulting structural adjustment, caused by attraction of resources from one industry to another, will be complex and require careful studying.[10]

In valuations of the program, the EC Commission has found the outcome consistently favourable for the Community itself. According to the quantitative estimates, the direct and indirect effects will in the medium run:

i) cool the economy, deflating consumer prices by 6.1 per cent on average,
ii) trigger economic activity that adds on average 4.5 per cent to the EC's GDP,
iii) relax budgetary and external constraints and thereby improve the balance of public finances by 2.2 per cent of GDP on average,
iv) create 1.8 million new jobs, reducing the jobless rate in Europe by approximately 1.5 per cent, and
v) improve the external balance by 1.0 per cent of GDP.

In addition to the major scenario, the EC Commission also considers the possibility that governments will give up some gains from fiscal consolidation and lower inflation. This would make a 6.5 to 7.5 per cent increase in GDP and a 4.4 to 5.7 million increase in employment attainable. The deflating of consumer prices would then be between four and five per cent, and the external balance worsen somewhat.

The figures are uncertain but indicate the probable direction of 'static' effects. As stressed by Smith and Venables (1988) on the basis of industrial simulations, there should also be greatly reduced profits and an exit of many firms. Several writers have pointed out the possibility of great

[10] The prices at which expanding sectors attract factors of production need not reflect socio-economic values due to e.g. imperfect competition. Helpman and Krugman (1985) present some conditions under which more competition would increase welfare under such circumstances.

'dynamic' effects. Geroski (1988) speaks for more innovation due to intensified competition, while Baldwin (1989) argues that more profitable investment would raise the steady-state capital labour ratio – permanently adding a quarter to a full percentage point to growth. These figures are even more uncertain, but they point to the possibility of very large benefits over time.

An estimation of the welfare effects of 1992 requires not only consideration of the effects within the EC itself. The presented calculations have all assumed unchanged barriers with respect to non-EC countries. In practice, there may be either an 'opening' or a 'closing' of the Community to external flows of trade and investment. The EC's behaviour vis-à-vis the rest of the world, and responses from the outside, will influence the final outcome.

4.7 EC Protectionism

The deregulation of Europe through the Single Market will no doubt be helpful for European economic development. Further gains may be achieved through a functioning EES, i.e. the removal of West European DTBs, and also East European economic reforms. The result will be reduced trade obstacles for outsiders as well. The reduction in DTBs will provide economies of scale to Japanese and other East Asian firms as well as to other outsiders which approach European markets.

While the EC plans to replace existing national barriers to trade with measures that are common for the Community, the Commission has assured that the average level of external protection will not be increased. This liberal stance was supported by the composition of commissioners instituted in Brussels last year (The Economist, 1989). Pearce and Sutton (1986) maintained that the EC as a whole is 'unlikely to shift to a systematically more protectionist stance. Such a shift would require a greater similarity among member states' levels of competitiveness and attitudes...'. In fact, the EC has a vested interest in trade, with its external exports amounting to 20 per cent of world exports and nine per cent of its own GDP.

In spite of these arguments, there is a lack of rules for the external trade policy in the White Paper, and the current development does not lend support to the official stance of the EC Commission. In 1988, about half of all known VERs protected the EC market, and an increasing number targeted Asia. Table 17 shows that the increase in VERs between September 1987 and May 1988 was 100 per cent in the EC, which can be compared to 74 per cent in the rest of the world.[11] The increase was the most pronounced against developing countries (160 per cent), and espe-

[11] Table 17 should be viewed with caution. Some increases may have been magnified by a reclassification of actions during the period. The table includes e.g. unilateral EC actions such as EC surveillance and undertakings in settlement of antidumping actions.

cially high in agriculture and food products (220 per cent), electronic products (200 per cent), textiles and clothing (171 per cent) and 'others' (500 per cent).

Brussels has announced that most national quantitative restrictions on imports are to be scrapped by 1992, but some goods have been said to be excepted. Concerning subsidies, the White Paper does not contain any precise and concrete proposals regarding the time and implementation of their removal, as it does for EC's inner border controls. It has been more or less assured that those subsidies that hurt other member countries will disappear by 1992, but this may increase the willingness to use such subsidies against third countries. Furthermore, it has not been made clear how the national quotas on textiles allowed under the MFA will be shared, and the expensive agricultural policy is a constant source of distress.

With the introduction of VERs and OMAs, Europe is displaying a tendency to follow the U.S. by putting up its own protectionist measures. However, it is particularly the threat of antidumping proceedings which has emerged as a powerful bilateral instrument to get around GATT in the EC. Obtaining community-wide VERs is difficult in the EC, since approval of the Council of Ministers is normally blocked by West Germany, Britain and the Netherlands. The EC therefore tried in the Tokyo round to enforce an amendment of Article XIX of the GATT which would enable importers to act unequivocally and selectively against 'disruptive imports', meaning imports from new suppliers. The EC claimed this to be a requirement for the acceptance of the rest of the Tokyo round, but the threat was not pursued in the end. Now, antidumping has enabled the Commission to acquire what it did not get in the Tokyo round.

As reported by Messerlin (1987 and 1989), the EC antidumping law has progressively given rise to trade measures inconsistent with GATT, and the impact has been severe. The policy is administered by an office within the Commission with a political 'appeal court' that belongs to the Executive rather than the Legislative Branch. In contrast to Article XIX, which does not allow discrimination between countries, antidumping proceedings are concerned with companies. Hindley (1988, 1989) and Palmeter (1989) show that practically any exporter can be found guilty of dumping. A bias appears both because of the calculation principles, and of the way they are used.

When calculating a market reference price at home, the EC Commission supposedly looks for the average, but gives itself the right to neglect certain domestic prices. Concerning export prices the Commission systematically neglects those that are above the home market reference price, arguing that 'negative dumping' has no legal existence, and treating these export prices as if they had been at the reference price. If prices have the same mean and spread abroad as in the home market, the principle of disregarding 'negative dumping' makes it certain that dumping will be 'discovered'.

Between 1980 and 1986, the EC decided on 213 affirmative cases of antidumping, many of which touched only narrowly defined goods (Finger and Olechowski, 1987). The seriousness cannot be judged on the basis of the number of cases, however, but hinges on the linkage to VERs. It is commonly argued that the firms targeted are based in countries that use discriminatory trade policies themselves. The prime reason is hardly protective barriers at home, but rather the absence of readiness to agree to VERs, which is clearly seen from the cases made against Hong Kong.

An exporter informed that he is suspected of dumping generally faces an easy choice. Either he avoids problems by raising prices, acquiring a higher profit margin but suffering reduced sales, or he goes through a costly legal process, the outcome of which is more or less predetermined. Subsequent to the verdict the firm cannot expect a higher profit per unit on its remaining sales but must count on a duty. Messerlin (1989) reports that antidumping measures have reduced imported quantities by 40 per cent three years after the initiation of the investigations, and that the average ad valorem equivalent has been about 23 per cent.

As discussed in Andersson (1989), the pressure for protectionism may intensify as the Single market is realized. Domestic firms squeezed by increased competition from other EC countries are tempted to seek compensation in the form of external protection. The abolition of subsidies in defence of competitors within the EC will make funds available for discrimination of outsiders over the budget. While external competition hurts many producers, it is mainly consumers that benefit from it. The former tend to be relatively well organized and apt to achieve political leverage, while the latter often have little to say.

Japan, the Asian NIEs and the East Asian countries following their trail are particularly likely targets of discrimination in the EC by 1992. The EC-Asian trade is imbalanced in favour of East Asia, and it is less important for the EC than for Asia as it comprises a much smaller share of total trade for the former. The declining applicability of GATT and the most-favoured-nation principle enables protectionism against East Asia specifically. Summing up some of the arguments already made in this and the preceding chapter, and adding a few points, the following factors might favour a discrimination in the EC of imports from East Asia:

i) Irrespective of 1992, the need of the U.S. to achieve balance in its external trade will exert a continuous downward pressure on the dollar.[12] The Asian NIEs, with their currencies tied to the dollar and their concentration on the U.S. market, are forced to diversify their exports away from it, while the European market is becoming more lucrative. As import quotas in the EC are filled, Asian exports will

[12] In the short run, this may naturally be overshadowed by changes in consumer behaviour, shifts in interest rates, the need of investments for developing the lagging economy in former East Germany, etc.

appear increasingly threatening and the demand for protectionism against them will increase.

ii) Protectionist measures which can effectively be used selectively against imports are already available in the EC. This may put protectionists in the favourable position of merely preserving the prevailing order, while the burden of overturning it will rest with the advocates of liberalization.

iii) The French government, which has advocated raised external protection as the interior is reduced, has gained support by the added membership to the EC of Greece, Spain and Portugal. Countries with less advanced industries are generally most adverse towards competition, and the newcomers in the EC have a lot to gain from preventing an increase in imports from Asia in e.g. leather, footwear, textiles, clothing, and steel. As pointed out in connection to Figure 2, EC imports from developing countries have shifted the most towards Asia, with Europe (in this case including Spain and Portugal) in the second place.

iv) When the internal barriers to trade, such as Article 115, are abolished and pressure builds up for 'inner-liberalization compensating' protection against third countries, North America and EFTA are in a relatively stronger bargaining position than Japan and the developing countries. As noted, East Asian countries are the most likely targets among the developing countries.

In the financial markets, universal banking is set to prevail throughout the EC, and the "erga omnes" principle aims at extending the liberalization to all countries worldwide. It is true that the so-called "reciprocity clause" of the second banking directive requires the same access for EC banks abroad, which is believed to have speeded the establishment of American and Japanese subsidiaries in Europe before 1993 (when it becomes effective). Financial liberalization may also have been stimulated in the US and Japan, but it was unquestionably coming anyway. The risk of discrimination is relatively small in the financial markets, partly because the ethnical, cultural and political barriers will remain in Europe. In financial services, the problems of acquiring information and coping with monitoring costs strongly favour those that are incumbent in a market. The establishment of a single currency union and a common central bank should do away with the exchange rate instability within the EC and, hence, make Europe more accessible for outsiders. There are still problems with the design of an optimal monetary policy in the heterogeneous Community, however, and it remains uncertain how quickly the member states are willing to move in this field. In any case, customized relations rather than discrimination will remain the major impediments for foreign financial institutions in Europe (cf. Shigehara, 1990; Feldman, 1990).

4.8 The Viability of EC Protectionism

The risk of protectionism in the EC will probably be much influenced by the degree to which the 1992 program turns out to be beneficial for the EC itself. Given that the envisaged mobility in investment and labour diminishes the pockets of idle resources that today exist within the EC, the support for protectionism will decline. It should also be stressed that Germany, the economic giant in the EC, is a firm opponent of protectionism. The stronger Germany becomes, the more difficult it will be to turn the EC onto a protectionist trail.

Even to the extent that the protectionists would prevail over the free traders, it must be asked whether EC protectionism represents a 'viable' strategy to keep East Asian producers out from the Single Market. For a number of reasons, the probable answer to this question is 'no'. For example, a reduced percentage of sales of the average firm can be protected in a global economy, but export markets cannot be protected. In a more complex system it is increasingly likely that the sheltering of one producer hurts another one downstream. Controls of steel imports will damage automobile factories, tariffs on chips will raise costs for computer manufacturers, and so on. Hence, the costs of protectionism will ultimately be felt intensely by producers as well, not only be spread thin over a mass of unsuspecting consumers.

Protectionist measures in the EC also have the effect, already highly visible, of stimulating inward direct investment. By qualifying as insiders, foreign firms thereby hope to be able to price and sell freely within the Single Market. The last few years have seen an expansion of direct investment, particularly from Japan, reaching about U.S. $6 billion in 1987. Table 18 shows that the Japanese direct investment used to focus almost entirely on the U.K., but that it has become much more spread over many countries over recent years. The projects established are completely foreign owned, focus on activities in which they have a marked technological advantage vis-à-vis European firms, and tend to produce for several of the national markets. Most investments have gone to service industries, including finance and insurance, and electrical and transport equipment. The Japanese are followed most notably by the Koreans, who are planning to double their number of trading and manufacturing operations in the EC by 1992, according to Far Eastern Economic Review (1989).

With protectionism creating vested interests, which thrive in the absence of foreign competition and give rise to the kinds of costs discussed in the previous chapter, inward direct investment becomes a valuable substitute for free trade from the perspective of the recipient country. Because the EC consists of historically and culturally sovereign nations, one can expect competition between the individual members for the attraction of direct investment. Such competition has been observed between the American states, or between developing countries (Guisinger, 1985).

The more effective the external protectionism of the EC becomes, the more desirable direct investment, and the more fierce the competition between the individual EC countries will become. It can, of course, be expected that the EC countries will seek to coordinate their polices with regard to inward investment, but such coordination has proved difficult in practice. There has not yet been much interest in discussing harmonization of tax rates, for example. In any case, protectionism coupled with demands for stringency against foreign investors would create strong incentives for the individual member countries to cheat on the collective. The resulting tensions could threaten to tear the EC apart from the inside. Disputes over the location of Japanese car manufacturing in the U.K. have already entered into Brussels. At the same time, the Danes, the Irish or the Dutch are not eager to pay more for Japanese cars in order to permit the French and the Italians to avoid adjustments.

The EC countries do counter the undertaking of direct investments through imposition of taxes or various performance requirements, such as local content rules. The latter force foreign firms to buy a certain proportion of their input locally. Again due to their heterogeneity, however, it is unlikely that the EC countries will be able to agree to policies which lead to any strong deterrence of inward direct investment. Direct investment will most likely continue to flow freely into the EC, and escape with a good deal of the rents created by a possible spurt in protectionism.

There is an additional set of factors which may make discriminatory trade and investment policies in the EC costly for the EC itself. These concern the importance of the East Asian markets in future business activities. A closed EC market will allow European firms to continue their neglect of East Asia.

There can be little doubt that a long term commitment is necessary if efforts to break into the Japanese markets are to be successful. Even if there are fewer trade barriers than is usually alleged, there are great obstacles and high costs associated with market entry. A powerful language barrier, alien business and cultural practices, high land costs, the multilayer distribution system, and high costs of living, particularly for expatriates, and so on, could mean a long stretch of years before any economic rewards materialize. Still, foreign firms which have managed to establish themselves in the Japanese market are often exceptionally profitable. East Asians are careful with product quality and enjoy stable and reliable business relationships. In order to share in the future growth of the region, it is high time to be active there today already.

The price to pay for not moving ahead into Japan could cancel out all other receipts for additional reasons. Success in East Asia today may well be necessary for the future ability to withstand the business strategies of Japanese and other East Asian firms in Europe as well as in other markets. Japanese firms tend to compete fiercely among themselves within their home market before they go abroad, and then move more or less simultaneously in their international crusades. At present the Japanese, followed by the Koreans and the Taiwanese, are expanding their business activities throughout the huge and rapidly growing markets in East Asia. The threatened closure of the U.S. market, and the doubts of the future openness of the EC, make this emphasis on Asia even more desirable from a Japanese viewpoint. Through this, the Japanese further enhance their efficiency when exploiting international differences in factor costs and access to natural resources.

We have already suggested that a solid position at home is the basis for Japanese corporations abroad. Those foreign firms which have managed to withstand competition abroad most successfully are often precisely those which have weathered it in Japan already. Tetra Pak of Sweden is one example, Abegglen and Stalk (1985) name others. As discussed by them, the failure of foreign firms to take advantage of the many opportunities that prevail in Japan is largely due to ignorance and a curious disinterest. If not only Japan but also the rapidly growing East Asian region as a whole is left to be dominated by Japanese firms, they will have an even stronger basis to start out from the day they decide to launch an attack on the Single Market anyway.

It can be concluded that the opportunities of creating the Single Market should outweigh the fears of a 'fortification' of Europe through taxes or NTBs. That is, the fears should subside with the realization that such 'armaments' would be costly not only for outsiders, but much more so for Europe itself. If nations and international bodies are 'rational', the EC should be an open market place.

5. A European Asian Agenda

5.1 The European Agenda

The European agenda is massive. Most attention so far has been paid to the creation of the Single Market, with all its remaining difficulties. The struggle to accommodate the EFTA countries, whether through membership or the achievement of a functioning EES, poses additional problems. The reconstruction and affiliation of Eastern Europe constitutes an even more formidable challenge. Some might say that the difficulties must be tackled one at a time. The different matters are interrelated, however, and must be dealt with within one context.

The difficulties of handling all these issues must not obscure the importance of the European policy vis-à-vis East Asia. The previous chapters have suggested a severe underexploitation of potentially valuable opportunities for trade and investment between these two regions. One of the regions is the most dynamic that exists; the other is about to form the world's largest single market through an unprecedented phasing out of barriers to trade. The European-East Asian relationship is likely to emerge as a major factor in the shaping of rules for trade and investment world wide over the coming decades.

The present situation makes it necessary for Europe to develop a better planned and more imaginative East Asian Policy. The reason is not the least that Europe itself is very much on the East Asian agenda. As can be seen in Table 19, the share of exports from the Asian-Pacific region going to Europe was at a high of 24.7 per cent in 1960, compared to only 18.5 per cent to the U.S. In 1985, these figures were reversed to only 13.7 per cent going to Europe and 29.5 per cent to the U.S. In the last few years, Europe has again become an important target for East Asian exports, while the share going to the U.S. is diminishing.

East Asia is currently expanding and reorienting its trade and investment activities, partly in the European direction. While the East Asians consequently are busily preparing to benefit from the European market, the Europeans are so engaged in creating it – and using it – that they do not have enough time to learn how to exploit the East Asian opportunities. This means that the already large imbalances in trade and investment between the regions will most likely become even bigger. In this situation it is not acceptable for Europe to sit back and focus on its own problems, postponing the matter of forming its relationship with other regions, particularly East Asia.

5.2 Demands on a European Agenda for East Asia

The relationship between Europe and East Asia is partly a matter of attitudes. For example, it is not quite as difficult to export to or invest successfully in Japan as is often said. Japanese firms tend to view the other East Asian markets as highly stable and safe, while European firms often view them as highly uncertain. Still, Europeans typically enjoy a great deal of good-will in East Asia compared to the Japanese.

Japan-bashing has the opposite effect of preventing Westerners from looking for opportunities for business. While many Americans more or less in panic call for a closing out of Japanese interests, some Europeans take the equally dangerous and unwise viewpoint that 'what goes up, must come down'. Behind such a relaxed attitude lies some kind of belief that the Europeans will become notably stronger with the completion of the Single Market in Europe by 1992, and/or that it will be possible to close out the Asians from the market. As seen in the previous chapter, however, outsiders will also benefit from the completion of the single market in the absence of increased external protectionism, and it is highly doubtful whether there is any consistent and effective policy which can close them out. There is, in any case, no such policy which is favourable for social welfare in the European Community itself.

The attitudes that prevail in Europe today give rise to far too many misapprehensions and easy excuses for not trying to export and invest particularly in Japan. As noted by Commissioner Andriessen (28.2.89):

'It is increasingly clear that the development of European exports to Japan depends as much on the interest of Community companies in the market as on the removal of trade barriers.'

Actions under a European agenda for East Asia should, at the least, fulfill the following demands:

a) Strengthen the European economy by fully exploiting trade and foreign investment opportunities in East Asia.
b) Promote good relations with the increasingly important East Asian countries and make it possible to avoid friction with East Asia.
c) Help to preserve a liberal world economic order which would mean good opportunities for free trade and capital movements.
d) Allow policies which facilitate growth of the developing countries in Asia and elsewhere.
e) Create the basis for cooperation concerning common resource issues, such as a sound management of the oceans and the atmosphere.

5.3 Multiple Levels

A European agenda for East Asia, and its specific design and implementation, is not a simple matter. First of all, it must be devised on many different levels. Trade and investments between two regions as disparate in institutional and cultural conditions and geographical distance as Europe and East Asia are not an isolated phenomenon. On the contrary, the success of such activities is critically dependent on a satisfactory level of information about what business opportunities are available and how to approach them in an effective manner.

Hence, progress is likely to require increased economic relations between the regions in general terms. The task of remedying the presently low level of knowledge about East Asia in Europe lies especially heavily on the universities. These must set up research and teaching programs which make coming generations of policy makers and business people more apt to make good use of opportunities in East Asia. Still, the actual work of exploiting trade and investment opportunities, and in the process minimizing the causes and costs of frictions, must ultimately be taken care of by private corporations. These firms must also implement incentive programs which make it possible for employees to engage actively in work with East Asia. Their support, or pressure for, research and educational programs on the region may also be necessary to achieve a satisfactory scale and quality in such programs.

European governments also have a role to play in the context of spurring an optimal amount of information on a distant region like East Asia. In more general terms, governments are in a position to facilitate an efficient functioning of business activities across national boundaries, not least by removal of their own obstacles to well-functioning international markets (as in the case of the bureaucratic obstacles to trade within the EC). Finally, governments have a responsibility to secure rules for private business activities that ensure an optimal management of common resources.

5.4 Items on a European Agenda for East Asia

There are many items on a European agenda on East Asia. The purpose of this section is to suggest some of those which we regard as most important. We bring up the following:

a) Provision of information

First of all, it is necessary to acquire a much better knowledge of and access to information on the European – East Asian relationship. This includes the provision of data on the nature of the gravity shift that has taken place from the Atlantic to the Pacific, the nature (including opportunities and risks) of the new markets that have appeared in East Asia, and the characteristics and consequences of the new competition offered by East Asian firms. All these matters should be more extensively studied from a European viewpoint. The goal must be to facilitate a more constructive approach to East Asia among policy makers, business people and academics in Europe.

b) A more lively dialogue and better forums for contacts

Not only do we need improved information, but livelier contacts between the regions are necessary to stimulate European exports and investments in East Asia. The U.S. has cooperated with Japan and East Asia for a long time in many forums for government officials, business people, and academics. As contacts have been created this way, there is a greater understanding of the various opportunities as well as the friction in the interaction between the regions. The problem in the U.S. is rather the low level of education and knowledge among the population in general, which is typically below that in Europe. At present, the U.S. has much more friction with Japan and some of the NIEs than Europe has, but it is still a fact that the U.S. has managed to develop more intensive trade and investment contacts with the region. The following forums are examples of U.S.-East Asian contacts:

- The Pacific Basin Economic Council (PBEC), which was formed in 1967, brings together business leaders for annual conferences. Its aim is to 'improve business environments, strengthen the business enterprise system, generate new business opportunities, create new business relationships, and increase trade and investment within the Pacific Basin area'.
- The Pacific Free Trade and Development Conference (PAFTAD), which first convened in 1968, is an organization for academic economists.

- Since the early 1980s, a series of annual Pacific Economic Cooperation Conferences (PECC) has brought together government officials in a private capacity, as well as representatives of the academic and business sectors, for policy-oriented discussions.
- In 1989, the initiative was taken to upgrade the political level of Pacific meetings in order to make it possible to set up a forum for ministerial meetings as well.

Even if geographical and political factors, not to speak of governmental organizations, make it difficult to find the same ground for regular meetings and conferences involving Europeans and East Asians as in the Pacific, an effort should be made to set up Eurasian organizations and meeting places. After all, the flight time from Washington to Tokyo is longer than that from Berlin or Stockholm to Tokyo, and about the same as from Brussels to Tokyo.

The EC could assist in the formation of such initiatives. Politicians and bureaucrats have an interest in an expanded dialogue. Academics in Europe who have had typically little contact with East Asia, and business people who often have little experience from this region, would certainly benefit from improved contacts.

The EC, it should be noted, runs a Center for Industrial Cooperation in Tokyo together with the Japanese. The intention is to improve the possibilities for EC business people to acquaint themselves with the Japanese economy. The EC also operates an Executive Training programme, under which it finances an 18 month period in Japan for young executives. Given the great need, however, these efforts represent too little interaction.

c) Integration

The creation of the Single Market in the EC will, if properly managed, strengthen the economic capacity of Europe and European firms. The creation of the Single Market will certainly enable greater advantages to scale in European production. More importantly, however, there must be an upgraded level of competition in Europe if technical progress and innovation are to catch up.

The fact is that a successful 1992 program is much needed to make the Europeans better equipped to take advantage of new markets as well as counter the new competition from East Asia. This requires, however, that intensified competition is not prevented by either governments or the strategic behaviour of large firms. At present, governments and companies alike seem to favour mergers, cartel building and extensive collaboration between firms as measures to counteract the expected burst in competition before it has even emerged. This tendency is potentially dangerous and a reappraisal of antitrust attitudes and policies will be necessary if it continues.

The level of competition within the EC will ultimately be strongly influenced by the EC's external policy. Concerning the European countries still outside the EC, the creation of a functioning EES is presently a matter of high priority. In order to have not only access to the Single Market but also a say concerning its features, however, we have already implied that these countries may have little choice but to become members of the Community. As members, countries such as Sweden and Norway would also lend support to an open external policy for the Community as a whole.

Europe needs a successful integration of the Common Market itself as well as of the markets of the neighbouring European economies. Even more than that, however, it needs an open Community.

d) An open trade policy

An open trade policy will serve Europe's interests in its relations with East Asia and Japan much better than a closed one. To make a fortress of the Single Market would counteract the expected favourable impact of the 1992 program. Merging and/or collaborating huge European firms would share the profits of the vast market. At the same time they would be sheltered from pressure for dynamic changes, prices would be allowed to remain high, and the European firms would be even more confident to refrain from expanding their activities in other regions, including East Asia.

The argument brought forward in favour of protection is, of course, that it will be used to provide assistance in the short run only. Typically, however, those accorded the privilege of subsidy – management as well as labour – in order to acquire a longer time for adjustment, begin to think that adjustment may not be necessary at all. Firms forming cartels with their present competitors may similarly start thinking that they can avoid competition. When foreign competition comes – as it inevitably does – those lured to believe that they can stay away from it will be particularly badly prepared.

Moreover, we have argued that the EC is a heterogeneous organization, consisting of individual nations. For these reasons, external protectionism would be likely to set up centrifugal forces which would threaten to tear the EC apart from the inside, at least until the integration process has reached a stage where national considerations, as we know them now, have disappeared. The problems are illustrated by the difficulties of devising a policy for trade in cars produced through direct investment within the Single Market. Should there be local content rules – and could there be without creating substantial problems? And could import obstacles be raised against cars produced by Japanese factories in the U.S., for example? It can be noted that the U.S., in trade disputes with the EC, has supported the interests of Japanese companies operating factories in the U.S.

Finally, we have observed U.S. protectionist movements. Experiencing a decline in its relative international power and faced with macro-economic imbalances, it is likely that the U.S. will continue to reduce its support of principles of free trade – which has been one of the foundations of post-war growth world wide. Under such circumstances it is of great importance that a self-confident Europe provides the leadership which is needed to preserve an open world economic system. Whether this will actually be the case hinges mostly on the European stance against East Asia, which is the only region with which the EC now experiences large trade deficits.

e) Macro-economic policies for competitiveness

An open trade policy must be combined with macro-economic policies which support economic stability and competitive cost levels. We have seen that deficits usually set up protectionist pressures. Rather than serving as a cure, however, protection tends rather to aggravate them by slowing growth as the pressure for raised productivity is mitigated. To borrow a comment from George Stigler: 'the bad thing about depressions is not that people starve, but that they think badly'. The same is true for trade deficits.

If, as currently in the U.S., total output is lower than the absorption of resources through investment and consumption, the difference must come from the rest of the world, and is reflected in a deficit in the current account. This is unavoidably so as long as this savings deficit prevails. Such imbalances must be corrected through macro-economic policy changes in the country with the deficit or surplus. A coordination of macro-economic policies within Europe may be helpful in preventing a repetition of the U.S. development. The reason is that coordination provides scope for the implementation of effective measures throughout countries. On the other hand, there must be a defence against centrifugal forces exerting a pressure for various kinds of 'compensations', an excessive amount of which would worsen the prospects for sound macro-economic policies. Addressing these issues is not least necessary for the adoption of a common currency, and a credible monetary policy by a central bank for the European Community.[13]

f) Pressures to 'open Japan'

To put pressure on protectionist markets to open up may be a constructive exercise. It must not, however, be used as a means of protecting one's own market. Our experience, notably with the antidumping policy in the EC, shows that this easily becomes the case. The machinery for exerting

[13] A central bank for the EC was proposed by the Delors Report (1989). As foreseen by the central bankers, there may be serious tensions between the new bank and national fiscal authorities.

pressure on another country, in this case Japan, must be explicitly designed so as not to serve as a temptation for implementation of trade barriers at home.

It should be conceded that Japan, and certainly South Korea and Taiwan among the Asian NIEs, still operate NTBs which ought to be eliminated. In addition, there are detrimental DTBs as a result of government policies as well as corporate practices. Unlike taxes and NTBs, DTBs do not systematically switch domestic expenditure away from imports. Instead, they affect the functioning of the domestic economy, and often reduce its efficiency. Thus, their removal will first and foremost make the liberalizing country more competitive. It would facilitate the access of goods, services, and investment in general, including those provided from abroad.

If structural impediments such as the Japanese multi-layer distribution system could be eliminated, much capital and labour could be freed to enter the automobile, home electronics, and computer industries. This is not to say that Europe, or the U.S., should cease to press for the break up of structural impediments, as access to the Japanese market would be better for everybody – foreign as well as Japanese producers. The effect will be even greater prospects for trade in both directions, and this is therefore what we should expect.

It may still be argued that there are particular aspects of Japanese barriers to trade which need to be subject to foreign pressure purely for the sake of abolishing the discrimination of foreigners. One relates to the reception of new technologies in Japan. The task of investing in R&D hinges on the expectation that 'monopoly' rents can be captured swiftly, before the new knowledge has permeated to competitors. The introduction and distribution of goods, which are 'new' due to innovations or discoveries which have temporarily provided its producer with an economic edge, in many instances seem particularly difficult in Japan. When a delaying boycott against the spread of new products can save the Japanese from dissolving rents to foreigners, there appears to be a different game going on compared to most other countries. Domestic company groups, with overt or covert support by public institutions, may block the goods until they can launch their own variant and get ahead in the Japanese market.

Cases with this kind of unfair competition may not be easy to identify, but the task requires a close and focused observation of the Japanese market. This is where the EC should put in its resources, so as to support the same option for its own firms to launch new products in Japan as Japanese firms should have in Europe. Requiring abolition of trade barriers in Japan with respect to a product such as foreign cars makes no sense, since foreign firms have no competitive edge in this product any longer. Rather than following the American quest for sweeping structural reforms, it may be better to pinpoint the specific cases when unfair competition can be demonstrated in Japan. In these cases, there could be a requirement of immediate change as a condition for the introduction of new products by Japanese corporations in the Single Market.

It should be noted that Japanese business groups do practice various strategies which may effectively prevent foreigners from succeeding in the introduction of new goods in Japan. As described by Abegglen and Stalk (1985), for example, they may seem to turn a blind eye while a foreign firm launches a costly marketing campaign which opens up a new consumer interest. Once this has been done, the Japanese run in with close substitutes which are priced at the lowest possible level, capitalizing on the marketing expenses of the foreign firm and quickly ousting it from the market. This kind of strategy may not seem 'nice', but it is not unfair in any legal sense, and the Japanese are certainly not alone in this case of behaviour – they are only better organized and informed at times. Such strategies should not be countered by trade policies, but by improved contacts and stronger ties between Japan and Europe.

g) Corporate strategies

As previously stated, governments and business people in East Asia today pay a great deal of attention to Europe. For several reasons, it is vital for European firms to devise and implement corporate strategies which exploit the opportunities that prevail in East Asia more consistently. Japan and other East Asian countries are already large and profitable markets for many European firms. Still, they continue to attract fairly scant interest in European headquarters.

As was dealt with in the previous chapter, neglecting to enter East Asia today raises the risk for an overwhelming assault by East Asian firms at home tomorrow. Leaving East Asia to Japan would provide this country with an even larger and more rapidly growing base to serve as a solid preparation ground for further expansions. As an answer, European firms must not seek protection, but rather develop their operations in East Asia on a long-term basis, and let the incentives to do so transcend their own organizations.

Against this background, it must be recommended that European firms take an active part in the studying of long term business strategies of Japanese and other East Asian firms. The many success stories of foreign exporters and investors – including American ones – should be studied. Skills relevant for the East Asian markets should be cultivated. Trainee systems could be formed to provide insights into East Asian business systems, strategies and markets. A business experience from East Asia could be given special merit value for young executives in their careers. Market studies and other efforts which usually precede exports and direct investment could be directed towards better ascertaining the opportunities in East Asia. It may be possible to recruit influential Japanese and other East Asians to sit on the board of the mother corporation of truly global firms, and so forth.

h) Cooperation rather than confrontation

When there are different and partly conflicting interests it may seem that there is no reason not to advocate one's own position. Economic transactions and contracts do not generally amount to a zero sum game. Typically, both parties profit from agreements which can be made freely. This is the basic argument why free trade and open competition is in everybody's interest, and why fierce competition between firms should not be counteracted. At the same time, there are instances when the outcome of economic activities can be improved by regulations that are marked by cooperative solutions on an overriding level. A topical example is that of common resources, which tend to be public goods. The expansion of industrial activities and the growing human population have in recent decades increasingly burdened the global environment. It has become more and more evident that the lack of property rights, concerning e.g. clean air and water, prevents an optimal management of our natural resource base by the functioning of free markets.[14] Some of the most serious problems arise because resources are commonly used by different nations which have their own legislations.

A country whose emissions damage another country would account for the whole cost of pollution abatement, but not reap all the benefits. The same may hold for a country which has a financial incentive to exploit, and deplete, its biological diversity. This reduces the willingness to cut emissions or the level of exploitation to the level which would be desirable from a global perspective. Likewise, the possibility of polluters to move activities abroad may diminish a country's ability to cut down on emissions. The 'polluter pays' principle, which is generally accepted in theory, is in practice an ineffective instrument to achieve an optimal level of pollution abatement or natural preservation across countries. Among the consequences can be mentioned: the risk of a thinning of the earth's ozone layer, global warming, acidification in Europe and North America, the devastation of tropical rain forests, etc. In the case of chlorofluorocarbons (CFCs), which are reported to damage the ozone layer, developing countries like India and China require substantial compensations for replacing CFCs with substitutes in new industries. These countries see themselves as carrying a disproportionate share of the financial burden caused by a stop to the use of CFCs.

The appreciation of environmental values tends to be higher in developed countries, such as Japan and those in Western Europe. These have fairly crowded, well educated and relatively well-off populations in common. It is also here that we find the most extensive legislations for

[14]As with protectionism in goods and services, the costs of excessive pollution are carried by the large number of 'ordinary consumers', while the profits tend to be reaped by a small number of relatively well-organized firms, or by governments.

environmental protection. Partly due to the proximity of Eastern Europe, the EC is now aware of the need for international solutions to environmental problems. Japan is similarly close to heavily polluted younger industrial nations, and has announced an ambition to adopt a leading position in regard to international environmental problems.

Instituting a sound management of the environment will take the ability to develop and implement mechanisms which confront economic actors world wide with effective incentives to achieve the total emissions which are acceptable from a global view point. It will take a good deal of flexibility to find solutions which are generally acceptable. There can be little doubt that an open world economy will be conducive to finding such solutions. Still, getting the results will require someone's initiative and leadership. As in the case of trade policies, the U.S. is resuming a defensive position with its decline in competitiveness, which was demonstrated e.g. at the Bergen Conference (May 8th – 16th 1990) of the ECE countries on the global environment. Led by European countries, and struggling not to have the U.S. boycott the outcome, the conference agreed only on a weak commitment to strive for reduced CO^2 emissions.

Major reductions in CO^2 emissions will require multi-million investments in new equipment and technology. A joint commitment in Europe and Japan to lead the way would open up a new area for mutually beneficial exchange between the regions. So far, however, their ambitions have not gone much beyond words. Japan and the EC are, for example, the dominating importers of tropical timber, the careless extraction of which causes excessive deforestation in developing countries. Of the 33 nations currently exporting tropical timber products, only 10 will have any forest left in ten years time according to the Economist (1989). The loss of biological diversity and climatic stability which goes with this destruction incurs losses on all humanity.

i) Upgrading of European universities

Typically, the major U.S. universities have high powered Centers on Japanese and East Asian studies. No university in Europe has good institutions of this type. This is a major weakness which, if unrepaired, will inevitably put Europe at a disadvantage in interactions with East Asia. Universities and schools in Europe must therefore conduct research and develop their curricula so as to make it possible for the next generation to acquire a better understanding of East Asia in general.

The quality of the human work force is a major competitive power in today's technically and economically sophisticated world. Such quality, including the level of knowledge, adaptability and flexibility, is partly a matter of the overall educational level. Here, Europe today has an edge over the U.S., which is lagging behind as far as the general public is concerned. The Japanese are farther ahead still, however, and the Koreans are almost possessed by education and training. To match the emerging competition of highly skilled work forces in East Asia it is essential that European universities rise to new standards. The educational systems in Europe are in a relatively good position for a revitalization, but there is a need to advance the top universities, as well as improve schools in general.

6. Summary

The categorization of a first, a second and a third world has become obsolete. The second no longer exists, the third is breaking apart as East Asian dynamism enables some countries to break out of the trap of underdevelopment, and the first world has lost its economic dominance. Security issues are no longer at the immediate core of the international agenda, but the focus is shifting towards economic issues.

What should be a European agenda for East Asia? It has been argued that the root of East Asian dynamism lies in an actively pursued export-oriented development strategy. There has been a demonstration effect on the rest of the world, and new opportunities as well as risks have emerged. Protectionism has been spurred, most markedly in the U.S., which is giving up its position as champion of free trade. There is also a fear of non-tariff barriers to imports and domestic trade barriers throughout the developed countries. On the other hand, there has been a demonstration effect of super-gains from trade, the planned economies are opening up and seeking a change of their systems, and there are strong tendencies towards regional integration, particularly in the EC.

While the relationship between Europe and East Asia is underexploited, it is now at the core of which way the world economy is going. Japanese and other East Asian firms are taking major steps to increase their activities in Europe. The Europeans, on the other hand, are preoccupied with their own restructuring, and pay little attention to the economies in East Asia – which are the most expansive in the world.

Against this background, it is highly likely that the already large trade and investment imbalances between Europe and East Asia will widen. In spite of the promises that have been made, such a situation poses a risk of a closing of the European market against goods from East Asia. Such a 'fortification' should not be in the interest of the Europeans themselves. Since export markets cannot be protected and direct investment would enable the outsiders to divide and conquer the EC from the inside, it is hardly possible to close them out. The cost of trying would be particularly high as protectionism would allow European firms to remain inactive in East Asia. Those firms that effectively counter the Japanese in their own market are often those that have got to know them in Japan. Leaving the expanding markets of East Asia to be dominated by Japanese firms will allow them to grow even stronger before European firms encounter their competition.

To enable a sound and mutually beneficial interaction between the regions, it is important for Europe to design a more inspired agenda for East Asia as soon as possible. This paper concludes with a number of items for such an agenda. These must be devised on many levels and stimulate a change in attitudes on the part of politicians, business people and academics. The points brought up relate to the provision of information on East Asia, a livelier dialogue between the regions, better forums for contacts, a successful integration of the EC which results in more fierce competition between firms, an open trade policy in the EC against outside countries, sound macro-economic policies, some pressures to 'open Japan', corporate strategies which enable greater success in East Asia, cooperation rather than confrontation concerning common resources, and an upgrading of the quality of European universities.

Table 1

Population, Area, and Income of Pacific Basin Countries

Region	Population (millions 1987)	Area (1000 sq. km)	GDP billions U.S.$ 1987	GNP per capita U.S.$ 1987	Share of total PB GDP 1987
Japan	122	378	2,376	15,760	59.8
Korea	42	98	121	2,690	3.0
Taiwan	20	36	91	4,990	0.3
Hong Kong	6	1	36	8,070	0.9
Singapore	3	1	20	7,940	0.5
Malaysia	16	330	31	1,810	0.8
Thailand	54	514	48	850	1.2
Indonesia	171	1,905	70	450	1.8
Brunei	0.3	6	4	15,390	0.1
Philippines	58	300	34	590	0.8
Papua New Guinea	4	462	3	700	0.1
Australia	16	7,687	183	11,100	4.6
New Zealand	3	269	32	7,750	0.8
China	1,068	9,561	293	290	7.4
U.S. Pacific States	37	2,368	628	14,690	15.8

Sources: World Development Report, World Bank; Republic of China; U.S. Bureau of the Consensus; Main Economic Indicators, OECD.

Table 2

Shares of Various Asian-Pacific Groups and Groupings and of the United States, Europe (OECD), and Non-Asian-Pacific Basin Less Developed Countries (LDCs) in World Population, Area and Income (excl. USSR and East Europe)

	Population		Area		GDP	
	Mill. 1987	Per cent of world total	1000 sq. km.	Per cent of world total	Bill. USD 1987	Per cent of world total
Japan	122	2.6	378	0.4	2,378	16.0
N.E. Asia	190	4.1	513	0.5	2,624	17.7
ASEAN	303	6.5	3,056	3.1	207	1.4
S. Pacific	20	0.4	8,418	8.7	19,550	1.5
Asian NICs	71	1.5	136	1.4	268	1.8
Asian-Pacific LDCs (exkl China)	375	8.1	3,653	3.8	458	3.1
Asian-Pacific region	516	11.1	11,987	12.4	3,049	20.5
China	1,068	23.1	9,561	9.9	293	2.0
U.S. Pacific states	37	0.8	2,386	2.5	629	4.2
Total Pacific Basin	1,621	35.0	23,934	24.7	3,971	26.7
U.S.	244	5.3	9,373	9.7	4,497	30.3
Europe (OECD)	408	8.8	4,269	4.4	4,791	32.2
Non-Asian Pac. LDCs	2,395	51.7	61,760	63.7	2,227	15.0

Sources: See Table 1.

Table 3

Changes in Various GDP Ratios, 1960-1987

Ratios	1960	1970	1980	1985	1986	1987
Japan GDP over world GDP	3.7	8.0	10.6	12.3	15.0	15.6
Asian-Pacific GDP over world GDP	7.8	11.5	15.5	17.7	19.7	20.0
Pacific Basin GDP over world GDP	16.2	20.0	21.6	25.2	26.4	26.1
Pacific Basin GDP over Atlantic Basin GDP	38.5	45.9	49.4	65.3	65.9	62.9
Asian-Pacific GDP over U.S. GDP	18.0	29.7	58.4	48.3	61.4	67.8
Asian-Pacific GDP over European GDP	27.5	37.4	43.9	67.7	68.0	63.7

Sources: See Table 1.

Table 4 (continued)

Changes in Asian-Pacific Trade Flow Ratios, 1960-1988, Per cent

Ratios	1960	1970	1980	1985	1987	1988
Trade of Asian-Pacific LDCs over trade of the other LDCs	21.7	30.0	28.8	42.6	57.7	59.5
Manufactured exports of Asian-Pacific LDCs over total manufac. exports of all LDCs	30.9	41.6	64.3	72.9	74.2	n.a.
Manufactured exports of Asian-Pacific NIEs over total manufactured exports of all LDCs	24.2	36.2	56.2	64.7	66.8	n.a.

Sources: Direction of Trade, IMF; Republic of China.

Table 5

Imports to the Asian-Pacific Region from Principal Countries and Country Groups, 1960-1988

Country	1960	1970	1980	1985	1987	1988
	(U.S.$ Billions)					
United States	2.9	9.4	51.9	56.5	70.8	98.0
Canada	0.4	1.3	6.8	7.2	9.5	12.8
Europe (OECD)	2.9	6.8	33.4	41.1	64.1	82.6
Sweden	0.08	0.2	1.6	1.9	2.5	3.1
Non-Asian-Pacific LDCs (excl China)	1.7	6.6	90.0	53.1	39.8	62.9
China	0.4	1.0	10.8	17.7	25.8	34.1
USSR, Eastern Europe	0.1	0.9	3.0	2.0	3.5	4.5
Asian-Pacific countries	3.6	12.2	87.7	114.9	155.7	196.8
TOTAL	12.0	38.2	283.6	305.6	369.2	491.7
	(Per cent of total Asian-Pacific imports)					
Unites States	22.5	24.1	17.5	18.5	18.3	19.8
Canada	2.8	3.3	2.3	2.4	2.5	2.6
Europe (OECD)	22.1	17.6	11.3	13.4	16.6	16.7
Sweden	0.6	0.6	0.6	0.6	0.6	0.6
Non-Asian-Pacific LDCs (excl China)	12.9	17.1	30.4	17.0	10.3	12.7
China	2.8	2.6	3.6	5.8	6.6	6.9
USSR, Eastern Europe	1.1	2.3	1.0	0.7	0.9	0.9
Asian-Pacific countries	28.4	31.6	29.6	37.6	40.3	39.8
TOTAL	92.6	98.6	95.7	95.4	95.5	99.4

Sources: See Table 4.

Table 6

Exports to the Asian-Pacific Region as a Percentage of the Total Exports of Each Exporting Country or Country Group, 1960-1988. Per cent

Country	1960	1970	1980	1985	1987	1988
United States	13.1	19.2	21.2	22.7	25.7	27.4
Canada	6.6	6.8	8.6	7.2	8.8	9.8
Europe (OECD)	5.8	4.6	3.7	4.6	5.2	5.6
Sweden	3.0	3.0	4.8	5.8	5.1	5.5
Europe (OECD) excl intra-European trade	13.4	13.6	11.4	12.7	17.2	19.0
Sweden excl intra-European trade	10.7	11.6	16.9	18.4	18.4	19.7
Non-Asian-Pacific LDCs (excl China)	6.5	12.5	15.8	13.4	9.2	9.4
China	19.5	54.1	54.2	59.5	57.8	61.9
USSR, Eastern Europe	3.3	9.9	5.1	4.0	6.0	7.0

Sources: See Table 4.

Appendix to Table 6

Share of exports of European countries to Asia-Pacific in 1988

Country	Per cent	Country	Per cent
Belgium	3.6	Austria	3.2
Denmark	7.3	Finland	5.1
Holland	4.0	Iceland	8.3
Ireland	4.3	Norway	4.0
Italy	5.3	Sweden	5.5
France	4.6	Switzerland	10.8
Greece	3.4	Turkey	4.1
Portugal	3.4		
Spain	3.3		
UK	8.6		
West Germany	5.9		

Table 7

Principal countries and Country Groups Importing from the Asian-Pacific Region, 1960-1988

Country	1960	1970	1980	1985	1987	1988
	(U.S.$ Billions)					
United States	2.3	9.7	66.1	126.5	162.7	178.6
Canada	0.2	0.9	4.6	8.1	10.8	13.7
Europe (OECD)	3.3	6.8	52.3	52.1	98.3	117.9
Sweden	0.1	0.2	1.4	2.1	3.9	4.7
Non-Asian-Pacific LDCs (excl China)	1.9	4.6	42.6	38.3	32.9	58.2
China	0.1	0.8	7.6	22.4	22.1	27.6
USSR, Eastern Europe	0.4	0.9	7.6	5.9	5.1	6.4
(Imports from Asia-Pacific as a percentage of total)						
Unites States	15.3	22.8	25.7	35.0	38.4	38.8
Canada	3.7	6.7	7.5	10.3	12.0	12.6
Europe (OECD)	5.8	4.6	5.8	6.6	8.6	9.2
Sweden	2.8	2.9	4.2	5.7	9.7	10.4
Non-Asian-Pacific LDCs (excl China)	7.8	11.0	10.4	11.2	8.5	13.4
China	4.7	4.4	39.0	52.5	51.2	49.9
USSR, Eastern Europe	2.7	8.6	11.7	9.6	7.9	8.6

Sources: See Table 4.

Table 8

Import Penetration Ratios, Total NIEs, 1970 and 1985
(percentages)

Countries	Product groups							
	Total manufacturing		Textiles, clothing, leather, footwear		Electrical machines and appliances		Radio, TV	
	1970	1985	1970	1985	1970	1985	1970	1985
Germany, Fed.Rep.	0.38	1.40	1.33	7.96	0.04	1.32	0.38	5.36
France	0.15	0.79	0.11	2.08	0.01	0.73	0.06	2.39
United Kingdom	0.41	1.42	2.10	7.74	0.14	1.15	0.37	4.11
Italy	0.27	0.91	0.34	1.18	0.07	0.52	0.40	3.91
Sweden	0.65	1.80	4.03	18.72	0.02	1.09	0.20	5.31
United States	0.49	2.41	1.53	11.16	0.44	5.93	1.55	7.54
Canada	0.43	1.98	2.08	9.99	0.08	2.23	0.90	11.82
Japan	0.30	0.85	1.17	3.82	0.10	0.73	0.19	0.68
Australia	0.49	3.09	2.50	11.55	0.12	4.98	0.11	16.23

Source: OECD (1988).

Table 9

Export Intensities

(Exports of the U.S., EC and Sweden to a number of East Asian countries and country groups in pro mille of GDP of the U.S., EC, Sweden, and Japan, respectively)

Country	1970	1975	1980	1987
Japan				
U.S.	4.61	6.05	7.74	6.33
EC	2.08	1.94	2.14	3.67
Sweden	1.98	2.14	2.85	4.07
South Korea				
U.S.	0.63	1.11	1.74	1.81
EC	0.22	0.40	0.43	0.98
Sweden	0.06	0.10	0.34	0.97
Japan	4.01	4.49	5.09	5.62
Taiwan				
U.S.	0.36	1.04	1.74	1.70
EC	0.19	0.45	0.51	0.99
Sweden	0.12	0.29	0.51	1.39
Japan	3.21	3.60	5.03	5.00
Asian NIEs (SK, T, HK, S)				
U.S.	1.63	3.29	5.62	5.32
EC	1.67	2.02	2.70	4.12
Sweden	0.78	1.04	3.44	4.92
Japan	12.60	13.89	18.35	16.94
Thailand				
U.S.	0.15	0.23	0.47	0.35
EC	0.37	0.29	0.33	0.44
Sweden	0.27	0.25	0.69	0.52
Japan	2.20	1.92	1.82	1.26
ASEAN				
U.S.	1.08	2.14	3.42	2.21
EC	1.87	2.17	2.41	2.30
Sweden	1.32	1.96	4.89	3.25
Japan	8.88	11.85	12.36	6.61

Sources: Direction of Trade Statistics, IMF; International Financial Statistics, IMF; World Tables 1988/89, World Bank; Inspectorate General of Customs, Taipei; Taiwanese exchange rates from Nomura Research, Tokyo.

Table 10

Export Intensities

Exports of the U.S., EC and Sweden to a number of East Asian countries and country groups in per cent of total export of the U.S., EC, Sweden, and Japan, respectively. (For EC and Sweden, western European trade is excluded from total trade.)

Country	1970	1975	1980	1987
Japan				
U.S.	10.76	8.89	9.42	11.17
EC	3.47	2.54	2.87	5.38
Sweden	3.79	2.91	4.00	5.17
South Korea				
U.S.	1.47	1.64	2.12	3.20
EC	0.38	0.52	0.58	1.44
Sweden	0.11	0.13	0.47	1.23
Japan	4.23	4.03	4.13	5.77
Taiwan				
U.S.	0.84	1.52	2.11	3.00
EC	0.31	0.59	0.69	1.46
Sweden	0.23	0.39	0.71	1.76
Japan	3.39	3.22	4.09	5.12
Asian NIEs (SK, T, HK, S)				
U.S.	3.81	4.83	6.82	9.38
EC	2.79	2.65	3.62	6.03
Sweden	1.49	1.41	4.83	6.24
Japan	13.29	12.46	14.90	17.38
Thailand				
U.S.	0.35	0.33	0.57	0.61
EC	0.61	0.38	0.44	0.65
Sweden	0.52	0.34	0.97	0.66
Japan	2.32	1.72	1.48	1.29
ASEAN				
U.S.	2.54	3.14	4.15	3.90
EC	3.13	2.84	3.24	3.37
Sweden	2.52	2.66	6.86	4.12
Japan	9.36	10.62	10.03	6.78

Sources: See Table 9.

Table 11

Export Intensities of Manufactures

Exports of manufactures (SITC groups 5-8) of the U.S. and EC to Japan in per cent of GDP/total exports/total exports of manufactures/total exports to Japan. For EC internal trade excluded. (In parentheses excluded.)

	1970	1980	1985
U.S.			
Share of GDP	0.193	0.320	0.281
Share of total export	4.5	3.9	5.2
Share of total exports of manufactures	6.6	6.0	7.7
Share of total exports to Japan	42	42	52
EC			
Share of GDP	0.186	0.184	0.266
Share of total export (incl. internal trade)	1.00	0.77	0.96
Share of total export (excl. internal trade)	n.a.	1.8	2.0
(excl. western European trade)	2.9	2.4	2.7
Share of total exports of manufactures (incl. internal trade)	1.3	1.1	1.3
Share of total exports of manufactures (excl. internal trade)	2.6	2.1	2.6
Share of total exports to Japan	87	84	82

Sources: International Trade Statistics Yearbook (Vol I), 1983, 1987, UN; Direction of Trade Statistics, IMF; International Financial Statistics, IMF; World Tables 1988/89, World Bank.

Table 12

Import Intensities

(Imports from an East Asian country into the U.S., EC, Sweden, and Japan as pro mille of GNP of importing country)

Country	1970	1975	1980	1987
Japan				
U.S.	6.2	7.8	12.3	16.0
EC	3.0	6.5	6.3	9.8
Sweden	3.8	6.9	7.7	15.1
South Korea				
U.S.	0.39	1.00	1.65	4.03
EC	0.09	0.72	0.93	1.66
Sweden	0.39	0.69	1.23	2.32
Japan	1.12	2.62	2.87	3.44
Taiwan				
U.S.	0.56	1.15	2.51	5.30
EC	0.21	0.71	0.91	1.62
Sweden	0.12	0.30	0.77	1.84
Japan	1.06	1.38	2.00	2.92
Asian NIEs (SK, T, HK, S)				
U.S.	2.0	3.6	6.8	13.1
EC	1.4	3.6	4.2	5.7
Sweden	2.1	2.9	4.4	6.9
Japan	3.1	5.3	6.9	7.9
Thailand				
U.S.	0.11	0.15	0.32	0.54
EC	0.22	0.40	0.57	0.67
Sweden	0.06	0.18	0.24	0.45
Japan	0.93	1.45	1.06	0.76
ASEAN				
U.S.	1.0	2.5	4.8	4.0
EC	1.6	2.7	3.0	2.8
Sweden	0.9	1.1	1.8	1.8
Japan	9.1	12.7	20.1	7.8

Sources: Direction of Trade Statistics, IMF; International Financial Statistics, IMF; World Tables 1988/89, World Bank; Inspectorate General of Customs; Taiwanese exchange rates from Nomura Research.

Table 13

The EC's External Trade

Countries	External trade millions U.S.$			Share of total external trade, per cent		
	1982	1987	1988	1982	1987	1988
U.S./Canada	111	168	186	18	21	21
EFTA	116	200	221	19	25	25
Japan	26	58	70	4	7	8
Asian NIEs	19	43	53	2	5	6
ASEAN	12	16	19	2	2	2
China	5	12	15	1	2	2
Other	322	303	327	53	38	37
Internal trade	660	1114	1260	108	139	142

Source: Direction of Trade Statistics, IMF.

Table 14

Stock of Foreign Direct Investment in Japan and the U.S., Reported by Home Country (million U.S.$)

	1971	1981	1983	1984	1986	
U.S.						
in Jap.	1,821	6,762	7,661	7,936	11,333	
in W.E.	n.a.	n.a.	n.a.	n.a.	n.a.	
West Germ.						
in Jap.	n.a.	573	685	687	736	(1985)
in U.S.	n.a.	11,380	13,671	15,385	15,217	(1985)
Netherl.						
in Jap.	n.a.	n.a.	n.a.	339	n.a.	
in U.S.	n.a.	8,633	11,702	13,815	n.a.	
U.K.						
in Jap.	39	380	n.a.	841	n.a.	
in U.S.	1,935	16,181	n.a.	35,179	n.a.	
Japan						
in U.S.	918	11,341	16,675	20,035	35,596	
in W.E.	725	5,076	6,942	8,878	14,277	

Sources: International Financial Statistics, IMF; UNCTC, 1988.

Table 15

Stock of Foreign Direct Investment in U.S.A., West Germany, U.K., Thailand, and Japan, as Reported by Host Country (million U.S.$)

Country		1971	1981	1983	1984	1986	
U.S.A							
from	WE	10,337	72,264	92,874	108,115	141,547	
	Jap	-227	7.697	11,336	16,044	23,433	
West Germany							
from	WE	n.a.	16,224	15,178	14,566	14,647	(1985)
	U.S.	n.a.	13,581	13,333	11,895	11,578	(1985)
	Jap	n.a.	1,276	1,368	1,521	1,797	(1985)
U.K							
from	WE	3,521	13,345	n.a.	4,871	n.a.	
	U.S.	1,935	16,181	n.a.	35,179	n.a.	
	Jap	39	380	n.a.	841	n.a.	
Japan							
from	WE	151	842	1,039	1,180	1,637	
	U.S.	572	1,761	2,441	2,655	3,407	
			1970	1975	1980	1987	
Thailand							
from	EC		4	64	157	383	
	Sweden		0.2	0.9	1.3	10.7	
	U.S.		17	202	324	792	
	Japan		16	138	287	824	

Sources: International Financial Statistics, IMF; UNCTC, 1988; Data printouts obtained from ESCAP.

Table 16

Economic Indicators

Country	Average Annual Growth Rate (per cent) GDP		Industry		Unemployment (per cent of labour force)
	1965-80	1980-86	1965-80	1980-86	1987
Germany, Fed.Rep.	3.3	1.5	2.9	0.7	7.9
France	4.4	1.3	4.6	0.6	10.5
Netherlands	3.7	1.0	3.6	0.5	12.6
Belgium	3.9	0.9	4.4	0.5	11.2
United Kingdom	2.2	2.3	1.2	2.0	10.3
Italy	3.9	1.3	4.2	0.2	11.0
United States	2.8	3.1	1.9	3.2	6.2
Japan	6.3	3.7	8.5	5.0	2.8
Sweden	2.8	2.0	2.2	2.5	1.9
Korea, Rep.of	9.5	8.2	16.5	10.2	-
Thailand	7.4	4.8	9.5	5.0	-

Source: World Bank, OECD (1988b).

Table 17

VERs in the EC, May 1988

(percentage increase since September 1987 in parentheses)

Major known VERs (Excluding the MFA)	World Wide	EC Total	EC Wide	National	Restrained exporters
Total	261 (93.3)	138 (100.0)	87 (77.6)		Ind.c., 50 (56.2) Dev.c., 65 (160.0) Ea.E.c., 23 (108.3)
Steel	52 (175.0)	15 (25.0)	14 (16.6)	1; U.K.	Ind.c., 7 (75.0) Dev.c., 3 (0.0) Ea.E.c., 5 (0.0)
Agricultural and food products	55 (175.0)	40 (110.5)	36 (89.5)	4; France, Ireland, Italy	Ind.c., 13 (62.5) Dev.c., 16 (220.0) Ea.E.c., 11 (83.3)
Automobiles and transport equipment	17 (21.4)	13 (18.2)	2 (0.0)	11; France, Italy, U.K., Spain, Portugal	Ind.c., 13 (18.2)
Textiles and clothing	72 (157.1)	21 (200.0)	18 (157.1)	3; Germany, U.K.	Dev.c., 19 (171.4) Ea.E.c; 2 (-)
Electronic products	19 (72.7)	16 (100.0)	5 (0.0)	11; France, Italy, U.K.	Ind.c., 7 (40.0) Ea.E.c., 9 (200.0)
Footwear	14 (75.0)	11 (120.0)	1 (0.0)	10; France, Italy, U.K.	Dev.c., 8 (60.0) Ea.E.c., 3 (-)
Machine tools	7 (0.0)	3 (0.0)	2 (0.0)	1; U.K.	Ind.c., 3 (0.0)
Other	25 (177.8)	19 (375.0)	10 (900.0)	10; Benelux, Denmark France, U.K.	Ind.c., 7 (600.0) Dev.c., 10 (500.0) Ea.E.c., 2 (100.0)

Ind.c.= Industrialized countries; Dev.c. = Developing countries; Ea.E.c. = Eastern European Countries
Source: Direction of Trade Statistics, IMF.

Table 18

The Geographical Distribution of the Japanese Direct Investment Stock in Europe, 1970-1987

Countries	Share of Japan's direct investment stock in Europe					
	1970		1980		1987	
	Value (U.S.$)	Per cent	Value (U.S.$)	Per cent	Value (U.S.$)	Per cent
Belgium	20	3.1	291	6.5	863	4.1
France	22	3.4	354	7.9	1,300	6.2
West Germany	16	2.5	498	11.1	1,935	9.3
Luxembourg	8	1.3	105	2.3	4,072	19.3
Netherlands	3	0.5	298	6.6	3,166	15.0
Spain	4	0.6	173	3.9	883	4.2
U.K.	544	85.1	2,010	44.9	6,598	31.3
Other EC	11	1.8	304	6.8	845	4.0
Total EC 12	628	98.3	4,033	90.2	19,682	93.5
Total Europe	639	100.0	4,472	100.0	21,047	100.0

Source: Dunning and Cantwell (1989).

Table 19

Exports from the Asian-Pacific Region to Principal Importing countries and Country Groups as a Percentage of Total Asian-Pacific Exports, 1960-1988. Per cent

Country	1960	1970	1980	1985	1987	1988
United States	18.5	26.8	22.5	29.5	32.6	29.7
Canada	1.8	2.6	1.6	2.1	2.2	2.1
Europe (OECD)	24.7	17.7	16.5	13.7	18.0	18.6
Sweden	0.6	0.5	0.5	0.5	0.8	0.6
Non-Asian-Pacific LDCs (excl China)	16.3	12.0	16.2	11.6	9.6	10.0
China	0.8	2.1	2.8	6.1	4.6	5.1
USSR, Eastern Europe	2.6	2.2	2.4	1.4	0.9	0.9
Asian-Pacific Countries	26.5	32.5	36.2	30.5	31.2	33.5
TOTAL	91.2	95.9	98.2	94.9	99.1	99.9

Sources: See Table 4.

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