

The EU-Japan relationship in the World Trade Organisation

**- Analysis on social forces from Neo-Gramscian perspective:
the impact of social forces in the making of hegemony as consensual order -**

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Preface

At the time when Japan was experiencing robust economic growth and Europe was accelerating its integration, a number of researchers noticed the importance of investing in their bilateral economic relationship, which was formerly obscured by their respective 'special' relationships with the United States. When their trade frictions came to the surface, their trade relationship began to attract more attention.

In the meantime, world trade entered a new phase with the creation of the World Trade Organisation (WTO) in 1995. As the successor of the General Agreement on Tariffs and Trade (GATT), the WTO became a new arena for member countries to make trade agreements and solve trade frictions with their trade partners.

In this thesis, we will investigate the relationship between the EU and Japan in the WTO. The thesis will look closely at social forces and investigate how various social forces have influenced the position of the EU and Japan, as well as the WTO. On top of that, we will also analyse how the function of the WTO has influenced the EU and Japan, and their relationship in the multilateral trading system.

Trade conflicts have often been seen as trade tensions between national states. In fact, the WTO deals only with member countries (with the exception of the EU). However, trade tensions may well break out not between national states but between individual sectors, such as agriculture and steel, which sectoral interests then turn to their national states for support. This indicates that even trade friction is not simply antagonism between national states, but between national and transnational fractions of classes. States have been utilised by transnationally oriented dominant groups which intend to integrate their countries into emergent global capitalist structures.

This thesis therefore raises questions about liberal trade theory concerning its serious gap between theory and actual practices, and suggests an alternative approach to structural issues of the state-centric approach to world politics. While we consult neo-liberal institutionalist theory to investigate the role of the WTO and its influence upon the EU-Japan relationship, we will analyse the interaction of various social forces within the EU and Japan from a neo-Gramscian perspective. In this way, we will try to direct attention to relations between social interests in the struggle for consensual leadership rather than concentrating solely on state dominance. Focusing on the role of international organisations and social forces, the aim of this thesis is to investigate how the EU and Japan have developed 'coordinated action' and 'joint negotiating stances' on particular trade issues, notably on agriculture and steel trade. Furthermore, as our central research

questions, this thesis investigates what has been the overall effect of the WTO on the development of the EU-Japan trade relationship, as well as how the WTO has provided an impetus to promote certain patterns in EU-Japan relations. Through this thesis, I aim to contribute to the understanding of the roles of social forces in the interaction in international organisations.

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Abbreviation

AD - anti-dumping

AMS - Aggregate Measurement of Support

ASEAN - Association of Southeast Asian Nations

CAP - Common Agricultural Policy

CVD - countervailing duty

DSB - Dispute Settlement System

EBC - European Business Community

EC - European Community

EU - European Union

FAO - Food and Agriculture Organisation of the United Nations

FDI - foreign direct investment

FY - fiscal year

GATT - General Agreement on Tariffs and Trade

GDP - Gross Domestic Product

GM - Genetically Modified

GMOs - Genetically Modified Organisms

IMF - International Monetary Fund

IPE - International Political Economy

IR - International Relations

LDCs - Least Developed Countries

LDP - Liberal Democratic Party, Japan

MAFF - Ministry of Agriculture, Forestry and Fishery, Japan

MFN - Most-Favoured Nation

MITI - Ministry of International Trade and Industry, Japan

MOF - Ministry of Finance, Japan

MOFA - Ministry of Foreign Affairs, Japan

NGO - Non-Governmental Organisation

NTB - Non-Tariff Barrier

OECD - Organisation for Economic Cooperation and Development

SPS - Sanitary and Phytosanitary Agreement

OMA - Orderly Marketing Agreements

SEM - Single European Market

TBR - Trade Barrier Regulations

TPM - Trigger Price Mechanism

UNCTAD - United Nations Conference on Trade and Development

URAA - Uruguay Round Agreement on Agriculture

US - United States

VER - Voluntary Export Restraint

VRA - Voluntary Restraint Agreement

WTO - World Trade Organisation

Chapter 1
Introduction

1. Introduction

1-1. The EU-Japan relationship in the WTO

As the 21st century was approaching, the international economy was at a historic turning point. Concerning the international trade regime, the conclusion of the General Agreement on Tariffs and Trade (GATT) Uruguay Round led to the establishment of the World Trade Organisation (WTO) in 1995. With the birth of the new organisation, the world economy became even more integrated and interrelated. Economically and politically, global society was evolving into a more fluid and multipolar international order. As a result, the world has become interdependent at an unprecedented level. That interdependence has generated a number of challenges for the international trading system. As two of the world's major economic powers, the European Union (EU)¹ and Japan have an important role to play in the management of this system.

A close look at today's international trade negotiations in the WTO reveals a particular relationship between members. Since the establishment of the WTO, the EU and Japan have started an intense relationship on some trade issues at an unprecedented level. Their relationship is particularly intense on agriculture and steel issues, although they seem to have different agendas and interests on both trade issues. In order to find out why the EU and Japan have intensified their relationship, we need to address the following two points.

First, analysing the relationship between members in the WTO, the role of the international organisation needs to be addressed. Second, we need to pay more attention to various actors involved in trade negotiations. Since its establishment, the WTO has been dealing only with states. Because of this nature, so far, the international patterns of relationships between bureaucrats and international firms have been largely neglected and have not been thoroughly researched or understood. However, in today's international trade, various interests of domestic forces are involved. They first create the domestic consensus by influencing the negotiation stances of each member country and try to extend their position to the international level. Therefore, in our context, it is necessary to focus on various actors and the role of the organisation which may have an affect on today's relationship between the EU and Japan.

¹ I refer in this thesis to the 'EU' for all events after the entry into force of the Maastricht Treaty in November 1993. The EEC, established in 1958, changed its name and became the European Community with the entry into force of the Maastricht Treaty in November of 1993. Therefore, for the time before 1993, both 'EEC' (European Economic Community) and 'EC' (European Community) are going to be used interchangeably.

1-2. Analytical framework

Trade conflicts have often been seen as trade tensions between national states. In fact, the WTO deals only with member countries (with the exception of the EU). However, even when some members have conflicting interests on one trade issue, they may coordinate their negotiating stances on other trade issues. Thus, as we will see in later chapters, trade tensions may well break out not between national states but between individual sectors, such as agriculture or steel, which then turn to national states for support.

In this sense, there is a view that even trade friction is not simply antagonism between national states, but between national and transnational fractions of classes. States have been utilised by transnationally oriented dominant groups which intend to integrate their countries into emergent global capitalist structures.²

William I Robinson asserts, “fierce competition in the globalisation epoch takes place among dense networks of transnational corporate alliances and through struggles within every country and within transnational institutions”.³ As their interests are global, transnational capitals must take an active political and economic interest in each country and region in which they operate. They may turn to any national state to gain competitive advantage as part of their corporate strategy. If, as William I Robinson asserts, “globalisation is not a ‘national’ project but a class project without a national strategy, or rather, with a strategy that seeks to utilise the existing political infrastructure of the nation-state system and simultaneously to craft transnational state structures”,⁴ an exclusive state-centric focus may fail to capture the essence of the EU-Japan trade relationship. In order to overcome the shortcomings of the state-centric approach, we will analyse the issue from a neo-Gramscian perspective, which focuses on social forces.

Thus, focusing on the role of the international organisation and social forces within the EU and Japan from a neo-Gramscian perspective, the aim of our analysis is to investigate how the EU and Japan have developed ‘coordinated action’ and ‘joint negotiating stances’ on particular trade issues, notably on agriculture and steel trade. Furthermore, as one of our central research questions, we investigate what has been the

² Andreas Bieler and Adam David Morton, ‘Introduction: Neo-Gramscian perspectives in international political economy and the relevance to European integration’ in Andreas Bieler and Adam David Morton (ed.), ‘Social forces in the making of the new Europe’, (New York, Palgrave Publishers, 2001), P16, 17

³ William I Robinson, ‘Gramsci and Globalisation: From Nationstate to Transnational Hegemony’, in Andreas Bieler and Adam David Morton, ‘Images of Gramsci’, (New York, Routledge, 2006), P174, 175

⁴ William I Robinson, ‘Gramsci and Globalisation: From Nationstate to Transnational Hegemony’, P174, 175

overall effect of the WTO on the development of the EU-Japan relationship, as well as how the WTO provided an impetus to promote certain patterns in EU-Japan relations.

1-3. Hypothesis

Thus, I will use the above characteristics of the neo-Gramscian perspective as an analytical device for the analysis of the relationship between the EU and Japan, in order to look at the condition of hegemony in today's world. I will investigate how, after the US-centered hegemony, the EU and Japan may be forming a new hegemony (or supremacy) in today's world order. Moreover, my interest focuses on how social forces may mould a new consensus domestically, and then affect the rule-making of an international organisation. We also pay attention to the question of how an international organisation such as the WTO has been able to contribute to the creation of general conditions for transnational capital.

Taking into account the above central questions, the main hypothesis will be: By creating the conditions for the hegemony of transnational capital, utilising and strengthening the system or function of the WTO, elite capitalist social forces within the EU and Japan have joined forces beyond national boundaries and attempted to create new international rules and norms in favour of their interests. In other words, depending on the trade issues, various social forces within the EU and Japan, with the same or similar interests, have effectively utilised the international organisation and significantly contributed to the creation of general conditions of hegemony by influencing the trade policy of each government. In this sense, thanks to the creation of an international organisation, such as the WTO, cooperation between such elite social forces in different countries is facilitated by moulding a new consensus at the international level, thus contributing to the creation of "new hegemony" in the world economy. Once such a consensus is made at the international level within an international organisation, new international rules or norms may even override domestic rules and will start functioning as the global standard. Through empirical research on the EU-Japan relationship in the WTO, the above hypothesis will be examined in the thesis.

1-4. The EU-Japan trade relationship: a brief overview

When the WTO was established in 1995, Japanese Gross Domestic Product (GDP) was 5218 billion US dollars, the second largest after the United States (US), whereas the total GDP of the EU was a staggering 8407 billion US dollars, surpassing the US. Their economic size makes them important trade partners to one another. In the same

year, total trade between them amounted to 144 billion US dollars.⁵

There are two solid sides to the Japan-EU-US triangle: the relations between Europe and the US and between the US and Japan. The third side, the relations between Europe and Japan, is poorly developed with regard to trade and investment as well as knowledge. There are a number of explanations for this situation. One is that Europe is very much preoccupied with its own development and restructuring. Another is Japan's US-focused bilateralism in its foreign and security policy which does not leave much room for developing other relationships.

The political relaunch of the EC in the mid-1980s culminated in 1987 with the adoption of the Single European Act (SEA) and the acceptance of the programme to create a Single European Market (SEM) by 1992. Japan's interest towards the EC dramatically increased since the SEM programme (or the 1992 programme) launched in 1987. Prior to the programme, Japan's attitude to the EC was ambivalent, since the credibility of the European Commission (the executive branch of the EC) as an international negotiation counterpart, was often questioned. Coordination of trade policies among EC member states was far from perfect. As a result, the Japanese government tended to prefer dealing with individual member states, giving Brussels only a secondary role.

The 1992 project was as much a political as an economic project. Its architects, particularly the European Commission, viewed the creation of the internal market as a means to justify more integrated political structures and stronger EC institutions to regulate it. A politically unified EC would be a more powerful international actor because the 'politics of scale' would provide it with more clout than could be wielded by its Member States acting alone. The 1992 project was designed to enhance the EC's 'supranational' power, or its power to define and pursue collective interests which transcend national boundaries, authorities or interests.⁶

Realising the impact of the SEM programme, Japan changed its attitude towards the EC. The two most important implications of the programme for Japan were: (1) the

⁵ Atsuko Abe, 'Japan and the European Union: Domestic Politics and Transnational Relations', (London, Athlone Press, 1999), P3

⁶ John Peterson argues that the US bilateral trading relationship with Japan contrasted sharply with its relationship with the EC. By the late 1980s, the Community accounted for nearly a quarter of US exports, while Japan took only about 12 per cent. The EC remained a critical market for American goods in high-growth, expanding industries. Nearly 45 per cent of American exports to the EC were high technology goods compared with only 29 per cent of US sales to Japan. / see Park, 'Trading Blocs and US-Japan Relations in Pacific Trade and Cooperation', *International Trade: Regional and Global Issues*, (The Macmillan Press, 1994) P66

programme made the EC the biggest single market, including the automobile sector; and (2) it increased European competitiveness in the international economy. While this large single economy encouraged Japanese producers to increase business with the Europeans, European protectionism alarmed the Japanese. Driven by both business opportunities and a fear of 'Fortress Europe', the end of 1980s and the early 1990s found a rapid increase in Japanese Foreign Direct Investment (FDI) into the EC. At the official level too, the Japanese government indicated its anxiety over the possible exclusive effect of the SEM ('fortress Europe').

Therefore, the deepening integration of the European Union was an important factor for EU-Japan relationships. The SEM granted the EU significant leverage in terms of international trade policy, because it could determine conditions of access to the largest unified market in the world. The expansion to Central and Eastern Europe, along with the introduction of the Euro as a common currency in 1999, enabled the EU to further increase its weight as a trade entity.

The changing bilateral economic relationship between the EU and Japan has been researched by many scholars. For example, Albrecht Rothacher analyses the development of European Community (EC)-Japan economic relations since the early post-war years.⁷ William R. Nester's work, *'European Power and the Japanese challenge'* approaches their relationship by analysing the individual policies and policymaking from the view point of competition between them.⁸ Atsuko Abe's *'Japan and the European Union'* was an attempt to analyse EU-Japan relations from various IR perspectives, focusing on the impact of Japan's decision-making on the bilateral relationship.⁹

A number of scholars often characterised the EU-Japan bilateral trade relationship as confrontational (see Chapter 2). However, particularly since the establishment of the WTO in 1995, it has been frequently observed that the EU and Japan have coordinated their negotiating stance on particular trade issues, notably agricultural and steel issues. Such coordination of negotiating stances seems to be increasing and being consolidated at an unprecedented level in the history of their past trade relations. However, while considerable research has been conducted on EU-Japan bilateral trade relations, such new developments of the EU-Japan relationship in the WTO have not yet been thoroughly investigated.

⁷ Albrecht Rothacher, *'Economic Diplomacy between the European Community and Japan 1959-1981'* (Aldershot, Gower Publishing Company, 1983)

⁸ William R. Nester, *'European Power and The Japanese Challenge'*, (Basingstoke, Macmillan, 1993)

⁹ Atsuko Abe, *'Japan and the European Union: Domestic Politics and Transnational Relations'*

1-5. The WTO as an international organisation

The WTO is the legal and institutional foundation of the multilateral trading system. The WTO is unique both in the context of its contractual obligations and in the enforcement mechanism built into its system for resolving disputes. At the end of an integrated dispute settlement process that covers a wide range of trade-related policies in the areas of goods, services, and the protection of intellectual property, the organisation provides member countries with multilaterally authorised trade sanctions. In contrast to other international economic organisations, the WTO has an enforcement mechanism which is an effective way of sanctioning member countries that are found to be in violation of the institution's rules and that refuse to change their illegal behaviour.¹⁰ As a result of major changes agreed in the Uruguay Round, the dispute settlement process in the WTO has become much more automatic by prohibiting individual countries from blocking the process.¹¹

The important role played in the world economy by the GATT/WTO is widely accepted. Since its creation in 1947 the GATT has grown in membership from an initial set of 23 countries to a roster that now includes more than 150 countries. The expanding GATT/WTO membership reflects the success that this organisation has had in facilitating tariff reductions. Through the eight rounds of trade-policy negotiations that have been sponsored by the GATT, culminating with the completion of the Uruguay Round in 1994 and the creation of the WTO, the average tariff rates on industrial goods have fallen substantially. The past success of the GATT/WTO justifies its role as an international organisation.¹²

Along with its dispute settlement process, the WTO is an organisation devoted to developing and administering rules to counter protectionism in the global trading system. Although the WTO's dispute settlement procedure is concerned explicitly with the function of rule observance, by far the greatest amount of energy within the WTO is devoted to rule making.¹³

An important research question here is whether the development of formal rules helps or hinders the process of global liberalisation when those rules are not entirely

¹⁰ Richard Blackhurst, 'The capacity of the WTO to fulfil its mandate' in Anne O Kruger (ed), 'WTO as an international organisation', (Chicago, University of Chicago Press, 1998), P47

¹¹ Blackhurst, 'The capacity of the WTO to fulfil its mandate', P32

¹² Kyle Bagwell and Robert W. Staiger, 'The Economics of the World Trading System', (Cambridge, the MIT Press, 2002), P1-11

¹³ David Vines, 'The WTO in relation to the Fund and the Bank', in Anne O Kruger (ed), 'WTO as an international organisation', (Chicago, University of Chicago Press, 1998), P79

consistent with the domestic political concerns of major players. As the trade policies of the large trading nations in Europe, the United States, and Japan are in large part driven by domestic concerns over trade issues, there are significant questions as to the degree to which international norms or rules can be negotiated that go against those domestic interests.¹⁴ Therefore, for both the EU and Japan, rule-making in the WTO is of great importance.

2. Theoretical framework

In today's world trade, trade negotiations involve many diversified actors within the state. Each actor has its own goals for agenda setting, rule-making and decision-making within the WTO. Under these circumstances, conventional state-centric IR theory is not enough to analyse the issue. In order to analyse such complexity of world trade issues, and the EU-Japan relationship in the WTO, a neo-Gramscian perspective, particularly its 1.) notion of hegemony, 2.) focus on social forces and 3.) attention to the role of international organisation, may give us a useful insight into the ever changing spatial and territorial structure of power in the global political economy.¹⁵

2-1. A Neo-Gramscian perspective on hegemony and the post-war economy

'Hegemony' was a concept used by Gramsci to analyse the relation of forces in a given society. A hegemonic order was one where consent, rather than coercion, primarily characterised the relations between classes, and between state and civil society.¹⁶ Developing Gramsci's ideas internationally, Robert W. Cox has demonstrated that it is possible to conceive of new forms of state, hegemony, and the formation of 'historic blocs' on a world scale. While conventional IR theory considers hegemony as a single dimension of dominance based on the economic and military capabilities of states, the neo-Gramscian perspective developed by Cox broadens the domain of hegemony. According to Cox, hegemony is "the articulation and justification of a particular set of interests as general interests. It appears as an expression of broadly based consent, manifested in the acceptance of ideas and supported by material resources and institutions, which is initially established by social-class forces occupying a leading role within a state,

¹⁴ Anne O Kruger, 'An Agenda for the WTO', in Anne O Kruger (ed), 'WTO as an international organisation', (Chicago, University of Chicago Press, 1998), P403

¹⁵ Adam David Morton, "Unravelling Gramsci", (London, Pluto Press, 2007), P112

¹⁶ Stephen Gill and David Law, 'Global hegemony and the structural power of capital' in Stephen Gill (eds) 'Gramsci, Historical Materialism and International Relations', (Australia, Cambridge University Press, 1993), P93

but is then projected outwards on a world scale.¹⁷

Cox argues that a US-led hegemonic world order, labelled Pax Americana, prevailed until the early 1970s. It was maintained through the Bretton Woods system of fixed exchange rates and institutions such as World Bank and the International Monetary Fund (IMF). Moreover, it was based on the principle of “embedded liberalism”, which allowed the combination of international free trade with the right of governments to intervene in their national economy in order to ensure domestic stability via social security and the partial redistribution of economic wealth. (Although there is a view that the postwar order may be better understood in terms of the dominance of a protectionist form of regulation of the market economy.)¹⁸

Gill and Law named four elements as the key international elements in the post-1945 regime of accumulation which generated uniquely rapid economic growth throughout the industrialized capitalist world. First, the construction of a US-centred economic, security and political structure for the non-communist world, ensuring peaceful conditions at the capitalist core. The second, closely related issue was the ability of the US to maintain the growth of global aggregate demand through its balance of payment deficits, partly generated by heavy overseas military expenditure. The third element was the substantial congruence of ideas, institutions and policies among the leading capitalist nations, in a system of “embedded liberalism”. This involved the emergence and consolidation of the ideology of the mixed economy. Along with the rise of the Cold War, this was important in the reconstitution of the legitimacy of the liberal-democratic form of rule in the West and in Japan. A fourth element was the cheap and plentiful supply of raw materials, especially oil.

In order to cement this order, as Gill and Law termed the word, a new *international historic bloc* of *social forces*, centred in the US, came to be the socio-political centrepiece of the post-war alliance in the “West”. The leading elements in this constellation sought to internationalise New Deal principles and to extend opportunities for exports and/or foreign direct investment, both in manufacturing and extractive industries.¹⁹

The concept of an international historic bloc means much more than an alliance

¹⁷ R.W. Cox, ‘Social Forces, States and World Orders: Beyond International Relations Theory’, *Millennium Journal of International Studies* Vol.10 (2) (London, London School of Economics, 1981), P126-155

¹⁸ Ruggie, J.G., ‘International Regimes, Transactions and change: Embedded liberalism in the Postwar Economic order’, in *International Organization* 36(2), (Cambridge, The MIT Press, 1982), P379-415

¹⁹ Gill and Law, ‘Global hegemony and the structural power of capital’, P96

of capitalist interests across national boundaries. It implies that elements of more than one class were involved and its basis was more organic and rooted in material and normative structures of society, that is 'in the governmental and social institutions and civil societies of a number of countries, including weak states...[hence] the alliance of social forces it comprises is seen as "natural" and legitimate by most of its members'.²⁰

The forms and functions of the US-led hegemony, however, began to alter following the world economic crisis of the 1970s. This overall crisis, both of the world economy and of social power within various forms of state has been explained as being the result of two particular tendencies: the internationalisation of production and the internationalisation of the state, which led the thrust towards globalisation.²¹

Since the erosion of pax Americana principles of world order in the 1970s, there has been an increasing internationalisation of production and finance, driven, at the apex of an emerging global class structure, by a 'transnational managerial class'. Taking advantage of differences between countries, there has been an integration of production processes on a transnational scale with transnational corporations.

Jong H. Park argues that among the changes during that period, there was a shift of activity in both economic and international economic policy from the Atlantic to the Pacific basin countries. This shift started with the emergence of Japan as a Pacific and world economic power and the remarkable success of industrialisation in East Asian countries. At the same time, the rise of a unified Europe (Europe 1992) accentuated the split of the Atlantic basin. Thus, the world economy was seen to be heading towards a tripolar economic order dominated by the three big economic giants; the US, the EU and Japan.²²

Among various actors in the multi-layered trading environment, the United States is a very important factor in EU-Japan relations. Not only the United States' position in the international political economy, but also its special relationships with both the EU and Japan, make it inevitable that European and Japanese decision-makers weigh the influence of the United States in dealing with each other. Furthermore, as hegemonic stability theory argues, the United States played a significant role in establishing today's environment of the international political economy, as well as the establishment of international organisations. According to Donald C. Hellmann, one international relationship, the US-Japan alliance, has totally overshadowed all others in the post-war

²⁰ Gill and Law, 'Global hegemony and the structural power of capital', P97

²¹ Morton, "Unravelling Gramsci", P123

²² Park, 'Trading Blocs and US-Japan Relations in Pacific Trade and Cooperation' in Michael Landeck (ed), 'International Trade: Regional and Global Issues', P66

period.²³ Atsuko Abe argues that misunderstanding and indifference, which dominated EC-Japan relations until the end of the 1980s, were partly due to the role of the United States in the world structure. As a result of both the EC and Japan emphasising their respective bilateral relationships with the United States in their foreign policies, they obscured their importance to each other.²⁴

2-2. Neoliberal Institutionalism

Keohane's work, "After Hegemony" provided the most compelling theoretical justification for the existence and role of international institutions in world politics. Neoliberal institutionalism has developed to be the main alternative to realism for understanding international relations.

With trends such as the increasing prominence of "non-state actors" including multinational corporations, nongovernmental organisations and international institutions, the importance of the neoliberal paradigm has made neorealism a less powerful explanation of international relations.

The main element of neoliberal institutionalists is an emphasis on non-state actors, including international institutions. Through this emphasis, neoliberal institutionalists focus on the importance of cooperation as well as confrontation in international politics, in contrast to realists' and neorealists' emphasis on military force and coercion.

However, both realists and neoliberal institutionalists also share the view that states are critical actors in world politics. Neoliberal institutionalism takes a broader view of various actors and includes "sets of governing arrangements" that involve "implicit or explicit principles, norms, rules and decision making procedures around which actors' expectations converge."

In other words, international institutions are a broader category of actor than organisations, which they subsume. Thus, for neoliberal institutionalism, world politics is institutionalised, although to differing extents in different issue areas and regions. Almost every area of global cooperation has been formalised into an international institution, and many of them have expanded their membership, such as the World Bank, IMF, the WTO, and the EU. What we have seen on specific issue areas in the WTO shows that the institutions have grown to reach many issue areas that were once considered purely

²³ Donald C. Hellmann, 'Japanese Politics and Foreign Policy: Elitist Democracy within an American Greenhouse', in Takashi Inoguchi and Daniel I. Okimoto, 'The Political Economy of Japan – Volume 2', (Stanford, Stanford University Press, 1988), P356

²⁴ Abe, 'Japan and the European Union: Domestic Politics and Transnational Relations', P3

domestic.

Neoliberal institutionalists assert that in which condition countries create and join international institutions is key. Keohane's theory argues, that a country, being rational, will only demand and join international institutions if those institutions can provide net benefit for them relative to the reversion point. Benefit can be considered as reduced transaction costs, increased information flow, and reduced uncertainty. In providing these functions, international institutions help states negotiate mutually beneficial agreements that they otherwise would not be able to arrange.

Such international institutions with their enhanced function mean that the institutionalisation of world politics is becoming increasingly legalised, and this legalisation is having important effects on international cooperation.²⁵

In the institutionalised and legalised world politics, trade relations are an area of “complex interdependence”. Complex interdependence seems to prevail, and institutionalised cooperation is becoming the norm. Interdependence means mutual dependence, not necessarily symmetric, which brings benefits for all parties involved. Even in situations where everyone gains from cooperation, some actors will have a greater ability than others to influence the shape and content of the cooperative arrangement. In the institutionalised world politics, there is no single hierarchy of power resources, and states vary in their capacities to influence outcomes by issue areas. The EU and Japan can be influential in one issue area, but less powerful in other issue areas. Examining a particular issue area can demonstrate the importance of distinct power resources for different transnational and non-state actors.

Realism and neorealism have generally focused on conflicts among states and especially on the use of military force and capability. However, realists also agree that countries can at times cooperate, and alliances and balancing are important forms of cooperation central to realist theory. Neoliberal institutionalism has gone further and tried to explain institutionalised cooperation sustained policy coordination among states often guided by norms, rules, and practices codified in treaties, agreements, or international organisations. In such arrangements, countries often relinquish a substantial degree of sovereignty and autonomy over important policy areas. For such institutionalised cooperation to exist, countries must comply with the norms and rules embodied in the institutions. And they must generally comply both when they benefit and are adversely affected. A distinctive point about the evolution of neoliberal institutionalism has been the

²⁵ Helen V. Milner & Andrew Moravcsik (eds), 'Power, Interdependence, and Nonstate actors in world politics', (Princeton University Press, New Jersey), P8-13

move from cooperation to institutionalised cooperation or global governance.

Such arguments of neoliberal institutionalism on cooperation are correspondent to our research. As we will see in chapter 2, the EU and Japan also positively contributed to institutionalised cooperation through GATT and later the WTO. The substantial reduction in tariffs through successful GATT trade rounds also provides strong evidence for the neoliberal institutionalist theory about the role of institutions in fostering cooperation.

However, in the era of institutionalised cooperation, a question remains, to what extent and under what conditions countries comply with the rules, norms, and practices of the international institutions to which they belong.²⁶ In order to answer this question, what is crucial is the role of non-state actors, not only in international institutions but also in private sectors.

2-3. Private actors

Helen V. Milner asserts that neoliberal institutionalism points out the growing role of private sectors in world politics, but it has not carefully assessed the costs and benefits of such cooperation. Who benefits from international cooperation and global governance is an important issue that early work on neoliberal institutionalism did not address. In neo-Gramscian perspective, attention is given to social-class forces and processes and how these relate to the development of states in contrast to conventional state-centric approaches in IR.²⁷

In conventional state-centric approach, the state tends to be viewed as a unitary actor, often with little reference to the importance of domestic politics. This means, that in relations with other states, governments adopt a united front, based on an agreed consensus concerning the national interest of the state. In reality, domestic political forces all have an interest in the nature of the international regimes which directly affect their interests. Such conflicting domestic forces may mean that the concept of 'national interest' is highly problematic. As in much realist writing, there is also a tendency to overlook transnational social forces, and the role of non-state actors.²⁸

In the area of trade, depending on the issue, banks or large multinational enterprises are just as important as states. Steven McGuire's work, for instance, provides the best illustration of the relationship of firms and states in the development and conduct

²⁶ Milner & Moravcsik, 'Power, Interdependence, and Nonstate actors in world politics', P19-21

²⁷ Morton, "Unravelling Gramsci", P119

²⁸ Stephen Gill and David Law, 'The Global Political Economy', (The Johns Hopkins University Press, 1988), P38, P39

of international trade policy. He notes that “International trade matters are less and less about ‘trade’ as conventionally defined. Rather they are about the complex interplay between corporate strategies and government regulatory regimes.”²⁹ Jan Aart Scholte, Robert O’Brien and Marc Williams point out the cases where non-state actors have even bypassed the government authorities and have sought direct contact with the WTO in order to interrogate and lobby the multilateral institution itself.³⁰

In the neo-Gramscian view, the state is not unquestioningly considered as a distinct institutional category, or thing in itself, but conceived as a form of social relations through which capitalism and hegemony are expressed. Therefore, hegemony is first consolidated domestically within the state, and then it may go beyond a particular social order, and further move on a world scale and develop into the world order. Once it moves on a world scale, it could connect social class forces across different countries.³¹

Such view is particularly important in our context, as Bernald M. Hoekman and Michel M. Kostecki argue that the foreign trade policy-making process is generally torn by conflicting objectives of national interest-groups, as well as by external considerations. Industry associations, labour unions, regional authorities, consumer lobbies and different government departments all interact in determining the policy outcome.³² Stephan Woolcock argues that because of the diverse interests of various actors, participating governments in multilateral trade negotiations are often pulled between contradictory pressures and may spend more time to negotiate internally than with their trade partners.³³

In this sense, transnational capital is not simply represented as an autonomous force beyond the power of the state but instead is represented by certain classes or fractions of classes within the state. There are contradictory and heterogeneous relations internal to the state, which are induced by class antagonisms between nationally and transnationally based capital and labour.

²⁹ Steven McGuire, ‘Firms and governments in international trade’ in Brian Hocking and Steven McGuire (eds), ‘Trade Politics, International, Domestic and Regional Perspectives’, (London, Routledge, 1999), P147-161

³⁰ Jan Aart Scholte with Robert O’Brien and Marc Williams, ‘The World Trade Organization and civil society’ in Brian Hocking and Steven McGuire (eds), ‘Trade Politics, International, Domestic and Regional Perspectives’, (London, Routledge, 1999), P163

³¹ Morton, “Unravelling Gramsci”, P121

³² Hoekman, Bernard M. and Kostecki, Michel M. ‘The Political Economy of the World Trading System – From GATT to WTO’, (Oxford, Oxford University Press, 1995), P24

³³ Stephan Woolcock, ‘European Trade Policy – Global Pressure and Domestic Constraints’, in Helen Wallace and William Wallace(eds.), ‘Policy Making in the European Union’, (Oxford, Oxford University Press, 2000), P373

Today, capital is so internationally mobile, especially between the major capitalist economies. Following the neo-Gramscian focus on social-class forces as the main actors, the transnational restructuring of capitalism within globalisation led to the emergence of new social forces of capital and labour.

Transnational social forces are supportive for the global economy. The transnational managerial class, other elements of productive capital such as manufacturing industry, import-export businesses, financial capital such as banking, insurance industry have been supportive of this transnationalisation of capital. Thus, transnational capital has been more and more supported and promoted by forms of elite relationship that have forged common perspectives between business, state officials, and representatives of international organisations, favouring the logic of capitalist market relations.

In contrast, nationally based capital, engendered by national production systems, may oppose an open global economy, due to their reliance on national or regional protectionism against global competition.³⁴ Yasusuke Murakami and Yutaka Kosai assert that the deepening of interdependent relations on many levels and the trend toward internationalisation of goods, money, corporations and other economic entities that transcend national boundaries is coming into conflict with the political tendency to give priority to national interests, and this is the cause of all manner of friction among nations.³⁵ Thus, there are significant divisions between transnational and national capital in terms of their stances toward global economy.

Taken into this point, which is addressed in our research, particularly in the agricultural and steel issue, is the importance of focusing on particular issue areas to understand the key players and their power resources in a world of complex interdependence. What we will attempt in the following chapters is to find out who are the main actors and what kinds of resources they can use to realise their goals and how they utilize the institutions. In this sense, private sectors as non-state actors are becoming more and more important in numerous issue areas of world politics and the governance in a globalised world.

Today multilateral trade negotiations are facing great difficulty to proceed with trade liberalisation. Every WTO trade round faced delays and teetered on the edge of collapse and in some cases ended in dramatic failure. Early members of the GATT were

³⁴ Adam David Morton, "Unravelling Gramsci", P124

³⁵ Murakami, Yasusuke. and Kosai, Yutaka. (eds), 'Japan in the global community', (Tokyo, University of Tokyo Press, 1986), P16-17

developed countries, which tended to share a preference for lower tariffs for industrial products which they exported, and for higher tariffs for textiles and agricultural goods, which were produced more cheaply abroad. As a result, the international trade regime remained asymmetric, tolerating high subsidies and barriers to trade in agricultural goods. The Uruguay Round extended it to cover services, foreign direct investment, intellectual property rights, and more importantly it started to deal more intensively with trade liberalisation in agriculture. In the case of agriculture, represented by the formation of Carins Group, WTO members are divided on this issue area. Our following chapters illustrate the point that when institutions are used for cooperation on multiple issues, gradually expanding membership may create a bias against deepening cooperation.³⁶

Classical liberal trade theory suggests that international trade liberalisation should be considered as a public good that is easily provided because everyone's optimal strategy is to liberalise. If it is so, why are the WTO trade negotiations stalled, and why are some member countries adamantly against agricultural trade liberalisation? Our research will show that there is a clear gap between theory and practice. As in the liberal trade theory, if trade liberalisation is a public good, why does the EU not abandon its market-distorting export subsidies, and why does Japan not open its rice market? What is behind the gap between the theory and practice is the increasing influence of private actors or social forces.

Some WTO members often face strong domestic lobbies in agriculture, textile, steel and other sectors, creating pressure for trade restrictions. Given these political constraints, countries may be either unwilling or unable to sustain processes of economic liberalisation by themselves. While some countries continue to fully implement their market-opening commitments, others could slow or halt theirs. But their counterparts may find this unacceptable, and react by renegeing on their own commitments.³⁷

The importance of domestic actors and its influence upon multilateral trade negotiations has been neglected or given less attention, since the WTO is the organisation which dealt only with states (with exception of the EU). However, as our empirical research will show, in today's complex trade negotiations, the role played by domestic actors is becoming increasingly important.

2-4. Two-level approach

³⁶ Milner & Moravcsik, 'Power, Interdependence, and Nonstate actors in world politics', P47

³⁷ Milner & Moravcsik, 'Power, Interdependence, and Nonstate actors in world politics', P166

A close observation of private sectors gives us the answer to the issue which the state centric approach did not address. In the case of the EU-Japan relationship, the EU countries and Japan share similar national interests in some trade issues. However, the question remains, who decides what the national interests are?

Since the WTO now covers a number of cumbersome trade issues, some trade issues have become very sensitive to the national interest of WTO member countries, because in some trade areas, domestic industries are politically influential and becoming increasingly vocal to shape the trade policy or 'national interest' of the state. Negotiators, trade officials and politicians are not able to ignore the pressure from domestic industry. In this sense, the states' negotiation stances or trade policy are now deeply interwoven with the demand of various private actors.

Putnam pointed out the linkage between international negotiation and domestic consensus building.³⁸ Putnam warns that unitary-actor assumption is often radically misleading, since the state-centric literature is an uncertain foundation for theorizing about how domestic and international politics interact. He cites Robert Strauss's comment on trade negotiations during Tokyo Round:

"During my tenure as Special Trade Representative, I spent as much time negotiating with domestic constituents (both industry and labor) and members of the U.S. Congress as I did negotiating with our foreign trading partners"³⁹

Unlike state-centric theories, Putnam's two-level approach recognises the inevitability of domestic conflict about what the 'national interest' requires. According to him, the politics of many international negotiations can usefully be conceived as a two-level game. At the national level, domestic groups pursue their interests by pressing the government to adopt favourable policies, and politicians seek power by constructing coalitions among those groups. At the international level, national governments seek to maximise their own ability to satisfy domestic pressures, while minimizing the adverse consequences of foreign developments.

In this sense, in order to predict the direction of the EU-Japan relationship, it would be very important to investigate their relations to private actors or various social forces from the two-level approach by focusing on the linkage between domestic and international negotiations. In today's world politics, interests of various actors or social

³⁸ Robert D. Putnam, 'Diplomacy and domestic politics: the logic of two-level games' in *International Organisation* 42, 3 Summer 1988, P427-P460

³⁹ Putnam, "Diplomacy and domestic politics: the logic of two-level games', P433

forces are interwoven. Adding to the difficulty of investigating each actor, in the case of the EU, research is required to look at policy coordination within the EU toward the WTO trade negotiations.

Putnam asserts that a preliminary Level 1 agreement (at a national level) cannot be amended at Level 2 (at the international level) without reopening the Level 1 negotiations.⁴⁰ This indicates, so long as the agricultural industry remains powerful and influential within the EU and Japan and their negotiations stances remain unchanged, we can predict that the EU and Japan somehow will maintain a positive relationship with each other. Based on this cooperation, the EU and Japan also may continue their joint effort to fight against US unilateralism. However, multilateral trade negotiations have been experiencing great difficulty in recent years. Many of the members casted doubt on multilateral trade negotiations and started to conclude bilateral trade agreements, represented by FTA, with specific trade partners. As agriculture remains the main obstacle in the WTO negotiations, it is necessary to investigate if the EU and Japan, as two of the biggest stakeholders on the issue, can cope with domestic voices and contribute to the progress in the WTO trade talks. Or will the politically influential agricultural industries within the EU and Japan still not allow their negotiators to make any concessions on the issue, even at the expense of collapse of multilateral trading system? Whether acting jointly or individually, the EU and Japan's position in the WTO heavily depends on the Level I agreement, which is the national level of discussion.

2-5. New constitutionalism

Now we look at the role of international organisations in connection with transnational corporations and international capital mobility, monetary and information flows and communications links. Transnational corporations lobby their parent governments in order to obtain policies favourable to their operations overseas; such lobbying also takes place with regard to host governments, as well as international organisations. However, in comparison with domestic networks, international networks generated between business, state officials, bureaucrats, and members of international organisations, have not been thoroughly researched or understood.⁴¹

In his detailed analysis of the role of the Trilateral Commission, Stephen Gill has greatly contributed to the understanding of this process as part of the changing character of the US-centred hegemony in the global political economy and international governance

⁴⁰ Putnam, "Diplomacy and domestic politics: the logic of two-level games", P437

⁴¹ Gill and Law, 'Global hegemony and the structural power of capital', P103

framework. Gill locates the global restructuring of production within a context of structural change in the 1970s, when there was a transition from an international historic bloc of social-class forces during the post-Second World War period towards a transnational historical bloc. This linked interests and identities beyond national boundaries and classes and created the conditions for the hegemony of transnational capital.

Gill recognises the current transnational historical bloc as supremacy but not hegemony. The term “supremacy”, which implies the form of rule based on economic coercion, is used when a situation of hegemony is not apparent and when dominance is exercised through a historical bloc over split opposition.⁴² According to Gill, the politics of supremacy are organised through two key processes: the new constitutionalism of disciplinary neoliberalism and the spread of market civilisation based on market efficiency, discipline and confidence.

New constitutionalism is an international governance framework, which separates economic policies from broad political accountability in order to make governments more responsive to the discipline of market forces but less responsive to democratic forces.⁴³ Such a framework leads to a political and legal reconstruction of capital through the agency of a neo-liberal transnational historical bloc. This is a political integration of interests derived from various social classes and nations which co-ordinate national, regional and global dimensions of accumulation.⁴⁴ Thus, new constitutionalism is regarded as the move towards the construction of legal or constitutional devices to remove new economic institutions from democratic accountability.⁴⁵

The business and government leaders of different countries intend to establish the general conditions of the existence of the international order, although they do not share the interest on all issues. In order to establish such an international order, international organisations accept a framework of thought that serves the interests of capital and exerts influence and sometimes even pressure on national governments.⁴⁶

Due to the need of creating such general conditions for transnational business transactions, an international organisation needs to act in accord with the national government. Therefore, the role of the international organisation becomes more and more important. In the area of world trade, Gill’s new constitutionalism gives a useful

⁴² Morton, “Unravelling Gramsci”, P126, P127

⁴³ Bieler and Morton (edt.), ‘Social Forces in the making of the new Europe’, P47

⁴⁴ Bieler and Morton, ‘Social Forces in the making of the new Europe’, P54

⁴⁵ Morton, “Unravelling Gramsci”, P127

⁴⁶ Gill and Law, ‘Global hegemony and the structural power of capital’, P104

perspective to the question of how the WTO has been playing a central role to provide general conditions for transnational capital.⁴⁷

3. Structure of the thesis

Chapter 2 examines the EU-Japan economic relationship inside and outside the GATT/WTO framework. The timeframe is set from 1952 when Japan applied for GATT membership to 1995 when the EU and Japan attempted to solve their first trade dispute in the WTO on Japan's liquor tax system through the WTO trade dispute settlement system. With this timeframe, the chapter analyses both confrontational and cooperative issues between the EU and Japan and examines how the establishment of the WTO influenced their bilateral trade relations and their relationship in the WTO today.

Chapter 3 examines the EU-Japan relationship on WTO agricultural trade negotiations. As agricultural trade is one of the most important issues for the EU and Japan, the details of their individual positions and their differences are also going to be examined. The chapter also explains the EU and Japan's joint strategy on farm trade negotiations. As for the timeframe, the analysis is conducted from the GATT Uruguay Round (1985-1995), through the Seattle Ministerial Conference (30. November -3 December 1999) and the Doha Ministerial Conference (9-13 November 2001) to the two-day meeting between the five major farm traders (Australia, Canada, the EU, the US and Japan) held in Nara, Japan in July 2002. This timeframe enables us to see the development of the EU-Japan relationship and its effect on WTO agricultural trade negotiations.

Chapter 4 analyses the EU-Japan relationship on steel trade in the WTO. Their relationship on steel issues is, in the first place, framed by the increasing protectionism of the United States especially since 1997 to which the EU and Japan felt the need to reply with their lawsuits in the WTO Dispute Settlement System. Steel trade disputes had often been put to the WTO Dispute Settlement Procedure. Because the nature of the steel trade issue is relevant to the GATT/WTO, the chapter conducts separate investigations on each steel dispute in which the EU and Japan have taken part. The timeframe is set from 1997, when steel trade led to tensions between the EU, Japan and the US (concurrent with the outbreak of the Asian financial crisis in 1997), until the end of 2003 when the WTO ruled against US safeguard measures on its steel imports. This timeframe allows us to investigate three different trade measures introduced by the US, and the EU-Japan relationship to these trade measures.

⁴⁷ Gill and Law, 'The Global Political Economy', P36

Finally Chapter 5, the conclusion, is a brief summary of the findings in an attempt to assess the EU-Japan relationship before and after the establishment of the WTO, and the EU-Japan relationship on agricultural and steel trade issues. The findings of the research from each chapter will be analysed in relation to the hypotheses of chapter one. A final analysis will be made of the role of elite capitalist social forces from the EU and Japan in utilising the WTO to create capitalism to facilitate the common interests and a “new hegemony” of transnational capital.

Chapter 2

The EU-Japan economic relationship inside and outside the GATT/WTO framework

Introduction

It is broadly acknowledged that the EU and Japan have deepened their relationships on a variety of trade issues in the World Trade Organisation.⁴⁸ This chapter analyses the relationship between the EU and Japan before the establishment of the WTO. This retrospective investigation will allow us to evaluate the growing role of multilateral trade negotiations in the EU-Japan trade relationship which was initially predominantly bilateral. In the first part of this chapter, I will give an overview of this initial period which was marked by many confrontational issues and bilateral dispute settlements.

In addition to each trade dispute between the EU and Japan, it will be observed, how various domestic social forces influence trade policy of each side. Having a close look at how governments and private sectors are interacting and shaping trade policies or negotiation stances in bilateral/multilateral trade negotiations is also the objective of this chapter.

Part 1. Europe and Japan outside the GATT/WTO framework

1. Overview

1-1. Japan's entry into the GATT and European opposition

Post-war relations between Europe and Japan started on the wrong foot as was clearly illustrated by Europe's negative attitude towards Japan's GATT membership. When Japan applied for GATT membership in 1952, it faced strong opposition from the United Kingdom and British Commonwealth countries such as Australia and South Africa.⁴⁹ Other European countries were also concerned about a repetition of 'Japan's pre-war dumping offensives of low-wage products, its pirating of intellectual property, the misleading information given about the origins, contents, or quality of its goods, and its export subsidies'.⁵⁰ These negative experiences made all European states rally against any concessions to Japan.⁵¹

⁴⁸ See for example, Naohisa Murakami, 'WTO – sekaiboueki no yukue to Nihon no sentaku' (Tokyo, Heibonsha, 2001) P136; Shinji Hattori, 'Global-ka wo ikiru nihon-nougyou' (Tokyo, NHK Press, 2001) P13,14; Georg Wiessala, 'The European Union and Asian Countries', (London, Sheffield Academic Press, 2002), P107

⁴⁹ Kenji Ishikawa, 'Japan and the challenge of Europe 1992', (London, Pinter, for the Royal Institute of International Affairs, 1990), P13

⁵⁰ Nester, 'European Power and The Japanese Challenge', P203

⁵¹ On European rejection of Japan's entry into GATT, see: Frank McDonald, 'The European Union and the Triad', in Frank McDonald and Stephen Dearden (eds), 'European Economic Integration – third edition', (Essex, Pearson Education Ltd., 1999), P367

US policy towards Japan made a striking contrast to the strong European resistance. The US allowed Japan almost unlimited access to its domestic market until the late 1960's and strongly promoted Japan's membership of international economic organizations such as the GATT and the Organisation for Economic Cooperation and Development (OECD). American motives were a mix of 'Cold War concerns about building up Japan as the "workshop" and economic anchor of East Asia and the Pacific, and spreading the burden of tolerating Japanese neomercantilism'.⁵²

The United States offered tariff concessions to the Europeans in exchange for their granting Japan Most-Favoured-Nation (MFN) status. MFN was the first article of the GATT which regulates that a country should not discriminate between its trading partners, and it should not discriminate between its own and foreign products.⁵³ Although European states strongly insisted on their rejection of Japan's accession to GATT and MFN status, the United States succeeded in persuading two-thirds of GATT members to sign the treaty, and Japan became finally a GATT member in 1955.⁵⁴ West Germany, the other vanquished nation, had already been allowed to enter the GATT in 1951,⁵⁵ However, even after Japan became a GATT member, fourteen countries including European countries such as the United Kingdom, Belgium, the Netherlands and later France, refused to extend MFN treatment to Japan. These countries invoked Article 35, which provided for the non-application of the GATT agreement between particular parties. Citing Article 35 of the GATT was the first discriminatory measure against Japan to be adopted by Western European countries after the war.⁵⁶

Among the European countries which originally rejected granting MFN status to Japan, Germany became the first to extend MFN status to Japan, although the German government acknowledged its action as risky.⁵⁷ Japan resented its unfair treatment and demanded immediate change when a GATT meeting was held in Tokyo in 1959. However, it was only in 1962 that Britain finally abandoned this protection, and Article 35 was replaced by each country's own restrictions at the end of 1988.⁵⁸

GATT membership was important symbolically as it showed that Japan had once

⁵² Nester, 'European Power and The Japanese Challenge', P203

⁵³ WTO information paper, 'Trading into the future' 2nd edition revised in April 1999, P5

⁵⁴ Nester, 'European Power and The Japanese Challenge', P203

⁵⁵ More details on European discriminatory measure toward Japan in: Michiko Ikeda, 'From GATT to the WTO (GATT kara WTO he)', (Tokyo, Chikuma Shinsho, 1996), P60-102

⁵⁶ About the European refusal of MFN status to Japan, see: Ishikawa, 'Japan and the challenge of Europe 1992', P13,14

⁵⁷ T. David Mason and Abdul M. Turay (eds), 'Japan, NAFTA and Europe', (New York, St. Martin's Press, 1995), P65, 66

⁵⁸ Ishikawa, 'Japan and the challenge of Europe 1992', P120

again become a member of the international community. It was also an important step in the broadening of Japan's export frontiers.⁵⁹ However, European discriminatory attitudes towards Japan left a tense atmosphere in Euro-Japanese relations.⁶⁰

1-2. The economic rise of Japan and European concerns in the 1950s

In 1955, when Japan was allowed to join the GATT, its exports accounted for only 2.4 per cent of total world exports, and its exports of industrial products amounted to just 4.2 per cent of total world trade of industrial products. This export share was much lower than in the 1930s. For example, in 1938, Japan's share was approximately 5.8 per cent in world exports. Japan's economy in the 1950s was still weak, and its Gross National Product (GNP) per capita and wage level were much lower than those of the developed countries. Japan's exports were dependent on labour intensive products and its imports were predominantly industrial raw materials, fuel and foodstuff.

On the other hand, several Japanese industries, such as steel and shipbuilding, expanded their capacity and increased rapidly their world share.⁶¹ For instance, the Japanese shipbuilding industry became number one in 1956 with 20 per cent of total world orders. High investment and improved industrial equipment enhanced the productivity of Japanese industries, and Japan's flexible industrial structure allowed to increase the export of manufactured goods.⁶²

The country's lack of natural resources made it imperative for Japan to be heavily involved in international trade. To fuel a modern economy, Japan has always had to import large quantities of raw materials. To pay for these raw materials, it has similarly been compelled to export large quantities of manufactured goods.⁶³

At the same time, such a rapid recovery of Japanese industry from the defeat in the Second World War was increasing European concerns about Japanese trade policy.

⁵⁹ Toru Nakakita, 'Trade and capital liberalisation policies in postwar Japan', in Juro Teranishi and Yutaka Kosai, 'Japanese experience of economic reforms', (Chippenham, Antony Rowe Ltd, 1993), P344

⁶⁰ Gordon Daniels and Reinhard Drifte, 'Europe and Japan, Changing relationship since 1945', (Ashford, Paul Norbury Publications, 1986), P15

⁶¹ In the post-war period, industries such as steel, shipping, automobiles, petrochemicals, computers and integrated circuits played a principal role in the process of modernizing the Japanese industrial structure. See: Motoshige Itoh, Masahiro Okuno, Kazuharu Kiyono, Kotaro Suzumura, 'Industry Promotion and Trade', in 'Industrial policy of Japan', (Tokyo, Academic Press Japan, 1988), P258

⁶² For details on Japanese industries and exports in the post-war era, see: Takashi Inoguchi and Daniel I. Okimoto, 'The Political Economy of Japan – Volume 2', (Stanford, Calif, Stanford University Press, 1988), P174, P175

⁶³ T. J. Pempel, 'Policy and Politics in Japan', (Philadelphia, Temple University Press, 1982), P47

European countries were concerned that Japanese exports of cheap products would swamp their domestic markets.

Simultaneously, the GATT made a good start by aiming at lowering tariffs through multilateral negotiations. At first, GATT rounds of trade negotiations focused only on lowering tariffs on import goods in recognition that removing trade barriers was the most effective way to expand world trade. Negotiations produced excellent results and made industrial countries' tariff rates on manufactured products fall remarkably. Through the success of lowering tariffs under GATT leadership, the world economy had successfully expanded. By the 1960s, European economies were booming and Japanese exports benefited directly from the expanded European market. This experience made the Japanese conscious of the importance of the European market as Japan's export destination. In the 1960s, the EC countries and Japan started to deepen their involvement in international trade politics. In the 1960s, Japan became a member of the main industrial countries by joining the OECD and signing a number of treaties of commerce with European states.⁶⁴ Simultaneously, the Japanese economy started to grow rapidly.

1-3. Growing trade frictions since the 1960s

International trade conflict appears often as the result of a change in the balance of economic power among nations.⁶⁵ This theory applies also to Euro-Japanese economic relations in the 1960s. In the context of Japan's economic impact upon Europe, Europeans perceived Japan's economic success since the 1960s as a threat to their industries, not only in their domestic market but also in important third markets.⁶⁶

Despite the wide range of discriminatory practices of GATT members, Japan's exports increased at a higher rate than that of the whole world. This implies that a majority of GATT member countries imported Japanese products in spite of discriminatory trade impediments.⁶⁷

Under these circumstances, Europeans started to perceive Japan's exports as a threat during the second half of the 1960s when Japan's economy rapidly roared past those of Italy, Britain, France, and Germany, and Japanese products began outselling

⁶⁴ Mason and Turay, 'Japan, NAFTA and Europe', P65,66

⁶⁵ Masaru Yoshimori, 'Psychological Aspect of Euro-Japanese Trade Frictions: A Japanese Viewpoint', in Gordon Daniels and Reinhard Drifte, 'Europe and Japan, Changing relationship since 1945' (Ashford, Paul Norbury Publications, 1986), P57

⁶⁶ Daniels and Drifte, 'Europe and Japan, Changing relationship since 1945', P92

⁶⁷ Ryutaro Komiya, 'The Japanese Economy: Trade Industry, and Government', (Tokyo, University of Tokyo Press, 1990), P47

those of their European rivals everywhere.⁶⁸ In 1965, Japan achieved a trade surplus with the United States. Since 1968, the EC had never had a trade surplus with Japan, while its deficit was steadily growing.⁶⁹ As the trade surplus widened through the 1960s and 1970s, trade conflicts occurred more frequently.

Trade problems between Europe and Japan were further aggravated after the oil crises in 1973 and 1979.⁷⁰ A massive rise in the price of oil and the cost of other raw materials forced Japan to export even more and triggered huge Japanese trade frictions with both the United States and Europe.⁷¹ The industries which particularly felt the impact of Japanese exports were textiles, shipbuilding, steel, automobiles, and electronic products which were sensitive sectors for European countries.⁷²

After the two oil crises, Europeans blamed Japan more frequently for trade imbalances.⁷³ When Japan's surplus with the EC reached 5 billion dollars in 1978, the Community called for substantial action to reduce the Japanese trade surplus.⁷⁴ As for the balance of visible trade, relatively sound Japanese economic performance after the oil crisis was in striking contrast to the worsening economic situation in Europe. Europe regarded Japan's economic success as a consequence of its protectionist trade policies and practices.⁷⁵ Such trade frictions, triggered by the oil crises, was the most urgent problem of Japanese trade policy in 1970s.⁷⁶

1-4. The trade imbalance between Europe and Japan in the 1980s and 1990s

Their trade frictions continued in the 1980s.⁷⁷ The Japanese export boost came at a moment, when world trade and economic growth had slowed down and European

⁶⁸ Nester, 'European Power and The Japanese Challenge', P197

⁶⁹ Ishikwawa, 'Japan and the challenge of Europe 1992', P44,

⁷⁰ Yoshimori, 'Psychological Aspect of Euro-Japanese Trade Frictions: A Japanese Viewpoint', P50

⁷¹ Endymion Wilkinson, 'The Economic and Non-Economic Dimensions of Euro-Japanese Relations', in Daniels and Drifte, 'Europe and Japan, Changing relationship since 1945' (Ashford, Paul Norbury Publications, 1986), P33

⁷² Inoguchi, 'Japan's International Relations', P20

⁷³ Yoshimori, 'Psychological Aspect of Euro-Japanese Trade Frictions: A Japanese Viewpoint', P50

⁷⁴ Daniels and Drifte, 'Europe and Japan, Changing relationship since 1945', P20,

⁷⁵ Yoshimori, 'Psychological Aspect of Euro-Japanese Trade Frictions: A Japanese Viewpoint', P50

⁷⁶ Motoshige Itoh and Kazuharu Kiyono, 'Foreign trade and direct investment', in Ryutaro Komiya, Masahiro Okuno and Kotaro Suzumura (eds), 'Industrial policy of Japan', (Tokyo, Academic Press Japan, 1988), P174

⁷⁷ On the EC-Japan trade imbalance in the 1980s, see: Hiromi Ohki, 'Economic Relations between Japan and the EC' in European Economic Studies, 'Euro Cooperation', (Paris, The Europartners' Group, 1992), P5-20; Manuel Enrique Gonzales, 'The European Community's Exports to Japan' in European Economic Studies, 'Euro Cooperation', (Paris, The Europartners' Group, 1992), P33-48

countries were suffering from inflation and high unemployment rates.⁷⁸ As their trade imbalance became politically sensitive, tension between Europe and Japan mounted.

In the 1980s and 1990s, trade relations between the EC/EU and Japan had often been characterised by conflict and tension. The root of these trade conflicts must be seen in the persistent trade deficit which the EC/EU continued to have with Japan. The EC/EU's trade deficit with Japan increased remarkably in the 1980s and 1990s. The EC's trade deficit deteriorated by 42 per cent between 1986 and 1992. The EC's deficit with Japan was a major element in the EC's chronic trade deficit with the rest of the world, amounting in the 1990s on average to more than half of the EC/EU's overall external trade deficit.⁷⁹

The long-term structural trade imbalance between the EC and Japan was determined by Japan's export promoting and import reducing measures. In 1992, Japan belonged to the EC's five largest export markets; it had ranked only eleventh in 1980. Japan's propensity to import appeared to be low compared with European countries. In 1990, for example, its per capita imports were significantly lower than those in the top four of the EC. While Germany, France, Britain and Italy had imports per head amounting to 4,460 dollars, 4,150 dollars, 3,890 dollars, and 3,160 dollars respectively, per capita imports in Japan were significantly lower with 1,900 dollars. Japan also compared unfavourably, when imports as a proportion of GDP are considered. In 1990, the merchandise imports to GDP ratio was 8 per cent in Japan. In the EC, on the other hand, merchandise imports (including intra-EC trade) amounted to 24 per cent in 1988. Since formal trade barriers, with the exception of agriculture, were low in Japan, Europeans considered that informal trade barriers must have played a part in bringing about such a comparatively low import propensity.

Behind the EC-Japan trade imbalance were Euro-Japan structural differences in export/import relations. Japan's share of EC imports rose from a mere 1 per cent in 1958 to 4 per cent in 1975 and reached 11 per cent in 1992. As an export market, Japan had been less significant for the EC. While Japan was, after the US, the largest import source for the EC, it ranked only fifth in 1992 as an export market after the US, Switzerland, Austria and Sweden although its share of EC exports had been increasing over the years.

In 1992, the EC provided 14 per cent of Japan's imports; the main non-EC

⁷⁸ Wilkinson, 'The Economic and Non-Economic Dimensions of Euro-Japanese Relations', P34

⁷⁹ Stephen D. Krasner, 'Japan and the United States: Prospects for stability', in Inoguchi and Okimoto, 'The Political Economy of Japan', (Stanford, Calif, Stanford University Press, 1988), P394

suppliers of Japan's imports were the US and China who met 23 and 7 per cent of Japan's import demand respectively. The US had been by far the largest external market for Japan where some 28 per cent of all Japanese exports went. The EC represented the second largest export market for Japan with nearly one fifth of all its exports being sold in the European domestic market in 1992.⁸⁰

The trade relationship between the EC and Japan was, in quantitative terms, fairly interdependent. But Japan appeared to be relying more on Europe for both its exports and imports; the EC, on the other hand, seemed to need Japan for meeting its import demand but had so far not been able to direct a sizeable proportion of its total external exports to reach Japanese customers.⁸¹

2. The main complaints of each side and their respective countermeasures

The cause of the trade imbalance was perceived differently in Europe and Japan. Europe, which was affected more negatively by the trade imbalance, argued that the Japanese were responsible for creating the trade imbalance. Europe pointed out two main factors which it believed resulted in a European disadvantage in trade with Japan. Japan, on the other hand, refused to accept these arguments. Mutual recriminations were followed by a number of retaliatory countermeasures.

2-1. European perception of Japanese unfairness – 1.) Closed nature of Japan's market

Interventionist Japanese policies were seen as a major factor behind the success of key sectors, such as automobiles and electronics.⁸² Policies to protect and promote infant industries may be justified for a developing country, and thus were acceptable for Japan in the 1950s and 1960s.⁸³

However, in the late 1960s, Japan's balance of payments began to turn positive.⁸⁴ After this period, Japan's trade partners strongly requested the removal of the remaining

⁸⁰ About Japanese exports to the EC, see: Jean Macron, 'Japanese Export to the EC' in European Economic Studies, 'Euro Cooperation', (The 'Europartners' Group, 1992), P49-65

⁸¹ Klaus Heidensohn, 'Europe and World Trade', (London, Pinter, 1995) P108, 109

⁸² On Japan's industrial promotion in the automobile sector, see: Hiromichi Mutoh, 'The Automotive Industry', in Ryutaro Komiya, Masahiro Okuno and Kotaro Suzumura (eds), 'Industrial Policy of Japan', (Tokyo, Academic Press Japan, 1988), P307-331

⁸³ Yoko Sazanami, Shujiro Urata and Hiroki Kawai, 'Measuring the costs of protection in Japan', (Washington DC, Institute for International Economics, 1995) P1-3

⁸⁴ Ryutaro Komiya and Motohige Itoh, 'Japan's international trade and trade policy, 1955-1984', in Takashi Inoguchi and Daniel I. Okimoto (eds), 'The Political Economy of Japan Volume2', (Stanford, Stanford University Press, 1988), P190

import quotas and reduction of tariff and NTBs.⁸⁵ Broadly speaking, two types of measures, tariffs and non-tariff measures protected domestic producers in Japan. Different types of restrictions were applied to different sectors.⁸⁶

Japan reduced tariff rates after the conclusion of the Kennedy Round (1964-1967). With the intention of reducing the trade surplus, in 1972, Japan reduced tariff rates on all (with few exceptions) processed agricultural products, manufactures, and mining products by 20 per cent. As a result, Japanese tariff rates were reduced substantially, and the tendency toward tariff escalation was mitigated.

As compared with other industrial countries, Japanese tariff rates were as high as the United States, the UK and the EC before the start of the Kennedy Round. They declined however more than any other country's rates between 1968 and 1975, especially between 1973 to 1975. Finally, they decreased to a level lower than those of the United States, the EC and the UK by the middle of the 1970s. By the early 1980s, the major trading partners generally agreed that Japanese tariff rates were reduced to the lowest level among major industrial countries.⁸⁷

While Japan's import tariffs had been declining, Europe argued that Japanese import tariffs were merely replaced by complex NTBs.⁸⁸ Since becoming a GATT member and until the beginning of the 1980s, the Japanese had repeated their claim that there were no serious trade barriers impeding foreign products in Japan. It was argued by William R. Nester that the essence of Japanese neo-mercantilism was the targeting of strategic industries for development by protecting them from competitive imports and assisting their conquest of the global market.⁸⁹

Facing European criticism since the end of the 1960s, Japan had pursued policies of reducing NTBs in an attempt to promote imports.⁹⁰ In 1982, when the Japanese government for the first time officially acknowledged the existence of NTBs,⁹¹ it started to review the rules regarding import procedures, standards, and testing which had been subject to foreign criticism.⁹²

⁸⁵ Komiya and Itoh, 'The Political Economy of Japan Volume2', P190

⁸⁶ Sazanami, Urata and Kawai, 'Measuring the costs of protection in Japan', P19, P43

⁸⁷ About Japan's tariff reduction, see: Komiya and Itoh, 'The Political Economy of Japan Volume2', P191-193

⁸⁸ About Japanese non-tariff barriers, see: Haruko Fukuda, 'Japan and world trade – the years ahead', (Glasgow, Saxon House, 1973), P81-P94, see also: Charlie G. Turner, 'Japan's Dynamic Efficiency in the Global Market – Trade, investment, and economic growth', (Westport, Greenwood Publishing Group, 1989), P74-77

⁸⁹ Nester, 'European Power and The Japanese Challenge', P133-135

⁹⁰ Komiya and Itoh, 'The Political Economy of Japan Volume2', P209

⁹¹ Daniels and Drifte, 'Europe and Japan, Changing relationship since 1945', P95

⁹² Komiya and Itoh, 'The Political Economy of Japan Volume2', P209

In relation to the NTBs, Japan's *Keiretsu* system became a particular target of criticism from foreign exporters. Keiretsu are the industrial conglomerates which are related through cross shareholding and exchanging goods and services within the same group. A major Keiretsu traditionally had three sectors: production, distribution and capital. Keiretsu created a peculiar distribution system. Keiretsu tended to purchase within the group, even if the products were more expensive or of inferior quality. Keiretsu transactions within the group generally accounted for 30 percent of total transactions which were made by Keiretsu. The big nine trading firms which accounted for over half of Japanese import and export were particularly notorious for their discriminatory purchasing practices.⁹³ Foreign exporters vigorously criticized this Japanese peculiar distribution system as a NTB for foreign products.⁹⁴

There were two main effects of the Keiretsu system; first as a barrier to imports, second as stimulation for innovation. In the absence of imports, Japan was a test market for Japanese firms (where also reduction of prices as a result of economies of scale could be achieved) which subsequently exported the tested products at competitive prices to the rest of the world.⁹⁵

2-2. European perception of Japanese unfairness – 2.) Japan's export strategy

Critics of Japanese trade policy contended that, by insulating domestic industries from foreign competition, and by providing them with a platform from which to export aggressively, the Japanese government enabled domestic firms to gain valuable ground in the global race for industrial leadership.⁹⁶

From the 1950s until the late 1960s, the Japanese trade policy strategy consisted of the promotion of exports.⁹⁷ This was done through subsidies, provision of low-interest loans for promising export industries, preferential tax treatment of income from exports and exploration of new export markets. Such governmental measures resulted in low

⁹³ For details on Keiretsu, see: Nester, 'European Power and The Japanese Challenge', P117; see also; Bill Emmott, 'Japan's Global Reach – The influence, strategies and weakness of Japan's multinational companies', (London, Century Business, 1992), P135-141

⁹⁴ Especially retail distribution was one of the areas identified by its trade partners as constituting a serious, structural non-tariff barrier, see: Okimoto, 'Political Industry: The Domestic Structure of Trade', in Inoguchi and Okimoto, 'The Political Economy of Japan', P328

⁹⁵ Marcel F. van Marion, 'Liberal trade and Japan: the incompatibility issue', (Heidelberg, Physica-Verlag, 1993), P94

⁹⁶ Sazanami, Urata and Kawai 'Measuring the costs of protection in Japan', P1-3

⁹⁷ On the development of Japan's export trade, see: Fukuda, 'Japan and world trade – the years ahead', P41-64

costs and strong incentives for export industries.⁹⁸

Foreign competitors had frequently accused the Japanese government of artificially stimulating exports. The main attack was on government export promotion and market expansion programmes, official export financing and tax policies. Western trade interests argued that such programmes, by increasing the competitiveness of Japanese exports, had hampered the export prospects of US and EC products. It was pointed out by Radha Sinha that the Japanese export stimulation programmes were well organised but, on the other hand, Japan was not the only country with such programmes. All the major competitors (the US, West Germany, the UK, France, Italy and Canada) had similar programmes. In fact, the UK, France and Italy had more rigorous programmes than those of Japan.⁹⁹

It was argued that the real problem was the fact that Japan's exports destroyed key European industries. Peter J. Katzenstein pointed out that Switzerland, the EC's biggest trade partner, maintained a more balanced trade, while the EC's trade relations with Japan was almost always confrontational. He argued that Japan adopted a strategy that aimed at the domination of global markets, while Switzerland searched out profitable market niches for selling high quality, customized products.¹⁰⁰ The fact that not only the EC, but also the majority of Japan's trading partners had a deficit with Japan, led to the assumption that the problem might lie with the Japanese side, not merely with the lack of the EC's competitiveness.¹⁰¹

An even more serious factor for the EC was the fact that Japan had been particularly successful in exporting 'sensitive' products such as motor vehicles and consumer electronic equipment. Japan's increasing import penetration of EC markets and its low level of intra-industry trade had, not surprisingly, led Europeans to suspect Japanese 'dumping' of industrial products on EC markets while at the same time restricting access to their own markets.¹⁰²

Masamichi Hanabusa argued that because Japanese exports were concentrated in terms of sectors and countries, their impact was felt all the more strongly by specific industrial sectors or specific importing countries in Western Europe. In fact, in the 1970s,

⁹⁸ Komiya and Itoh, 'The Political Economy of Japan volume2', P178

⁹⁹ Radha Sinha, 'Japan's options for the 1980s', (London, Croom Helm, 1982), P80-82

¹⁰⁰ Peter J. Katzenstein, 'Japan, Switzerland of the Far East?' in Takashi Inoguchi and Daniel I. Okimoto, 'The Political Economy of Japan – Volume2', (Stanford, Stanford University Press, 1988), P276

¹⁰¹ Wilkinson, 'The Economic and Non-Economic Dimensions of Euro-Japanese Relations', P43

¹⁰² On the industrial strategies of the EC and Japan, see: James W. Dudley, '1992, strategies for the Single Market', (London, Kogan Page Ltd., 1989), P46-49

60-70 per cent of Japan's total export to EC markets was machinery and equipment and about half of these exports consisted of five items, namely TV, radio receivers, tape recorders, automobiles and ships. Hanabusa pointed out that in the case of the exports of the EC member countries and the United States, such concentration was not apparent.¹⁰³

Facing the concentration of Japan's exports, national governments, as well as the Community, were obliged to protect their interests. Exports concentrated in specific industrial sectors strengthen protectionist tendencies in the importing country. According to Hanabusa, it was often one industrial sector that had suddenly been placed under strong competitive pressure from actual or prospective concentrated exports coming from outside Western Europe that spearheaded protectionist campaigns. The active campaign against Japanese exports to EC markets in 1976 was believed to have been closely connected with the depressed state of the shipbuilding industries in EC countries. Fast-expanding Japanese automobile exports to the British market were an important element underlying trade tension between Japan and Britain in 1976-77.

It was evident that this problem of concentration of Japan's exports on certain specific products had contributed significantly to the sour atmosphere concerning Japanese imports in various Western European countries. The resentment of threatened industries was often psychologically aggravated by the fact that many of them felt they had never had a chance to build up a market share in Japan in the 1960s while they were licensing technology to Japanese firms. It was often pointed out that in order to avoid further trade conflicts with Western Europe, it was crucial for Japanese exporters to avoid concentration on specific exports, once the Japanese share of the market for these products had reached a high level. Japan needed to spread the impact of their exports over a greater diversity of products.¹⁰⁴

2-3. Japan's perception of European unfairness – 3.) Japan as a scapegoat

Facing European criticism, most Japanese were convinced that they were made scapegoats for Europe's own internal economic problems.¹⁰⁵ In 1977, the Vice Minister of the Ministry of International Trade and Industry (MITI), Masuda Minoru stated: 'Europeans find it politically convenient to blame Japan for their recession and

¹⁰³ Masamichi Hanabusa, 'Trade problems between Japan and Western Europe', (London, the Royal Institute of International Affairs, 1979), P54-58

¹⁰⁴ Hanabusa, 'Trade problems between Japan and Western Europe', P54-58

¹⁰⁵ Yoshimori, 'Psychological Aspect of Euro-Japanese Trade Frictions: A Japanese Viewpoint', P51

unemployment problems...'¹⁰⁶

In early 1981, the French government said that each Japanese car imported created five unemployed.¹⁰⁷ This comment was followed by the blocking of Japanese cars at Le Harve. However, Japanese cars represented hardly 3% of the total French market, as compared with a share of over 25% for other imported cars. The Japanese car industry concluded that the French accusation was made due to the approaching presidential campaign.

The Japanese pointed out the fact that imports from Japan accounted for only 4.6% of the Community's total imports from the non-EC area, while imports from the Community accounted for 5.6% of Japan's total imports in 1980.¹⁰⁸ Japan argued that the Japanese market was also more open than the European one in terms of tariff rates and quotas. Japan argued that the troublesome trade surplus was not the result of exotic NTBs of a conspiratorial character, but the product of Japanese technology, efficiency and marketing.¹⁰⁹

The struggle of European firms to penetrate the Japanese market resulted in the EC's concept of 'balance of power'. Mounting trade tensions drove the EC since the mid-1980's to seek 'reciprocity' in its trade relationship with Japan, which became 'a guiding EC principle'. In September 1986, the European Commissioner for External Relations, Willy De Clerq made the following comment regarding 'reciprocity' at the GATT Uruguay Round: "The Community feels that many of the present tensions affecting world trade find their origin in the fact that concessions negotiated between the various contracting parties have in reality not resulted in effective reciprocity. It is therefore essential that the Ministerial Declaration should establish the objective of achieving a genuine balance in the benefits accruing to contracting parties from the GATT".¹¹⁰

The EC sought to put 'reciprocity' as 'a condition of access to the newly integrated markets in service, investment, government procurement and other areas not covered by GATT'. The Japanese government reiterated that the Japanese market was the most open in the world and vehemently protested against the EC's concept of

¹⁰⁶ International Herald Tribune, 16 March 1977, cited in Yoshimori, 'Psychological Aspect of Euro-Japanese Trade Frictions: A Japanese Viewpoint', P51

¹⁰⁷ Yoshimori, 'Psychological Aspect of Euro-Japanese Trade Frictions: A Japanese Viewpoint', P52

¹⁰⁸ Masamichi Hanabusa, 'The Trade Dispute: A Japanese View', in L. Tsoukalis and M. White (eds), 'Japan and Western Europe', (London, Frances Pinter Publisher, 1982), P120

¹⁰⁹ Daniels and Drifte, 'Europe and Japan, Changing relationship since 1945', P20

¹¹⁰ On the EC's 'reciprocity', see Nester, 'European Power and The Japanese Challenge', P225, P226

‘reciprocity’. Japan regarded the EC’s call for ‘reciprocity’ as ‘Japan-bashing’.

Japan also disagreed with the EC’s view of Japan’s alleged protectionism. On tariffs, EC tariff protection was higher than in the US and Japan, even including the full implementation of the Uruguay Round commitments. NTBs, such as variable levies in agriculture, VERs in industrial sectors (e.g., those imposed by the Multi Fibre Agreement (MFA) in textiles and clothing or by the EC car agreement in Japan), quotas on imports from centrally planned economies, anti-dumping measures and technical barriers to trade have played a significant role in protecting the EC market.¹¹¹

2-4. European countermeasures - Anti-dumping duties

Japan’s increasing import penetration of EC markets resulted in European suspicion that the Japanese were ‘dumping’ industrial products on EC markets. Usually, manufacturers who sell off products below cost in foreign markets, do so on a very limited scale to shift marginal production or old stock. However, Japanese export strategies differed from such cases. The Japanese perceived that reducing the price in foreign markets was a useful strategy to obtain market shares. Japanese products sold below cost drove European counterparts out of the market. This aggressive Japanese export strategy gave the EC no other alternative than to impose regulations against Japanese dumping.

The EC’s Anti-Dumping Regulation stated that a product was considered to have been dumped if its export price to the Community was less than the ‘normal value’ of the product in its domestic market.¹¹² If the EC came to the conclusion of a dumping act by its trade partners, the ‘dumping margin’, calculated by the price difference, might be imposed on the imported product. In the past, such EC anti-dumping measures were aimed at low-value added goods and semi-finished products from developing countries. In the 1980s, however, the EC’s use of anti-dumping allegations was also directed to high-value added goods, mainly the products imported from Japan. Between 1980 and 1982, there were only 8 cases in which the EC conducted anti-dumping investigations against Japan and other newly industrialised Asian countries. Between 1986 and 1988, the number of cases rose to thirty. The rise of the EC’s anti-dumping investigations reflected Japan’s success in consumer electronics and information technology industries. The EC’s

¹¹¹ Patrick A. Messerlin, ‘Measuring the costs of protection in Europe – European Commercial Policy in the 2000s’, (Washington DC, Institute for International Economics, 2001), P29-37

¹¹² On the EC’s use of anti-dumping see Phillip Oppenheim, ‘Trade Wars – Japan versus the West’, (London, Butler & Tanner Ltd., 1992), P8

anti-dumping investigations affected a wide range of products, such as video recorders, videotapes, electronic typewriters, colour televisions, CD players, photocopiers, computer printers, mobile telephones and microwave ovens. The EC came to use its anti-dumping measures more frequently than any other countries. Between 1981 and 1987, more than 281 investigations were concluded. Although only a quarter of those resulted in imposing anti-dumping duties, half led to ‘the acceptance of special undertakings by which importers agreed to raise their prices’. Besides, many of these cases resulted in VERs.

In addition to the material impact of anti-dumping regulations, the EC began to use it as a threat for seeking confidential import restrictions. In 1989, when the EC claimed that Japanese semiconductor makers had been selling microchips at a loss since the mid-1980s, the EC threatened Japan effectively with anti-dumping duties. Japanese chipmakers yielded to its threat and concluded a price maintenance agreement with the EC.

The unfair nature of the EC’s anti-dumping regulations was pointed out by several independent bodies. The GATT also recognised the misuse of anti-dumping duties by some countries, and urged member countries to follow the GATT anti-dumping code. However, the GATT anti-dumping code was so vague that the EC anti-dumping law could still be used.

Unlike ‘Super 301’ of the United States for cases of unfair competition, the EC did not possess effective countermeasures except its anti-dumping duties. A GATT trade panel in the 1990s ruled against the EC’s use of anti-dumping measures, but the EC regulations were only reluctantly amended, while the EC continued to ‘argue for a retention of significant discretionary powers for contracting parties’.¹¹³

2-5. European countermeasures - Voluntary Export Restraints

Facing the deterioration of their trade imbalance, governments also tend to use VERs and Orderly Marketing Agreements (OMAs). Both measures restrict exports with quotas instead of tariffs. Governments made use of managed trade in an attempt to prevent trade disputes from escalating into full-fledged trade war.¹¹⁴

The tension between Europe and Japan over Japan’s trade surplus led to some jointly agreed trade policies which added elements of ‘managed trade’ to Euro-Japan

¹¹³ Brian Bridges, ‘Hesitant superpower’, (London, Research Institute for the Study of Conflict and Terrorism, 1992), P7

¹¹⁴ For the detail of the use of VERs, see: Nester, ‘European Power and The Japanese Challenge’, P177, 178; see also: Turner, ‘Japan’s Dynamic Efficiency in the Global Market – Trade, investment, and economic growth’, P57

trade relations. Facing the inadequacy of GATT rules, the EC and Japan sought a bilateral settlement of their trade disputes. When the Japanese export surplus became an even more serious problem, Japan accepted a number of VERs with its European trade partners. The subjects of VERs were textiles and colour televisions in the 1960s, steel and shipbuilding in the 1970s, and cars and electronics in the 1980s.¹¹⁵ Japan accepted such VERs in order to avoid more severe European bilateral measures towards Japanese exports and to prevent trade conflicts from developing into a highly political conflict with the EC.

William R. Nester argued that VERs were beneficial to both foreign and domestic firms.¹¹⁶ While domestic firms were protected from a flood of import products, exporters were guaranteed a certain market share. Nester explained Japanese tactics with VERs as follows: Firstly, the Japanese start with sustained dumping attacks in strategic industries, such as automobiles, semiconductors or microelectronics. After a large market share is achieved and the foreign government threatens to retaliate, the Japanese sit down at the table for negotiation. Once VERs are agreed, under the secured market share, Japanese firms can raise the prices in order to compensate their previous losses in the dumping campaign. With its 'trade brinkmanship', Japanese firms enjoyed both market share and profits.

2-6. Japanese countermeasures - Foreign Direct Investment

In the middle of the 1980s, in an attempt to circumvent anti-dumping duties, the Japanese increasingly started to invest in the EC which had so far not received any substantial Japanese investment. Until 1969, the Bank of Japan controlled outward capital flows and only allowed overseas investment in case they were considered essential to Japan's national economy.¹¹⁷ Therefore, Japanese investments were merely orientated towards raw material procurement. In the early 1970s, production in Japan became more expensive: cost of land, labour and raw materials increased. Fuel prices, rising costs for shipping and in addition the upward float of the yen worked against production in Japan. To avoid these costs, and to circumvent tariff or quota barriers, and in order to secure export markets better, Japanese companies hesitantly started manufacturing investment in

¹¹⁵ Stephen Woolcock and Hiroko Yamane, 'RIIA special paper, EC-Japanese trade relations: what are the rules of the game?', (London, the Royal Institute of International Affairs, 1993), P12; On VERs between the EC and Japan on cars, see: Christopher Milner and David Allen, 'The external implications of 1992', in Dennis Swann (ed), 'The Single European Market and Beyond', (London, Routledge, 1992), P167-170

¹¹⁶ Nester, 'European Power and The Japanese Challenge', P177

¹¹⁷ The first paragraph of 2-6 is based on: Albrecht Rothacher, 'Economic Diplomacy between the European Community and Japan 1959-1981', P195

Europe.

During the 1980s, global increase of investment flow occurred among all major economic powers. Above all, Japanese FDI recorded a sevenfold increase during the decade. The massive outflow of Japanese FDI from the mid-1980s was encouraged by the 'high yen'. The strength of the yen enabled Japanese firms to invest more vigorously in the EC whereas the cost of investment had been too high in previous years.¹¹⁸ Without the great appreciation of the yen, Japanese investment into the EC would neither have been possible nor profitable. Although the major area of Japanese FDI was mainly in financial services, the manufacturing sector also attracted increasing FDI from Japanese investors.

In the 1980s, Japanese and Europeans suggested joint research projects and building Japanese factories in Europe in an attempt to mitigate their trade frictions.¹¹⁹ The European governments reacted positively to Japanese FDI and facilitated the inflow of Japanese capital. Instead of leaving decisions to industrialists, some of the European national and local governments became significantly involved in encouraging Japanese FDI to their regions. The positive European reaction was due to the intention of revitalising local economies which were facing an industrial downturn. Although European high labour costs were not encouraging Japanese investment, Japanese factories gradually increased in Europe. In the mid-1980s, Japanese firms began to invest in Europe vigorously to safeguard and expand their gains from their earlier offensive trade approaches.

More substantial Japanese FDI began in 1988. Japanese FDI into the EC steadily increased, recording over 14 billion dollars in Fiscal Year (FY) 1989 from 2 billion dollars in 1985. In FY 1990, Japanese FDI into the EC dropped slightly to 13.3 billion dollars, and more remarkably in the next FY marking 8.8 billion dollars. A series of decreased flows was due to the slowed economic growth in Europe and the 'bubble' of assets increasing from 260 million dollars in FY 1987 to 1.1 billion dollars in FY 1991. The EC's FDI into Japan increased also by around 20 per cent per annum in the late 1980s.¹²⁰

The rapid increase of Japanese FDI into the EC was also driven by business

¹¹⁸ From the second paragraph of 2-6, on Japan's FDI in Europe in the 1980s is based on: Abe, *Japan and the European Union: Domestic Politics and Transnational Relations*, P3, 4, 60, 61; On Japanese investment in the EC, see also: Lodovico Lucioli, 'Japanese investments in the EC', in *European Economic Studies*, 'Euro Cooperation', (The Europartners' Group, 1992), P67-85

¹¹⁹ This paragraph is based on: Daniels and Drifte, 'Europe and Japan, Changing relationship since 1945', P20

¹²⁰ Bridges, 'Hesitant superpower', P5

opportunities and anxiety about the potentially exclusive effects of 'Fortress Europe'. The Japanese tried to entangle Europe with investments which were meant to breach any new tariff walls of 'Fortress Europe' after 1992.¹²¹ In addition, the establishment of the so-called screwdriver assembly plants in the European market circumvented anti-dumping duties.¹²²

The EC's frustration with some aspects of Japan's FDI was enhanced by the fact that European direct investment in Japan remained relatively small in contrast to Japanese FDI in Europe.¹²³ The imbalance in investment paralleled the trade imbalance and raised yet again European criticism of the closed nature of the Japanese market.¹²⁴ From 1951 to 1988, Japan invested 30.164 billion dollars, 16.2 per cent of its total FDI, in the EC, while EC members spent only 3.013 billion dollars, which was 23.6 per cent of its total in Japan.¹²⁵ Thus, Japanese investments reinforced gains made through exports. In March 1990, Japanese investments into the EC reached 42 billion dollars. Japanese investment concentrated in Britain with 37.6 per cent of total FDI in the EC. Holland received 24.0 per cent of Japanese investment, followed by Luxemburg with 12.8 per cent, Germany with 8.2 per cent, France with 6.9 per cent, Spain with 3.7 per cent, and Belgium with 3.2 per cent. 3.6 per cent of Japanese FDI was directed to other member countries. In 1991, Japanese investment concentrated on Britain and France with 187 and 122 factories, respectively. Despite this rapid increase of Japanese investment into the EC, they constituted merely one quarter of the 164 billion dollars of American investment into the EC.

France, which had been most critical of the trade imbalance with Japan, attracted an increasing amount of Japanese FDI because various French regulations encouraged Japanese firms to invest in the country in order to avoid trade barriers. Another reason to diversify FDI across Europe was to mitigate criticism that Japan was using Britain as a Trojan Horse to enter the EC. Japanese investment revitalised many depressed regions in the Community. Hence, it was difficult for the EC to integrate member countries' different opinions into a common policy towards Japanese investment.

Without FDI, Euro-Japan relations may not have improved as much as they have since the beginning of the 1990s. They helped to overcome a European inclination

¹²¹ Nester, 'European Power and The Japanese Challenge', P251

¹²² Ishikawa, 'Japan and the challenge of Europe 1992', P8

¹²³ On European investment in Japan, see Haken Hedstrom, 'Direct EC investments in Japan', in European Economic Studies, 'Euro Cooperation', (Paris, The Europartners' Group, 1992), P87-111

¹²⁴ Abe, Japan and the European Union' P4

¹²⁵ Nester, 'European Power and The Japanese Challenge', P187

towards protectionism and established a favourable climate with local communities.¹²⁶ As a result the Japanese succeeded in entangling trade partners in a network of trade, investment, finance, and technology which also created a degree of political dependence. Under this Japanese strategy, trade partners were not able to retaliate, because retaliation might hurt themselves.¹²⁷

3. Case illustration of 'Euro-Japanese bilateral trade resolution' - VERs on automobiles

Euro-Japanese trade confrontation and subsequent retaliatory countermeasures can be clearly seen in the EC-Japan automobile trade dispute. This case represents many of the above analysed characteristics which aggravated Euro-Japan trade relations. Furthermore, this case shows several factors which hindered Euro-Japan cooperation in a multilateral context.

Japanese car imports had been a sore point in EC-Japan relations since the end of the 1970s, which led to MITI monitoring since 1986 and finally resulted in a EC-Japan agreement in July 1991.¹²⁸ The 1991 agreement called for the liberalisation of the European car market from the end of 1999.¹²⁹ Under the terms of a 1991 'understanding' between the EC and Japan, they agreed informal annual limits on the export of cars and light commercial vehicles to the EC to allow the Community to gradually open its market to full competition.¹³⁰ The automobile dispute symbolised the troubled trade relations between the EC and Japan in the 1980s and exemplified their inclination for a bilateral dispute settlement in the pre-WTO era.

The automobile industry in Europe is the leading industrial sector contributing significantly to employment and the value added in EC manufacturing. By the 1970s, as the global economic prosperity began to falter, trade in cars began to grow. Japan, whose production was rising rapidly, exported a growing proportion of that production, from 30 per cent of its output in 1971 to about 55 per cent by the early 1980s. Most of these exports reached the United States but a small number went to Western Europe.

By the late 1970s, the energy crisis affected the sale of 'gas guzzlers' in the United States. Consumers switched to smaller, more economical cars. The market share of

¹²⁶ Reinhard Drifte, 'Japan's foreign policy in the 1990s: from economic superpower to what power?', (Basingstoke, Macmillan Press, 1996), P107, P108

¹²⁷ Nester, 'European Power and The Japanese Challenge', P178

¹²⁸ Abe, 'Japan and the European Union', P56; On EU-Japan Auto Agreement, see; Desmond Dinan, 'Ever closer Union – an introduction to European Integration', (New York, Lynne Rienner Publishers Inc., 1994), P499-501

¹²⁹ The Financial Times, 2 September 1993

¹³⁰ The Financial Times, 31 August 1993

Japanese-made cars rose from 12 to 21 per cent between 1978 and 1980. The powerful automobile lobby in Europe fought very hard to hang on to its privileged conditions while the manufacturers from Japan tried very hard to penetrate this market further through exports, local production and strategic alliances.

Traditionally, Europe has not had an open market for automobiles. This is partially because many European automotive firms were either government owned or government dominated. With regards to production, European producers do not have the global links of their US and Japanese competitors. Several European firms retreated from global markets while the Japanese firms advanced.¹³¹

3-1. The completion of the Single European Market and the automobile import surge from Japan

At least until 1993 when the SEM was completed, the 'European market' was composed of twelve individual markets. There were national imports restrictions imposed by any of the twelve member countries against goods from outside of the EC. This was possible because EC countries were allowed to keep the GATT-acceptable import restrictions they had established before they joined the Community. The most famous of these was the quota system which allowed Italy to impose a quota on Japanese cars from the 1950s onwards, in retaliation for the import limits that Tokyo - worried about competition from Europe - had first imposed on Italian cars. Spain and Portugal also had Japanese car import quotas which they acquired before they entered the EC. By contrast, France had no legal recourse in Brussels. Instead, it exploited the fact that there were differing technical standards for cars in the Community to keep the Japanese share of the French market low.¹³²

Highly protectionist countries, such as France and Italy, imposed quantitative controls on Japanese car imports. France allocated Japan a quota of 3 per cent of its market (85,000 units in 1991), whereas the Italian government admitted only 13,000 units in 1991, including those distributed via other member states. Britain set a ceiling of 11 per cent for Japan's market share. Countries without indigenous car manufacturers, such as Denmark, Greece and Ireland, assumed a more liberal trade stance, allowing the free inflow of Japanese-made automobiles. In contrast to these two groups, Germany did not have any formal barriers, but managed to keep the market share for Japanese cars at

¹³¹ Fahri M. Unsal and Sandra Richard, 'European automobile markets after 1992, in Michael Landeck, 'International Trade – Regional and Global Issues', (London, The Macmillan Press, 1994), P11-25

¹³² The Financial Times, 5 August 1991

around 15 per cent, much lower than shares in Denmark, Ireland and other non-restricted markets. Some believed a ‘gentlemen’s agreement’ allowed for a stable share of Japanese cars in the German market as well as in Belgium and the Netherlands, although Japanese manufacturers denied this and attributed the relatively smaller Japanese presence in the German market to the strength of German manufacturers.¹³³

There were requests from some member governments to stop non-EC goods coming into their national markets from other EC states. Such national import restrictions offended the single Community market idea, because they interrupted the free circulation of goods. It was the official dogma of the European Commission that such restrictions had to go by January 1, 1993. After that date, there were supposed to be no more customs posts between EC states, and therefore no systematic way of keeping tabs on intra-EC trade. However, some governments, such as Spain, France and Italy would ask Brussels to impose a temporary cordon, if any sensitive sector of their industry was hit by imports from outside the EC.¹³⁴

Since 1987, when the Commission started getting serious about trying to phase out Article 115 protection altogether, there had been a fall-off in government requests to Brussels for permission to close their borders to non-EC goods circulating in the rest of the Community. The Commission had been rejecting a rising percentage of these requests. For example, the EC executive had been steadily enlarging the Italian market share for Japanese cars. Italy's quota allowed the direct import of only 2,800 passenger cars and 800 all-terrain vehicles a year from Japan. But the Commission used the Article 115 procedure to steadily increase the number of Japanese cars coming into Italy from other EC countries – from 10,000 in 1989, 17,000 in 1990 and 22,000 in 1991. In addition, since 1987, Brussels had refused to let Italy put any block on indirect imports of Japanese jeeps.¹³⁵

The SEM forced those countries with protectionist policies to face freer competition from Japanese manufacturers, along with tougher competition from other European manufacturers. At the same time, the Single Market motivated Japanese automobile producers to invest in production facilities within the EC.¹³⁶ The potential profits from the emerging single market lured the Japanese car makers into Europe, an attraction enhanced by their fear of the creation of a ‘Fortress Europe’ that would

¹³³ Abe, ‘Japan and the European Union’, P57

¹³⁴ The Financial Times, 5 August 1991

¹³⁵ The Financial Times, 5 August 1991

¹³⁶ On Japanese automobile industry in the EU, see: R. W. Vickerman, ‘The Single European Market – prospects for economic integration’, (Hemel Hempstead, Harvester Wheatsheaf, 1992), P122-129

discriminate against foreign products and prevent Japan from benefiting from an expected market expansion. As a result of the SEM, national quotas for Japanese car imports became anachronistic, as cars could enter freely via member states not having import restrictions.

However, member states had not yet agreed how to treat these 'transplant' cars under the new Community-wide quota on Japanese car sales to Europe, due to come into force after 1992. In 1991, EC member countries were also divided on how Japanese cars made in the US should be treated, when they came into the European market. In January 1991, the UK claimed that Japanese cars built in the US had to be admitted freely into EC markets, because their place of origin put them outside the existing quotas on Japanese cars. The British government claimed that it would be illegal for the EC to restrict imports of the Ohio-made Honda which the company was due to start selling in Europe in spring 1991.¹³⁷

Behind the British claim was a sharp division between EC member countries on how to deal with transplant cars, as well as a British desire to reinforce the strength of Britain's already firm position in UK-made Nissans. Free access for US-made Hondas would undermine the objections from the French and others to Britain's claim that there should be no European restrictions on UK-made Nissans, thus weakening efforts to limit Japanese access to the single market for European-built cars after 1992. The UK insisted that international rules defining origin as the place of 'last substantial transformation' would apply, making the cars incontrovertibly American. Therefore, under the rules, there would be no legal possibility for the Community to restrict their shipments.

Japan joined the UK to criticise the EC's rigid attitude towards Japanese cars from transplant factories. In July 1991, Japan tried to forge a free-trade alliance with the US, Canada and Britain against continental Europe at the G7 summit in London. The Japanese government was deeply disturbed by moves in the EC to limit access to continental markets of products made by British subsidiaries of Japanese companies.¹³⁸

Japanese car imports and local Japanese car production in Europe remained the most sensitive outstanding problem to be resolved in the creation of the SEM from the end of 1992.¹³⁹ Japanese manufacturers had since 1979 increased their capacity by 7 million units world-wide and were planning to add capacity of another 2 million units a

¹³⁷ The difference between the UK and the EC on Japan's transplant cars, see: *The Financial Times*, 9 January 1991

¹³⁸ *The Financial Times*, 15 July 1991

¹³⁹ For the European automobile markets after 1992 and the challenge of Japanese auto producers, see Unsal and Richard 'Competition in the European Automobile Markets after 1992', in Michael Landeck (ed.), 'International Trade: Regional and Global Issues'

year by the mid-1990s. Lindsey Halstead, chairman of Ford of Europe concluded that the Japanese would be the first beneficiary of a SEM.¹⁴⁰

3-2. EC-Japan agreement on VERs

In an effort to prevent the Euro-Japan relationship from deteriorating, Japan decided to conclude a bilateral agreement with the EC on Japanese car exports. In April 1993, after months of wrangling, Japan agreed with the EC to reduce its car exports by 9.4 per cent on the basis of forecasts that the EC market would decline by 6.5 per cent to around 13 million units in 1993. In 1993, new car sales in Western Europe as a whole were already down 17.2 per cent between January and June and, in its forecast, the European Automobile Manufacturers' Association predicted that demand would be decreasing even further. According to the association, without further reductions, Japan's market share would rise to substantially more than the 13 per cent in 1993, compared with less than 11 per cent in 1992. The European Commission asked the Japanese delegation to reduce the 1.09 million exports envisaged for 1993 in the 'understanding' of governing access to the EC market during the Community's transition to an open market in new cars by 1999.¹⁴¹

Despite the bilateral agreement, the European car market had declined more than expected. In July 1993, the EC asked Japan for a change in its export ceiling, as the market was to show a 'substantial deviation' from forecasts. The Japanese government claimed that, while Japan recognised the fall in demand in the EC car market, revising a formally agreed quota after only three months would undermine the credibility of the bilateral agreement. Robert Verrue, chief EC delegate to the talks, admitted that due to the bilateral agreement in April, Japanese car exports to the Community had fallen sharply in the April-June period by about 30 per cent. However, the decline of new car sales in the EC had proved much steeper than expected.

In August 1993, European Commission officials flew to Tokyo to persuade Japan to improve on the commitment made in April and to discuss the scale of further cuts.¹⁴² A few weeks later, the Commission and Tokyo reached an agreement on cutting Japanese shipments of cars and light commercial vehicles to the EC by 17.6 per cent, to 980,000 in 1993, compared with an earlier limit of 1.089 million set in April.¹⁴³ This meant a cut of

¹⁴⁰ The Financial Times, 5 March 1991

¹⁴¹ Japan's agreement with the EC on Japan's car exports, see: The Financial Times, 16 July 1993

¹⁴² The Financial Times, 31 August 1993

¹⁴³ The April accord was based on a forecast that EC demand would fall by 6.5 per cent in

Japanese car sales in the EC by about 100,000 in 1993, while the market would shrink by a total of at least 2.4 million.

While welcoming the effort by both sides to adjust their market forecasts, European carmakers remained dissatisfied with the agreement regarding the level of the cut. Jacques Calvet, chairman of Peugeot Citroen most vehemently criticised the agreement as 'unacceptable and suicidal for the European car industry.'¹⁴⁴ Other European car industry leaders also attacked the new car trade deal between the EC and Japan, saying it was unacceptable for Tokyo to boost its market share during the EC sector's worst decline since the Second World War. The board of directors of the European Automobile Manufacturers Association claimed that the deal meant the possible increase of Japan's EC market share (forecasted to be at least 12.5 per cent in 1993, up from 11.3 per cent in 1992), and that it would run counter to a 1991 EC-Japan agreement limiting Japanese car exports to the EC.¹⁴⁵

Responding to European dissatisfaction, Japan decided to make a further concession. In March 1994, Japan's MITI agreed to restrict the rise in car exports to the EU to 0.4 per cent in 1994, reducing Japanese car industry hopes for an export-led recovery.¹⁴⁶ However in the first eight months of 1994, new car sales in the EU rose by an estimated 5.9 per cent to 7.911 million according to the figures from the European Automobile Manufacturers Association. Japan started to seek a bigger quota for car and light commercial vehicle exports to the EU because this higher than expected demand in Europe.¹⁴⁷ Following the sharp fluctuations of European car market growth, the EU and Japan held a number of meetings to adjust their agreement made in April 1993 to the actual situation.

3-3. European concerns about US unilateral pressure on Japan

While the EU and Japan were conducting successive rounds of negotiations on the Japanese car export quota, Japan was under strong US pressure to set numerical targets for purchases of US vehicle parts by Japanese carmakers.¹⁴⁸ The US was aiming at

1993, while the new deal was based on a fall of 15.9 per cent. / The Financial Times, 8 September 1993

¹⁴⁴ The Financial Times, 2 September 1993

¹⁴⁵ The Financial Times, 8 September 1993

¹⁴⁶ The Financial Times, 21 March 1994

¹⁴⁷ The Financial Times, 22 September 1994

¹⁴⁸ US pressure resulted, on 24 March 1994, in the Japan Automobile Manufacturers' Association's announcement of a voluntary plan to increase access to the Japanese market for foreign vehicles and parts. It was offered as an alternative to US requests for government-led action to open the country's vehicle market. / The Financial Times, 25

opening Japan's market to foreign cars and car parts.¹⁴⁹ The US Administration had committed itself to reducing the budget deficit and increasing national savings and US competitiveness, while Japan promised to achieve a significant reduction in its trade surplus with the US, as well as a significant increase in import penetration.¹⁵⁰ Europeans expressed clear dissatisfaction with US pressure on Japan for a result-oriented approach. Concerns expressed by the EU gave ground to Japan for rejecting US demands for numerical targets. Moreover, MITI was attempting to shift domestic public opinion against these targets. This Japanese strategy was effective in drumming up criticism of the US policy, not only in Japan but also overseas.¹⁵¹

Frustrated with Japan's resistance, the US threatened to impose trade sanctions in retaliation for failure to meet US demands to open Japan's markets for cars and car imports. The Japanese government claimed that its market was already open and threatened to retaliate by taking the US to the WTO over the issue. While rebuffing US demands leading to managed-trade, Japan offered the US a number of measures aimed at encouraging car imports into Japanese market. In May 1995, Japan proposed to raise the amount of tax benefits available to wholesalers and retailers of imported manufactured goods, including cars, and to the sales subsidiaries of foreign manufacturers. US and Japanese carmakers which re-imported their vehicles were expected to benefit from the higher level of tax benefits. However, Europeans were not satisfied, as the proposed changes in Japan's import promotion tax schemes were unlikely to encourage European car sales to Japan. Europeans were calling on the Japanese government to amend its proposed measure to benefit all car importers 'without discrimination'.¹⁵²

In 1997, the weaker yen pushed Japan's worldwide vehicle exports up. In the first six months of 1997, Japanese car exports to the US showed their strongest growth spurt since 1980, prompting fears of renewed trade friction. According to the Japan Automobile Manufacturers' Association, vehicle shipments to the European Union increased by 23.3 per cent, while exports to the US rose by 22.3 per cent.¹⁵³ In 1998, Japanese exports to Europe surged by 32 per cent in the 11 months to November, according to the figures from Japan Automobile Manufacturers Association. Anthony Millington, representative of

March 1994

¹⁴⁹ On American protectionism and its effort on opening Japanese market, see: Nakakita, 'Trade and capital liberalisation policies in postwar Japan', in Teranishi and Kosai, 'Japanese experience of economic reforms', P358-360

¹⁵⁰ The Financial Times, 27 January 1994

¹⁵¹ The Financial Times, 13 April 1995

¹⁵² The strong criticism came from the European Automobile Manufacturers Association (ACEA). / The Financial Times, 11 May 1995

¹⁵³ The Financial Times, 29 July 1997

ACEA, the European industry association in Tokyo, claimed that; 'This is the clearest indication the Japanese are exporting their way out of their troubles at the expense of somebody else.'¹⁵⁴

Despite their own criticism of Japan's trade policy, the Europeans also stood against US unilateral trade policy. While the US maintained its pressure on Japan for a bilateral dispute settlement with the threat of unilateral trade sanctions such as Super 301, Europeans remained sympathetic to Japan's resistance against strong US pressure. European carmakers drew a clear line between US insistence that the Japanese market was closed to foreign competitors, and the demand for numerical targets. One of the European carmakers defended the Japanese government by saying that US products did not meet the rapidly shifting demands of Japanese consumers, and the issue was not something the government could mandate.¹⁵⁵ European brands were better established in the Japanese market after the European car manufacturers had spent much time and money on developing brand identity in the Japanese market, which the Americans failed to do.¹⁵⁶ The Financial Times also criticised that the US had to accept the obligation to reduce its unilateralism. The paper claimed that the US was pretending that disputes with Japan were somehow special and should be handled outside the GATT rules, although the US did not have the sole right to decide when and how individual service sectors should be opened up.¹⁵⁷

3-4. Japanese Foreign Direct Investment into the European market

While criticising US unilateralism, the EU also directed criticism against Japanese FDI. In 1998 when the Japanese car import surge into the European market had been attracting European criticism, a bigger threat to European carmakers were the car factory transplants which the Japanese were building in the region. Earlier in January 1998, Toyota unveiled plans to invest 150 million pounds (241.5 million dollars) and expand engine production in the UK. The extra investment followed its decision to invest 4 billion FFfr. (656.8 million dollars) in a second European car plant in northern France to produce 150,000 new vehicles a year. Announcement of the new factory created a stir among European carmakers, concerned about rising overcapacity in their home market.

¹⁵⁴ The Financial Times, 15 January 1998

¹⁵⁵ The comment came from David Blume, Vice-president of Rover Japan. / The Financial Times, 1 August 1997

¹⁵⁶ The comment was made by Anthony Millington, director-general of the Tokyo office of the European Automobile Manufacturers' Association. / The Financial Times, 1 August 1997

¹⁵⁷ The Financial Times, 21 May 1991

This Toyota expansion was the most conspicuous move by Japan's leading carmaker to step up its presence in the region. Other Japanese carmakers, such as Nissan and Honda, were also expanding their facilities in the UK, while Mitsubishi Motors had a joint venture with Volvo in the Netherlands aiming to increase output in Europe.¹⁵⁸

Already by the late 1980s, the rush of Japanese car factories into the EC area provoked criticism among the Europeans. European carmakers derided Japanese car factories as 'screwdriver plants' because these factories mostly used imported Japanese parts. In 1988, the French government, supported by domestic manufacturers, objected vehemently to accepting such cars as European-made and sought to include them in the Japanese import quota. Although Japanese manufacturers managed to raise local content gradually, European criticism on Japanese transplant intensified in 1990s.

The investments reflected a resolve among Japanese carmakers to win a greater slice of the European market. For Japanese carmakers, expansion in Europe became important at this point in their global business strategy, mainly due to the mature market at home. The share of Japanese sales in the US had reached a politically sensitive level of about 24 per cent. Raising exports to expand sales became increasingly risky. The situation raised the importance of Europe as an export market to soak up excess production in Japan and maintain domestic capacity utilisation.¹⁵⁹ One of the reasons why Japan's car industry accepted the small increase in exports without complaint was the fact that their overall EU sales would be little affected as a result of the build-up in European-based production.¹⁶⁰ Japanese FDI in Europe significantly increased as a result of the 1992 programme. The sharp rise of the yen against the US dollar after 1985 also facilitated Japanese FDI in Europe. This accounted for the general trend of Japanese manufacturers transferring production abroad.

The Euro-Japan automobile trade dispute represents the essence of Euro-Japanese trade confrontation, mutual misunderstanding and subsequent retaliatory countermeasures which aggravated Euro-Japan trade relations. At the same time, this case revealed several factors which hindered Euro-Japan cooperation in a multilateral context. These factors which became obstacles to Euro-Japan cooperation are going to be analysed in the next section.

¹⁵⁸ Nissan planned to raise Nissan's unit sales in Europe from 450,000 in 1997 to 550,000 in 1998, 10 per cent increase. Honda targeted sales of 300,000 by the year 2000, a rise of 36 per cent.

¹⁵⁹ The Financial Times, 15 January 1998

¹⁶⁰ The Financial Times, 21 March 1994

4. Conclusions of Part 1 - Obstacles to Euro-Japan cooperation

The brief overview of Euro-Japan trade relations and the case illustration of their automobile dispute suggests that Euro-Japan relations both in the bilateral and multilateral context had been rather confrontational until the establishment of the WTO in 1995. As the multilateral level is of greater relevance in this thesis, I will in the following sections distill from the previous analysis the factors and circumstances which long prevented Euro-Japan cooperation and conflict settlement within the GATT.

4-1. The EU-Japan trade imbalance and Japan's import structure

The main culprit for the EC/EU-Japan trade imbalance was considered by the EC/EU to be Japan's import structure (See 2.2.). It was pointed out that Europe and Japan were basically exporting the same range of manufactured products. However, Japan only imported roughly half as many manufactures as the EC/EU.¹⁶¹ By the 1970s, Japan imported only a relatively small amount of industrial goods. The imports of manufactured goods had never reached more than 30 per cent of total imports. The amount even fell to 20 per cent in 1975 and 22 per cent in 1980 because of the high oil price. Japan's low import rate was due to the fact that Japan used import quotas and tariffs to restrict the imports of the products, which could be produced domestically in Japan. These measures were meant to protect newly established Japanese domestic industries from foreign competitors.¹⁶² The Japanese import structure was in striking contrast to the United States and most European countries which imported both absolutely and relatively a far greater amount of manufactured goods.

Endymion Wilkinson suggests structural circumstances. Both Europe and Japan are poorly endowed with natural resources.¹⁶³ As a result, their trade was restricted almost entirely to industrial products. 'Japan's trade with other major regions of the world: North and South America, Australia, the Middle East, China and South-East Asia – all of which include raw materials as an important element of their exports to Japan'.¹⁶⁴ Therefore, their trade relations with Japan were more complementary than Europe's. This fact forced Europe and Japan to stand in direct competition with each other. The Euro-Japan trade imbalance was therefore partly caused by the Japanese import structure which was

¹⁶¹ Reinhard Drifte, 'Euro-Japanese Relations: Realities and Prospects', in Daniels and Drifte (eds), 'Europe and Japan, Changing relationship since 1945', P94, P95

¹⁶² Komiya and Itoh (eds), 'The Political Economy of Japan volume2', P177

¹⁶³ Wilkinson, 'The Economic and Non-Economic Dimensions of Euro-Japanese Relations', P33, 43, 44

¹⁶⁴ Wilkinson, 'The Economic and Non-Economic Dimensions of Euro-Japanese Relations', P33

affected by 'geographical setting and historical pattern of external trade and industrial and economic policies followed by its government'.¹⁶⁵

4-2. Different perceptions of rules of the games

Behind the confrontation between Europe and Japan was also a difference in the perception of the 'rules of the games'. Japan's trade surplus towards Europe remained consistent, while the Europeans were struggling to increase exports into the Japanese market. European frustration caused by this trade imbalance resulted in a European perception of Japan's 'unfairness'. An important element of European (and also American) criticism towards Japan was, above all, the view that the trade imbalance with Japan was the consequence of having different rules of the game. This European perception was seen in a comment made by the then French Prime Minister, Edith Cresson: 'Japan is an adversary who does not respect the rules of the game and whose overwhelming desire is to conquer the world.... Japanese investments are not like others. They destroy jobs. Those who can't see that must be blind.... We hear all too often that we must open up our markets, which really means first to the Japanese.'¹⁶⁶

European criticism focused first on Japanese export strategies. Europeans suspected that Japanese manufacturers were 'dumping' their products onto the European market. Japan insisted that it was common and legitimate business practice for companies investing in new products to sell them at prices below costs in the initial marketing phase. Europeans claimed that such practices were unacceptable and refused a compromise under which, if an exporter persisted with low prices into a second or third year, dumping might be considered to have occurred and anti-dumping duties could be charged retroactively.

Along with Japan's export strategy, Europeans criticised Japan for its closed market. Japan's various standards and approval systems for safety and consumer protection, importing procedures, and government procurement policies were considered by foreigners as discriminatory against imports. It was exactly in these areas where foreign complaints about Japan's NTBs concentrated, although it was difficult to define what exactly were these NTBs and to judge whether Japanese domestic standards and approval system were barriers to imports.¹⁶⁷

¹⁶⁵ Wilkinson, 'The Economic and Non-Economic Dimensions of Euro-Japanese Relations', P43, 44

¹⁶⁶ The Economist, 'Edith the First' 18 May 1991, quoted in: Mason and Turay, 'Japan, NAFTA and Europe', P60

¹⁶⁷ Komiya and Itoh, 'The Political Economy of Japan volume2', P208

Japan disclosed its perception of the rules of the game in a June 1992 report of the Committee on Unfair Trade Practices and Measures which was working under the auspices of MITI. The Report ranked the EC second in its list of Japan's trade partners which allegedly used unfair trade practices, highlighting notably the European use of anti-dumping as unfair.

In addition Europe and Japan condemned each other for the illegal use of market protection measures. The fact was that Europe and Japan applied different types of market protection measures as forms of state interventionism.¹⁶⁸ Japan depended on structural or regulatory obstacles, while the European system was more dependent on statutory protection such as anti-dumping. Both kinds of obstacles continued to fuel the Euro-Japan trade confrontation despite multilateral reforms achieved through successive GATT trade negotiating rounds. Although GATT succeeded in the reduction of tariffs, the removal of NTBs and the tightening of anti-dumping rules were left untouched. It was generally accepted in 1986 that the anti-dumping code needed to be tightened up and that controversial national laws against dumping should be changed to comply with a credible international set of rules.¹⁶⁹

4-3. Limitations of the GATT rules and lack of a coherent European foreign trade policy

One of the factors which aggravated Euro-Japan frictions was the fact that the GATT did not provide clear international trade rules. From 1948 to 1994, GATT provided the rules for much of world trade and contributed to the high growth rates in international commerce.¹⁷⁰ GATT had succeeded in reducing tariff rates to a significantly low level, but the credibility and effectiveness of the GATT became challenged by the governments' attempts to circumvent GATT rules and principles.

In the 1970s and early 1980s, when the United States and Europe suffered from a series of economic recessions, governments devised other forms of protection in order to protect domestic economic sectors. Facing high unemployment and constant factory closures, European and American governments started to seek the solution in bilateral market sharing agreements with competitors. In agriculture, governments embarked on increasing their subsidies to protect the agricultural sector.

¹⁶⁸ Robert Gilpin, 'Where does Japan fit in?', in Kathleen Newland (ed), 'The International Relations of Japan', (London, Millennium Publishing, 1990), P7

¹⁶⁹ The Financial Times, 18 December 1991

¹⁷⁰ The WTO, 'Trading into the future: the introduction to the WTO – Roots from Havana to Marrakesh', (http://www.wto.org/english/thewto_e/whatis_e/tif_e/fact4_e.htm)

The erosion of the GATT system became visible and frequent in the 1970s.¹⁷¹ Bilateral trade in certain products between exporters such as Japan, Korea, Taiwan, and Hong Kong and their importers such as the European countries and the United States became restricted by formal or informal agreements, such as VERs, the Trigger Price Mechanism (TPM), the Basic Price System (BPS), and OMAs. For example, the regulation of VERs was clearly beyond the reach of GATT rules, because both the importing country and the exporting country did not complain to the GATT.¹⁷²

The overuse of such bilateral solutions demonstrated that the GATT system had been designed to deal only with barriers to trade at national borders, but it had not been able to neutralize the alleged advantages gained from national variations in culture, industrial organization, and macroeconomic policy.¹⁷³ Such defects of the GATT system obviously delayed the solution of EC-Japan trade frictions. In fact, European allegations of the closed nature of the Japanese market, represented by the Keiretsu System, the complex distribution system or NTBs were not covered by the GATT rules.¹⁷⁴

In addition to the limitations of the GATT system, one can point out that the lack of a coherent European foreign trade policy towards Japan caused a delay in the establishment of a sound Euro-Japan partnership. The incomplete process of European integration resulted in the lack of a coherent European foreign trade policy which also showed in the apparent absence of a common Community strategy towards Japan's trade policy.¹⁷⁵ The Community was preoccupied with dismantling internal trade barriers, assimilating new members, and negotiating successive GATT rounds. As a result, the Community remained divided between two sides: protectionist, tough-line states (such as France, Italy and Spain) and free trade, soft-line states (such as Germany, Denmark and Britain). In fact, in 1972, the Community failed to negotiate an overall commercial treaty with Japan which would have provided safeguards in the event of a sudden increase of Japanese products.¹⁷⁶ Japanese companies also tried to avoid EC anti-dumping duties on imported excavators, and import duties on Japanese electronic typewriters. To some extent, Japanese companies managed to minimise the import duties and tax penalties they had to bear.¹⁷⁷

¹⁷¹ Komiya, 'The Japanese Economy: Trade Industry, and Government', P52, 53

¹⁷² Charles W. L. Hill, 'International Business: competing in the global marketplace - third edition', (Boston, Irwin/McGraw-Hill, 1999), P5

¹⁷³ Ishikawa, 'Japan and the challenge of Europe 1992', P12

¹⁷⁴ Drifte, 'Japan's foreign policy in the 1990s', P44

¹⁷⁵ Daniels and Drifte, 'Europe and Japan, Changing relationship since 1945', P103

¹⁷⁶ Daniels and Drifte, 'Europe and Japan, Changing relationship since 1945', P20

¹⁷⁷ Glenn D. Hook, Julie Gilson, Christopher W. Hughes and Hugo Dobson, 'Japan's International Relations – Politics, economics and security', (London, Routledge, 2001),

In its foreign relations, Japan made good use of bilateral solutions. William R. Nester argues that Japan's strategy was to 'divide and conquer'. According to Nester, Japan took full advantage of the EC's divisions.¹⁷⁸ Japan always avoided dealing with the EC as an international organization. Instead, Japan played off one member state against the other.¹⁷⁹ Japanese exporters could always overcome French or Italian protection by sneaking in additional imports via the backdoors of more open countries such as Germany or Britain. This Japanese strategy had clearly exacerbated European disarray and divisions. The lack of a coherent European foreign trade policy was thus 'a significant obstacle to the development of Euro-Japanese political relations'.¹⁸⁰

Part 2. Europe and Japan in the GATT/WTO framework

5. Europe and Japan in the GATT

As we have seen previously, Euro-Japan relations in the GATT started on the wrong foot due to European opposition to Japan's GATT membership and its maintenance of discriminatory measures against Japan. Besides, their bilateral trade conflicts hindered their establishment of cooperative trade relations. Despite these facts, as two of the world's biggest economies, both Europe and Japan had contributed to the successful conclusion of trade rounds in the GATT.¹⁸¹ In fact, their relations in the GATT rounds were generally seen as cooperative in the sense that the rounds were successfully concluded achieving a number of objectives through their mutual cooperation, along with their cooperation with other GATT contracting members. Their common objective throughout the GATT rounds was to expand world trade by removing tariffs and facilitating the world trade environment. However, from round to round, there were differences in the degree of their commitment, as well as different objectives. This section, therefore, traces the development of Euro-Japan commitment in the GATT trade rounds and investigates their relationship in the multilateral trade negotiations.

5-1. The Kennedy Round (1964-1967)

P270, 271

¹⁷⁸ Nester, 'European Power and The Japanese Challenge', P224, 251

¹⁷⁹ Japanese policy has been assisted by the varied and inconsistent restrictions imposed by various Community countries and the mutual differences among European states. See: Gordon Daniels, 'Japan in the post-war world – Between Europe and the United States', in Daniels and Drifte, 'Europe and Japan, Changing relationship since 1945', P20

¹⁸⁰ Daniels and Drifte, 'Europe and Japan, Changing relationship since 1945', P103

¹⁸¹ For a brief history of Euro-Japan relations until the Uruguay Round, see: Marie Conte-Helm, 'The Japanese and Europe', (London, The Athlone Press Ltd., 1996), P23-46

In the 1960s, the GATT was holding the Kennedy Round (1964-67) and dealt with further tariff reductions and an anti-dumping agreement. Reflecting the booming world trade, further tariff reductions were enacted efficiently. The tariff rates of the major industrial countries, especially in terms of tariffs on manufactured goods, were lowered substantially. This time period was also seen as the beginning of the EC and Japan's positive involvement in lowering tariffs on manufactured goods.¹⁸²

The Kennedy Round was conducted under the strong leadership of the US and the EC. Japan, on the other hand, did not seem enthusiastic about an active participation in the trade round and industry, above all its manufacturing industry, was clinging to protectionism. Japan's economic policy was not in accordance with the GATT principles and the reduction of tariff rates was seen as threatening to industries which did not have enough international competitiveness, rather than as an opportunity to expand exports. These concerns prompted Japan to move towards strengthening tariff protection in agricultural and manufacturing industries. As a result of governmental protection and support, Japanese manufacturing industries had improved their international competitiveness in the 1960s. With the improved competitiveness of manufacturing industries, Japan obviously gained a lot of benefits from the successful conclusion of the Kennedy Round with its resultant lowered tariff rates. These positive outcomes of the multilateral trade rounds made Japan realize the utility of mutual tariff reductions. Japan was conscious that when it reduced tariff rates simultaneously with its trading partners, the result was an expansion of world trade as a whole, providing even more export opportunities. This recognition changed Japan's passive and protectionist trade stance after the Kennedy Round.¹⁸³

Although the Kennedy Round further liberalised world trade by increasing the share of trade benefiting from tariff cuts, the EC and a number of other trading nations obtained justifiable exemptions from tariff-cutting agreements and these exceptions led to bilateralism replacing multilateralism. The short and long-term agreements for textiles and clothing were cases in point. The EC started to use quotas to curtail its imports of textiles and clothing from more efficient producers, notably in developing countries.

Another important feature of the Kennedy Round for both the EC and Japan was the introduction of agreed procedures for anti-dumping legislation. While provisions made in the Kennedy Round did not prove to be very significant, the fact that anti-

¹⁸² Michael J. Trebilcock and Robert Howse, 'The regulation of international trade – Second Edition', (London, Routledge, 1995), P53

¹⁸³ The development of GATT/WTO trade rounds is best described in the WTO information paper, 'Trading into the future' 2nd edition revised in April 1999

dumping issues were on the world trade agenda was indicative of changes taking place in commercial policy. Issues other than tariffs became significant. For the first time world trade negotiators also identified agriculture and NTBs as relevant items for future world trade negotiations.¹⁸⁴

5-2. The Tokyo Round (1973-1979)

In the 1970s, the GATT negotiations of lowering tariff rates entered a new phase. The Tokyo Round (1973-79) started to attempt to tackle trade barriers which did not take the form of tariffs, and which were therefore called NTBs. Such trade impediments were now considered obstacles to trade facilitation and were to be removed to achieve further trade liberalization. Besides, the GATT system itself was under consideration for reforms during the Tokyo Round.

The Tokyo Round brought about the biggest multilateral trade negotiations after the Kennedy Round and its participants increased to 99 countries. Trade negotiations were largely dominated by the US, the EC and Japan, as they together accounted for about 50 per cent of world trade at that time. Because of the nature of the GATT, which was originally a 'rich men's club,' the US and European countries had more than their fair share of political and economic power, as was also the case in other international organisations such as the IMF and the World Bank. Although the US and the EC attempted to extract concessions from each other, much of the protracted negotiations degenerated into 'Japan-bashing' by the US and the EC.¹⁸⁵

Unlike in the Kennedy Round, Japan displayed leadership throughout this ambitious trade round. It was said that Japan and the US were the most active participants. Japan played a leading role in advancing negotiations by offering tariff reductions for a large number of items. Furthermore, Japan ratified all the agreements, being at the forefront of other participating countries. Japan's leadership made the GATT face NTBs for the first time. This active Japanese participation reflected the Japanese perception that the multilateral free-trade regime should be strengthened and preserved in order to reflect Japanese trade interests more effectively. Active participation was also crucial for Japan to establish its international position in the multilateral trade regime.

The EC, Japan, the US and many of the major industrial economies faced economic difficulties after the first oil crisis. Rising concerns about severe inflation, overcoming balance-of-payments difficulties, and the deepest depression since the

¹⁸⁴ Heidensohn, 'Europe and World Trade', P157

¹⁸⁵ Sinha, 'Japan's Options for the 1980s', P98, 99

Second World War made participating countries take a more protectionist stance through the trade negotiations. This economic turmoil all over the world was obviously one of the greatest reasons why the Tokyo Round took a long time from announcement to conclusion. Besides, during the round, there were certain issues, on which member countries were not able to reach an agreement, such as agriculture.¹⁸⁶

There was a large dose of bilateralism, especially in the tariff negotiations. The principal negotiations were inevitably between the US and the EC. Along with US-EC bilateral negotiations, both the US and EC conducted bilateral tariff talks with Japan. While the EC drew a significant volume of concessions from Japan, the Japanese argued that they could not go any further given the EC's quantitative restrictions (mostly Voluntary Export Restraints) on Japanese goods.¹⁸⁷ During the Tokyo Round, Japan agreed to reduce its standard tariffs on industrial products by nearly 50 per cent, the EC by 27 per cent and the US by 31 per cent.

The Tokyo Round also attempted to create formulating rules of commercial policy on a global level. The negotiations were about commercial policy in general rather than merely aspects of tariffs. The Tokyo Round made some progress towards tackling problems caused by the use of NTBs. Codes were introduced to cover some areas affected by NTBs. These included a code preventing governments from discriminating against external producers via appropriately devised product standards; a code requiring governments to offer domestic foreign firms equal chances in being awarded contracts (public procurement); a code prohibiting direct export subsidies; and a code permitting the use of CVDs to deal with unfair competition arising from, for example, dumping. Negotiators failed, however, to make informal safeguard actions like VERs subject to Article XIX (which was designed to offer trading nations 'emergency protection' in cases of fair but unduly strong import competition). Thus, VERs which had grown in importance continued to be informal safeguard actions, normally negotiated bilaterally and outside the GATT rules.¹⁸⁸

The package also contained eight international codes on NTBs and three arrangements on trade in agricultural products. The MITI welcomed the signing of the

¹⁸⁶ The issues were: safeguards, certain problems of developing countries, further liberalization of trade in agricultural products, dispute-settlement procedures, trade in services, trade-related international investment, problems related to high-technology industries, illegal products and the adoption of a unified international classification system.

¹⁸⁷ L. Alan Winters, 'The Road to Uruguay Round' in *The Economic Journal*, Vol. 100, No. 403, (Royal Economic Society, Dec. 1990), P1288-1303

¹⁸⁸ Heidensohn, 'Europe and World Trade', P157, 158

agreement and hoped that this would inhibit growing protectionist moves in the EC and the US. During the course of negotiations, the EC showed a considerable degree of scepticism about Japanese motives. This was reflected in the EC's withdrawal, just before the signing of the agreement, of their initial offer to remove import restrictions on 33 of a total of 64 Japanese imports. The EC cited the following as the main reasons for such action:

- 1.) The Community's dissatisfaction with Japanese offers for liberalising trade, particularly its tariff-cuts, which were considered to be inadequate;
- 2.) Dissatisfaction with measures to be taken by Japan in response to the removal of EC discrimination against Japanese imports; and
- 3.) The failure of the new trade package to incorporate a code on safeguards (emergency import controls).

At the time, safeguards were often used by the EC and the US either against Japan or developing countries. Therefore, there was an attempt to revise Article 19 of the GATT rules which permitted the imposition of safeguards. The EC argued that they had the right to impose quantitative restrictions first and to consult the exporting countries later. Japan initially had serious reservations on the revision of Article 19, but later showed some willingness to accommodate. The Japanese government thought that such a provision might ultimately be an advantage to Japan in keeping out competitive imports from developing countries, such as Korea, Hong Kong, etc.

The Tokyo Round proceeded by overcoming severe economic difficulties. Both the EC and Japan worked together toward a successful conclusion of a number of agreements and preserving the multilateral trading system. An important area which was largely left untouched by the agreements reached at the conclusion of the round was trade in agricultural produce. Agriculture continued to be a highly protected sector with the protection giving rise to trade frictions among industrialised countries.¹⁸⁹ In general, the Tokyo Round was fruitful for both the EC and Japan. However, from Japan's point of view, the initiation of the Multilateral Trade Negotiations during the Tokyo Round had still not reduced the pressure from the US and the EC on Japan.¹⁹⁰

5-3. The Uruguay Round (1986-1994)

¹⁸⁹ Heidensohn, 'Europe and World Trade', P157, 158

¹⁹⁰ Sinha, 'Japan's Options for the 1980s', P98-102

Even by the time the Tokyo Round had been completed, it was clear that the General Agreement needed to be extended and revised in order to incorporate key aspects of trade such as NTBs, bilateral quantitative restrictions, emergency protection and agriculture. When a preparatory committee was established in November 1985, it was far from clear at that stage whether, for example, agriculture, services, intellectual property rights and foreign investment would be included in the global package of negotiations. The Uruguay Round was finally launched in September 1986 in Punta Del Este and it was agreed to define trade flows more broadly by including areas such as services, intellectual property rights, foreign investment and agriculture.¹⁹¹

All the main world traders pursued very specific objectives. They were prepared to make concessions in some areas, if they could make progress in others. The EU was keen on seeing restrictions removed on intellectual property rights, foreign investment and services. The EU also favoured further tariff reductions; in return it appeared to be willing to reduce protectionism in sectors such as clothing and textiles and, to a lesser extent, agriculture. The EU also seemed prepared to resort less to safeguard measures, CVDs and anti-dumping duties.

On agriculture, the US and the EU bridged their differences in agriculture in a deal known as the 'Blair House Accord'. Great progress was also made on other subjects. By July 1993, the US, EU, Japan and Canada, often called 'Quad', made significant progress on tariff reductions and market access. It required one more year for all of the relevant issues to be resolved. In April 1994, negotiations on market access for goods and services were concluded.

On the whole, the Uruguay Round was a long but productive trade round for both the EU and Japan. As a result of the round, tariffs on industrial products were to be reduced by more than one-third. Also, in agriculture, subsidies were to be substantially reduced. Furthermore, fair trade and market access rules were to cover a wide range of services, and protection of patents, copyrights and intellectual property were to be included into the GATT rules. Finally, in order to implement the achieved agreements, the WTO was established. Despite the success of the Uruguay Round, the agricultural issue prolonged the discussion among member countries. While the EU and Japan stubbornly resisted a drastic liberalization of agricultural trade, the US and other food exporting countries urged the EU and Japan to soften their protectionist stance.

5-4. Strengthening international trade rules

¹⁹¹ Heidensohn, 'Europe and World Trade', P158

The Kennedy, Tokyo and Uruguay rounds were characterised as a remarkable success. While EC/EU-Japan bilateral trade relations appeared to be rather confrontational, they both had been committed to the successful conclusion of GATT rounds. Multilateral Trade Negotiations in the GATT gave the EC/EU and Japan a new arena where they could work on common objectives which were significant for the entire world trade and, therefore also beneficial for both the EC/EU and Japan. As a result of the Uruguay Round, member countries agreed to establish a more powerful organisation to deal with a wide range of trade matters. The creation of the WTO was reflected by the strong desire of the EC/EU and Japan to have a stronger trade institution. Thus, this section of the chapter, examines what factors contributed to the current EU-Japan cooperation in the new multilateral context.

Both the EC/EU and Japan supported the creation of the WTO, as they wanted stronger multilateral trade rules, in order to solve trade disputes with their trade partners, as well as disputes between themselves. The Japanese perceived that the EC/EU was failing to live up to the agreed multilateral rules of the GATT, and drifting more and more towards the use of results-based trade policies. Japanese policy makers thought that when facing Japanese competition, the EC/EU effectively refused to be bound by the GATT rules. Japan argued that the EC/EU strayed from the GATT rules and found a unilateral interpretation of the rules to fit its own interests. Faced with growing import competition in sectors such as automobile, the EC/EU was seen as having rejected safeguard provisions provided in the GATT and having forced Japanese exporters to accept selective VERs. Japan also perceived that Europeans relied on unilateral interpretation of the anti-dumping rule or rules of origin as a means of reducing imports.

In terms of trade imbalances, Japan argued that European companies did not really try to penetrate the Japanese market but merely used the perceived closed nature of the Japanese market as an excuse. Japan was also concerned about the growing inclination of the EC/EU and US to use 'results-based' trade policies in areas of trade not yet covered by multilateral rules.¹⁹²

Europeans, on the other hand, perceived that the trade imbalance with Japan was due to its differences in business practices or domestic economic structures. Europeans argued that the GATT rules were not inadequate as they had little or no effect on improving the access to the Japanese market. In this sense, Europeans viewed that the GATT rules were in favour of Japan. For this reason, Europeans wanted tougher multilateral rules especially where they were internationally competitive. For instance, in

¹⁹² Woolcock and Yamane, 'RIIA special paper, EC-Japanese trade relations', P2, 5, 6, 7

the banking or pharmaceutical sector, European industries were determined to establish stronger multilateral rules in General Agreement on Trade in Services (GATS).

Albeit with different expectations, the conclusion of the Uruguay Round and the creation of the WTO were appreciated by both the EU and Japan. Tougher multilateral trade rules and an enhanced DSB were equally important to both the EU and Japan. They expected that the establishment of the WTO would provide the means of ensuring effective implementation of the rules.

5-4-1. European perspective

Although Europe considerably depended on the use of bilateral measures in order to cope with the Japanese trade surplus, there was also a strong desire on their part to strengthen multilateral trade rules. The greatest benefit was obviously the capability to restrain US unilateralist measure, such as Super 301.

Europe was conscious that it had less influence on Japanese trade policy compared with the US. Europe was concerned about US unilateral practices towards Japan, because the outcome of US-Japan trade would significantly affect Euro-Japan trade. For instance, if the US limited imports from Japan, Japanese products would surge into the European market. Therefore, Europeans disliked US-Japan bilateral solutions of trade issues. The EC/EU had always been concerned that Japan might surrender to US bilateralism. Since the final US stance on trade issues had such an impact on both Europe and Japan, policy makers in Europe and Japan came to recognize the importance of establishing a more politically and economically independent position from the US. In other words, through the consolidation of the GATT system, they appeared to start attempting to minimize the influence of the US-designed trade environment.

The EC/EU and the US vied for the most predominant role in setting and reshaping the rules of trade.¹⁹³ There was therefore a strong leadership competition between them. Europe also had an interest in a stronger rule-oriented multilateral trade discipline in order to contain US unilateral or bilateral trade remedies. In order to restrain US bilateral solutions, GATT principles such as non-discrimination status or MFN status were desirable for the EC/EU. Hence, during the Uruguay Round, the EC/EU shifted its stance from supporting bilaterally negotiated solutions to ones embodying more multilateral adjudication and started to support stronger GATT discipline.¹⁹⁴

¹⁹³ Takashi Inoguchi, 'Japan's Foreign Policy in an Era of Global Change', (Pinter, 1993), P85

¹⁹⁴ Woolcock and Yamane, 'RIIA special paper, EC-Japanese trade relations: what are the rules of the game?', P12

5-4-2. Japanese perspective

Japan was often accused of being a free rider in the international trade arena. Such a view comes from the perception of some observers that Japan was a willing beneficiary of the free-trade system when it came to taking advantage of the open markets of other countries. However, it was a reluctant participant in terms of opening its own domestic market to foreign competition.¹⁹⁵

Facing such accusation, Japan realised that full compliance with the GATT rules helped to counter result-based trade policies used by Europe or the US. Through acting as a model GATT member, Japan could refute other countries' use of GATT-incompatible measures aimed at countering Japanese advantages related to its political economic system which were outside of GATT regulations.¹⁹⁶ Within the GATT rules, Japan could also concentrate on improving its competitiveness. It was argued that Japanese willingness to comply with the GATT might be a result of the Japanese experience as the passive partner in an international trade system whereby the rules were set by the United States and Europe.¹⁹⁷

However, in the 1990s, Japan became increasingly vocal on US and EC/EU trade measures in conjunction with GATT trade rules. Noboru Hatakeyama, who took over in July 1991 as Japan's top international trade negotiator, announced to bring a new toughness to Japan's approach to trade issues. Hatakeyama claimed that until the 1990s, the Japanese stance had been to stress the importance of getting a solution regardless of the rules of the GATT and other international organisations, but Japan would no longer buy peace at any price in settling trade conflicts with the US, the EU and other trading partners.

His comment implied that Japan could in future challenge the trade practices of other countries more often, instead of always being on the defensive. Hatakeyama clearly stated that: 'Japan has been the recipient of rules which have been made by others. From now on we would like to contribute to the formulation of new rules.'¹⁹⁸ Hatakeyama, however, accepted some exceptions. He claimed that Japan had to be sensitive to the needs of other countries. According to him, VER agreements were a time-tested way of

¹⁹⁵ T. J. Pempel, 'From exporter to investor: Japanese economic policy', in Gerald L. Curtis (ed), 'Japan's foreign policy after the Cold War – Coping with change', (New York, M. E. Sharpe, 1993), P122

¹⁹⁶ Drifte, 'Japan's foreign policy in the 1990s', P89

¹⁹⁷ Woolcock and Yamane, 'RIIA special paper, EC-Japanese trade relations: what are the rules of the game?', P33

¹⁹⁸ The Financial Times, 21 August 1991

giving such protection without having to resort to protectionist legislation, therefore exceptions could be admitted as long as the fundamental principles of free trade came first.¹⁹⁹

The change of Japan's trade policy promoted Japan's commitment to the WTO, as well as its relationship with the EU in an attempt to restrain US unilateral trade measures.

6. Case illustration of 'Euro-Japanese multilateral trade conflict resolution' – The Liquor Tax case

The liquor tax dispute is a demonstration of the EC/EU and Japan resorting to a GATT-based (and later WTO-based) multilateral approach to trade conflict resolution, in contrast to the earlier automobile dispute which was addressed bilaterally. Moreover, it exemplifies the development from the inchoate conflict resolution mechanism in the GATT system to the more complex one of the WTO. As such the liquor tax dispute provides an ideal case illustration of the transition of EC/EU-Japan relationships in the GATT to the WTO.

The liquor tax system in Japan was a long-standing trade issue between the EC/EU and Japan, despite the marginal economic size of the liquor industry. Japanese domestic shochu (spirits made of rice, wheat or sweet potatoes) makers are dispersed all over Japan, and this trade dispute therefore attracted tremendous attention in Japan.²⁰⁰ Besides, taxation itself is a matter of domestic politics and sovereignty. However, the GATT regime already explicitly prohibited discriminatory taxation on imported products. Consequently, this trade dispute was not just a bilateral issue but also had a legitimate place in the multilateral trade regime.

Since the early 1980s the issue of alcoholic beverage exports had constantly been on the EC's agenda at regular official meetings between the EC and Japan. Japan was one of the major importers of Scotch whisky, along with other kinds of alcoholic beverages. With the economic downturn in the mid-1980s, Scotch whisky sales decreased considerably while sales of shochu grew rapidly. Although the proportion of European alcoholic beverage exports to Japan was not spectacular, the issue obtained enough importance to be a test case to assess how willing Japan was to cooperate with the EC.

6-1. The EC's challenge in the GATT to Japan's liquor taxation system

¹⁹⁹ The Financial Times, 21 August 1991

²⁰⁰ Naohisa Murakami, 'WTO Sekai boueki no yukue to Nihon no sentaku', P82

The Japanese liquor tax system was extremely complicated and the EC began to highlight it since the mid-1980s as a trade problem because it was perceived as discriminating foreign alcohol beverages. Most western countries tax alcoholic drinks according to their strength. The Japanese, however, had traditionally imposed duty on alcohol largely according to price and quality rather than strength.²⁰¹ The tax amount and rate, for example, depended on liquor type, alcohol percentage and beverage grade based on 'quality', this last item an uncommon one among industrialised countries. While there was a grading system for traditional beverages such as sake (rice wine) and shochu, there were no objective criteria to decide whether a certain product was of 'quality' or not. Therefore, a poor person's drink, such as crude sake or the rougher shochu was taxed less heavily than the rich person's premium grade whisky, or higher-quality sake.

Atsuko Abe explained that Japanese liquor tax law was based on four grounds: 1.) it promised substantial income for the government; 2.) it would deter people from excessive drinking; 3.) the social cost caused by excessive drinking would be paid by drinkers, not by the general taxpayer; and 4.) those who could afford to drink liquor were assumed to be financially capable of paying the tax because consuming liquor is not a daily necessity for the most part. Legal studies on taxation emphasised this last point as the main reason for imposing a liquor tax, although the Ministry of Finance (MOF) found the first point crucial since the ministry's priority lies in retaining tax revenue.

Japanese liquor taxation was based on an over-complex categorisation and grading of liquor, based on criteria such as alcohol percentage, raw materials and, in the case of distilled liquors, manufacturing methods. The complexity of the system was under serious criticism even in domestic circles. The system remained mostly unchanged from 1962 to 1989 despite criticism that the liquor tax system caused structural problems since it did not reflect economic and social change over time.

The EC considered such tax differentiation as discriminatory against European imports because it resulted in a higher tax on products with higher alcohol content such as whisky. There were three grades depending on alcohol percentage, providing a basis for different tax rates. Such a grading system levied a higher tax on products with higher alcohol content. On the other hand, shochu was considered a drink with a lower alcohol content so it had a much lower tax rate compared with other spirits.

In April 1986, the MOF and Commission officials began several rounds of negotiations. In July 1986, after a series of unsuccessful discussions, the Commission formally requested consultations with Japan under GATT Article XXII:1 on Japanese

²⁰¹ Oppenheim, 'Trade Wars – Japan versus the West', P49-51

customs duties, taxes and labelling practices on imported wine and alcoholic beverages. Two GATT consultations in August and September failed to produce satisfactory results.

Finally, Japan tried to settle the dispute on a bilateral basis, but failed so when the EC ultimately brought the issue to the GATT in late October. The EC claimed that Japan must reform its alcohol taxation system because it discriminated against imported products; it demanded Japan to lower the existing high tax rate on wine and whisky; and re-regulate the indication of origin rules more strictly, especially for wine. Tokyo maintained that shochu, traditionally a cheap spirit, was not comparable with imported whisky or brandy, which were luxury items. However, this argument was rejected by the 1987 GATT panel.²⁰²

Finally in November 1988, the GATT Council adopted the panel report that confirmed the Japanese defeat. The GATT notification forced the MOF to implement a drastic change in the liquor tax as part of the general taxation reform planned in 1988. In December 1988, the GATT General Assembly demanded that Japan implement the reformed taxation law during the FY 1988. Japan, however, had to face immense difficulty in persuading Japanese interest groups within the time allowed, while trying to win a compromise from the EC to postpone the reform. Domestic whisky makers fiercely opposed abolishing the grading system, fearing that it would seriously damage second-grade whisky sales.²⁰³

6-2. Japan's non-compliance with the GATT ruling

In April 1989, a new taxation system was launched, including a new liquor taxation. The Japanese government made some changes to its liquor taxation system by, for example, removing the difference in taxes between local and imported liquor. While welcoming the 1989 reforms, the Community insisted that it did not believe that the GATT panel's decision was fully implemented. In comparing tax rates as a percentage of retail prices, whisky was still considerably higher than shochu. There was growing EC criticism of Japan over the discriminatory taxation system which still remained despite the 1987 GATT panel ruling. Criticism that Japan failed to comply with GATT recommendations came at a sensitive time for Japan, which was moving towards a more GATT-oriented trade policy. The Japanese government, under growing pressure over trade from the US and EC, said it would refer to the GATT when trying to resolve thorny

²⁰² The Financial Times, 28 September 1995

²⁰³ Abe, 'Japan and the European Union', P106, 107

issues.²⁰⁴

At the annual ministerial meeting between the EC and Japan in January 1993 and meetings of senior officials in April 1993, the Commission suggested resubmitting the case to the GATT, unless Japan fulfilled its 1987 GATT ruling obligations by 1994. The EC became increasingly impatient after waiting five years for Japan to remove the last tax areas placing imports at a disadvantage.²⁰⁵

The excuse given by the Japanese had been that since shochu was made in rural areas it would be politically risky for the governing Liberal Democratic Party (LDP) to introduce steps that might hurt producers. The Japanese government also claimed that it would be just as difficult to reduce the tax on other spirits at a time when its revenues had suffered in the economic downturn.²⁰⁶ Japan also argued that shochu was part of the national culture because it was made by small rural distilleries across Japan, while Scotch makers insisted that more than half of all shochu was made by six large industrial groups involved in other activities such as pharmaceuticals.²⁰⁷

Kojiro Shiojiri, director of First International Economic Affairs, Ministry of Foreign Affairs (MOFA) in Japan, wrote to the Financial Times on 20 April 1993 that the new tax rates applied equally to domestic and foreign products, and therefore neither penalised foreign products nor broke GATT rules. He emphasised that the tax differentials were narrowed considerably as a result of the 1989 revision of Japan's Liquor Tax Law, which was undertaken in accordance with the recommendation of the 1987 GATT panel ruling.²⁰⁸

Refuting this statement, Ronald Brown, chairman of the European Business Council Liquor Committee, and Tim Jackson, President of the EC Association of Spirit Producers, sent a joint letter to the Financial Times. They claimed that European producers felt the Japanese government had not taken advantage of an opportunity for implementation of full liquor tax harmonisation as provided in the 1987 GATT council ruling. They pointed out that the GATT ruling was accepted by Japan and partially implemented in 1989, and full compliance was again formally requested in 1992 by the Commission. They questioned why Japan continued to protect the ailing domestic spirits

²⁰⁴ The Financial Times, 10 March 1993

²⁰⁵ EC dissatisfaction was expressed by the Richard Needham, UK Minister of State for Trade, in a meeting with Ichiro Aisawa, Parliamentary Vice-minister at the Ministry of International Trade and Industry. Needham added the UK's voice to growing EC criticism of Japan over the discriminatory taxation system. / The Financial Times, 10 March 1993

²⁰⁶ The Financial Times, 24 March 1993

²⁰⁷ The Financial Times, 18 May 1994

²⁰⁸ The Financial Times, 20 April 1993

industry at a time when its trade surplus continued to soar, and they emphasized that the MOFA and the Japanese government should face up to international GATT obligations.²⁰⁹

The gulf remained between the EC and Japan on whether Japan's liquor tax system had been sufficiently altered to be in compliance with the 1987 GATT ruling. In the meantime, under the auspices of the Uruguay Round trade talks, the Quad members (Japan, the US, the EC/EU and Canada) agreed, in July 1993, to abolish tariff barriers on imported spirits. Among the Quad members, Japan would be most affected, as high import duties were levied on its imports. However, Europeans had seen Japan's liquor tax system as a much bigger impediment to whisky exports than import duties, and continued trying hard to persuade Japan to change it.²¹⁰

In June and September 1993, the Commission raised the issue at the GATT. Facing consistent European pressure, the Japanese government decided to raise the tax rate on shochu, further narrowing the tax difference with whisky. However, as this still did not satisfy the EU, in May 1994, the liquor tax was reviewed again, resulting in a further rise of the tax on shochu.

The successive tax rise on shochu was still not enough to calm European criticism down. In November 1994, during two days of talks with Japanese officials in Tokyo, a delegation of liquor producers from the EU, the US and Sweden urged the Japanese government to use its 1995/96 budget to harmonise its liquor taxes. The Shochu's share of the distilled drinks market rose from 61 per cent in 1989 to 74 per cent in 1994. Imported drinks accounted for only 8 per cent of the Japanese market, compared with more than 30 per cent in most other developed countries.²¹¹

6-3. EU-Japan dispute settlement in the WTO

In the following year, Europe stepped up the pressure on the Japanese government. During a round of EU-Japan high-level consultations in Tokyo in February 1995, Horst Krenzler, EU Director General for external economic relations, strongly rebuked Japan's failure to comply with a GATT ruling on Tokyo's liquor tax system, threatening to call for the newly established WTO dispute settlement process.²¹² In April, Sir Leon Brittan, EU Chief Trade Negotiator also claimed that the EU would take the case

²⁰⁹ The Financial Times, 27 April 1993

²¹⁰ The number was given by the Scotch Whisky Association, which was leading the European delegation to Tokyo / The Financial Times, 8 July 1993

²¹¹ The Financial Times, 21 November 1994

²¹² The Financial Times, 11 February 1995

to the WTO.²¹³ Under tougher WTO dispute procedures, panel rulings had to be adopted and implemented unless there was a consensus against them or a successful appeal. The WTO, unlike GATT, could impose sanctions in the event of non-compliance.

Masayoshi Takemura, the Japanese Finance Minister, expressed regret about the EU's decision to bring the case to the WTO,²¹⁴ but the Japanese MOFA maintained, at least on the surface, their belief that the 1989 and 1994 reforms were sufficient.²¹⁵ In June 1995, the EU officially brought the case to the WTO. The MOF agreed to bilateral negotiations within the WTO dispute settlement mechanism, although it was unwilling to make any immediate change in tax rates.

These bilateral talks started on the 20 June 1995 but they did not resolve the issue, which led to the setting up an independent dispute panel. At the end of January 1996, the first open hearing for the panel was held. It became the first disputes panel settlement sought by the EU under the WTO. Six months later, the panel ruled against Japan by concluding that the difference in tax rates between shochu and whisky was against WTO rules.²¹⁶

The Japanese Finance Ministry had to choose between raising taxes on shochu to bring them in line with higher taxes on other spirits such as whisky, lowering the tax on whisky and the others to the level of taxes on shochu, or adjusting the tax rate on all spirits to somewhere in between.²¹⁷ Japan faced a tough decision, because lowering the tax rate on whisky to the level of that on shochu ran counter to the Finance Ministry's policy to increase tax revenues and improve the country's finances,²¹⁸ while increasing the tax rate on shochu would cause an outcry from domestic shochu makers. The domestic shochu industry lobbied the Japanese government intensely, claiming that shochu was a people's drink that could not be compared to more expensive alcoholic beverages such as whisky. The industry claimed that a bottle of shochu could be bought for about half the price of the cheapest bottle of whisky.²¹⁹ Despite the outcry from domestic shochu makers, the Japanese government decided to lower the tax on whisky by 58 per cent from October in 1997 and raised the tax on shochu, by between 1.6 and 2.4 times over five years. The decision of the Japanese government finally ended years of friction with Europeans over

²¹³ The Financial Times, 4 April 1995

²¹⁴ The Financial Times, 6 June 1995

²¹⁵ Abe, 'Japan and the European Union', P114

²¹⁶ The Financial Times, 12 August 1996

²¹⁷ The Financial Times, 8 October 1996

²¹⁸ Alcohol taxes netted about 2,000 billion yen (18 billion dollars) for the Treasury. / The Financial Times, 8 October 1996

²¹⁹ The Financial Times, 8 October 1996

Japan's liquor tax system.²²⁰

The liquor tax dispute illustrates EC/EU-Japan resort to a GATT/WTO multilateral resolution. This makes a striking contrast to their bilateral resolution in the automobile dispute which was discussed in the Part 1 of this chapter. Besides, this case shows importance of the role of the WTO to settle the trade disputes between the EC/EU and Japan. Therefore, despite the marginal economic size of the liquor industry, the analysis of the Euro-Japan liquor tax dispute is very meaningful.

Conclusions

This chapter investigated the relationship between the EU and Japan before the establishment of the WTO. The investigation in the chapter highlighted two prominent features; 1.) various domestic social forces have a significant impact on countries' trade policy. 2.) the lack of common international trade rules aggravated the trade relationship between Europe and Japan.

On the first point, the automobile case symbolised the troubled trade relations between the EC and Japan in the 1980s and exemplified their inclination for a bilateral dispute settlement in the pre-WTO era. Automotive industry is the leading industrial sector for both the EC and Japan and contribute to employment. Thus, the powerful automobile lobby in Europe fought very hard to hang on to its privileged conditions, while the manufactures from Japan tried very hard to penetrate this market further through exports. Thus, governments and carmakers often had a close tie. European automotive firms were either government owned or government dominated. Under the circumstances, relationship between government officials and automobile lobbies had a common ground for a cooperation.

On the second point, one of the factors which aggravated Euro-Japan frictions was the fact that the GATT did not provide clear international trade rules. While governments successfully lowered tariff rates through GATT rounds, they attempted to circumvent GATT rules and principles. As the cause of continuous trade conflicts, both sides concluded that different business practices or domestic economic structures had a significant effect on trade policies of each side. After the establishment of the WTO, as we have seen in liquor tax system, when the other side's trade practices are conceived as being incompatible with international trade rules, legal action is taken in accordance with WTO rules.

The above two points will be the main objectives of following chapters. As for the

²²⁰ The Financial Times, 17 December 1996

first point, the impact of various social forces on trade policies of the EU and Japan, we will investigate closely in the next chapter on agricultural trade. As for the second point, the role of the WTO and its dispute settlement system, we will investigate in the fourth chapter on steel trade issue.

Chapter 3
EU-Japan relationship on agricultural trade

Introduction

In this chapter, we will investigate the EU-Japan relationship in one of the most contentious issues in the WTO, agricultural trade. First, the chapter commences with the individual agricultural policy of the EU and Japan and highlighten the difference between them. Then we closely look at, how they have developed a positive relationship between them, by focusing on the role of institutions and various social forces.

Since agreements in the WTO trade negotiations directly affect them, farm lobbies or other stakeholders are actively involved to achieve their goals through their government.

Among various shapes of relationship between the EU and Japan, we particularly investigate the transnational connection between social forces within the EU and Japan, and their joint strategy, 'multifunctionality' of agriculture.

The chapter shows that the state is not a single unified actor in the international trade, but their policy is significantly influenced by the demand from various domestic actors within them.

1. Agricultural trade

While the GATT had been successful in reducing tariffs on manufactured goods, trade liberalisation talks essentially by-passed agriculture. It is more difficult to deal with agriculture on an international level, because the agricultural sector is a very entrenched domestic interest. Governments take a special custodial interest in the agricultural sector and intervene both in production and trade.²²¹ Domestic farming sectors receive a variety of subsidies from governments to promote rural development and modernise farming techniques. At the same time, competitive imports are often severely restricted by high tariffs and quotas.²²² Thus, from the beginning, agriculture was excluded from key GATT provisions. The first four rounds of GATT-based multilateral trade negotiations virtually ignored agricultural issues and the next three eventually had to drop them (See table 1).²²³

²²¹ Jon Woronoff argues that one would be mistaken to assume that 'industrial policy' could only be applied to manufacturing industries. However, the broadest most lavish exercise actually took place in agriculture. See: Jon Woronoff, 'Japanese Targeting', (Basingstoke, The Macmillan Press Ltd, 1992), P109-111

²²² Jimmye S. Hillman & Robert A. Rothenberg, 'Agricultural Trade and Protection in Japan', (Aldershot, Trade Policy Research Centre, Gower Publishing Company, 1988), P73-75

²²³ For a detailed history of agricultural trade in the GATT, see Dale E. Hathaway, 'Agriculture and the GATT: Rewriting the rules', (Washington DC, Institute for International Economics, 1987)

Many regional and other preferential trade agreements also largely excluded farm products in order to allow contracting parties some leeway. Even the Uruguay Round accepted a high and asymmetric level of tariffs and subsidies just in order to put them under at least some control.²²⁴

Table-1: The GATT trade rounds

Year	Place / name	Subjects covered	Countries
1947	Geneva	Tariffs	23
1949	Annecy	Tariffs	13
1951	Torquay	Tariffs	38
1956	Geneva	Tariffs	26
1960-1961	Geneva (Dillon Round)	Tariffs	26
1964-1967	Geneva (Kennedy Round)	Tariffs and anti-dumping measures	62
1973-1979	Geneva (Tokyo Round)	Tariffs, non-tariff measures, “framework” agreements	102
1986-1994	Geneva (Uruguay Round)	Tariffs, non-tariff measures, rules, services, intellectual property, dispute settlement, textiles, agriculture , creation of the WTO, etc.	123

Source: the WTO, 1999

Although average MFN tariffs in the Quad (Canada, the EU, Japan and the US) have fallen to about 5 per cent, tariffs for some agricultural commodities are over 100 per cent. Such tariff peaks are often concentrated on products that are of export interest in developing countries and include major agricultural staple food products, such as sugar, cereals and fish, tobacco, vegetables and fruit.²²⁵ The Uruguay Round resulted in significant tariff rises, as tariffication of NTBs in agriculture led to the imposition of high duties on agricultural products which had previously been constrained by import quota.²²⁶

The countries favouring farm liberalisation are led by countries including Australia, Brazil, South Africa and New Zealand which are grouped together in the so-called ‘Cairns Group’ of 15 agricultural fair trading nations, together with many

²²⁴ The Economist, Dec. 7th 2002, ‘Unleashing the trade winds’

²²⁵ On the issue of tariff peaks after the Uruguay Round and analysis of market access situation in global agricultural markets, see J. Fernandez, ‘Tariff peaks for agricultural and food products: their incidence and alternatives for their removal’, Journal of Agricultural Economics, Vol. 53, Number 1, (Agricultural Economics Society March 2002), P14-24

²²⁶ Bernard Hoekman, ‘Economic development and the WTO after Doha’, Discussion Paper No.3374, (Centre for Economic Policy Research, May 2002), P9

developing nations. Most of these countries either abandoned means of supporting their agricultural sectors, or never had them, such as in some developing countries.

At the other end of the scale sit Japan, Norway and Switzerland whose farmers are among the most protected in the world in terms of subsidies per head. But not far behind is the EU, which is a major agricultural trader. The Cairns Group and the US are interested in opening the EU market.

Table-2 lists top agricultural exporters and importers. As we can see in this table, Japan's food imports account for around 10 per cent of the world market. Japan is the world's third largest food importer. With a 10 per cent share of the agricultural imports, Japan's agricultural policy attracts the attention of its trade partners. Table-3 shows Japan's trade commodities and their proportions. Agricultural products amounted to 12.1 per cent of Japan's imports in 2001. As the percentage of agricultural imports in trade commodities is high, agricultural trade policy has great significance for Japan.

Table-2: Top agricultural exporters and importers, 2001

	Value \$bn	Share in world %		Value \$bn	Share in world %
Exporters			Importers		
EU members	215.53	39.0	EU members	235.51	39.7
EU to rest of world	57.81	10.6	EU from rest of world	79.78	13.5
United States	70.02	12.8	United States	68.40	11.5
Canada	33.57	6.1	Japan	56.94	9.6
Brazil	18.43	3.4	China	20.12	3.4
China	16.63	3.0	Canada	15.55	2.6
Australia	16.56	3.0	Mexico	12.79	2.2
Argentina	12.20	2.2	Korea, Rep.of	12.50	2.1
Thailand	12.06	2.2	Russian Fed.	11.40	1.9
Mexico	9.07	1.7	Hong Kong, China	11.06	-

Source: WTO, International Trade Statistics 2002

Table-3: Japan's Global Trade by Commodity - 2000

Imports	%	Exports	%
Machinery and Equipment	31.6	Electrical Machinery	26.5
Mineral Fuels	20.3	Machinery other than Electrical	21.5
Foodstuff	12.1	Transport Equipment	21.0
Chemicals	7.0	Chemicals	7.4
Others	28.9	Others	23.7

Source: Japan Tariff Association

The EU's stance on agricultural trade is conditioned by its status as one of the biggest agricultural exporters as well as importers. The EU's agricultural exports account for around 10 per cent of the world's exports, and its imports stand at around 14 per cent of the world's imports. The EU is the world's largest farm trader both in imports and exports (see Table-2). In 2000, EU imports of agricultural products totalled 58,200 million dollars which was 5.7 per cent of the total imports of all products (see Table-2). At the same time, the EU's export of agricultural products reached 58,000 million dollars (6.2 per cent of the total exports of all products). Only the US exported more farm products in 2000.²²⁷

Table-4: The EU's Global Trade by Commodity – 1999

Imports	%	Exports	%
Machinery and Vehicles	39.1	Machinery and Vehicles	46.3
Other manufactured articles	28.8	Other manufactured articles	27.1
Energy	10.0	Chemicals	14.0
Chemical	7.6	Food	5.8
Others	14.5	Others	6.8

Source: European Commission

The trade stance of the United States is somewhere between that of the Cairns Group and that of the EU and Japan.²²⁸ After the Uruguay Round, the US deregulated

²²⁷ European Commission Directorate-General for Agriculture, 'EU agriculture and the WTO', P6, (<http://europa.eu.int/comm/agriculture/external/wto/newround/full.pdf>)

²²⁸ About the trade stances of the US, the EC and Japan, and their commitments to GATT trade rounds, see Dale E. Hathaway, 'Agriculture and the GATT: Rewriting the

much of its agricultural sector and made some progress on decoupling compensatory payments to farmers from production. This decoupling meant that farmers were no longer given incentives to produce for non-existent markets. However, the US established about 15 million dollars worth of ‘emergency packages’ for farmers in 1999. Moreover, the US still grants to some of its farm sectors, including dairy and sugar, huge protection.²²⁹

There are substantial threats to agricultural trade as there are considerable gaps between the big agricultural traders. Food exporters such as the US and Cairns Group²³⁰ insist that the Japanese government’s justification for continued support for rice production and the European Union’s push to maintain a wide range of agricultural support mechanisms continues to distort world production and trade.²³¹ The EU and Japan’s agricultural policies are criticised for imposing considerable costs on consumers and taxpayers in countries where agriculture is highly supported.²³²

2. Japan’s agricultural trade policy

2-1. The closed nature of Japan’s agricultural market

Japan’s trade policy for agricultural products is notorious for its protectionism and is much criticised.²³³ While the average tariff on manufactured goods is 4 per cent, tariffs on agricultural goods are around 40 per cent. Although the Japanese agricultural sector accounts for just 2.1 per cent of the total GDP, the agricultural budget reaches about 10 per cent of the annual budget. Japanese farming products are well protected from foreign competition by the government’s huge farm support.²³⁴

Besides, Japan has used non-tariff measures to assist its agricultural sector. Non-tariff measures include administered domestic prices, and strict health and quarantine regulations.²³⁵ Such measures often upset its trade partners and attract a storm of criticism

rules’, P72-89

²²⁹ Financial Times, 29 November 1999

²³⁰ The Cairns Group was named after the venue of its first meeting in 1986. The Group includes Argentina, Australia, Brazil, Canada, Chile, Colombia, Fiji, Indonesia, Malaysia, New Zealand, Paraguay, Philippines, South Africa, Thailand and Uruguay. It represents 550 million people and around 20 per cent of global agricultural exports.

²³¹ On EU’s Agricultural market, see: Willem Molle, ‘The economics of European integration – third edition’, (Aldershot, Ashgate Publishing Ltd., 1997), P245-269

²³² F. Freeman & I. Roberts, ‘Multifunctionality, a pretext for protection?’, (ABARE Current issues, August 1999)

²³³ For an introduction to the issue of Japan’s agricultural protectionism, see Hillman and Rothenberg, ‘Agricultural Trade and Protection in Japan’, P6-36

²³⁴ On agricultural sector in Japan, its history and protectionist nature of Japanese agriculture, see: Toshihiko Kawagoe, ‘Deregulation and Protectionism in Japanese Agriculture’, in Juro Teranishi and Yutaka Kosai, ‘Japanese experience of economic reforms’, (Chippenham, Antony Rowe Ltd, 1993), P366-391

²³⁵ Heidensohn, ‘Europe and World Trade’, P114

from food exporting countries. Some of Japan's trade partners say that Japan's stubborn resistance to open its agricultural market casts doubt on Japan's officially proactive commitment to the multilateral trade liberalisation talks on industrial products.

High rates of agricultural protection are a relatively recent phenomenon in Japan. The average NRP²³⁶ (nominal rate of protection) of Japan in 1955 was 18 per cent, only about half the EC average of 35 per cent. It rose rapidly, reaching EC level in 1960 and Swiss level in 1965. The average NRPs increased from 1955 to 1970 not only in Japan but also in industrial countries in general. Real world prices of agricultural products declined during this period as a result of rising productivity and accumulated surpluses of grains in the United States and other major exporters.²³⁷

Unlike the EC, where domestic agricultural protection displaced imports, Japan's agricultural imports continued to rise despite the rapid growth of agricultural protection. In 1990, the total cost for general farm income support was estimated at over 3 per cent of GDP to support 3 million households. Support for agriculture in Japan exceeded that in the EC and the US, at around 90 billion dollars or 3 per cent of GDP. Support in Japan was about twice the level of that in the US at 1.6 per cent of GDP (or around 76 billion dollars). In the EC, the total subsidy for agriculture amounted to approximately 120 billion dollars or just over 2 and half per cent of GDP.²³⁸

Farm income subsidies amounted to 50 per cent in the EC/EU, 53 per cent in the US but about 230 per cent in Japan. Disposable income spent on food support amounted to 20 per cent in the EU, 17 per cent in the US but about 30 per cent in Japan. Clearly the level of agricultural support in Japan was higher than in the EC/EU and much higher than in the US in the 1990s.²³⁹

In November 2000, the WTO urged Japan to reform its agricultural policy, saying that it showed 'potentially important competition distortions'. Japan's average tariff on agricultural imports remains high and agricultural subsidies for farmers is well above the average of OECD member countries. The WTO pointed out the especially varied and complex Japanese tariff quota system, which covers over 200 agricultural

²³⁶ The average nominal rate of protection (NRP) is calculated by subtracting the value of agricultural output in domestic prices and dividing the difference by the value of agricultural output in international prices. / Fred. H. Sanderson (ed), 'Agricultural Protectionism in the industrialised world', (Washington DC, Resource for the Future, 1990), P184

²³⁷ Sanderson (ed), 'Agricultural Protectionism in the industrialised world', P185,

²³⁸ Alister McFarquhar, 'World Trade Pressures – Reform of EU Common Agricultural Policy and Food and Agricultural Policy in Japan', (Cambridge, University of Cambridge, 1996), P20

²³⁹ McFarquhar, 'World Trade Pressures – Reform of EU Common Agricultural Policy and Food and Agricultural Policy in Japan', P20

products. Weight-based custom duties, which are mainly applied to agricultural imports, range between 40.1 per cent and 983.7 per cent, if converted into ordinary value-based duties. This figure is far above Japan's average tariff rate of 6.5 per cent for 2000.²⁴⁰

2-2. Japan's rice regime and declining rice consumption

Japan's rice regime exemplifies Japan's rigid agricultural trade policy, which lacks flexibility to allow concessions in trade liberalisation talks on agriculture.²⁴¹ Alister McFarquhar asserts that support for farming in Japan is largely a matter of rice policy. The rice price was ten times the average world price in 1986 and by the early 1990s the rice mountain peaked at around 1.5 million tonnes against a consumption of about 10 million tonnes. Farm income support for rice was double the value of production in 1990.²⁴²

Rice has long been the staple food of Japan. Income from rice farming is about 25 per cent of Japan's total agricultural income, and most Japanese farmers derive part of their income from rice, either by growing rice or contracting paddy land for rice growing.²⁴³ Because of the high costs of producing rice in Japan, rice prices there are among the highest in the world. Rice exporting countries see marketing potential in Japan and have sought to persuade it to change the policies that insulate it from world rice markets.²⁴⁴ Among the rice exporting countries, the US is the most vociferous protester against Japanese agricultural policy. The US reiterated its dissatisfaction with access to Japan's rice market. The US also hinted at taking further action after bilateral consultations with Japan. The options included taking the case to the WTO. The US insisted that full market access for American rice had to be secured. The intensive US demand for opening Japan's agricultural market was due to the fact that Japan became the largest export market for US farm products in 1994.²⁴⁵ Japan accounted for 9.3 billion

²⁴⁰ The Japan Times, 17 November 2000

²⁴¹ On Japan's rice policy, see: Kawagoe, 'Deregulation and Protectionism in Japanese Agriculture', in Teranishi and Kosai, 'Japanese experience of economic reforms', P381-387

²⁴² McFarquhar, 'World Trade Pressures – Reform of EU Common Agricultural Policy and Food and Agricultural Policy in Japan', P19

²⁴³ Hisao Fukuda, John Dyck and Jim Stout, 'Rice sector policies in Japan', (United States Department of Agriculture, Electronic Outlook Report from the Economic Research Service, 2003), P2 / (www.ers.usda.gov)

²⁴⁴ Economic Research Service / USDA, Agricultural Outlook, April 1999, 'World Agriculture & Trade / Rice Tariffication in Japan: What does it mean for trade?' P1-4

²⁴⁵ On the issue of US-Japan agricultural trade since the Uruguay Round, see C.C. Meyerson, "Domestic Politics and International Relations in Trade Policymaking: The United States and Japan and the GATT Uruguay Round Agriculture Negotiations", Working paper, (Washington DC, Columbia University, International Studies Association,

dollars of the record 45.7 billion dollars in US farm exports in 1994, compared with 8.7 billion dollars in 1993, followed by the EU and Canada. US farm exporters depend heavily on the Japanese market.²⁴⁶

The US repeatedly claimed that Japan's commitment to open its domestic rice market, which was the result of the previous global trade liberalisation talks of the Uruguay Round, was not enough. The US also pointed out that imported rice rarely reached end consumers, instead it was either placed in storage or exported as food aid to other countries.²⁴⁷ The US claimed that the trade deficit with Japan remained a heavy burden for the US economy, therefore Japan should have increased rice imports from the US.²⁴⁸

Japan's rigid agricultural policy stems from its difficulties with surplus production since the 1960s. Because of its climate and land base for rice paddies, Japan is well suited for growing rice. However, until the 1950s, Japan's large population consumed more rice than the country could consistently produce. As society changed in the course of recovery from the Second World War and national income rose, rice consumption per person began to fall in 1963, a trend that has continued until the present time. As rice consumption dropped, Japan's government sought to raise the incomes of the many households planting rice. The government ceased rice imports and took other steps, such as purchases, to raise the domestic production price of rice. Farmers responded with higher production, leading to rising government stocks. As imports of foreign rice continue to increase, the declining numbers of consumers have barely had a chance to overcome their traditional bias against foreign rice, long considered inferior to domestic rice.²⁴⁹

2-3. Food self-sufficiency ratio

It is not only the Japanese government which has traditionally viewed its agricultural sector as something to defend to the last. Powerful farm lobbies provide part of the explanation, but there has also been a perception that countries should achieve a certain degree of self-sufficiency in food production and protectionism has been the means of achieving that. Food security has thus become one of the most important rationales for protecting the domestic agricultural market and the food self-sufficiency

40th Annual Convention, 1999)

²⁴⁶ The Financial Times, 18 May 1995

²⁴⁷ The Japan Times, 1 April 2000

²⁴⁸ The Japan Times, 11 July 2001

²⁴⁹ The Financial Times, 28 April 1998

ratio is a central figure in Japan's justification of agricultural protectionism.

The Japanese food self-sufficiency rate has been declining in recent years (See Table-5) and is the lowest among industrialized countries.²⁵⁰ Table-6 lists the degree of self-sufficiency of food by commodity. Apart from rice, more than 90 per cent of various crops depend on import from foreign countries. The self-sufficiency rate of wheat is 9 per cent, soybean 4 per cent and corn 0 per cent. In terms of the food self-sufficiency rate on a calorie base, just 40 per cent is covered by domestic production. Overall, 60 per cent of Japanese food depends on imports, and there is concern about a shortage of food in the case of a global food production crisis.

The annual report on food, agriculture and rural areas in Japan for the financial year 1999 emphasized the importance of the self-sufficiency ratio in Japan.²⁵¹ The ratio showed a decrease during the period 1965 to 1998, declining from 73 per cent to 40 per cent on a calorie basis and from 62 to 27 per cent on a grain basis. From a long-term standpoint, one of the major factors behind this declining trend is a fundamental change in Japanese dietary patterns, as reflected in the increasing consumption of animal products and fats and oils, which are largely dependent on imported grains. In recent years, both trends have slowed down, while the domestic production of wheat and soybean has been declining. This is a key factor behind the declining self-sufficiency ratio in the short term. As the world food supply/demand situation could be tight in the mid- and long-term, Japanese people are now showing great concern for the future, particularly in view of the very low food self-sufficiency ratio. Since there are certain limitations for stockpiling and imports, the government increasingly feels that it is important to increase domestic agricultural production as much as possible.

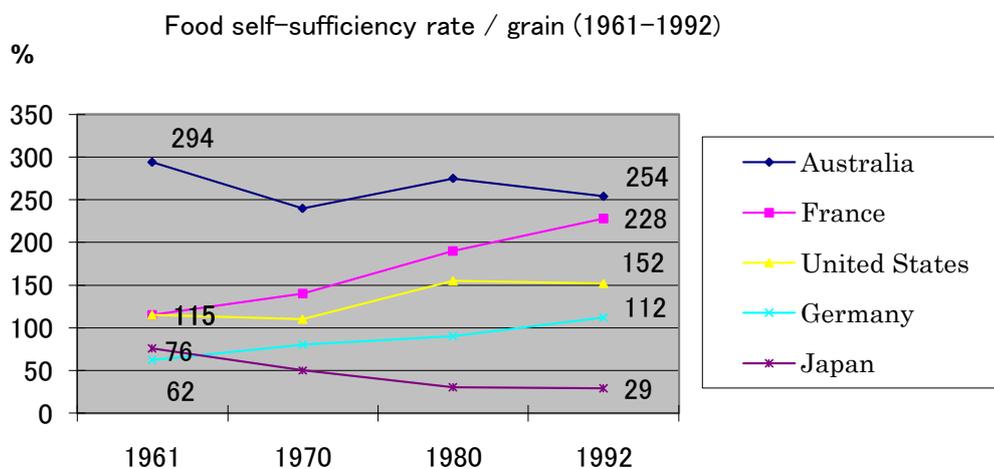
Regarding Japanese concern about the low level of food self-sufficiency ratio, Ryutaro Komiya cites as an instance soybeans. Soybeans are an essential foodstuff in Japan, used for tofu, bean paste soup and soya sauce. Japan was self-sufficient in soybeans until the 1920s when it started to import them from China. Although Japan became self-sufficient in soybeans again after the Second World War, Japan gradually liberalised its soybeans imports under US pressure. As a result, in 1973, Japan imported 95 per cent of the domestic consumption of soybeans, and approximately 90 per cent of these imports were from the US. However, because of a temporary domestic shortage of feeding-stuffs, in 1973, the United States put an embargo on soybeans exports. Even

²⁵⁰ The Japan Times, 26 April 1999

²⁵¹ Annual Report on Food, Agriculture and Rural Areas in Japan Financial Year 1999 (Summary) by Minister of Agriculture, Forestry and Fisheries, Japan. (<http://www.maff.go.jp/hakusyo/kaigai/ehakusyo99.htm>)

contracted shipments to Japan were stopped in the ports. Soybeans are fed to cattle in the US but in Japan they are a vital food element for humans. This incident (the so-called ‘Soyabean shock’) made Japanese aware of the importance of food self-sufficiency.²⁵²

Table-5:



Source: Japanese Ministry of Agriculture, Forestry and Fisheries

Table-6: Japan’s food self-sufficiency rate by commodity

Wheat	9%
Rice	95%
Corn	0%
soybean	4%
vegetables	83%
Fruits	49%
Beef	36%
Pork	58%
Chicken	65%

Japan’s food self-sufficiency rate on a calorie base - 40%

↓

60% of Japanese food depends on imports.

Source: Japanese Ministry of Agriculture, Forestry and Fisheries

²⁵² This episode was mentioned by Ryutaro Komiya, Professor of Economics at Aoyama-Gakuin University in Japan, in a panel discussion held at the conference Japan in a Global Economy at the Stockholm School of Economics. See: Thomas Andersson (ed.), ‘Japan: A European Perspective’, (London, the Macmillan Press, 1993), P52, 53

2-4. International criticism and the relationship between farmers and the LDP

Many specialists dismiss the Japanese government's concern with food self-sufficiency as inappropriate.²⁵³ Anderson disagrees with the claim that a high level of food self-sufficiency is necessary to maintain food security.²⁵⁴ He argues that this claim is inconsistent with the usual definition of food security, which is that everyone always has access to the minimum supply of basic food necessary for survival. Lower rather than higher consumer prices for food would by that definition boost the number of food-secure people, suggesting that lower import barriers and export subsidies should be called for. But he concedes that becoming more dependent on imports raises questions about the preparedness of foreign exporters to assure a stable supply. For that reason, food importers may call for stronger discipline on the exceptions to GATT Article XI.1 which prohibits export restrictions other than export taxes. For example, Article XI.2 permits temporary quantitative export restrictions to relieve critical food shortage in an exporting country.²⁵⁵

The IMF recognises food security as a legitimate concern. However, the IMF argues that food security could be addressed through increased trade rather than subsidies, preferential treatment of select groups of producers or restrictions on trade.²⁵⁶

As Anderson points out, if Japan's claim of food security is inconsistent with real market mechanisms, does this then mean that Japan's low self-sufficiency rate is merely an ostensible reason for the closed nature of Japan's market? It is often pointed out that Japan's agricultural trade policy has its foundations in the country's political system. In spite of the dwindling number of farmers, Japan's farm lobby remains hugely influential, partly as a result of the overrepresentation of rural constituencies in the Diet.

The ruling LDP has strong roots among a rural population that has become even more important in recent years as urban voters have grown dissatisfied with LDP politics. The farming sector has long been a traditional support not only for the ruling LDP but also for the Social Democratic Party of Japan, the former major opposition party. This is due to the electoral system and the insufficient adjustment of certain electoral districts to the demographic shift to urban areas. As a result, the voting system is weighted in favour

²⁵³ For a discussion of Japan's agriculture and foreign economic relations, see, for example, Hillman and Rothenberg, 'Agricultural Trade and Protection in Japan', P60-85

²⁵⁴ Professor Kym Anderson is the Professor and Executive Director of the Centre for International Economic Studies in School of Economics University of Adelaide

²⁵⁵ Kym Anderson, "Agriculture, WTO, and the next round of multilateral trade negotiations", (Australia, School of Economics and Centre for International Economic Studies University of Adelaide, 1998)

²⁵⁶ International Monetary Fund, 'Trends and Issues in the Global Trading System', (1999), P134

of the farming population. While the farming population may be falling, the number of people dependent on the large farm associations, such as Nokyo, which provide everything from life insurance to fertilisers, is still very large. They have a powerful ally in the Ministry of Agriculture, Forestry and Fishery (MAFF) and a close relationship with politicians in the government.²⁵⁷ As a result, the political significance of protecting the agricultural sector is extremely high, not leaving much leeway for concessions in agricultural trade negotiations.²⁵⁸

2-5. The food safety argument

Japan's emphasis on food safety compounds the problem posed by Japanese agricultural import restrictions. The difficulty in dealing with food safety issues can be clearly seen in bilateral trade disputes. As in the case of the argument about food security, some observers point out that Japan's attitudes to food safety diverge so widely from some other WTO members that they may prove impossible to reconcile.²⁵⁹ If so, more trade disputes over food safety appear inevitable.

A conspicuous example is a bilateral dispute with the United States on Japan's testing requirements for imported apples. The US complained that Japanese quarantine testing procedures for agricultural commodities were unnecessarily complex and burdensome and violated a WTO requirement that testing be based on scientific principles and risk assessment. The US trade authorities criticised that Japanese quarantine testing procedures were systematically discriminating against US farm exports.²⁶⁰ In response to the US complaint, the WTO panel ruled that Japan's testing requirements for imported apples and other produce breached fair trade rules. The panel report confirmed an interim finding that the Japanese measures requiring each variety of a product to be separately tested for the destructive codling moth were not backed by sufficient scientific evidence. The panel said Japan had the right to take appropriate measures to avoid importing the codling moth pest, which does not exist in Japan. But it had not tried to establish scientific backing for its strict procedures, as WTO rules require. The panel report marked a further step in defining WTO rules on what constitutes adequate scientific evidence for

²⁵⁷ The Financial Times, 29 November 1999

²⁵⁸ For a discussion on the relationship between the LDP and Japanese agricultural policy, see: Jennifer A. Amyx, "The Political Economy of Japanese Agriculture", (The Australian National University), P59-72 (<http://www.rirdc.gov.au/reports/GLC/00-176-Part2.pdf>)

²⁵⁹ On Japan's food safety policy, see Mitsuhiro Ushio, 'Food Safety Regulatory Issues', (Food and Agriculture Organization of the United Nations & World Health Organization, 2003), (http://www.fao.org/DOCREP/MEETING/004/Y2010E.HTM#P15_336)

²⁶⁰ The Financial Times, 18 April 1997

high food safety standards, a sensitive and controversial area. At the same time, this bilateral dispute with the US clearly showed Japan's closed nature with respect to the agricultural market in relation to food safety issues.

3. The EU agricultural trade policy

3-1. The Common Agricultural Policy

The agricultural policy of the EC/EU member states had been regulated since very early on at Community-level as stipulated in Articles 32 to 38 in Title II of the EC Treaty.²⁶¹ The memory of post-war food shortages was still vivid and thus agriculture constituted a key element from the outset of the EC. Moreover, the founding of the Common Market was based on a balance of interests between countries with predominant agricultural interests versus those with mainly industrial interests.

The Treaty of Rome defined the general objectives of the CAP. The principles of the CAP were set out at the Stresa Conference in July 1958. In 1960, the CAP mechanisms were adopted by the six founding Member States and two years later, in 1962, the CAP came into force.

The CAP is comprised of a set of rules and mechanisms, which regulate the production, trade and processing of agricultural products in the EU, with attention being focused increasingly on rural development.²⁶² Among the European Union's policies, the CAP is regarded as one of the most important policy areas.²⁶³ Not only because of its share of the EU budget (almost 50 per cent, decreasing over the years), the vast number of people employed in the agricultural sector and the extent of the territory directly affected, but also because of its symbolic significance, and the extent of sovereignty transferred from national to European level. The significance of the CAP nowadays is also portrayed by the fact that it is directly related to the Single Market and the Economic and Monetary Union (EMU), two key areas in achieving European integration.

²⁶¹ EUROPA, Activities of the European Union, Summaries of legislation, 'Agriculture: introduction', (<http://europa.eu.int/scadplus/leg/en/lvb/l04000.htm>)

²⁶² For details of the Common Agricultural Policy, see: Jacques Pelkmans, 'European Integration – Methods and Economic Analysis – second edition', (Essex, Pearson Education Ltd., 2001), P202-222; Frank McDonald and Stephen Dearden (eds), 'European Integration – fourth edition', (Essex, Pearson Education Ltd., 2005), P302-324; Edward Nevin, 'The Economics of Europe', (London, the Macmillan Press, 1990), P146-174; Susan Senior Nello, 'The European Union – Economics, Politics and History', (Maidenhead, McGraw-Hill Education, 2005), P215-243; Fiona Butler, 'The EC's Common Agricultural Policy (CAP)' in Juliet Lodge (ed), 'The European Community and the challenge of the future', (London, Pinter Publishers, 1993), P112-130

²⁶³ About the CAP and its reform since the Uruguay Round, see: Patrick A. Messerlin, 'Measuring the costs of protection in Europe – European Commercial Policy in the 2000s', P79-132

The objectives of the CAP, as set out in Article 33 of the EC Treaty, are:

- 4.) to increase agricultural productivity by promoting technical progress and by ensuring the rational development of agricultural production and the optimum utilisation of the factors of production, in particular labour
- 5.) to ensure a fair standard of living for the agricultural community, in particular by increasing the individual earnings of persons engaged in agriculture
- 6.) to stabilise markets
- 7.) to assure the availability of supplies
- 8.) to ensure that supplies reach consumers at reasonable prices

The CAP succeeded in reaching its initial goals.²⁶⁴ As a result of CAP, EU agricultural production is like in Japan heavily subsidised. It encouraged both production and productivity, stabilised the markets, secured supplies and protected farmers from fluctuations in world markets.²⁶⁵

3-2. Export subsidies

In contrast to Japan, the EU decided not only to subsidise production but also export of agricultural products in order to cope with the problem of overproduction and the goal of protecting farm incomes. Subsidising agriculture means that production and input use in subsidising countries are higher than would be the case in the absence of protection. The maintenance of high levels of protection in the EU under the CAP has resulted in excessive intensification of input use, resulting in the deterioration of the rural environment and natural resources. It is pointed out that reducing protection in the EU would lead to a reduction in EU farm production and a significant decrease in farm input use. Agricultural exporters in other countries would also benefit from the resultant

²⁶⁴ Richard Baldwin & Charles Wyplosz, 'Manuscript for The Economics of European Integration – 8. The Common Agricultural Policy', (2003), P10-19, (http://heiwww.unige.ch/~baldwin/papers/BW/Chap8_CAP_Jul03.PDF)

²⁶⁵ See, S.A. Baker, 'The cost of the C.A.P.' in *Journal of Economic Affairs*, April 1982, Vol. 2, Issue 3, (Oxford, Blackwell Publishing, 1982), P178

relative increase in world prices for a range of agricultural commodities. Furthermore, support of agriculture costs nearly twice as much as agricultural wages in the EU.²⁶⁶

In order to make European agricultural exports competitive with the much lower world market prices, the EU decided to pay ‘restitution’ or ‘export refunds’ equal to the difference between EU and world prices. However, such a practice of exporting goods at a price that is below cost is condemned as ‘dumping’. Under WTO rules for non-food items, this is normally not permitted, especially when the practice is driven by government subsidies. Until the Uruguay Round, however, the WTO placed few restrictions on the dumping of agricultural goods.

The problem with dumping is that it depressed world prices for food and thereby infuriated food exporters based outside of the EU. The biggest losers from the CAP’s dumping were the largest food-exporting nations, notably those grouped in the Cairns Group. Most countries practice some form of import protection on food, so while the CAP’s tariffs were harmful to the world market, they were not viewed as particularly out of line with rest of the world’s practice. The subsidised exports of food, however, were more unusual.

Brussels asserted that its subsidies were within WTO rules. But the Cairns Group argued that while they were within the legal limits, export subsidies were inconsistent with the spirit of the rules. They argued that the EU had exploited a loophole in the rules by accumulating subsidy entitlements when world prices were high.²⁶⁷

The differences in policies on export subsidies had also prompted exchanges between Brussels and Washington. In October 1999, Franz Fischler, the EU Agriculture Commissioner, refuted US criticism of the CAP, arguing that it was an attempt to deflect attention from the US’ reluctance to negotiate on politically sensitive sectors. He said agricultural support spending was actually falling in the EU but rising in the US. His comments followed a warning by Pascal Lamy, EU Trade Commissioner, that Washington’s modest trade policy objectives could prevent the trade negotiations from proceeding.²⁶⁸

The EU’s criticism of US agricultural policy stems from the fact that the United States has been subsidising agricultural production as well as the export of agricultural products. The export subsidies under the US Export Enhancement Programme have been very costly to the US, have added only very modestly in proportional terms to the EC/EU budgetary cost of the Common Agricultural Policy, and have imposed large costs on

²⁶⁶ Freeman & Roberts, ‘Multifunctionality, a pretext for protection?’

²⁶⁷ The Financial Times, 25 September 1998

²⁶⁸ The Financial Times 16 October 1999

agricultural products exporting countries.

3-3. The food safety argument

While Japan has no agricultural export subsidies, both the EU and Japan share concerns about food safety. The EU-US confrontation over the safety of beef is a good illustration. In 1997, the WTO dispute panels ruled against the EU ban on hormone-treated beef, because it had not been preceded by a proper scientific risk assessment. The case was the first big test of the WTO's new food safety rules – called SPS, or sanitary and phyto-sanitary rules. These were designed to reduce conflicts over the issue. They require safety regulations that exceed internationally agreed standards to be justified by scientific evidence. But although the WTO hormones' ruling is widely seen as a landmark, it raises as many questions as it answers. Both Brussels and Washington interpreted the decision as a victory but disagreed over whether it required the beef ban to be lifted immediately. The EU said it had the right to establish, on a scientific basis, a level of consumer protection which it considers appropriate, even if it is higher than the level resulting from international health standards.²⁶⁹

4. The EU and Japan in the Uruguay Round (1986-1994)

4-1. The Uruguay Round: its inauguration and conclusion

Protectionist agricultural trade policies of GATT contracting members, such as that of the EC/EU and Japan, resulted in extreme distortions of agricultural trade. The period since the 1950s has seen substantial growth in agricultural protectionism in the advanced industrial economies spreading to newly industrialising economies.²⁷⁰ Those tendencies accelerated in the 1980s.²⁷¹ The growth of agricultural protectionism in industrialised countries has contributed to the long-term downward trend in the international price of farm products relative to that of industrial products. The extent of decline of the relative price of food, together with the EC/EU's provision from the latter 1970s of export subsidies to dispose of its policy-induced surplus, stimulated the US to defend its export markets by subsidising US farm exports as well – a move that contributed to international food prices falling by 1987 to their lowest level that century in real terms.

²⁶⁹ The Financial Times, 29 October 1998

²⁷⁰ On the issue of protectionism in the industrialised nations, see Sanderson (ed), 'Agricultural Protectionism in the industrialised world'

²⁷¹ For details on agricultural trade in the 1980s, see Hartwig de Haen, Glenn L. Johnson and Stefan Tangermann (eds), 'Agriculture and International Relations', (Basingstoke, The Macmillan Press, 1985)

As a consequence of these policy developments, the deadweight welfare losses in those protectionist countries from distorting their food markets more than doubled over the 1980s, while the benefits to their farmers as a group increased by about 50 per cent. According to one set of estimates from a multi-commodity model of world food markets, the annual benefits of these policies to farmers in Western Europe, the United States and Japan rose from 94 billion dollars to 141 billion dollars over the 1980s (in 1985 US dollars), while the cost to consumers in those countries rose from 120 billion dollars to 216 billion dollars. The study estimates the direct global loss of economic welfare as a result of the food policies of the industrialised countries to have trebled in the 1980s, rising from 16 billion dollars to 50 billion dollars. That does not include the costs of lobbying for and administering these policies, nor that of the collection and by-product distortion costs of raising government revenue needed to finance the subsidies, let alone the indirect cost these policies imposed in terms of holding up the Uruguay Round's conclusion.²⁷²

In the early 1980s, there was a growing concern that agricultural protection would continue, unless explicitly checked. Agricultural products exporting countries argued that real liberalisation means providing substantial improvement in market access, the elimination of trade-distorting subsidies and fairer trade rules.²⁷³ These international circumstances surrounding agricultural trade made it unavoidable for the GATT to include farm policies in the Uruguay Round.

The Punta del Este Declaration, which launched the Uruguay Round in July 1986, stated that the central objective for reforming the conduct of agricultural trade was 'to bring all measures affecting import access and export competition under strengthened and more operationally effective GATT rules and disciplines'.²⁷⁴ This clearly committed all GATT contracting members to allow their domestic agricultural policies to be the subject of international negotiations, as well as trade policies aimed directly at restricting imports and expanding exports at the expense of foreign competitors.²⁷⁵

Keeping agriculture on the agenda for the Round was the initial concern of the

²⁷² For protectionism and trade measures used for agricultural protection, see Jimmye S. Hillman, 'Technical Barriers to Agricultural Trade', (Boulder, Colo, Westview Press, 1991)

²⁷³ The Financial Times, 29 November 1999

²⁷⁴ K. A. Ingersent, A. J. Rayner and R. C. Hine (eds), 'Agriculture in the Uruguay Round', (New York, St. Martin's Press, 1994), P60

²⁷⁵ For the linkage between the Uruguay Round's agricultural trade negotiations and domestic agricultural policy reform, especially that of the US and the EU, see Robert Paarberg, 'Agriculture Policy Reform and the Uruguay Round: Synergistic Linkage in a Two-Level Game?' in *International Organization*, Vol. 51, No.3 (Cambridge, The MIT Press, Summer 1997), P413-444

agricultural products exporting countries, such as the Cairns Group.²⁷⁶ It succeeded in attracting unprecedented attention to the agricultural issue during the Round, overcoming opposition from the EC/EU and Japan. The Cairns Group achieved its aim because of the solidarity of the group on agricultural issues. Declining agricultural export earnings was a political priority in all Cairns Group countries. Since the Uruguay Round, the Cairns Group, as a grouping of producers of agricultural products, has been a significant player in the GATT.

For the US, agriculture was also the top priority for the Uruguay Round. The US deemed the effort necessary to open significant new opportunities for American agricultural exporters as well as to strengthen the global trading system so that all countries might compete on equal terms. On agriculture, the top US priority was to regain its market share of world trade in agricultural products, which had declined during the early 1980s, by negotiating through the GATT the abolishment of all forms of agricultural support and protection. The US was strongly supported by the Cairns Group.²⁷⁷ Among a variety of proposals tabled in late 1987 and early 1988 for the Uruguay Round, the US proposal was very radical.²⁷⁸ The US proposal was for a sweeping elimination of all trade-distorting agricultural subsidies by the year 2000, or over a ten year period (the so-called zero option). It is unlikely that the US really believed that the EC and Japan would accept the zero option. The first negotiating proposal by the US in July 1987 was an ideological trial balloon launched by the US in the hope that political and economic trends would be favourable to achieving the desired result.²⁷⁹ EC officials felt the United States was insincere and only trying to scuttle an agreement by starting from a position everyone knew was unacceptable. Behind its strong stance on agricultural trade, the US also had an ulterior political objective, namely to reassert US political and economic hegemony by forcing the EC and Japan to tear down their trade barriers. Many officials in Reagan's administration (1981-1989) felt that the EC and Japan should help make a bigger contribution to the cost of US efforts to manage the international political

²⁷⁶ For the commitment of the Cairns Group to the Uruguay Round, see for example, Richard A. Higgott and Andrew F. Cooper, 'Middle Power Leadership and Coalition Building: Australia, the Cairns Group and the Uruguay Round of Trade Negotiations' in *International Organization*, Vol. 44, No. 4, (Cambridge, The MIT Press, 1990), P589-632

²⁷⁷ Ingersent, Rayner and Hine (eds), 'Agriculture in the Uruguay Round', P36-108

²⁷⁸ On the trade policies of the US, the EC and Japan and details of their proposals for the negotiations in the Uruguay Round, see Australian Bureau of Agricultural and Resource Economics, 'Proposed strategies for reducing agricultural protection in the GATT Uruguay Round –A synthesis and assessment', (Canberra, Pirie Printers, 1990)

²⁷⁹ Ingersent, Rayner and Hine (eds), 'Agriculture in the Uruguay Round', P 33

economy.²⁸⁰

The EC's stance on agriculture during the Uruguay Round was reactive rather than innovative. The EC's position in the Round stemmed from the following four points: 1). the presence of many small, inefficient producers in several countries unable to compete in open world markets, 2). the power of agricultural groups in its political system, 3). the non-farm wealth to afford farm subsidies, and 4). problems of reaching consensus on change among the 12 countries on any issue. Due to those points, the EC was not able to exert leadership. Among the above four points, owing to conflicting interests of its members, it was particularly problematic to develop a common negotiating strategy. The Council of Ministers eventually agreed to the talks, provided that discussion covered everyone's direct and indirect forms of support for agriculture, not just the EC's.²⁸¹

Rather than forward its own proposals for reform, the Community chose to react to proposals for reform tabled by others, most notably by the United States and the Cairns Group. The EC remained implacably opposed to the zero option on any time scale. Although the EC was prepared to contemplate modifying the CAP, it would not consider phasing it out. Throughout the Uruguay Round, the EC was under pressure from its agricultural trading partners which wanted improved market access to the EC market for their exports, as well as an end to subsidised competition in third country markets. Besides, there was internal pressure for reform for mainly budgetary reasons.

Japan generally welcomed the initiation of the Uruguay Round, seeing in it a way to stem the rising protectionism in the US. Even the Japanese farm lobby, under strong bilateral pressure from the US to open the Japanese rice market to external competition, sought to use the Round as a shelter from this bilateral pressure. It was hoped that because of Japan's huge export surplus with the US, the protection of Japanese agriculture might emerge more favourably from multilateral rather than from bilateral negotiations, due to the support of other major food importers, such as the EC. This explains why, in April 1986, the Japanese government stated that it was not prepared to deal with the rice issue bilaterally, but only through the Uruguay Round of multilateral trade negotiations. For the Round, the Japanese government was prepared to make minimum concessions on agriculture in the negotiations as were needed to ensure the success of the Round as a whole. Japan's attitude towards the Round was based on Japan's belief that, in the past, the primary aim of GATT negotiations on agriculture was

²⁸⁰ Brian Hocking and Steven McGuire (eds), 'Trade Politics, International, Domestic and Regional Perspectives', (London, Routledge, 1999), P59

²⁸¹ Brian Hocking and Steven McGuire (ed.), 'Trade Politics, International, Domestic and Regional Perspectives', (London, Routledge, 1999), P59

to benefit exporters at the expense of importers. Therefore, as the world's largest importer of agricultural products, Japan saw its role to defend the interest of food importers.²⁸²

In November 1988, the US submitted a Framework Proposal which was specifically designed to set the agenda for future negotiations and as a guide for the Mid-Term Review of progress made during the first two years of the Uruguay Round negotiations. A framework agreement reached in the Mid-Term Review specified that the primary long-term objective of the Multilateral Trade Negotiations was "to provide for substantial progressive reductions in agricultural support and protection sustained over an agreed period of time, resulting in correcting and preventing restrictions and distortions in world agricultural markets". This commitment was reaffirmed by heads of the seven major industrial nations at the summit meeting held in Houston in July 1990.²⁸³ A central element of the Framework Proposal was the 'tariffication' of all agricultural trade NTBs. It meant that all NTBs should be converted to their tariff equivalents and bound. The US and the Cairns Group proposal contrasted with that of the EC and Japan which continued to refuse substantial alteration of their support policies and preferred market sharing arrangements. However, in the middle of the Uruguay Round, the US and the Cairns Group signalled a willingness to move away from the zero option and compromise towards a more realistic position of a short-term roll back of agricultural support, export subsidies and trade barriers.

Towards the end of the negotiations, the EC and Japan's stance also changed. The EC's stance became more flexible in certain respects, largely as a result of rising internal pressure for a fundamental reform of the CAP. Despite the internal opposition to reduce agricultural protection, the Japanese government took some steps to relax barriers to agricultural imports. In June 1988, Japan decided to abandon all quota restrictions on beef and fresh oranges from April 1991.

Throughout the Round, the position of Japan was close to that of the EC. Japan was prepared to make concessions equivalent to those conceded by the EC. Japan's position did not change after September 1990, although Japan was prepared for last minute compromises at the abortive 'final' meeting of the Uruguay Round held in Brussels in December of that year. For that purpose, members of the ruling party were in Brussels as it was expected that the EC would make some further concessions on agriculture in exchange for gains made in other areas of the negotiations and to ensure the success of the Round as a whole. Japanese politicians needed to be there in case Japan

²⁸² Ingersent, Rayner and Hine (eds), 'Agriculture in the Uruguay Round', P63-142

²⁸³ Luther Tweeten, 'Agricultural Trade – Principles and Policies', (London, Westview Press, 1992), P218

had to consider making last minute adjustments to its own position in response to moves by the EC.²⁸⁴

The WTO Agreement on Agriculture reached in the Uruguay Round stated that it recognised ‘that the long-term objective of substantial progressive reductions in support and protection resulting in fundamental reform is an ongoing process.’²⁸⁵ Members agreed that negotiations for continuing the process would be initiated one year before the end of the implementation period, taking into account: (a) the experience to that date from implementing the reduction commitments; (b) the effects of the reduction commitments on world trade in agriculture; (c) non-trade concerns, special and differential treatment to developing country members, and the objective to establish a fair and market-oriented agricultural trading system, and the other objectives and concerns mentioned in the preamble to this agreement; and (d) what further commitments are necessary to achieve the above mentioned long-term objectives’.²⁸⁶ Shinji Hattori, Professor at Toyo University, argues that the agreement was made on the basis of a compromise reached between the US-Cairns Group and the EC/EU-Japan. In the agreement, he wrote, we see the expression of ‘substantial progressive reductions’. The term ‘substantial’ was included due to the demand from the US and other agricultural products exporting countries. The term ‘progressive’ was mentioned in the agreement because of the demand from the EC/EU and Japan. He also argues that the agreement refers to the term ‘long-term objective’, because of the demand from the EC/EU and Japan, which intended to play for time on agricultural reform. The term ‘an ongoing process’ was put in the agreement by the US and Cairns Group which wanted to emphasise the continuation of agricultural reform.²⁸⁷

However, this EC/EU-Japan relationship does not mean that the EC/EU and Japan maintained cooperation throughout the Round. Their stance for the tariffication of border measures, for instance, showed a clear difference. The issue of tariffication of border measures was highly important for Japan due to the concern of opening its rice market. Although Japan was strongly against tariffication, the EC/EU partially accepted the principle of tariffication. On the issue of export subsidies, Japan favoured its elimination, while the EC/EU was stubbornly against it.²⁸⁸ Japan proposed a freeze on

²⁸⁴ Ingersent, Rayner and Hine (eds), ‘Agriculture in the Uruguay Round’, P38-149

²⁸⁵ The WTO, ‘Agreement of Agriculture Article 20, Continuation of the Reform Process’, (www.wto.org/english/docs_e/legal_e/14-ag.doc)

²⁸⁶ The WTO, ‘Agreement of Agriculture Article 20, Continuation of the Reform Process’, (www.wto.org/english/docs_e/legal_e/14-ag.doc)

²⁸⁷ Shinji Hattori, ‘Global-ka wo ikiru nihon nougyou’, P23-26

²⁸⁸ Ingersent, Rayner and Hine (eds), ‘Agriculture in the Uruguay Round’, P150-151

export subsidies which would subsequently be phased out, a reduction of domestic subsidies which lead to trade distortions and negotiated improvements in market access. Shinji Hattori argues that in the Uruguay Round's agricultural negotiations, there was no 'strategic cooperation' between the EC/EU and Japan. According to him, Japan maintained the same distance from the US as from the EC/EU in terms of its negotiating position. The EC/EU and Japan did not make their cooperation clear, while the US and Cairns Group showed clear cooperation.²⁸⁹ The US sought to isolate the EC/EU by emphasising common interests with some members of the Cairns Group and Japan.²⁹⁰ Interested in easing bilateral economic but also security relations with the US, throughout the talks Japan generally 'kept its head low' while US and EC/EU officials engaged one another. David N. Balaam argues that Japan's negotiating style reflected an effort to appear cooperative and a team player, thereby playing a more positive role in the international system.²⁹¹

In November 1992, the US and the EC/EU settled most of their differences on agriculture in a deal known informally as the "Blair House Accord". By July 1993 the "Quad" (US, EC/EU, Japan and Canada) announced significant progress in negotiations on tariffs and related subjects, such as market access. It took until 15 December 1993 for every issue to be finally resolved and for negotiations on market access for goods and services to be concluded. On 15 April 1994, the deal was signed by ministers from most of the 123 participating governments at a meeting in Marrakesh, Morocco.

4-2. Conclusion of the Uruguay Round and its impact on Japanese and EU agricultural policy

The concluded Uruguay Round's Agreement on Agriculture had three main aims: a reduction in farm export subsidies, an increase in market access and cuts in domestic producer subsidies.²⁹² The tariffs on agricultural products were now bound and were to be reduced over the implementation period (1995-2000). Another important element of the agreement was the Aggregate Measurement of Support (AMS) for industrial country

²⁸⁹ Hattori, 'Global-ka wo ikiru nihon nougyou', P104, P105

²⁹⁰ John Peterson also argues that throughout the Round, "US negotiators proved resourceful and creative in isolating the EC on the agricultural issue". - John Peterson, 'Europe and America in the 1990s', (Aldershot, Edward Elgar Publishing Limited, 1993), P16

²⁹¹ Hocking and McGuire (eds), 'Trade Politics, International, Domestic and Regional Perspectives', P62, 63

²⁹² For details of the Agriculture Agreement made in the Uruguay Round, see the WTO, 'Agriculture fairer market for farmers', (http://www.wto.org/english/thewto_e/whatis_e/tif_e/agrm3_e.htm)

farmers. AMS was agreed to be reduced by a four-fifth of its 1986-88 level by the turn of the century.²⁹³

As a result of the Uruguay Round, agriculture finally became a mainstream issue of the WTO, which allowed other agreements in the Uruguay Round to be concluded.²⁹⁴ In addition, it was agreed to reopen agricultural negotiations by the end of 1999 to continue the process of agricultural reform.²⁹⁵ Moreover, the requirement to transform NTBs into tariffs, to quantify the AMS and to notify all subsequent policy changes to the WTO's Committee on agriculture were major contributions to transparency. The new rules and obligations were expected to constrain further agricultural protection growth in both advanced and newly industrialised countries. The wider effects of an overall GATT deal were expected to boost incomes in many countries, leading to rising demand for food products. This in turn was predicted to be likely to feed through into higher prices.²⁹⁶ It was hoped that these new rules would promise greater certainty and stability in international food markets in the next century. However, implementing the agricultural reforms agreed in the Uruguay Round involved only very modest liberalisation by 2000, with plenty of room for disputes over compliance during the implementation period and the need for further reductions in the future.²⁹⁷

The conclusion of the Uruguay Round left a considerable impact on the EU and Japan's agricultural policy.²⁹⁸ Throughout the cumbersome trade negotiations of the Uruguay Round, the EC/EU and Japan negotiated individually on the agricultural issue, while the US and Cairns Group formed a united front against the EC/EU and Japan. The EC/EU and Japan faced strong pressure from the US-Cairns Group coalition. This put the EC/EU and Japan on the defensive and forced them to agree to wide-ranging concessions

²⁹³ Anderson, "Agriculture, WTO, and the next round of multilateral trade negotiations"

²⁹⁴ Although agriculture became a mainstream issue in the WTO, there is an argument that the Uruguay Round Agreement on Agriculture still shelters it from generally applicable rules. About the shortfalls of the agreement, see Bernard O'Connor, 'Journal of World Trade 37(5) / A Note on the Need for More Clarity in the World Trade Organisation Agreement on Agriculture', (Hague, Kluwer Law International, 2003), P839-846

²⁹⁵ The Organisation for Economic Co-operation and Development provides a comprehensive assessment of the trade negotiations in the Uruguay Round, see the OECD, 'Assessing the effects of the Uruguay Round', 1993, see also, Tiren Nguyen, Carlo Perroni and Randall Wigle, 'An Evaluation of the Draft Final Act of the Uruguay Round', *The Economic Journal*, Vol. 103, No. 421, (Royal Economic Society, 1993), P1540-1549

²⁹⁶ *The Financial Times* 16 December 1993

²⁹⁷ Anderson, "Agriculture, WTO, and the next round of multilateral trade negotiations"

²⁹⁸ The impact of the Uruguay Round Agricultural Agreement on the US, the EU and Japan is estimated quantitatively in, Glenn W. Harrison, Thomas F. Rutherford, David G. Tarr, 'Quantifying the Uruguay Round', *The Economic Journal*, Vol. 107, No.444, (Royal Economic Society, 1997), P1405-1430

in the farm trade negotiations. This led to drastic changes in their farm trade policies.

The main issue for Japan in the Uruguay Round was its closed rice market and the combined pressure from the US and the Cairns Group forced the Japanese government, against very strong resistance from domestic political interest groups, to end its total closure to foreign exports. It proved very difficult to convert the total ban on rice imports into a monetary levy.²⁹⁹ Japan refused initially to agree to even a partial opening of its rice market in the Uruguay Round, citing the devastating effect of cheap imported rice on domestic producers. Refusing to replace the total ban with a tariff scheme, Japan accepted at the end of 1993 the Minimum Access which obliged Japan to import a minimum amount of rice which would be gradually increased until 2000. Under this scheme, Japan had to import 4 per cent of the domestic rice demand in the first year of opening the market to imports.³⁰⁰ In 1995, the Japanese government imported 410,000 tonnes of foreign rice, mostly from the US, China, Australia and Thailand, according to the MAFF. Of that amount, as much as nearly 70 per cent, or 280,000 tonnes, ended up as inventory kept in case of emergencies, and 90,000 tonnes went towards processed foods such as miso (a soup paste), while just 30,000 - 40,000 tonnes was distributed as rice for straightforward consumption, mostly in ethnic food restaurants, according to a ministry official.³⁰¹ Imported rice was also used as food aid for developing countries, including North Korea.³⁰² In 1997, imports rose to 511,000 tonnes. Combined with the 310,000 tonnes left over as inventories, Japan had 821,000 tonnes of imported rice.

The Minimum Access had led to a slow but steady increase in imported rice. As domestic farmers felt strong pressure from the production surpluses, they realised that a tariff scheme was more effective in protecting domestic agricultural industries from foreign competition. The introduction of the tariff scheme allowed Japan to raise the annual rate of rice imports by only 0.4 per cent during fiscal 1999 and fiscal 2000, compared with 0.8 per cent under the Minimum Access system. At the end of 1998, domestic farmers accepted the government's proposal for a tariff scheme. The ruling LDP, the agricultural ministry and the Zenchu, the farm lobby, agreed to switch from a system of import quotas to tariffication. In April 1999, Japan introduced weight-based tariffs of

²⁹⁹ About Japan's perspective on the conclusion of the agricultural negotiations, see Mitsuibussan-boueki-keizai-kenkyuuzyo, 'WTO – Nihon keizai ha dou kawaruka', (Nihon-Nouritsu-Kyoukai-Management Centre, 1995), P281-283

³⁰⁰ The Japan Times, 9 December 2000

³⁰¹ The Financial Times, 28 April 1998

³⁰² For the issue of Japanese Minimum Access and food aid, see JAPAN ECONOMIC REVIEW, Weekly Review, No.17 – May 1, 1998, 'Food aid and Japan's rice market', (<http://www.jei.org/Archive/JEIR98/9817wN1.html>)

about 1000 per cent, which is a flat tariff of 351.17 yen per kg and cut it to 341 yen per kg in April 2000, in a move that allowed it to avoid boosting the Minimum Access level. Japan was allowed to slow the pace of growth in mandated rice imports if it adopted tariffs before FY 2001.³⁰³ This tariffication raised the price of popular brands of US rice to 500 yen, or 25 per cent more than quality brands of domestic rice. This tariff rate triggered outrage among its trading partners.³⁰⁴ The US and Australian governments immediately expressed concern that 1000 per cent tariffs could cripple their rice exports to Japan.

Objections to the Japanese tariff quota system were also raised by the EC/EU, Argentina and Uruguay. They claimed that the Japanese tariff rates were excessive and would block their agricultural exports to the Japanese market. Under a 1980 decision by the GATT, any WTO member country can raise objections to a change in another member's tariff policy within three months of the change being reported to the WTO secretariat. Despite the objections from some countries, Japan introduced the tariff regime without the WTO's formal recognition. The EC/EU, Australia and Argentina dropped their objections to Japan's tariff scheme soon after it was introduced, as Japan explained that Japanese tariff rates were calculated in compliance with the WTO rules.³⁰⁵ Uruguay, which exports about 5,000 tons of rice to Japan annually, was the only consistent opponent but in the end followed suit after strong persuasion from Japan. As Uruguay withdrew its objections, the WTO secretariat had issued a letter confirming that all 140 WTO members approved Japan's tariff scheme for rice. While the new scheme liberalised Japan's politically sensitive rice market, it levied heavy tariffs on foreign rice imports, except rice imported under the 'Minimum Access' deal.

A government-controlled import system, for example, makes it difficult for retailers to offer steady supplies, even if they wanted to. Under the system, the Japanese government holds a tender for the high quality rice destined for sale to consumers four times a year. The tenders have generally been held every quarter but importers are not given precise information on the timing of the sales or the quantities being offered. As a result, large supermarket operators have no plans to offer customers imported rice, even though they found reasonable demand for the imported rice. The MAFF acknowledged that only a small amount of imported rice goes to supermarkets but said this is simply a result of poor market demand. However, the government clearly has no interest in making

³⁰³ The Japan Times, 9 December 2000

³⁰⁴ The Financial Times, 17 December 1998

³⁰⁵ Naohisa Murakami, 'WTO – Sekaiboueki no yukue to Nihon no sentaku', (Tokyo, Heibonsya, 2001), P132, 133

it easier for consumers to become more familiar with imported rice.

Apart from the interest of protecting its agricultural sectors, another problem the Japanese government faces is that while it has agreed to liberalise the rice market in the Uruguay Round, it faces an excess of domestic production. Japanese consumers have been eating more bread and pasta and less rice. In the year 1997, the surplus came to 3.62 million tonnes.³⁰⁶ The Japanese agreement on Minimum Access at the end of the Uruguay Round was made by a coalition government which did not include the LDP.³⁰⁷ The LDP and the farm lobby have never forgiven the responsible politicians and officials for that. Japan's agreement was registered as a significant defeat and the ruling conservative parties do not want a repeat of that.³⁰⁸ Rice farmers have called for a repeal of the Uruguay Round agreement. There are many members of the ruling LDP who also want to see a repeal of the agreement.³⁰⁹

The main issue for the EU was the export subsidies. In terms of export subsidies, the EU faced cuts in subsidies to its domestic farm producers. Europe has managed to preserve direct payments to farmers as compensation for falling prices. Although income support for farmers must be reduced by 20 per cent in developed countries over the life of the deal – 13.3 per cent in developing countries – the EU gained exemptions for some direct payments. This means farmers could still be paid for growing less and for structural adjustment which is an important part of reform of the CAP. The EU farm industry was predicted to see its income decline in the short term, although this could be attributed more to CAP reform than to the GATT settlement. In the long run, farmers could make up for reductions in the artificially high support prices by increasing output or improving productivity. At the same time, introduction of tariffs for imports rather than NTBs would provide European farmers with even greater protection than they enjoyed before. But these tariffs were going to be reduced by 36 per cent over six years for developed countries, and 24 per cent for developing countries over 10 years.

According to the Uruguay Round agreement, the value of subsidised exports had to be reduced over six years under the terms of the Blair House Accord. The reduction is prescribed as 36 per cent below the base period of 1986 to 1990. At the same time, the

³⁰⁶ The Financial Times, 28 April 1998

³⁰⁷ The Minimum Access deal was made by the non-Liberal Democratic Party administration of Prime Minister Morihiro Hosokawa. On the issue of non-LDP coalition government and tariffication of Japanese rice regime, see S. MacKnight, 'Weekly Review – Japan flip-flop on rice import', No.2, (Japan Economic Institute Report, January 15, 1999) (<http://www.jei.org/Archive/JEIR99/9902w4.html>)

³⁰⁸ The Financial Times, 29 November 1999

³⁰⁹ The Financial Times, 17 December 1998

quantity of these subsidised exports had to be cut by 21 per cent. These provisions almost brought the entire agreement to its knees when the French government called for modifications, fearing their farmers would lose export markets. The US and the EC/EU later agreed to stage the cuts from a higher 1991-1992 base line, allowing European farmers to export an extra 8m tonnes of cereal over the six year period.³¹⁰

In the Uruguay Round, an agreement on cutting and setting a ceiling on the trade-distorting agricultural subsidies was made under American leadership. As a result, the American ceiling was set at 19.1 billion dollars, while the ceiling of the EC/EU was 69 billion euro. In 1996, US Congress passed the Freedom to Farm Act aimed at phasing out subsidies for most agricultural products. The US farm subsidies which were regarded as trade-distorting were reduced substantially to a level below its permitted ceiling. However, while trade-distorting subsidies were reduced, Washington started to provide a series of emergency payments to farmers. These emergency payments pushed up the total amount of US agricultural subsidies and spoiled the previous effort of 1996. Thanks to the introduced emergency payments, the US was suspected of breaking Uruguay Round commitments, although the US insisted that the utmost care was paid to follow the WTO's limits.³¹¹ The Uruguay Round Agreement on Agriculture (URAA), the Sanitary and Phytosanitary (SPS) Agreement (to limit the use of quarantine import restrictions to cases that can be justified scientifically)³¹² and the Dispute Settlement Agreement (which has greatly improved the process of resolving trade conflicts)³¹³, ensured that agricultural trade would be much less chaotic in future compared to the time prior to the formation of the WTO in 1995.³¹⁴ However, even after the introduction of those agreements, defects could be still found in them.

With regard to the food safety issue, the WTO recognises the right of governments to take measures to protect human, animal and plant health, as long as these are based on science, are necessary for health protection, and do not unjustifiably

³¹⁰ The Financial Times 16 December 1993

³¹¹ The Economist, May. 9th 2002, 'Dangerous activities'

³¹² The Agreement on the Application of Sanitary and Phytosanitary Measures (the "SPS Agreement") entered into force on 1 January 1995; see the WTO website, "Understanding the WTO Agreement on Sanitary and Phytosanitary Measures", 1998, (http://www.wto.org/english/tratop_e/sps_e/spsund_e.htm)

³¹³ Rules and procedures for settling disputes were adopted in December 1996; See the WTO website, "Uruguay Round Agreement - understanding on rules and procedures governing the settlement of disputes", (http://www.wto.org/english/docs_e/legal_e/28-dsu_e.htm)

³¹⁴ For the conflicts in relation to the food safety and agricultural biotechnology (such as GM foods) after the Uruguay Round, see Gilbert R. Winham, 'International regime conflict in trade and environment: the Biosafety Protocol and the WTO' in World Trade Review, (Cambridge, Cambridge University Press, 2003), P131-155

discriminate against suppliers. Governments continue to determine the food safety levels and animal and plant health protection in their countries. Neither the WTO nor any other international body does this. The SPS Agreement does, however, encourage governments to 'harmonise' or base their national measures on international standards, guidelines and recommendations, such as those from the Food and Agriculture Organisation (FAO) / World Health Organisation (WHO) / Codex Alimentarius Commission (food safety); the Office International des Epizooties (animal health); and the FAO International Plant Protection Convention (plant health).³¹⁵

In terms of food safety, neither the ruling of the DSB nor the SPS rules say how scientific risk assessment should be conducted, their findings interpreted or, most crucially, how much risk is sufficient to justify trade restrictions. The problem here is that scientific opinion is often not clear cut and is notoriously subject to change. Parts of the SPS rules agreed at US insistence in the Uruguay Round are also ambiguous. It is said that the rules were much affected by US interests. The Clinton administration aimed to stop countries using their food safety rules to keep blocking farm trade, however, it was equally determined to assert its right to bar imports that did not meet its own environmental standards.

Trying to have it both ways created a muddle. These inconsistencies and legal loop holes raise doubts about how far US faith in 'sound science' as the international benchmark for food safety regulations is realistic or politically feasible. In order to deal with the uncertainty of food safety rules, it has been discussed whether the WTO dispute panel should define their applications much more precisely. This means that it is necessary to specify how scientific evidence should be interpreted and set the minimum risk levels required to justify import curbs.³¹⁶

There has been a growing international concern at the use of food safety and animal and plant health regulations as barriers to trade. Increasing use of such actions led to the inclusion of an international agreement on sanitary measures in the Uruguay Round of global trade talks. Many WTO members, especially those from developing countries, fear that new food safety rules could be used as an excuse for protectionism.³¹⁷

Due to the continuing strong protection of agricultural trade by some member countries including the EU and Japan, it was said that the 1993 agreement of the Uruguay Round produced little liberalisation. In fact, tariffs were still set high in some agricultural

³¹⁵ The European Union, 'Agriculture: Continuing the reform', (<http://europa.eu.int/comm>)

³¹⁶ The Financial Times, 23 January 1998 and 15 April 1998

³¹⁷ The Financial Times, 15 April 1998

products importing countries such as Japan. However, the accord at least opened the possibility of further cuts in farm support in a future trade round. Agricultural liberalisation talks remained a critical issue for the EU and Japan.

5. The Seattle Ministerial Conference (30 November – 3 December 1999)

In the Seattle meeting, the EU and Japan were pressing for a broad-based round that would go much further than the already-programmed talks on agriculture and services, the so-called ‘built-in agenda’. They wished for a comprehensive round including tariff cuts for manufactured goods, competition policy and reform of anti-dumping rules. However, the US favoured a narrow round based mainly on negotiating improved market access for goods and services. The EU-Japan’s intention of broadening the agenda was seen as a manoeuvre to dilute inevitable concessions in agriculture.³¹⁸

The text released for the Seattle WTO Ministerial by the EU sent a rather negative message on agriculture. The EU insisted on the aspect of Article 20 of the URAA which could be easily used for protectionist purposes, in particular, by focusing on the effects of implementing the reduction commitments made under the agreement, and by taking into account the “non-trade concerns” (for Article 20 of the URAA and non-trade concerns; see 5-1). However, the EU did not mention the basic fact that Article 20 is titled ‘Continuation of the Reform Process’ and starts by “Recognising that the long-term objective of substantial progressive reductions in support and protection [...]”³¹⁹

The EU text offered no perspective about further EU tariff or export subsidy reductions or tariff-quota increases. Besides, the text stated that the coming negotiations should lead to the renewal of the “peace clause” (a provision that de facto excludes farm subsidies from the WTO dispute settlement regime) and should deal with the elimination of specific barriers, such as state-trading companies, export credit schemes, food aid and loan deficiency payments – all barriers used more by EU trading partners than by the EU. Moreover, the EU’s text insisted on “non-trade concerns” as legitimate restrictions in farm trade (see below 5-1).³²⁰

The initial EU approach was seen as tough negotiating tactics, consisting, at the beginning of the talks, of offering no concessions and demanding maximum concessions

³¹⁸ The Japan Times, 8 December 1999

³¹⁹ The WTO, ‘Agreement of Agriculture Article 20, Continuation of the Reform Process’, (http://www.wto.org/english/docs_e/legal_e/14-ag.doc)

³²⁰ Patrick A. Messerlin, ‘Measuring the costs of protection in Europe – European Commercial Policy in the 2000s’, (Washington DC, Institute for International Economics, 2001), P75-89

from its partners. In November 2000, the EU approved a negotiating proposal including the reduction of tariffs, export subsidies and domestic support. Though the proposal shows the EU's willingness to negotiate, its offers are still very limited: an overall average reduction of tariffs, with a minimum reduction per tariff line (contrary to the traditional EU approach toward manufacturing tariffs); only "further reductions" (not elimination) of export subsidies; and the maintenance of the existing domestic support (subsidy) regime. The EU's proposal was perceived by EU trading partners as open enough that in March 2001 they decided to start the second phase of agriculture talks in the WTO. However, throughout the Seattle Ministerial Meeting, the EU took an overall defensive position. It reflects the very limited domestic reforms achieved by the EU since the Uruguay Round.³²¹

Den Glickman, the then US Agriculture Secretary said that there was a tendency by the EU and other countries to want to preserve the status quo and that this was not acceptable to the US, because the status quo worked to the tremendous disadvantage of the US, which is export-dependent. However, critics accused the US of wanting it both ways, because it continued to protect its own market. Washington was planning 8.7 billion dollars in an emergency farm aid in 1999 to compensate for drought and low prices. Mark Vaile, Australia's Trade Minister said that this US move sent entirely the wrong signal to the international community, particularly to other subsidising countries, in the lead up to Seattle. In the US, some senators were already lobbying for the reintroduction of subsidy regimes. The rationale for that was the EU's failure to liberalise its own agricultural regime. For this reason, Trade Ministers preparing for Seattle believed that the EU must make the first move on agricultural reform. Failure to do so would strengthen the protectionist lobby in the US. However, the EU showed little enthusiasm for farm reform and demanded a broader agenda for the Seattle meeting. Brussels said a comprehensive negotiating agenda was needed, because hard-line EU defenders of the CAP would only agree to liberalise farm trade if they won trade concessions in other areas. Washington and many other leading farm exporting countries suspected the EU was out to thwart agricultural liberalisation by tying the WTO up in negotiations on other issues.³²²

Japan, in its proposal which was made as a preparation for the 1999 ministerial conference, particularly insisted on establishing a set of rules and disciplines which emphasised three objectives.³²³

³²¹ Messerlin, 'Measuring the costs of protection in Europe', P78, 79

³²² The Financial Times 19 November 1999

³²³ The Ministry of Foreign Affairs of Japan, 'Preparations for the 1999 Ministerial Conference Negotiations on Agriculture',

First, Japan insisted on the importance of multifunctionality of agriculture. Japan demanded the WTO to allow a smooth implementation of domestic agricultural policies which take into account differences in natural conditions and of historical background.

Secondly, regarding the multifunctionality of agriculture, Japan particularly emphasised the importance of food security. It mentioned that the instability of food supply/demand in the international market should be taken into consideration. Thirdly, Japan was also keen on redressing the imbalance in rights and obligations under the WTO rules between exporting and importing countries. This is due to Japan's perception that the URAA is not sufficient in terms of fair and equitable trade rules for food importing and exporting countries.

Japan explained its basic stance to the WTO members, particularly the like-minded members which share the idea of the importance of multifunctionality such as the EU, South Korea, Norway and Switzerland. They agreed that they should work in close conjunction in the Seattle negotiations.³²⁴

In order to fill the gaps, diplomats of some WTO member countries, including the US, the EU and Japan, held a meeting as a last attempt to forge a high-level political consensus on the contents of a new round. The EU, Japan, South Korea, Switzerland and Norway argued that the demand by food exporters was going far beyond the goals for the planned negotiations set out in the 1993 Uruguay Round agreement. Food exporters insisted that they would refuse to discuss any other aspects of the agenda until the terms of the planned negotiations on agriculture were settled. The EU acknowledged that agriculture, a key sticking point, was no longer a 'taboo' for the European Union, and indicated that it did not rule out moving towards the application of WTO rules to agriculture in the long-term, but would not accept this as a goal for the next set of global negotiations.³²⁵

Trade negotiations were locked over key portions of the draft declaration by Ministers which was supposed to set out the agenda for a new trade liberalisation round. The US, the EU and the Cairns Group were trying to thrash out a draft text on agriculture that would lay out a limited number of options. The EU opposed the US and Cairns Group's insistence on a reference to the elimination of export subsidies, while the EU was demanding references to food safety, quality and animal welfare, which the US and

(<http://www.mofa.go.jp/policy/economy/wto/min99/agri>)

³²⁴ The Ministry of Agriculture, Forestry and Fisheries, 'Annual Report on Food, Agriculture and Rural Areas in Japan FY1999 (Summary)', (<http://www.maff.go.jp/hakusyo/kaigai/ehakusyo99.htm#CHP1-5>)

³²⁵ The Financial Times 26 October 1999

Cairns Group found unacceptable.³²⁶ Behind the disagreement, there was the EU's effort to rally support behind its demand on agriculture. The EU was working on the draft text with other WTO members, including applicants to join the EU, Japan, Korea and other Asian countries, and South Africa. This plan was intended to galvanise talks on the preparation of the WTO agenda, which had been stalled for months by numerous disagreements over agriculture. This EU move was believed to be a pre-emptive tactic, aimed at Washington. The EU thought the US was trying to gather support for its own position and wanted to get its text on the table first.³²⁷ The European Union initiative was met by accusations that Brussels was trying to minimize the ambitions of new talks on agriculture. Suspicion was aroused, when the EU gathered some WTO members in order to discuss the EU's own version of a Ministerial text. Agricultural products exporting countries furiously criticised this EU move as a very divisive and harmful attempt to create a parallel process, although participants in the group denied this speculation.³²⁸

The negotiations to reduce agricultural protectionism became a major reason for the failure of the Seattle Ministerial Conference. Major agricultural traders had not much in common and agreed on little.³²⁹ The United States and the Cairns Group were pressing for further trade liberalisation on agricultural products. They demanded lower tariffs, cuts in domestic support and an end to export subsidies, which were mostly used by the EU. Developing countries, which depend on agricultural exports, were opposed to the members with a highly protectionist agricultural policy, such as the EU, Japan, South Korea, Norway and Switzerland.³³⁰ The US assailed the EU and Japan for erecting obstacles to reform agricultural trade. The EU and Japan's approach to the new round was criticized for being motivated by a desire to protect their highly distorting agricultural policies. The US also criticized the EU-Japan strategy for having the next round in the form of a 'single undertaking', which meant no agreements could be concluded until all negotiations finish. The US Undersecretary of Commerce, David Aaron argued that the EU-Japan strategy was a 'let's put everything in so nothing comes out' approach.³³¹ The EU, Japan, South Korea, Switzerland and Norway reiterated that demands by Australia and South American agricultural farm exporters to set ambitious objectives for planned

³²⁶ The Financial Times, 22 November 1999

³²⁷ The Financial Times, 1 December 1999

³²⁸ It was reported that a top EU trade official, Peter Carl invited a small group of counterparts to Geneva to discuss on the agricultural trade. / The Financial Times, 12 November 1999

³²⁹ The Economist, November 25th 1999, 'The battle in Seattle'

³³⁰ The Financial Times, 29 November 1999

³³¹ The United States Mission to the European Union, 'Aaron on EU, Japan proposal in WTO', Brussels, Belgium, October 26, 1999, (<http://www.useu.be/issues/aaron1026.html>)

negotiations on farm trade, went too far. Infuriated by this remark, Argentina, which is among the countries pressing for ambitious talks on liberalising agriculture, told the meeting that it would be better not to launch a round in Seattle that started with a flawed agenda.³³²

The Seattle Ministerial Conference failed to launch a new trade round. In Seattle, the negotiating parties were never on the same wavelength, and the meeting ended without any agreement. President Clinton reflected on the meeting and said that the failure of the Ministerial Conference was essentially substantive in nature. He argued, ‘the big blocs here were the Europeans and the Japanese on the one hand, the United States and the developing nations on the other hand. We all had positions that couldn’t be reconciled. The Europeans were not prepared at this time to change their Common Agricultural Policy, which accounts for 85 per cent of the export subsidies in the world. The Japanese had their own agricultural and other issues to deal with. The United States was not prepared to change its policy on dumping...’³³³ After the collapse of the Seattle meeting, the EU and Japan received fierce criticism. The US trade representative, Charlene Barshefsky and the US Undersecretary of State for Economic, Business and Agricultural Affairs, Alan Larson were extremely vocal in their criticism of the EU and Japan. According to them, the failure of the Ministerial Conference was due to the inflexibility by the EU and Japan on agriculture. They reiterated that the EU and Japan should have shown more flexibility on agricultural issues and create the conditions for the next round.³³⁴ While criticising the EU and Japan, it was reported that US President Bill Clinton told US Trade Representative Charlene Barshefsky that the US should also show more flexibility on agricultural issues.³³⁵

5-1. Diverse roles of agriculture and ‘multifunctionality’

During the Seattle Ministerial Conference, the EU and Japan stubbornly insisted that the diverse roles of agriculture should be taken into account in agricultural trade talks. Despite the wide gap in the opinion on agriculture, most countries agreed on the point that agriculture was not merely about producing food and fibre but also included other functions.³³⁶ The focus of the debate in the WTO therefore became whether ‘trade-

³³² The Financial Times, 26 October 1999

³³³ The Japan Times, 20 December 1999

³³⁴ The Financial Times, 9 February 2000

³³⁵ The Japan Times, 4 February 2000

³³⁶ David Blandford, Richard N. Boisvert and Linda Fulponi, ‘Nontrade Concerns: Reconciling domestic policy objectives with freer trade in agricultural products’, (American Agricultural Economics Association, 2003), P668-673

distorting' subsidies are necessary for agriculture to perform its multifunctional roles. Some members argued that all the objectives can and should be solved through non-trade-distorting 'green box' subsidies.³³⁷ These non-trade-distorting subsidies include food security stocks, direct payments to producers, structural adjustment assistance, safety-net programmes, environmental programmes, and regional assistance programmes which are not linked directly to production and prices. Other member countries argued that the non-trade concerns are closely linked to production, therefore subsidies based on production are needed. While the EU, Japan, South Korea and Norway lay emphasis on the need to tackle agricultural diversity as part of the non-trade concerns, some agricultural product exporting countries were concerned that non-trade concerns outside of the 'green-box' might be merely a special and differential treatment for some countries.³³⁸ Some countries argued that not only agriculture but also other economic activities including industry or services equally embrace non-trade concerns. If the WTO addresses non-trade concerns, it should deal with all areas, not only agriculture.³³⁹

Discourse on 'non-trade concerns' became fierce when the WTO circulated a revised draft of the WTO Ministerial Declaration in October 1999. Strong disagreement appeared between the EU and Japan on the one side and members of the Cairns Group and the Association of Southeast Asian Nations (ASEAN) on the other over the EU-Japan demand to include the so-called concept of 'multifunctionality of agriculture' into the revised draft ministerial text. The Cairns Group and the ASEAN countries insisted that 'multifunctionality' was merely a disguise for protectionism. At a meeting of the Commission on Sustainable Development, the Cairns Group expressed "concern at the reintroduction of protectionism, under the guise of the concept of multifunctionality, which could be counterproductive to achieving the goals of sustainable development".³⁴⁰ The EU and Japan argued that more consideration should be paid to the multifunctional role of agriculture, such as rural development, the environment and food security. The EU and Japan wanted Article 20 of the existing Agreement on Agriculture dealing with 'non-trade concerns' to be expanded by 'multifunctionality'.

³³⁷ See, J. Rude, 'Under the Green Box – The WTO and Farm Subsidies', in *Journal of World Trade* 35(5), (The Hague, Kluwer Law International, 2001), P1015-1033

³³⁸ For details on 'non-trade concerns', see the WTO, 'The issue, and where we are now - Non-trade concerns: agriculture can serve many purposes', (http://www.wto.org/english/tratop_e/agric_e/negs_bkgrnd17_agri_e.htm)

³³⁹ 'The WTO; Agriculture negotiations: Background', 'Phase 1: 'Non-trade' concerns and 'multifunctionality': agriculture can serve many purposes', (http://www.wto.org/english/tratop_e/agric_e/negs_bkgrnd10_nontrade_e.htm)

³⁴⁰ Faber Gerrit, 'The concept of multifunctionality and negotiations on agriculture in the WTO', (Utrecht School of Economics, 2002), P2

Article 20 of the Agreement on Agriculture recalls that ‘Commitments under the reform programme should be made in an equitable way among all Members, having regard to non-trade concerns, including food security and the need to protect the environment....’ Although ‘multifunctionality’ is not specifically mentioned, ‘non-trade concerns’ is clearly stated in the agreement.³⁴¹ However, the text does not make clear exactly what non-trade concerns are. This is why the debate on ‘non-trade concerns’ and ‘multifunctionality’ is contentious. The United States argued that the EU-Japan’s concept of ‘multifunctionality’ was not clear, therefore not worth considering until it obtained a better understanding. The United States, the Cairns Group and the ASEAN member countries insisted that agricultural negotiation should be conducted without any exceptions for agricultural products and in the same manner as industrial products.³⁴²

‘Multifunctionality’ is the term which was once coined by Japan, and which became the basic approach of the EU and Japan to the 1999 Seattle Ministerial Conference. The EU, Japan and some other WTO members use the term ‘multifunctionality’ as an ‘operationalisation of non-trade concerns’.³⁴³ The term is an attempt to encapsulate the diverse roles of agriculture. Although agriculture has many functions, the use of the word ‘multifunctionality’ has become a subject of contention. Parts of the disagreement stem from a lack of clarity on what multifunctionality means in practice.

As well as producing secure supplies of food and fibre, agriculture has an impact on the quality of life, in particular on the vitality of rural areas (rural employment, society and cultural heritage), recreation, tourism, biological diversity, soil and water systems, landscape, food quality and safety and the welfare of animals. The term ‘multifunctionality’ covers all of these diverse factors of agriculture. It is also complimentary and linked to sustainable agriculture and rural development. The relative importance of the various functions differs between localities, regions, countries or even groups of countries.

The Japanese particularly emphasised that environmental conservation or

³⁴¹ NGO background papers: World Trade, Food Production and the Diverse Roles of Agriculture – A discussion paper for the attention of delegates to the Intercessional meeting of the Commission for Sustainable Development (CSD 8), (http://csdngo.igc.org/agriculture/agr_rspb.html)

³⁴² Among the Cairns Group, Argentina and Uruguay demanded that the Ministerial text should mention the multifunctional character of trade in other sectors, such as service, intellectual property and trade in other non-agricultural goods. ICTSD Bridges weekly trade news digest, ‘WTO MEMBERS HAGGLE OVER AG DIRECTION’, 25 October 1999 (<http://www.ictsd.org/html/weekly/story2.25-10-99.htm>)

³⁴³ Gerrit, ‘The concept of multifunctionality and negotiations on agriculture in the WTO’, P2

protection of land from natural disasters is closely linked to domestic farming operations, therefore they should be protected.³⁴⁴ The EU defines the term ‘multifunctionality’ as follows: “Apart from its production function, agriculture encompasses other functions such as the preservation, the management and enhancement of the rural landscape, the protection of the environment, including against hazards, and a contribution to the viability of the rural areas”.³⁴⁵ Although the EU’s definition of multifunctionality is quite similar to that of Japan, the EU and Japan stressed different objectives. Japan and Norway stressed food security and the viability of marginal rural areas as the most significant by-products of agriculture.³⁴⁶ EU member states, particularly those in the South, stressed that the main by-product is not biodiversity and environmental protection, but rural development.³⁴⁷

The basic fact that agriculture serves multiple functions is recognised by both the OECD and the FAO. In 1998, an OECD Ministerial Meeting introduced the concept of ‘multifunctionality’ into that organisation, stating that “because of its multifunctional character, agriculture plays a particularly important role in the economic life of rural areas. There can be a role for policy where there is an absence of effective markets for such public goods, where all the costs and benefits are not internalised...”.³⁴⁸ Despite such acknowledgements, the term ‘multifunctionality’ has proved controversial. Its use by particular governments and organisations has generated suspicion that multifunctionality is merely an excuse for defending current agricultural policies and vested interests. Although some criticism of the invention or use of multifunctionality to defend current policy is valid, this does not refute the existence or importance of the multiple functions of agriculture.³⁴⁹

³⁴⁴ The Japan Times, 17 November 1999

³⁴⁵ Gerrit, ‘The concept of multifunctionality and negotiations on agriculture in the WTO’, P2, (http://www.cedla.uva.nl/20_events/PDF_files_news/wto/wto02/The%20Concept%20of%20Multifunctionality,%20Gerrit%20Faber.pdf.)

³⁴⁶ Consideration of multifunctionality is one of the most important points in Japan’s proposal to the WTO, see The Ministry of Foreign Affairs of Japan, ‘Negotiating proposal by Japan on WTO agricultural negotiations’, Committee on Agriculture Special Session, (21 December 2000)

³⁴⁷ Gerrit, ‘The concept of multifunctionality and negotiations on agriculture in the WTO’, P5

³⁴⁸ The OECD carried out the study on ‘Multifunctionality’ under the 1999-2000 Programme of Work of the OECD’s Committee for Agriculture. The study focuses on the production, externality and public aspects of multifunctionality. See OECD (2001), Multifunctionality. Towards an Analytical Framework. Paris, OECD

³⁴⁹ NGO background papers: World Trade, Food Production and the Diverse Roles of Agriculture – A discussion paper for the attention of delegates to the Intercessional meeting of the Commission for Sustainable Development (CSD 8),

Although much of the recent debate has focused on whether to use the term ‘multifunctionality’, the real point at issue is what it implies for actual policy making. Large differences in the degree and nature of multifunctionality exist between regions and between farm types within regions. For example, the availability of agricultural land and its proximity to local communities differs substantially between the EU and the US. This had produced different approaches to agricultural and environment related policies. ‘Multifunctionality’ requires policies tailored to the specific circumstances of different countries and regions. Governments must therefore have the appropriate degree of policy flexibility in accordance with their level of development. The EU and Japan argue that the ‘one-size-fits-all’ model of agriculture is inappropriate and cannot reflect the environmental, social and cultural diversity that exists around the world.³⁵⁰ The EU, Japan, South Korea, Norway and Switzerland which recognise the ‘multifunctional’ role of agriculture also formed a group called ‘multifunctional friends’.

There are powerful arguments against the EU-Japan’s ‘multifunctional’ concept, at least as an argument for broadly based agricultural protection. The US and the Cairns Group strongly disagreed with the idea of ‘multifunctionality’. The Cairns Group did not even accept the concept of ‘multifunctionality’. Japan rejected talks with the Cairns Group, until they accepted the idea of multifunctionality.³⁵¹

The US and Cairns Group’s rejection of ‘multifunctionality’ gained support from some academics. Among the critics, Freeman and Roberts criticise ‘multifunctionality’ for two reasons. Firstly, there are more effective and less costly ways of maintaining what people in society want. Secondly, subsidising agricultural production has been shown to also increase the negative effect of agriculture, including causing ongoing damage to rural environments. Freeman and Roberts argue that if the EU and Japan’s push for the recognition of ‘multifunctionality’ is successful, distortions to world markets and damage to efficient agricultural producers elsewhere, including developing countries, will continue. Potential benefits from trade negotiations on agriculture would be jeopardised. They say ‘multifunctional’ effects apply to all economic activities. Hence, acknowledging their significance specifically in international agreements on agriculture could be constructed as a means of continuing the kinds of exemptions that have so far largely

(http://csdngo.igc.org/agriculture/agr_rspb.html)

³⁵⁰ NGO background papers: World Trade, Food Production and the Diverse Roles of Agriculture

³⁵¹ Hisao Harihara, director of the international economic affairs division at the Ministry of Agriculture, Fisheries and Forestry made clear Japan’s position that unless the Cairns Group changed their attitude, there was no use talking on agriculture with the Group./ The Financial Times, 29 November 1999

excluded agriculture from the benefits of multilateral trade reform.³⁵²

5-2. The limits of EU-Japan cooperation

In spite of the fierce criticism from some WTO members, ‘multifunctionality’ remained the EU-Japan joint strategy in Seattle. Despite the fact that the EU and Japan have considerable differences in the structure of their agricultural sectors, their highly protectionist farming policies enabled them to join forces to fight against the vehement demand from the US and other food exporting countries to liberalise agricultural trade. The relationship between the EU and Japan, especially since the Uruguay Round, can be characterised as forming an alliance on agricultural trade talks. However in the Seattle Ministerial Conferences, the EU and Japan showed symptoms of disharmony in their trade cooperation.

Throughout the agricultural talks in Seattle, Japan took a particularly hard line, while the EU took a slightly more flexible line. The Japanese insisted that they would never agree to trade in farm products being treated in the same way as other industrial goods. Japan also indicated that it wanted more protection for its farm sectors.³⁵³ Meanwhile, the EU was prepared to commit itself to negotiating on export subsidies, domestic support and market access in agriculture, if other WTO members acknowledged that the talks took account of non-economic concerns in the agricultural sector.³⁵⁴

In Seattle, Japan was not happy about the emerging draft text which did not include a reference to the ‘multifunctional nature’ of agriculture. Meanwhile, Pascal Lamy did not discuss whether the EU insisted on including the word ‘multifunctionality’ in the text. The EU appeared to have settled for the term ‘non-trade concerns’, while Japan and Korea wanted stronger language making clear that agricultural trade could not be treated in the same way as other merchandise trade.³⁵⁵

As shown on the stance on multifunctionality, throughout the Seattle meeting, Japan’s negotiating stance on agricultural trade was more rigid than that of the EU. Japan’s stubborn refusal to discuss the agricultural issue raised suspicions that it did not intend to compromise. This is similar to the behaviour of Japanese negotiators in Japan-US trade negotiations. Michael Blaker analysed Japan’s strategy in Japan-US trade negotiations as follows; Japan employs “a wide array of techniques first to try to avoid

³⁵² Freeman & Roberts, ‘Multifunctionality, a pretext for protection?’, (ABARE Current issues, August 1999)

³⁵³ The Financial Times, 26 October 1999

³⁵⁴ The Financial Times, 1 December 1999

³⁵⁵ The Financial Times, 22 November 1999

discussing the subject at all and then to try to minimize the scope of discussions and the content of subsequent compromises.”³⁵⁶ Western diplomats suspected this Japanese reluctance to negotiate as a delaying tactic, in the hope that people would give up on agriculture. It was seen as the best way to achieve a successful round whereby Japan gave in on agriculture in exchange for progress in other areas. Given Japan’s claim to be a champion of the multilateral round, it was unlikely to want to be responsible for ruining the Millennium Round. Besides, while Japan and the US agreed on other issues, Japan was isolated on the issue of agriculture, where even the EU was more accommodating. One trade official criticised Japan’s trade stance saying that the question Japan has been facing is to what degree it is willing to take the opprobrium of being responsible for bringing the round down.³⁵⁷

The limited nature of EU-Japan cooperation on agricultural trade is also illustrated by the two sides’ different position towards the treatment of the Least Developed Countries (LDCs) in the WTO. After the collapse of the Seattle Ministerial Conference, the WTO was trying to put together a trade liberalisation package for the 48 LDCs to ensure their products receive tariff-free and quota-free access to markets in developing countries. The move was spearheaded by Japan, some European countries and Mike Moore, the WTO Director General. The US, the EU and Japan already allow most LDC products into their markets duty free but control sensitive products which, according to the LDCs, account for most of their important exports.

This issue is particularly important for the EU and Japan, as their protectionist agricultural policy is criticised by other WTO members. US Under Secretary of Commerce David Aaron said that the EU and Japan exacerbated the emergence of North-South divisions. He argued that economic development of developing countries is hampered by trade-distorting domestic supports and export subsidies, and tariff peaks which average about 40 per cent, equivalent to the level of industrial tariffs at the end of the Second World War.³⁵⁸ The Japanese Prime Minister, Keizo Obuchi said Japan was ready to open its doors to most goods from the poorest countries provided other developed countries did the same. Japan was trying to champion the cause of Asian nations within the grouping. The Japanese offer, made by Obuchi during his visit to

³⁵⁶ Michael Baker, Paul Giarra and Ezra Vogel, ‘Case Studies in Japanese Negotiating Behavior’, (Washington DC, United States Institute of Peace Press, 2002), P41-67

³⁵⁷ The Financial Times, 29 November 1999

³⁵⁸ The United States Mission to the European Union, ‘Aaron on EU, Japan proposal in WTO’, (Brussels, Belgium, October 26, 1999), (<http://www.useu.be/issues/aaron1026.html>)

United Nations Conference on Trade and Development (UNCTAD), was well received by some European nations but the US was less enthusiastic.³⁵⁹

In April 2000, the 'Quad' members Japan, the United States, Canada and the European Union reached a basic accord to provide preferential trade treatment to the world's poorest nations. Despite the constructive contents of the meeting, 'Quad' members were reluctant to specify the products from the poorest nations that would be entitled to preferential trade treatment because of politically sensitive sectors such as agriculture.³⁶⁰ Ahead of the third United Nations (UN) Conference on the LDCs in May 2001, the UN Secretary General Kofi Annan sent letters to Japan's Prime Minister Yoshiro Mori and leaders of the other major industrialised countries. The letters asked them to take political leadership in opening their markets wider to imports from the world's poorest countries. However, Japan was not able to respond to the expectations of the UN and the world's poorest countries. The ruling LDP was expecting a presidential election in the same year. Under the circumstances, the LDP had no choice but to reject further opening of the agricultural sector, because domestic farmers are traditional LDP supporters. Moreover, the MAFF was waiting for a new trade round. Before the inauguration of a new trade round, they did not want to consider whether to liberalise the agricultural sector. The success of the UN conference was important for the launch of a new trade round, because many developing countries were either opposed or reluctant to new trade talks. They believed that further trade liberalisation would only benefit developed countries at the expense of their interests. In a concession aimed at mitigating the reluctance of developing countries, Japan expanded its preferential import-tariff scheme for LDCs on industrial products, starting a month before the UN conference. However, Japan's preferential scheme did not include a huge chunk of agricultural products.³⁶¹

After this Japanese decision, more drastic concessions came from the EU. The EU announced that it would completely eliminate tariffs on all imports of both industrial and agricultural products from LDCs. The only exception was arms. Franz Fischler emphasised that the EU already imported more agricultural products from developing countries than the US, Australia, Canada, Japan and New Zealand put together; mostly at zero duty or with significant tariff preferences. At the same time, Fischler regretted that no other big operators had yet followed this EU initiative.³⁶² The EU's landmark decision

³⁵⁹ The Financial Times, 14 February 2000

³⁶⁰ The Japan Times, 2 April 2000

³⁶¹ The Japan Times, 27 March 2001

³⁶² The Financial Times, 2 November 2001

to phase out import duties, including those on agricultural products, was in stark contrast to Japan's concessions, which excluded agricultural products. In that regard, while admitting Japan's efforts to grant LDCs greater access to its market, Kofi Annan pointed out that imports from LDCs still accounted for only one per cent of Japan's total imports. Annan also requested Prime Minister Mori to exert his personal influence to increase Japan's imports from LDCs, not only of industrial products but also of agricultural products.

The EU wanted Japan to follow its decision and declare to free tariffs on all imports from the world's poorest countries at an annual summit of leaders from the Group of Eight in Genoa, Italy. Receiving the call from the EU, however, Japanese government officials dismissed the possibility for Japan to follow the EU's example. As the election for the Upper House drew nearer, it was impossible for Japan to take any liberalisation steps on agriculture. The LDP lacked a majority in the Upper House at the time. As the party depended on the farm vote, the party was vehemently opposed to liberalise the Japanese agricultural market. Japan's negative stance on agriculture embraced the possibility that the criticism would come not only from the US, Canada and Australia but also from the EU.³⁶³ In Japan, the Ministry of Economy, Trade and Industry (METI) and the MOFA had informally asked the MAFF to lighten the levies on farm imports. However, the MAFF rejected any concessions in agricultural trade, at least before the WTO trade negotiations on agriculture started. The adamant resistance of the MAFF stems from the fear that if Japan makes any concessions on farm trade before the new round, it will only face more pressure to open the Japanese market once the new round begins. Therefore, the uncompromising stance of the Ministry was an attempt to keep as many bargaining chips as possible for the new round.³⁶⁴

5-3. The EU and Japan after the Seattle Ministerial Conference

After the collapse of the Seattle Ministerial Conference, WTO member countries started with formal WTO talks in March 2000, which were aimed at further agricultural trade liberalization. Unlike in Seattle, the EU suddenly softened its stance on agricultural negotiations. The EU moved to serious negotiations on agricultural trade liberalisation. This EU move was the most positive since the failure of the WTO Ministerial Conference in Seattle. Concrete technical proposals on reducing agricultural support, including export subsidies, were put forward by autumn, alongside a rough timetable for the conduct of

³⁶³ The Japan Times, 7 July 2001

³⁶⁴ The Japan Times, 27 March 2001

negotiations. Despite this positive EU move, there was not much prospect for quick progress in the agricultural talks. The EU, Japan and other nations with protectionist agricultural policies did not have the ability to make more concessions on farm trade, because their concessions were limited by the lack of trade-offs in other areas. However, Brussels hoped that a broader set of trade talks would be launched by the time agricultural negotiators reached the difficult bargaining stage.³⁶⁵

While it showed a positive stance on agricultural liberalisation issues, another confrontation between the EU and other agricultural products exporting countries arose over the issue of the nomination of the chairman on the WTO negotiations. The formal start of WTO talks in March 2000, aimed at further agricultural trade liberalisation, was jeopardised when WTO members failed to agree who should chair the agricultural negotiations. The EU did not accept the nomination of Celso Amorim, Brazil's WTO ambassador and a former Foreign Minister, because Brazil was a member of the Cairns Group of agricultural exporters which was pressing for an end to other farm subsidies. The EU, which originally put forward its own candidate Michael Dowling, the former top official at the Irish Agriculture Ministry, proposed Nacer Benjelloun, the Moroccan WTO ambassador. Amorim, who had the support of most WTO members, was originally proposed as chairman of the sensitive agricultural negotiations. The EU denied any intention of delaying the meeting.³⁶⁶ However, as a consequence of the EU's objection against nominating Amorim as chair for the agricultural talks, the WTO round could not start in time. The EU's rejection raised the question whether the EU was serious about negotiating on agriculture and launching a new trade round.³⁶⁷

Japan, on the other hand, showed reluctance to proceed with agricultural trade talks. In 2001, Japan was expected to host the so-called Farm Trade Forum which has been held every two years since the 1980s, attended by Agricultural Ministers from Japan, the US, Canada, Australia and the EU. The conference's venue has been alternating among its five members, and the last meeting had been held in Montreal in 1999. Although Japan was to act as the host in 2001, it failed to set specific dates for the conference. The delay apparently derived from Japan's reluctance to further liberalise its politically sensitive agricultural sector. With a crucial election for the Upper House in the summer, Prime Minister Yoshiro Mori's government was under even stronger political pressure from his ruling LDP. Under these circumstances, Japan was becoming the target of criticism over its negative stance on further liberalisation of global farm trade.

³⁶⁵ The Financial Times, 14 March 2000

³⁶⁶ The Financial Times, 21 March 2000

³⁶⁷ The Financial Times, 24 March 2000

Therefore, the composition of the five member conference caused Japan particular concerns. As the US, Australia and Canada are staunch advocates of farm liberalisation, the EU is the only ally of Japan among the five economies. However, the MAFF denied any reluctance to convene the meeting. The Ministry declared that Japan was carefully considering the appropriate timing and content. According to the Ministry, even if Japan softened its stance on farm trade and showed willingness toward further liberalisation, Japan would only be able to do so after the WTO members reached an agreement to conduct comprehensive negotiations, covering not only a built-in agenda but also other areas. The MAFF official also acknowledged that the EU was preoccupied by serious domestic issues such as ‘Mad Cow’s Disease’ and was not able to concentrate on global agricultural negotiations.³⁶⁸ In the end, the forum on global agricultural trade did not take place in 2001. Japan wanted to postpone the biannual talks until 2002, because it was difficult for Japan to arrive at any concessions until a new general trade round was launched.³⁶⁹

This abandonment of the biannual Farm Trade Forum by the host nation Japan had been preceded by strong domestic manoeuvres of the farm lobby. At the ruling LDP’s special committee on agricultural trade held in October and November 2000, party legislators representing the farm sector had demanded the abolition of the minimum rice access provision. Representatives of the influential Central Union of Agricultural Cooperatives (Zenchu) attended the committee meetings in support of those legislators. Zenchu complained that rice was being imported at a time when farmers were being forced to reduce paddy acreage. The MAFF cautioned that Japan’s trading partners would not agree to the abolition or reduction of the import quota, but the LDP legislators argued strongly for the protection of farmers.³⁷⁰ In December 2000, several panels of the ruling LDP agreed to call on the government to demand the reduction of the Minimum Access levels on rice imports in the proposals for the next trade round. The decision was made at a meeting of trade-related Cabinet ministers ahead of the submission by WTO members of their proposals for agriculture and services.³⁷¹ LDP members insisted that access amounts should be set appropriately in view of food security as well as the domestic production and consumption level of each country. At the same time, LDP members insisted that Japan’s proposal should not include any specific figure regarding the level of access. This Japanese position differed from the demand of major exporters, such as the

³⁶⁸ The Japan Times, 15 February 2001

³⁶⁹ The Japan Times, 7 July 2001

³⁷⁰ The Japan Times, 7, 8 February 2001

³⁷¹ The Japan Times, 9 December 2000

United States, Australia or other Asian countries. They wanted to see Japan's Minimum Access level increased substantially.³⁷²

Japan's proposal to the WTO in 2001, which included reducing its minimum import quota for rice and creating new safeguards against foreign access to its markets, was based upon the following five major points:

- Consideration of the multifunctionality of agriculture
- Ensuring food security as the basis of society in each country
- Redressing the imbalance between rules and disciplines applied to agricultural products exporting countries and those applied to importing countries
- Consideration for developing countries
- Consideration for the concerns of consumers and civil society

The Japanese government insisted that these five points reflect the general consensus of the people of Japan, after having received opinions from a wide range of members of the society, such as agricultural producers, the food industry, consumers and NGOs. Besides, it was stated clearly in the proposal that Japan was in no position to agree on the outcome of negotiations, if this only enabled a small number of competitive exporting countries to benefit from the international agricultural market.³⁷³

The proposal became controversial among WTO member countries. While it received support from food importing countries such as South Korea and some European countries, farm exporting countries led by Australia severely criticised the Japanese proposal on global farm trade. The latter accused Japan of pushing non-trade concerns at the negotiating table. Japan's position on agricultural trade was regarded as nothing but an excuse for actually putting off talks focused on agriculture. Harsher criticism came from Latin American countries. Uruguay described the Japanese proposal as impracticable and self-serving and said it was just 'a bad joke' to be ignored. The US even argued that Japan's proposal was a more regressive stance than the current agreement reached during the Uruguay Round.³⁷⁴ The MAFF, which had expected such criticism, showed no signs of backing down for domestic political reasons. The US insisted that Japan's proposal

³⁷² The Japan Times, 1 December 2000

³⁷³ The Ministry of Foreign Affairs of Japan, 'Negotiating proposal by Japan on WTO agricultural negotiations', Committee on Agriculture Special Session, (21 December 2000)

³⁷⁴ The Japan Times, 7, 8 February 2001

held back WTO trade talks. Japan's other proposals, including a reduction in the Minimum Access level and invoking safeguard measures, were also criticised and described as a form of protectionism. Japan refuted US criticism saying that Japan's proposals could not be considered as protectionist whereas the US position could be criticised for paying only attention to exporting countries.³⁷⁵

The EU proposal was given a far less critical assessment than Japan's although some WTO members expressed their dissatisfaction with it. However, they recognised the constructive elements of the EU's proposal, although the proposal was judged insufficient in certain areas, including subsidies. The proposal received a more favourable response at the WTO mainly because the EU favoured in general the opening up of its market to developing countries. The EU had to rebuild its CAP ahead of the admission of Eastern European nations. Unlike Japan, the EU wanted to see an early conclusion on negotiations over trade in agricultural products.³⁷⁶

6. Relationship between the EU and Japan in the Doha Ministerial Conference (9-13 November 2001)

Ahead of the Doha Conference, in an unprecedented way of EU-Japan cooperation, the EU and Japan issued a special joint statement at a regular bilateral ministerial meeting in January 2000.³⁷⁷ In the early 2001, in order to cement the cooperation with the EU, Japan's Agriculture, Forestry and Fisheries Minister, Yashio Yatsu went to Europe and held a meeting with EU Agricultural and Fisheries Commissioner Franz Fischler. The meeting called for the relaunch of a new trade round after the failure of the Seattle meeting, but the ministers also reiterated their common position on trade talks. The ministers discussed a wide range of trade issues. They also reconfirmed their common strategy on agricultural negotiation, the 'multifunctionality' of agriculture.³⁷⁸ Although details of the meeting were not made public, it was reported that both sides were satisfied with their discussions.³⁷⁹

However, in addition to reconfirming the common position with the EU, Japan had another agenda for the meeting with the European side. Among the various

³⁷⁵ US Trade Representative, Robert Zoellick held a meeting with Tsutomu Takebe, Japanese Agricultural Minister and criticised Japan's proposal which included the 'multifunctionality' clause. / The Japan Times, 11 July 2001

³⁷⁶ The Nihon Keizai Shimbun, 26 February 2001

³⁷⁷ From the homepage of the Ministry of Foreign Affairs of Japan, 'EU-Japan joint statement on the WTO', (<http://www.mofa.go.jp/region/europe/fmv0001/eu-joint.html>)

³⁷⁸ The Japan Times, 5 January 2000

³⁷⁹ The Japan Times, 17 January 2001

agricultural negotiating issues, Japan's prime concern was how to achieve an international acknowledgement of Japan's stance on Minimum Access. In order to explain Japan's stance on the slow growth in mandated rice imports into Japan, along with the meeting with Fischler, Yatsu had a meeting with WTO Director General Mike Moore, ministers of European Union member states, the FAO and other officials. Yatsu asked them to acknowledge Japan's position on a slower pace of expansion for mandated rice imports.³⁸⁰ His intention highlights the fact that the issue of rice imports was at the centre of Japan's concern among the non-trade concerns, and achieving recognition of its stance on mandated rice was as important as cementing a common strategy with the EU.

6-1. Cooperation between the EU and Japan and their conflicting interests

Starting with Yatsu's visit to Europe, ministers of both the EU and Japan intensified their effort to consolidate their cooperative stance on agriculture. In October 2001, Foreign Ministers of the EU and Japan held meetings in order to reconfirm their trade stances on agricultural issues in the context of a new round.³⁸¹ In a meeting held between Japanese Foreign Minister Makiko Tanaka and European Trade Commissioner Pascal Lamy it was agreed that a ministerial meeting should not set a specific direction on farm trade, and agricultural liberalisation should be promoted in a way that met the requirements of each country. They also reaffirmed their intention to continue their cooperation on agricultural talks and oppose drastic farm trade liberalisation. An important point of their meeting was that Tanaka and Lamy also agreed that Japan and the EU maintain their cooperation on a variety of other issues, such as investment and competition policies and trade rules related to the environment. Lamy called for support from Japan for talks on establishing trade regulations in relation to environmental concerns. In response to this call, Tanaka said that Japan would extend as much support as possible.

However, the stance of both the EU and Japan, which transpired at this meeting, was in striking contrast to that of other major farm products exporting countries. The Cairns Group argued that the ministerial declaration should include specific commitments, such as applying the same rules to agricultural products as those for industrial products and the abolition of export subsidies.³⁸²

In an attempt to tackle the cumbersome agricultural negotiations and to start a new trade round, the WTO launched on 10 November 2001 five days of high-level talks

³⁸⁰ The Japan Times, 17 January 2001

³⁸¹ The Japan Times, 14 October 2001

³⁸² The Japan Times, 14 October 2001

in Doha, Qatar. Thorny issues such as agricultural negotiations remained unsettled even after the 5 day meeting. WTO members had been divided over a draft text setting out guidance for WTO negotiations on agricultural trade even before the Doha meeting. The broadly worded text, compiled by Stuart Harbinson, chairman of the WTO's ruling general council, called for comprehensive negotiations aimed at 'substantial improvements in market access, reductions of all forms of export subsidies and substantial reductions in trade-distorting domestic support'. There were also references to special and differential treatment for developing countries. However, specific wording on agriculture had been omitted from the draft, reflecting the sensitivity and importance of the issue for almost all WTO members. Members of the Cairns Group said the draft text did not go far enough in committing WTO members to slash government aid for farmers, an objective also supported by the US.³⁸³ In particular, the draft text did not refer to the eventual elimination of all trade-distorting domestic subsidies, a key element of the group's platform. The EU and Japan, on the other hand, complained that there was insufficient emphasis on non-trade concerns, such as food safety and protection of the environment, which the text simply says 'will be taken into account'. About 40 ministers discussed non-trade aspects of agriculture, such as food security and environmental conservation. The EU and Japan yet again emphasized the importance of non-trade concerns on agricultural negotiations. The Cairns Group criticised the Japanese argument for lacking clarity in its definition of non-trade concerns. Led by Australia, the Cairns Group reiterated that farm trade should be conducted under the same rules as those of industrial goods.³⁸⁴ The EU, Japan, South Korea, Norway and Switzerland insisted that non-trade concerns should be a prominent component of the WTO negotiations. This, along with negotiations on the environment, was seen by the EU as essential to bring the more reluctant member states such as France on board for big cuts in farm subsidies.³⁸⁵

On the issue of export subsidies, the EU was struggling against overwhelming opposition to water down language in the proposed agenda.³⁸⁶ It was of great importance for WTO members, in particular for developing countries, that the Doha agreement called for the elimination of agricultural export subsidies. However, the matter became more cumbersome when it came to state aids which governments use as political

³⁸³ The Financial Times, 9 October 2001

³⁸⁴ The Japan Times, 11 November 2001

³⁸⁵ The Financial Times, 9 October 2001

³⁸⁶ Thomas C. Beierle, 'Agricultural Trade Liberalisation – Uruguay, Doha, and Beyond', *Journal of World Trade* 36(6), (Hague, Kluwer Law International, 2002), P1089-1110

instruments.³⁸⁷ The EU was under strong pressure from France to reject a reference to ‘phasing out’ farm export subsidies. France was facing elections early the following year. France’s refusal to accept wording in the draft agenda that called for the ‘elimination’ of farm subsidies remained one of the biggest stumbling blocks in negotiations. The Cairns Group was pressing the EU to reduce its generous agricultural subsidies under the CAP, worth 90 billion dollars a year. The Cairns Group insisted that the aim of negotiations should be a substantial reduction in, with a view towards phasing out, agricultural export subsidies. The French Economy Minister, Laurent Fabius said that ‘no European’ could accept such a clause, as it implied a pre-determined endpoint for the negotiation.³⁸⁸ France dropped its opposition only when the EU succeeded, after all-night talks, in inserting a qualification and in obtaining a stronger WTO commitment to negotiate on trade and environment.³⁸⁹ The EU and the US remained divided over the pace and extent of lowering trade barriers to their agricultural markets and how to deal with export subsidies. Besides, the EU in particular insisted that its concessions could be conditional on broader trade-offs being made in a global trade round. It was also demanding comparable reductions in US help for its farming sector, including ‘disaster assistance’ and extensive use of export credits and food aid, which the US rejected. The EU admitted that it was isolated on this particular issue. Even Japan, with its highly protected agricultural sector, was unwilling to back the EU line. Japan and Norway, which also objected to the wording previously, finally declared to accept it. The EU’s intransigence reinforced other countries’ resistance to its attempts to secure WTO negotiations on investment, competition policy and environment, which Brussels said it needed to agree on in the new round.³⁹⁰

The EU was also isolated on the ‘precautionary principles’, which is the right to establish the level of protection that it deems appropriate. It covers cases where scientific evidence is insufficient, inconclusive or uncertain and preliminary scientific evaluation indicates that there are reasonable grounds for concern that the potentially dangerous effects on the environment, human, animal or plant health may be inconsistent with the level of protection chosen by the EU.³⁹¹ The EU noted that agreement on a shared

³⁸⁷ Hoekman, ‘Economic development and the WTO after Doha’, P20

³⁸⁸ BBC News, 14 November 2001, ‘Progress at trade deal talks’

³⁸⁹ The Financial Times, 15 November 2001

³⁹⁰ The Financial Times, 13 November 2001

³⁹¹ European Commission Directorate-General for Agriculture, EU-US and the WTO Agriculture, P3

(www.unece.org/trade/agr/meetings/ean/bangkok_2001_08/market%20access%20eu/eu-us-wto.pdf)

principle for precaution would ensure that it was not an excuse for protectionism. Japan, the US and Brazil asked for clarification from the EU as to the definition of this principle. There was discussion on the status of this principle in public international law. Several delegations noted that WTO rules could accommodate the reasonable use of the concept of precaution. Australia, Malaysia, Brazil, and Norway noted that the application of precaution would vary depending on a case-by-case analysis and, that its use was context-specific.³⁹² Japan made clear that it did not support the idea of 'precautionary principles'.³⁹³ Being isolated on the issue, the EU finally abandoned its plans to try and put the 'precautionary principles' at the heart of trade and environmental issues.³⁹⁴

Overcoming deep divisions, on 14 November 2001, the 142 members of the WTO agreed to launch a new trade liberalisation round. WTO Director General, Mike Moore, called the five-day meeting 'historic'.³⁹⁵ In general, Japan saw its views for the most part reflected in the declaration. Japan was satisfied that the Doha declaration did not require farm products to be subject to the same trade rules as those governing industrial goods. Such commitments had been strongly desired by the Cairns Group, while Japan and others were opposed to setting a specific outcome before the conclusion of farm trade negotiations. Although the EU failed to bring 'precautionary principles' into discussions, both the EU and Japan were satisfied with the inclusion in the Doha declaration of a clause saying that non-trade aspects of agriculture were going to be taken into consideration in liberalizing the agricultural sector.³⁹⁶

6-2. The EU-Japan relationship after the Doha Ministerial Conference

The intensity of the EU-Japan relationship became less visible after the Doha Ministerial Conference. Instead, the EU-Japan relationship after the Doha Ministerial Conference was shaped by the sudden announcement of an American law to subsidise agriculture and relatively strong proposals by the European Union to revise the CAP.

After the new trade round was launched in November 2001 in Doha, a sudden change occurred in US agricultural policy. The US introduced a huge number of farm bills agreed by the House and the Senate. In 2002, an election year, lawmakers of Congress were significantly affected by the political clout from farm states and caved into

³⁹² TRADE AND ENVIRONMENT NEWS BULLETINS, 20 February 2000, Committee on Trade and Environment's (CTE) meeting on 13-14 February 2001, (http://www.wto.org/english/tratop_e/envir_e/te035_e.htm)

³⁹³ The Japan Times, 14 October 2001

³⁹⁴ BBC News, 13 November 2001, 'EU under pressure at trade talks'

³⁹⁵ The Financial Times 15 November 2001

³⁹⁶ The Japan Times, 16 November 2001

their demands. Ann Veneman, Agricultural Secretary under the Bush Administration, suggested a more non trade-distorting support unlinked from production, and more focused on the environment. However, her suggestion was ignored by Congress and did not obtain any support from the President. This sent an incoherent message to the rest of the world. US officials in Geneva pushed trade liberalisation, while lawmakers in Washington decided to provide trade-distorting farm subsidies. Official numbers indicated that the US farm bill would increase government spending on agriculture by 80 per cent, which would account for an additional 82 billion dollars over ten years. Many observers argued that this was a conservative estimate. The bill covered a number of agricultural products. New payments which were adapted to America's biggest crops, such as soybeans, corn and wheat, were related to prices and production and therefore highly trade-distorting.³⁹⁷ On 16 May, before the two-day annual meeting of the OECD in Paris, the US announced that the farm bill kept US domestic agricultural support within the 19,000 million dollar annual limit set by WTO rules and contained a 'circuit breaker' provision which allows the Agricultural Secretary to intervene in case the ceiling is breached. The US insisted that the WTO annual domestic support limit for the EU was more than 61,000 million dollars and for Japan about 31,000 million dollars. As justification of the farm bill, the US insisted that unless there was a negotiation for a new reform package, the US should be allowed to have this level of support.³⁹⁸ Technically, the US farm bill did not breach the WTO commitments, but the introduction of the bill reduced the credibility of the United States as an advocate of the reduction of such subsidies.³⁹⁹

Concurrently with the introduction of the new US farm bill, the EU showed signs of moving towards the reform of its notorious Common Agricultural Policy. In striking contrast with US retrogression from agricultural liberalisation, Franz Fischler delivered, on 10th July 2002, a proposal on the reform of the CAP which aimed at decoupling subsidies and production, while redirecting the use of the CAP at social goals, such as encouraging land use. Under his proposal, farmers would no longer be paid for over-production. Instead, they would receive flat payments.⁴⁰⁰ His proposal was especially supported by NGOs such as Friends of the Earth, WWF, RSPB and Alp Action. According to those organisations, European citizens did not want to waste taxpayers'

³⁹⁷ The Economist, 9 May 2002, 'Dangerous activities'

³⁹⁸ US Department of State, 'US Trade ,Official Outline Position on Steel, Agriculture', (16 May 2002), (<http://usinfo.state.gov/topical/econ/wto99/02051601.htm>)

³⁹⁹ Timothy Josling, 'Key Issue in the World Trade Organizaion Negotiations on Agriculture', (American Agricultural Economics Association, 2003), P663-667

⁴⁰⁰ The Economist, 5 October 2002, 'Cleansing the Augen stables'

money anymore on natural devastation and unhealthy food (destruction of bio-diversity, soil erosion, widespread pollution) and inequality (70 per cent of funding for 20 per cent of farmers), for which the CAP is responsible.⁴⁰¹

In 1999, the EU had negotiated internally a major set of farm reforms, Agenda 2000, and said it would be the basis of its negotiating position in the next round. Trade Commissioner Pascal Lamy insisted the EU was willing to negotiate but not able to say whether it would move further than Agenda 2000.⁴⁰² Agenda 2000 implemented the Common Agricultural Policy's first budget freeze in 40 years but did not agree on the means to achieve it.⁴⁰³ The CAP had notoriously recorded 90 per cent of highly trade-distorting subsidies. The number decreased to 20 per cent in 2000. The CAP's export subsidies had resulted in a huge production surplus and had caused significant expenses for the EU's taxpayers and consumers. Nearly half of the EU's annual budget, around 40 billion Euros (39 billion dollars), was spent on the CAP, benefiting farmers who account for less than 5 per cent of the total workforce. The OECD indicated that when indirect subsidies such as price supports and tax-breaks for farmers are added to direct payments, the aid for farmers accounted for 104 billion Euros in 2001, compared with 50 billion Euros in the US. EU farmers get around 35 per cent of their incomes from subsidies, compared with 21 per cent in the US and 1 per cent in New Zealand.

Despite huge CAP expenses and their main aim to protect small farmers, the CAP in effect promoted the integration of small farmers into large agribusinesses. In accordance with the McSharry reforms set up in the early 1990s, the EU attempted to shift its farm support from production-linked subsidies to direct income payments to farmers. The EU had to tackle urgently the reform of the CAP in consideration of EU enlargement to Central and Eastern Europe.⁴⁰⁴ The ten new member countries were expected to be fierce defenders of the CAP.⁴⁰⁵ The Dutch government unveiled its concern that if the CAP was not reformed before its enlargement of ten new members,

⁴⁰¹ Bulletin Quotidien Europe No.8272, (7 August 2002), 'Climbing Mont Blanc to support proposes CAP reforms' (Agence Europe)

⁴⁰² The Financial Times, 29 November 1999

⁴⁰³ See, George Philippidis and Lionel J. Hubbard, 'Agenda 2000 reform of the CAP and its impacts on member states: a note', Journal of Agricultural Economics, Vol. 54, Number 3, (Agricultural Economics Society, November 2003), P479-486

⁴⁰⁴ For a discussion on the CAP and EU enlargement, see Robert W. Ackrill, 'EU enlargement, the CAP and the cost of direct payments: a note', Journal of Agricultural Economics, Vol. 54, Number 1, (Agricultural Economic Society, March 2003), P73-78 ; Manuel Ahijado Quintillan and Ruben Osuna Guerrero, 'The European Union and Enlargement to the East (1999-2006)', Journal of Political Economy, Vol. 29, No.2, (M.E. Sharpe Inc., Summer 1999), P74-104

⁴⁰⁵ The Economist, 13 July. 13th 2002, 'Cleansing the Augean stables'

farm spending would rise by a further 20 billion Euros a year. In addition to the Netherlands, Germany, Britain and Sweden were pushing for the CAP reform, as they are net payers into the CAP.⁴⁰⁶ However, at the same time, they were prepared to abandon their insistence on immediate reform. They were aware that if they insisted too much on reform, it might cause a delay of EU enlargement.⁴⁰⁷

As for producer support of farmers, American farmers receive almost as much as EU farmers. American agricultural support is, however, conducted through direct payments which are supposed to be separated from prices and production and therefore regarded as less trade-distorting than the CAP in the EU. However, a few years before the Seattle Ministerial Conference, the US provided 'emergency' help to farmers hit by low farm-product prices. The 'emergency' help accounted to 8.7 billion dollars in 1999 (as mentioned in 4-2 and 5). Besides, the US maintains high protection for some agricultural commodities, such as sugar, peanuts and dairy products.⁴⁰⁸

The 2002 US farm bill grants 190 billion dollars to American farmers over ten years. In this regard, if the CAP was reformed in accordance with Fischler's proposals, it was possible for the EU to take a more offensive stance in the agricultural negotiations. However, certainly aware of this possibility, the US unveiled an ambitious proposal about liberalisation of agricultural trade, two weeks after Fischler delivered his CAP reform plan. Aiming at more liberalisation of agricultural trade, the proposal indicated that the US wanted to abolish export subsidies and drastically reduce other trade-distorting farm support over five years. The proposal also demanded negotiators in Doha to set a date for abolishing all tariffs and distorting subsidies.⁴⁰⁹ However, even this ambitious proposal was not enough to mitigate the outrage over the US 2002 farm bill.⁴¹⁰

The Berlin summit in 1999 had established a threshold for the CAP budget until 2006 and permitted its existence until 2013.⁴¹¹ Germany withdrew from its insistence on immediate CAP reform in return for a French promise that from 2007 on, costs would be capped at the 2006 level plus one per cent a year.⁴¹² On January 22nd, Fischler formally unveiled his proposal and reiterated the importance of the CAP reform. He wanted the reform plan to start in 2004, before the new member countries join the EU.

⁴⁰⁶ The Economist, 13 July. 13th 2002, 'Will these modest proposals provoke mayhem down on the farm?'

⁴⁰⁷ The Economist, 5 October 2002, 'Reform? Forget it'

⁴⁰⁸ The Economist, 25 November 1999, 'The battle in Seattle'

⁴⁰⁹ The Economist, 27 November 2002, 'A ray of hope'

⁴¹⁰ The Economist, 31 August 2002, 'Steel, rolled'

⁴¹¹ The Economist, 13 July 2002, 'Cleansing the Augean stables'

⁴¹² The Economist, 2 November 2002, 'Charlemagne'

Japan managed to continue to protect its rice market by applying high tariffs to rice imports beyond a Minimum Access quota.⁴¹³ In 2002, Japan proposed that the WTO set average tariff rate reductions for all farm products and minimum reduction rates for each specific item, thereby enabling member nations to decide more flexibly on cuts as long as they achieve both targets. Behind Japan's proposal was its desire to protect its rice market. This proposal ran counter to the US proposal to substantially cut tariffs across the board. The US proposed that the WTO aim at cutting all tariffs by no more than 25 per cent over a five-year period. Without exception the cuts would mean larger reductions on high tariff items, including rice. The US also called for a 20 per cent across the board rise in minimum tariff-free import quotas, which the Japanese apply to rice. Under this Japanese proposal, similar to the one applied at the Uruguay Round, WTO member countries would be allowed to use their discretion on tariff reductions. Japan, for example, would be able to lower the tariff on rice only by the required minimum rate set for each item, and instead reduce tariffs on other farm products by larger amounts to achieve the overall farm-product average reduction target.⁴¹⁴

Japan was still calling for tariff cuts and other liberalisation steps to be minimised, with individual member countries to have autonomy in addressing market access matters on individual farm products. The Japanese government wanted to buy some time until the domestic agricultural industry increased its global competitiveness, by curbing imports of farm products as much as possible. The WTO negotiations on farm trade covered tariff cuts and other improvements in market access, reductions in export subsidies and cut in subsidies paid to domestic farmers. On matters of market access, Australia and other nations with strong competitive positions were asking for a massive, uniform liberalisation, while European Union members and Japan were seeking to keep high tariffs in place. In addition, Japan intended to ask for a cut in the amount of foreign rice Japan had to import under the WTO's Minimum Access programme, and the establishment of a new form of safeguard measures to block surging imports of fresh vegetables and other products. Japan also sought tough criteria for export subsidies, while asking for flexible rules on the provision of subsidies to domestic farmers.⁴¹⁵

In February 2001, Japan had expressed the expectation that its tariff scheme for rice would finally be recognised by the WTO as a legal trading regime. In April 1999, when Japan had introduced the tariff scheme for its rice imports, it was not approved by the WTO, because of strong opposition from some agricultural products exporting

⁴¹³ The Nihon Keizai Shimbun, 26 July 2002

⁴¹⁴ The Financial Times, 31 July 2002

⁴¹⁵ The Nihon Keizai Shimbun, 24 March 2002

countries, such as the European Union, Australia, Argentina and Uruguay. However, Japan had kept the new scheme running under domestic laws. Under the scheme, high import duties were imposed on foreign rice to protect politically powerful domestic farmers. Agricultural products exporting countries claimed that the Japanese tariff rates were excessive and blocked their agricultural exports to the Japanese market. Under a 1980 decision by the GATT, any WTO member country can raise objections to a change in another member's tariff policy within three months of the change being reported to the WTO secretariat. Despite the objections from some countries, Japan introduced the tariff regime without the WTO's formal recognition. In FY 1999, tariffs of about 351 yen per kg were levied. The EU, Australia and Argentina dropped their objections to Japan's tariff scheme soon after it was introduced. Uruguay, which exports about 5,000 tons of rice to Japan annually, was the only opponent and followed suit only after strong persuasion from Japan. As Uruguay withdrew its objection, the WTO secretariat had issued a letter confirming all 140 WTO members had approved Japan's tariff scheme for rice. While the new scheme liberalised Japan's politically sensitive rice market, it levied heavy tariffs on foreign rice imports, except rice imported under the 'Minimum Access' deal.⁴¹⁶

When the WTO opened a special session on farm trade talks in March 2001, a Japanese delegate spoke on the opening day of the special session. Japan again underscored the importance of the food security issue in agriculture. The delegate used the term 'multifunctionality' of agriculture to support the argument that agriculture should be part of an overall trade liberalisation agenda. Brazil and other farm product exporting countries represented in the meeting urged Japan to take a more positive role on farm liberalisation talks. They warned Japan that it could not expect progress in other areas under negotiation if the WTO failed to make progress on agriculture. Japan reiterated that agriculture required special consideration.⁴¹⁷

Besides, Japan's Agriculture Minister, Tsutomu Takabe, said the common formula on farm trade liberalisation to be worked out by the WTO members should not treat all products uniformly, in effect urging WTO member governments to let Japan exclude rice from the scope of trade liberalisation as part of the new round of multilateral talks. During a meeting with WTO General Council Chairperson Stuart Harbinson, Takebe said that each country has its own unique circumstances, therefore, each member government should be given the flexibility to exclude some items. The liberalisation formula was expected to specify the binding numerical targets of tariff cuts on farm

⁴¹⁶ The Japan Times, 20 February 2001

⁴¹⁷ The Japan Times, 28 March 2001

products and reductions of government subsidies. It calls on member governments to achieve their targets, expressed in percentage terms, over a certain period of time. These targets were put into a multilateral agreement.⁴¹⁸

In the two-day meeting in Nara (July 2002)⁴¹⁹, ministers of five major farm trading regions held a discussion focusing on the issue of increased US farm subsidies. Australia, Canada, the EU and Japan were all against the US law, which critics say runs counter to the WTO's free trade goal. Australia was especially critical of the US law, saying it would affect its export competitiveness. Japan, the EU and Australia agreed on opposition to the new US farm law designed to increase subsidies to US farmers. Canada also expressed concerns. Japan's Agricultural Minister, Tsutomu Takebe expressed his concern that the US was strengthening a tendency toward protectionism. Responding to critics, Ann Veneman argued against the law being branded as protectionism, but said it did not infringe on the country's subsidy cut commitment under the Uruguay Round and would not lead to increasing trade barriers.⁴²⁰

The meeting was meant for ministers to discuss how to proceed with WTO farm negotiations scheduled to set overall targets and rules for member's farm policy reforms by March 2003 as part of a three-year trade round launched in November 2001 in Doha with the deadline set for January 1, 2005. However, Japanese farm minister, Tsutomu Takebe made the most of being the host country of this meeting. Takebe arranged a tour for ministers to see rice paddies and stress the importance of rice from social aspects of agriculture. This was seen as Japan's desperate attempt to include various aspects of agriculture into the WTO farm trade negotiations. Although US Agricultural Secretary, Ann Veneman showed her understanding on the multiple purposes of agriculture, she adamantly demanded Japan to sever the link between such subsidies and production.⁴²¹

US calls for sharp cuts in tariffs on agricultural products and subsidies were intensified in bilateral talks which took place during these multilateral farm talks in Nara. The EU and Japan opposed the US proposal which ran counter to Japan's desire to maintain a high tariff against imported rice and the EU's desire to maintain support for farmers. During farm talks in 2000, Japan had insisted on reducing the Minimum Access

⁴¹⁸ The Nihon Keizai Shimbun, 4 May 2002

⁴¹⁹ Participants at the meeting, the fifth of its kind, were Japanese Agriculture, Forestry and Fisheries Minister Tsutomu Takebe, US Agricultural Secretary Ann Veneman, Agriculture, Fisheries and Forestry Minister, Warren Truss from Australia, Agricultural Minister Lyle Vanclief from Canada and Commissioner for Agriculture, Rural Development and Fisheries Franz Fischler from the EU. / The Nihon Keizai Shimbun, 26 July 2002

⁴²⁰ The Nihon Keizai Shimbun, 26 July 2002

⁴²¹ The Nihon Keizai Shimbun, 26, 27 July 2002

level and maintaining the high tariffs, a position in complete opposition to that of the US. While the US criticised Japan's high tariffs on imported rice, the EU was criticized by the US for its export subsidies. According to the US, back in 1999, the EU had provided about 70 times more subsidies than the US to help agricultural exports. The EU however insisted during the WTO ministerial talks in November 2001 that it would maintain a high level of export subsidies.⁴²²

A new US proposal was met with fierce opposition from other participants. The US proposed that the WTO farm negotiations should target the cutting of all tariffs to no more than 25 per cent, capping trade-distorting domestic subsidies at 5 per cent of farm output and scrapping export subsidies over a five-year period. The proposal was itself a response to unanimous criticism by the other four participants over the new US farm law stipulating an increase in the already heavy subsidies for its domestic agricultural industry. Although the US was in agreement with Australia and Canada over the need for sharp cuts in tariffs and the elimination of farm export subsidies, even the farm ministers from Canada and Australia, along with the EU and Japan, labelled the US farm law 'protectionist'.⁴²³

For the EU and Japan, this US proposal of uniform cuts in tariffs was too drastic, lacking consideration of non-trade functions and leading to unrealistic elimination. The EU and Japan also agreed that the US proposal lacked consistency with the farm policy reform efforts WTO members had made. Japan was against the proposals, since they required more reform from importers than exporters and lacked a commitment to slash export credits. The EU also regarded the proposals as unbalanced saying that they required other farm traders to move more compared with the US, and it was not an appropriate way to find a compromise in the negotiations. The US acknowledged that the proposals were drastic by setting a high starting point. The US hoped to receive support from Australia, New Zealand and other farm-exporting countries for its farm proposals. Australian Agricultural Minister, Warren Truss generally supported the US proposal as constructive but insisted on the abolition of export credits, on which the US subsequently agreed to negotiate specific reform.⁴²⁴

Despite their intensified talks at their two-day meeting, farm ministers merely agreed to continue talks to lead the rest of the world towards farm policy reform, while moving ahead with their own efforts. There was no specific progress of agricultural negotiations, since ministers from the five major trading economies failed to narrow the

⁴²² The Nihon Keizai Shimbun, 26 July 2002

⁴²³ The Nihon Keizai Shimbun, 26 July 2002

⁴²⁴ The Nihon Keizai Shimbun, 26, 27 July 2002

gaps on tariffs and subsidies.

Agriculture remained the arena where the EU and Japan came under pressure from food exporting countries. According to OECD data quoted by the WTO, the EU's support to producers fell from EUR 107.6 billion in 1999 to EUR 97.9 billion in 2000. However, the WTO pointed out that this fall in 2000 would be due less to structural reforms than to the rapid rise in prices on the world market and exchange rate developments.⁴²⁵ Japan still insisted on reducing the Minimum Access level and maintaining the high tariffs.

6-3. A new issue: genetically modified food

As explained above, food safety has been a particular concern for the EU as well as Japan, and no issue has more illustrated this concern than the introduction of genetically modified food.⁴²⁶

Genetically Modified Organisms (GMOs), which are created by genetic engineering, became an industry in 1996, when cotton and maize engineered to be resistant to insecticides and soybeans resistant to weedkiller were grown for profit in significant quantities for the first time.⁴²⁷ In November 1998, the EU and Japan held a first meeting on GM (Genetically Modified) foods, when the third EU-Japan high level consultation on consumer policy was held. The meeting involved ministers of health and welfare of both sides.⁴²⁸ In 1999, the issue of the GM foods came up for discussion at the WTO for the first time, when several members proposed the establishment of a working group in the Organisation to study GMOs in preparation for the Seattle Ministerial Meeting.⁴²⁹ However, since the Seattle Ministerial Meeting in 1999, the issue has not been discussed thoroughly, and no such working group saw the day. So far, only a handful

⁴²⁵ Bulletin Quotidien Europe No.8265, 'WTO gives critical report of EU agricultural and textile policies' (Agence Europe, 29 July 2002)

⁴²⁶ For the history of GM food issue in Europe and the impact of GM food issue on US-EU agricultural trade, see Pew Initiative on Food and Biotechnology, 'U.S. vs. EU: Examination of the trade issues surrounding genetically modified food', 2003 (<http://pewagbiotech.org/resources/issuebriefs/europe.pdf>)

⁴²⁷ NewScientist.com, Andy Coghlan, 'Genetically modified crops: a decade of disagreement', January 2006, (<http://www.newscientist.com/channel/opinion/gm-food/mg18925353.900-genetically-modified-crops-a-decade-of-disagreement.html>)

⁴²⁸ European Union, Delegation of the European Commission to Japan, EU News, 'The Third EU-Japan High Level Consultation on Consumer Policy', (http://jpn.cec.eu.int/home/news_en_newsobj519.php)

⁴²⁹ The WTO, 'SPS Agreement Training Module Chapter 8 – 8.1 Genetically Modified Organisms (GMOs)', (http://www.wto.org/english/tratop_e/sps_e/sps_agreement_cbt_e/c8s1p1_e.htm)

of trade disputes over GMOs⁴³⁰ have been brought to the WTO dispute settlement system.⁴³¹

Despite such a marginal number of trade disputes, the issue of GMOs is likely to be a major issue in the WTO agricultural trade negotiations and in trade disputes also involving the EU and Japan.⁴³² The issue of GMOs has been framed by the sharp differences between the EU and the US. However, Japan has also increasingly become interested in regulating the imports of GMOs from the view point of food safety. However, there have been differences between the EU and Japan on the matter of what kind of rules should be applied to the trade of GM foods.

Japan merely stressed the need for the WTO to address the issue of multilateral rules on GMOs and wanted the current WTO rules to be applied to the trade of GM foods. Japan attested to the efficiency of biotechnology but sought careful application of it in order to secure product safety and achieve public confidence, while it suggested promoting disclosure of information related to the safety of GM food and creating an international database on allergens and genes.⁴³³ Japan, Canada and Australia were pushing for a working group on biotechnology aimed at examining how WTO rules should apply to GM technology. Their proposal was also supported by the United States.⁴³⁴

The EU, on the other hand, considered the current WTO rules were not enough to deal with the issues of GMOs. The EU insisted that the consumers in the Union have a right to ask for protection that did not fall within the existing WTO rules. European Commission president, Romano Prodi called for a European food safety agency and told EU leaders that they must create strong, scientifically-based institutions for evaluating products such as GM foods.⁴³⁵ Franz Fischer suggested that the EU would like to

⁴³⁰ The disputes are against the EU for measures affecting the approval and marketing of biotech products with complaints of Argentina, Canada and the US. (DS293, DS292, DS291)

⁴³¹ The WTO, 'SPS Agreement Training Module Chapter 8 – 8.1 Genetically Modified Organisms (GMOs)'

⁴³² For a discussion on the Genetically Modified Organisms at the WTO, see Grant E. Issac and William A. Kerr, 'Genetically Modified Organisms at the World Trade Organization: A Harvest of Trouble', *Journal of World Trade* 37(6), (Hague, Kluwer Law International, 2003), P1083-1095, see also: The WTO, 'SPS Agreement Training Module Chapter 8 – 8.1 Genetically Modified Organisms (GMOs)', (http://www.wto.org/english/tratop_e/sps_e/sps_agreement_cbt_e/c8s1p1_e.htm)

⁴³³ The Japan Times, 14 March 2000

⁴³⁴ The Economist, 25 November 1999, 'The battle in Seattle'

⁴³⁵ The Financial Times, 16 October 1999

renegotiate the SPS to permit trade restrictions for reasons of consumer preference.⁴³⁶

Moreover, the EU wanted WTO rules to allow the ‘precautionary principles’, which allow member countries to restrict imports, until the safety of GM crops is satisfactorily proven.⁴³⁷ Denmark, together with some other European countries, insisted on ‘precautionary principles’ in order to ban the commercialisation of GM products. Europeans insisted on the need of labelling GM foods due to consumer protection.⁴³⁸ The US, the world’s largest exporter of GM foods, pointed out that food ingredients were altered not only by genetic modification but also by growers’ selection of desirable crops. The US opposed special safety checks only for GM crops.⁴³⁹

As seen above, the discussion on GMOs could become complicated, since the issues of GMOs are related to several WTO agreements, including SPS, Agriculture, Intellectual Property (TRIPS) and Technical Barriers to Trade (TBT). They have been discussed in the Trade and Environment Committee. Trade problems arise when countries have different regulations regarding the testing and approval procedures necessary to place GMOs and their products on the market, or when they disagree about labelling and identification requirements.⁴⁴⁰

Despite differences between the EU and Japan on the introduction of precautionary principles, the EU and Japan share the same stance in the issue of labelling the GM foods. Labelling issue first rose to the surface in relation to the trade of GM corn and soybeans. While accounting for the main producer of GM corn and soybeans, the US was the leading exporter for these commodities. In 1998, out of the 71.6 million acres of soya and the 73.8 million acres of corn grown in the US, 35.2 per cent of the former and

⁴³⁶ Nicholas Perdakis, William A. Kerr and Jill E. Hobbs, *Reforming the WTO to Defuse Potential Trade Conflicts in Genetically Modified Goods*, (Oxford, Blackwell Publishers, 2001), P379-398

⁴³⁷ For the difference between the US and EU in the way of implementing the precautionary approach in the WTO, see H. Ward, ‘Science and Precaution in the Trading System’, International Institute for Sustainable Development, The Royal Institute of International Affairs, (http://www.iisd.org/pdf/sci_precaution.pdf), see also, Peter Handstaff, ‘The Precautionary Principle, Trade and the WTO – a discussion paper for the European Commission Consultation on Trade and Sustainable Development’, (RSPB, 2000)

⁴³⁸ On the issue of labelling GM food products in the relation to the GATT rules on agriculture, see Rex J. Zedalis, ‘Labeling of Genetically Modified Foods’, *Journal of World Trade* 35(2), (Hague, Kluwer Law International, 2001), P301-347; C. F. Runge and L. A. Jackson, ‘Labelling, Trade and Genetically Modified Organisms’, *Journal of World Trade* 34(1), (Hague, Kluwer Law International, 2001), P111-122

⁴³⁹ The Japan Times, 14 March 2000

⁴⁴⁰ The WTO, ‘SPS Agreement Training Module Chapter 8 – 8.1 Genetically Modified Organisms (GMOs)’, (http://www.wto.org/english/tratop_e/sps_e/sps_agreement_cbt_e/c8s1p1_e.htm)

27.0 per cent of the latter were genetically modified.⁴⁴¹

Consumers in the EU, Japan, and some other countries began to demand that their food be produced without GM corn and soybeans. This presented a potential problem for US farmers and processors, because the EU and Japan were two of the largest markets for US corn and soybeans. The EU imported large amounts of soybeans and corn gluten, a byproduct of US ethanol production, while Japan was a large importer of corn and soybeans.⁴⁴²

In particular, labelling of the GM nature of food ingredients was compulsory in the EU.⁴⁴³ Following European moves on GMOs, the Japanese government also introduced labelling requirements for products containing GMOs, in response to consumer concerns.⁴⁴⁴ The tolerance levels for labelling differed among countries. There was a need for processors and traders to meet emerging mandatory GMO-labelling requirements in the EU, Japan along with Switzerland, Australia, New Zealand.

Japan's labelling regulations were perceived much more reasonable than those in the EU. The Japanese government required mandatory labelling when GM material was present in the top three raw ingredients and accounts for 5% or more of the total weight. It also admitted the presence of non-GM labels at the same tolerance level, if produced with identity preservation. For instance, tofu could be made from non-GM soybeans and be labelled as such or else it must be labelled as containing GM material. Exemptions to Japan's labelling requirements included feedstuffs, alcoholic beverages, and processed foods such as soya sauce, corn flakes, and other vegetable oils. In the EU, the threshold applied to each ingredient.

On a larger scale, labelling affects international trade. Consequently, the European and Japanese policy affected the choices of other agricultural exporting countries. Australian GM policies were partially designed to fit the labelling requirement for exports to the EU or Japan. Eastern European countries and Russia have probably decided to follow the EU's 1% threshold labelling requirement for trade reasons.

Along with the labelling issue, as a part of precautionary approach, the EU unilaterally imposed a moratorium on any new GMOs in Europe. The EU's long delays in

⁴⁴¹ Perdakis, William A. Kerr and Jill E. Hobbs, 'Reforming the WTO to Defuse Potential Trade Conflicts in Genetically Modified Goods', P379-398

⁴⁴² Bruce A. Babcock and John Beghin, CARD Briefing Paper 99-BP27, 'Potential Market for Non-GMO Corn and Soybeans', September 1999, (www.card.iastate.edu/publications/DBS/PDFFiles/99bp27.pdf)

⁴⁴³ For the EU legislation for labelling, see EUROPA, The European Commission, 'Economic Impacts of Genetically Modified Crops on the Agri-Food Sector' (<http://ec.europa.eu/agriculture/publi/gmo/fullrep/ch5.htm>)

⁴⁴⁴ The Financial Times, 22 October 1999

approving products, such as genetically modified corn, raised US frustration to boiling point and repeatedly threatened a trade war. The US insisted that there was clearly something wrong when the EU took up to three years to approve products, which the US, Canada and Japan approved in eight to twelve months.⁴⁴⁵

Besides, there was an argument that the EU bans on GMOs had little to do with public safety and much to do with EU agricultural policy. The EU did not want farmers to use techniques which expand output and increase the cost of the Common Agricultural Policy.⁴⁴⁶

Although this moratorium almost certainly broke the WTO rules, the United States initially did not challenge it in the WTO's DSB. US hesitation stemmed from their anxiety that such a lawsuit was politically risky.⁴⁴⁷ It might have not only aggravated European sentiment but also stimulated anti-GMO feeling in the US. Besides, like consumer health or food safety, there were some political differences among nations which the WTO dispute settlement mechanism could not solve.⁴⁴⁸ However, finally on May 13, 2003 the US government filed a complaint with the World Trade Organisation against the European Union's de facto moratorium on genetically engineered organisms.⁴⁴⁹

As seen above, on the issue of GMOs, there was no sight of any EU-Japan cooperation yet. Trade friction seemed to be appearing rather between the EU and the US, while Japan's position remained somewhere between them. On the one hand, advances in food technology were leading to a rapid increase in US production of genetically modified crops. At the same time, the growing influence of farm state representatives in Congress intensified US pressure on other countries to open their markets. On the other hand, the 'mad cow' crisis and other food scares in Europe made consumers and politicians gravely concerned about food safety. Feelings ran highest in Germany, Austria and the Nordic countries, where there had long been mistrust of products that were not naturally produced.⁴⁵⁰

Despite no sign of clear cooperation between the EU and Japan, they were often

⁴⁴⁵ The Financial Times, 15 April 1998

⁴⁴⁶ Hoekman and Kostecki, 'The Political Economy of the World Trading System, second edition', P84

⁴⁴⁷ There are significant policy differences between the US and the EU on the issue of trade of bioengineering foods such as GMO, see Margo Thorning, 'EU and US perspective on Climate, Trade and Bioengineering Policies', (Brussels, the ICCF, 2003), P5, 6 (<http://iccfglobal.org/pdfs/EU&US%20Perspectives071403.PDF>)

⁴⁴⁸ The Economist, 11 May 2002, 'Dangerous activities'

⁴⁴⁹ World Trade Organisation dispute on genetically engineered organisms, May 2006, (<http://eu.greenpeace.org/downloads/gmo/WTObriefing0602.pdf>.)

⁴⁵⁰ The Financial Times, 15 April 1998

criticised together from GM foods exporting countries. US Senator in Iowa, Chuck Gassley also fiercely criticized both the EU and Japan. He stated: 'As far as biotechnology is concerned, the only thing Europe, and now Japan, have to offer is fear. It's how the Europeans have protected their domestic agricultural markets from American competition for 30 years.'⁴⁵¹ He criticized Japan for getting set to require mandatory safety tests on genetically modified foods before they could be imported into Japan. He argued that Japan was taking this action even though genetically modified products produced in the United States must be approved by a food regulatory agency that the world looked to as the model for what a food safety agency should do. Regarding the consumer choice, some observers pointed out that in the EU and Japan, where GM labelling was mandatory, it was virtually impossible to find food products on the shelf labelled as containing GM ingredients. Therefore, the approach taken by the EU and Japan was not really giving consumers a choice.⁴⁵²

Considering the above US accusations against the EU and Japan and the overall controversy regarding GM food, GMO cases are the types of disputes which can be expected to become more frequent in the future. WTO members must deal with differences in regulatory regimes and attitudes towards risk.⁴⁵³ GM food issue might provide the WTO agricultural trade negotiations a new arena where agricultural trade liberalisation talks could be divided not only between the agricultural products exporting countries and importing countries, but also between GM food exporting countries and importing countries of such products. The issue of GMOs is still relatively new. Therefore, nothing can be said firmly on the EU-Japan cooperation on the issue. However, the fact that some countries, particularly the US, started to criticise both the EU and Japan on the issue of GMOs, there will be a possibility in the future that the EU and Japan would seek cooperation between them in order to protect their positions.

Conclusions

This Chapter investigated the development of the EC/EU-Japan relationship during the agricultural negotiations from the Uruguay Round to the Doha Ministerial

⁴⁵¹ From the website of United States Senator of Iowa, Chuck Glassley, 'Grassley Speech on Biotechnology and Trade', 2 May 2000, (<http://grassley.senate.gov/releases/2000/p0r5-02b.htm>)

⁴⁵² Colin A. Carter and Guillaume P Gruere, 'International Approach to Labeling Genetically Modified Foods', Agricultural marketing resource centre, Agricultural Issues Centre University of California and Department of Agricultural and Resource Economics University of California, Davis, March 2003

⁴⁵³ Hoekman and Kostecki, 'The Political Economy of the World Trading System, second edition', P84

Conference focusing on various social actors in each side.

Although both the EU and Japan have a vital stake in the promotion of a more open trade regime, the domestic importance of their agricultural sector, despite its marginal role in the overall economy of both sides, has prevented both economies from playing a more pro-active role in the Uruguay Round and Doha Rounds. First, the Europeans and Japanese did not show cooperative stances during the Uruguay Round, since their industrial structure in agriculture differed from each other. Namely, Japan, as one of the world's largest importer of agricultural products, intended to protect certain sectors of its agricultural market, while the EU, as the largest importer as well as the largest exporter of agricultural products, intended to maintain the CAP.

This chapter showed that the agricultural trade policies of both the EU and Japan are significantly affected by various social forces. 'State' is not unified actor. For instance, Japan's agricultural trade policy is influenced by various intentions from Japanese MITI officials, MAFF officials, politicians of ruling LDP, farms associations such as Nokyo or Zenchu.

The EU and Japan, though their industrial structure in agriculture are so much different, they opted for cooperation due to some shared concerns. What is noted here is that the EU or Japan are not a single decision maker, but their individual trade policies and their cooperation are a result of absorbing the demand from various social forces. Such ties across social forces could be joined internationally with other social forces, and could form an alliance. A good example here is Cairns Group. They are an alliance of both developed and developing nations which is formed only for agricultural issues.

The EU and Japan, on the other hand, intended to create an alliance across shared interests. For this purpose, the EU and Japan created the term, 'multifunctionality' of agriculture and tried to form an alliance internationally. They also extended the discussion on agricultural trade liberalisation to the issue of food safety, food security or even to environmental issues. In this sense, transnational connection among social forces could overcome the difference in industrial structure (as seen in the EU-Japan cooperation) and also the boundaries between the developed and developing countries (as the example of Cairns Group).

The US, the biggest trader for the EU and Japan, has been also concerned about the reaction of social forces. When the EU did not abide the WTO rules in approving GM foods into European market, the US did not challenge it in the WTO's DSB. US hesitation to take the issue to the WTO was due to the concern that such lawsuit might stimulate anti-GMO feelings and therefore politically risky. Since the issues connected to food

safety or food security are sensitive to society, states also need to consider and calculate the social reaction in trade partners. Not only the reaction of trade partners but also reactions of consumers in the export destination became significantly relevant. The case of GM food is a type of dispute that could be more contentious involving many social actors.

Thus, the EU and Japan relationship on agricultural issue can be seen as an attempt of powerful agricultural industry, as social forces, joining internationally. The relation between social forces and the decision making of government will be discussed in chapter 5, the final conclusion.

Chapter 4
EU-Japan relationship on steel trade

Introduction

In this chapter, we will investigate steel trade on which the EU and Japan are actively cooperating. Like agriculture, various social forces, non-state actors are involved in this issue. Adding to the relationship among social forces, this chapter effectively shows how the WTO, as an institution, enables its members to interact with each other.

Steel trade issue involves various trade disputes in the WTO. The EU and Japan have a number of trade disputes with their biggest trade partner, the United States. Steel industries in the EU and Japan, which were adversely affected by the protectionist US trade remedies, do not have membership in the WTO, since they are not 'state'. Therefore, they ask their government to represent their position. Thus, the WTO provides an arena indirectly for various domestic social forces to achieve their goals. Therefore, this chapter will investigate how the international institution facilitates the cooperation for member countries as well as various social forces within members.

Steel is one of the most commonly-used materials in the world. Its properties of elasticity, flexibility and ability of being recycled, coupled with its good value for money, make it the number one amongst those materials which are universally used.⁴⁵⁴ The importance of steel is also due to its multiple usage with a wide range of vital functions in economic life, from construction to machine tools.⁴⁵⁵

Over the past two decades, the EU and Japan have been two of the largest traders of steel products (See Table-7 and -8). The EU has been the largest steel exporter accounting for 11.0 % of world share in 2004. Japan has been the second biggest exporter of steel products accounting for 8.8% of world share in the same year. As an importer, the United States had the largest market accounting for 9.9% of world share in 2004.

⁴⁵⁴ EUROPA, trade issues, sectoral issues, steel sector,
(http://ec.europa.eu/trade/issues/sectoral/industry/steel/index_en.htm)

⁴⁵⁵ UNCTAD, 'New and dynamic sectors: Steel',
(<http://www.unctad.org/Templates/Page.asp?intItemID=3561&lang=1>)

Table-7: Leading steel and iron products exporters in 2004⁴⁵⁶

	Value (billion dollars)	Share in world trade in exports (%)			
		1980	1990	2000	2004
Exporters	2004				
The EU (25) (extra-EU exports)	29.20	-	-	11.4	11.0
Japan	23.29	20.4	11.8	10.4	8.8
The US	8.71	4.2	3.3	4.4	3.3

Source: WTO International Trade Statistics - 2004

Table-8: Leading steel and iron products importers in 2004

	Value (billion dollars)	Share in world trade in imports (%)			
		1980	1990	2000	2004
Importers	2004				
The US	28.12	10.1	9.5	12.5	9.9
The EU (25) (extra-EU imports)	24.34	-	-	7.6	8.6
Japan	5.57	1.1	4.1	2.4	2.0

Source: WTO International Trade Statistics – 2004

Table-9: World merchandise exports by product⁴⁵⁷

	1990	1999	2001
	Share	Share / amount	Share / amount
steel and iron	3.1 %	2.3 % (126 billion dollars)	2.2% (130 billion dollars)
agriculture	12.2 %	9.9 % (544 billion dollars)	9.1% (547 billion dollars)

Source: WTO International Trade Statistics – 2000, 2001

Among trade commodities, however, the steel trade is marginal in terms of world trade (See Table-9). Despite its relatively marginal position, steel trade provides an

⁴⁵⁶ See WTO International Trade Statistics – 2004, Table IV. 34, 'Leading exporters and importers of iron and steel, 2004 /

(http://www.wto.org/english/res_e/statis_e/its2005_e/section4_e/iv34.xls)

⁴⁵⁷ WTO International Trade Statistics – 2000, 2001. World merchandise exports by product, 2000, 2001

interesting insight into EU-Japan relationships in the WTO, since the steel trade caused a number of trade disputes in this institution. Out of all 335 trade disputes in the WTO (from 1995 until the end of 2005)⁴⁵⁸, there are more than 30 trade disputes related to steel products (26 cases are related to agricultural trade).⁴⁵⁹

The EU-Japan relationship on the steel issue is, in the first place, framed by increasing protectionism of the United States especially since 1997 to which the EU and Japan felt the need to reply with lawsuits in the WTO Dispute Settlement System.⁴⁶⁰ Because of the nature of the steel trade issue and its relevance to the GATT/WTO, it is essential to conduct separate investigations on each steel dispute in which the EU and Japan have taken part.

1. Steel trade and its background

1-1. Trade disputes on steel and interdependence of the US, the EU and Japan

Steel trade has witnessed a number of various remedies to address trade disputes. Out of 20 trade disputes regarding CVDs, 6 cases are related to steel products. Out of 60 trade disputes regarding anti-dumping remedies, 16 cases are related to steel products. Out of 34 trade disputes regarding to safeguards, 12 cases are related to steel products.⁴⁶¹ A large number of such import restrictions invoked against steel products effectively proves that steel is a very sensitive product, especially for its importers.

Among various steel trade disputes, the EU and Japan had been involved in 10 and 5 cases respectively (including 4 cases related to the 1916 Act and Byrd Amendment Act) which were all with the United States.

⁴⁵⁸ Dispute settlement; the dispute, 'Chronological list of disputes cases, (http://www.wto.org/english/tratop_e/dispu_e/dispu_status_e.htm)

⁴⁵⁹ For details of the disputes, see WTO home page, 'WTO Dispute settlement: the disputes', index of disputes / (http://www.wto.org/english/tratop_e/dispu_e/dispu_subjects_index_e.htm)

⁴⁶⁰ For the brief explanation of the function of the WTO Dispute Settlement System, see for example: Asif H. Qureshi, 'The World Trade Organisation – Implementing international trade norms', (Manchester, Manchester University Press, 1996), P97-107; and see also: John H. Jackson, 'Designing and implementing effective Dispute Settlement Procedures: WTO Dispute Settlement, Appraisal and Prospects' in Anne O. Krueger (ed), 'The WTO as an International Organisation', (London, The University of Chicago Press, 1998), P161-180

⁴⁶¹ WTO home page, 'WTO Dispute settlement: the disputes', index of disputes

Table-10: Iron and steel imports of the EU and the US by supplier – 1999 & 2001⁴⁶²

	The EU			
	1999		2001	
Suppliers	Value (million dollars)	Share (%)	Value (million dollars)	Share (%)
The US	655	1.1	635	1.2
Japan	402	0.7	486	0.9

	The US			
	1999		2001	
Suppliers	Value (million dollars)	Share (%)	Value (million dollars)	Share (%)
The EU	3994	24.4	4003	26.7
Japan	1772	10.8	1387	9.2

Source: WTO International Trade Statistics – 2000, 2001

Table-10 shows the relationship between the EU, Japan and the US in the steel trade. Both the US and Japan supply a large value of steel products to the EU. (For the EU, the US and Japan are two of the biggest exporters of steel products.) As for the volume of imports, the United States is a far bigger import market for both the EU and Japan. This table clearly shows that both the EU and Japan heavily depend on the US market. The interdependence between the EU, Japan and the US suggests that any drastic change in trade shares or trade amounts between two parties would also significantly affect the third party. There had always been a possibility that a sudden change in the economic environment might shift the balance between three of the biggest steel traders and develop into fierce trade disputes.

Facing steel trade frictions, the US introduced (or threatened to invoke) three different trade measures; 1.) unilateral approaches such as Section 301, 2.) anti-dumping measures and 3.) safeguard measures. Therefore, the chapter is divided into three main sections which explain the EU-Japan relationship in relation to various US trade remedies. The first section briefly outlines unilateral US moves and US bilateral pressure on the EU and Japan. This is followed by an analysis of EU-Japan relationships against various US anti-dumping laws. The third section presents an analysis of EU-Japan relationships

⁴⁶² WTO International Trade Statistics – 2000, IV. Trade by sector, 4.1 Iron and steel, Table IV. 37, 'Iron and steel imports of the EU and the US by supplier, 1999' and International Trade Statistics – 2001, Trade by subject, Table IV. 33, 2001, P26

against US safeguard measures.

The issue of anti-dumping and safeguards are closely related to the various steel trade disputes. For example, in case of Japan, out of 8 cases in which Japan initiated a complain against the United States, 6 cases were related to US anti-dumping or safeguard measures, and most of these measures were related to Japanese steel products.⁴⁶³ In case of the EU, out of 29 cases in which the EU as complaint had trade dispute with the United States, 9 cases are related to US anti-dumping or safeguard measures, and among the 9 cases, more than 4 cases are related to steel products.⁴⁶⁴ Since the issues of anti-dumping and safeguards are closely related to various steel trade disputes of this chapter, they are also going to be analysed briefly.

1-2. Historical background

In the late 1950s, the United States, which has been the largest trading partner for steel for both the EC/EU and Japan, started to suffer from the structural changes in the world's steel market.⁴⁶⁵ Since becoming a net importer of steel in 1959, the American domestic market became increasingly sensitive to world market developments.⁴⁶⁶ As a result, US steel trade policies moved towards protectionism, starting with VRAs (Voluntary Restraint Agreements) in the mid 1980s.⁴⁶⁷

The EC, in the meantime, also started to use protectionist measures. By the 1980s, it became the largest VRA exporter of steel mill products and fabricated steel products because of US-EC agreements. The EC accounted for a share of 42 per cent of VRA exports and 31 per cent of all exports to the US in 1989. The VRAs expired at the end of

⁴⁶³ These 6 anti-dumping cases are: (DS322) Measures relating to zeroing and sunset reviews, (DS249) Definitive safeguard measures on imports of certain steel products, (DS244) Sunset review of anti-dumping duties on corrosion-resistant carbon steel flat products from Japan, (DS184) Continued dumping and subsidy offset act of 2000, (DS217) Anti-dumping measures on certain hot-rolled steel products from Japan, (DS162) Anti-dumping Act of 1916.

⁴⁶⁴ These nine anti-dumping and safeguard cases are: (DS319) Section 776 of the Tariff Act of 1930, (DS294) Laws, Regulations and Methodology for Calculating Dumping Margins (Zeroing), (DS 262) Sunset Reviews of Anti-Dumping and Countervailing Duties on Certain Steel Products from France and Germany, (DS248) Definitive Safeguard Measures on Imports of Certain Steel Products, (DS225) Anti-Dumping Duties on Seamless Pipe from Italy, (Ds217) Continued Dumping and Subsidy Offset Act of 2000, (DS214) Definitive Safeguard Measures on Imports of Steel Wire Rod and Circular Welded Quality Line Pipe, (DS136) Anti-Dumping Act of 1916, (DS63) Anti-Dumping Measures

⁴⁶⁵ For the history of US protection of steel industry, see: Mary A. Yeager, 'Trade Protection as an International Commodity: The Case of Steel', *The Journal of Economic History*, Vol.40, No.1, *The Tasks of Economic History* (March 1980), P 33-42

⁴⁶⁶ Kent Jones, 'Politics vs. Economics in World Steel Trade', (Allen&Unwin Publishers, 1986), P91-102

⁴⁶⁷ Jones, 'Politics vs. Economics in World Steel Trade', P154, 155

March 1992 despite the fact that no international agreement banning subsidies to steel producers had been reached.⁴⁶⁸

Until 1988, the EC even maintained internal national steel production and trading quotas between its member countries, supposedly to allow for orderly capacity reductions to restructure the market. Phillip Oppenheim argues that despite the dismantling of these internal quotas, a series of limitations on imports of non-EC steel, originally imposed in the 1970s, remained in force during the 1980s. These included quotas and provisions, euphemistically referred to as ‘consulting arrangements’ and ‘price monitoring systems’, to ensure that importers do not bring steel in below a certain price. Among the exporting countries, Japan was most seriously affected along with South Korea, Finland and Norway.⁴⁶⁹

The EC also intervened in the EC steel market through subsidisation. Heavy government involvement in the steel industries of several EC member countries not only delayed adjustment, it also tainted trade relations.⁴⁷⁰ The US was also concerned about the trade distortions resulting from subsidies paid to and state aid provided for uneconomic European steel plants.⁴⁷¹

In the 1980s, trade tensions developed between the European and American steel industries. The steel industries in both the EC and US had had to adjust to very changed circumstances.⁴⁷² Demand had shifted towards less steel-intensive products; steel-saving substitution processes were introduced in, for example, the motorcar industry; and new suppliers arrived on the world market. Surplus capacity problems arose in both Europe and America.⁴⁷³

While steel-making capacity in the United States and the EC has declined since 1980, Japan was in the process of restructuring its steel industry and started to become one of the biggest steel exporters.⁴⁷⁴ Consequently, it became inevitable for Japan to have

⁴⁶⁸ Heidensohn, ‘Europe and World Trade’, P134, 135

⁴⁶⁹ Oppenheim, ‘Trade Wars – Japan versus the West’, P62

⁴⁷⁰ Jones, ‘Politics vs. Economics in World Steel Trade’, P157-167

⁴⁷¹ Heidensohn, ‘Europe and World Trade’, P134, 135

⁴⁷² For details on the European steel industry, see; Gernot Klepper, ‘The steel and metal industry’ in David G. Mayes, ‘The European Challenge’, (Hemel Hempstead, Harvester Wheatsheaf, 1991), P372-385

⁴⁷³ Heidensohn, ‘Europe and World Trade’ P134, 135

⁴⁷⁴ On Japan’s industrial promotion in steel sector, see: Hideki Yamawaki, ‘The Steel Industry’, in Ryutaro Komiya, Masahiro Okuno and Kotaro Suzumura (eds), ‘Industrial Policy of Japan’, (Tokyo, Academic Press Japan, 1988), P281-305; On the steel industry in Japan in relation to Japanese governmental promotion and protection, see: Jon Woronoff, ‘Japanese Targeting’, P100-103, P205-208; On Japanese steel industry and governmental support (especially in relation to MITI administrative guidance) see: Shigeto Tsuru, ‘Japan’s Capitalism: creative defeat and beyond’, (Cambridge, Cambridge

frictions with its trade partners on steel.⁴⁷⁵

As the background of the steel trade disputes, Kent Jones best describes the changing structure of the steel market and its development.⁴⁷⁶ According to him, the changing competitive structure of the world steel market triggered a protracted spiral of steel protectionism.⁴⁷⁷ Trade disputes among the big steel traders, such as the EC/EU, Japan and the US started first with steel trade protectionism in the EC/EU and the US, deeply influenced by the pressure from domestic steel industries. Kent Jones argues that developments in the relationship between the steel industry and government had placed trade policy in the US and the EC/EU on a collision course with the US-stated doctrine of open trade adopted in the post-war period. In the United States, an entrenched steel oligopoly had adopted the strategy of pursuing political channels, and was therefore in a strong position to resist. In the EC/EU, the growing trend towards governmental use of the steel industry as a means to build a strong economy indicated the likelihood of massive government intervention in the steel market, including trade restrictions, if adjustment pressures threatened the industry.

The US steel industry enjoyed a significant amount of special protection from imports. From 1969 to 1974, the EC and Japan negotiated VERs that limited their exports to the United States. In 1978, the administration initiated the TPM as part of its programme for the steel industry. The TPM was to have established a minimum price below which imports could not enter without being subjected to an expedited anti-dumping investigation. In 1982, the majority of the integrated US steel producers made an effort to obtain tariff protection under the anti-dumping and CVD laws. The EC agreed to quotas on steel exports of specific products under the US-EC arrangement. The US and the EC agreed to limit EC exports of certain carbon steel products to the United States to specified percentages of US consumption, and the US companies withdrew the anti-dumping and CVD petitions they had filed against the companies in the EC. In the meantime, Japan's steel products were subjected to the US 301 case. The US Trade Representative negotiated a voluntary restraint promise on steel exports with Japan, and Japan was said to provide its estimate of the next quarter's steel shipments to the US. There was a number of formal and informal quantitative restraints on steel imports

University Press, 1993), P98-100; On the Japanese steel industry since the 1950s in relation to MITI, see Ira C. Magaziner and Thomas M. Hout, 'Japanese Industrial Policy', (Berkeley, University of California, Institute of International Studies, 1980), P17-24, P55-67

⁴⁷⁵ Heidensohn, 'Europe and World Trade', P157-167

⁴⁷⁶ Jones, 'Politics vs. Economics in World Steel Trade', P157-167

⁴⁷⁷ Heidensohn, 'Europe and World Trade', P91-102

imposed by the US, thus both the EC and Japan had already significantly limited their exports to the US.⁴⁷⁸

Mary A. Yeager once argued that in the US steel industry, there has been a history of protectionism of artificial interference in natural market processes, and the American steel industry's inclination toward protectionism has been habitual.⁴⁷⁹ In the 1980s and 1990s, even as the US finally sponsored the creation of the WTO to arbitrate trade disputes, Congress also passed legislation which enabled more unilateral retaliation. During the 1980s, concern about Japan was at its height, and there were fears that imported goods would overwhelm the American industry, especially steel, electronics and autos. Despite the decline of those fears, the trade legislation it had engendered lived on.⁴⁸⁰

In the 1980s, world steel consumption had been relatively stable, having reached its highest level ever in 1989. However, in 1990, 1991 and 1992, world steel consumption fell.⁴⁸¹ Since then, steel became one of the most competitive items in world trade, as it faced chronic international overcapacity.⁴⁸²

Adding to the chronic overcapacity of steel products, the Asian financial crisis occurred in 1997, prompting the US to protect itself from a flood of steel imports emanating from its trade partners which in turn affected the US's biggest steel trade partners, the EU and Japan.

2. Steel trade and unilateral measures

2-1. The EU and Japan facing the US

2-1-1. Steel import surge into the US market

With the outbreak of the Asian financial crisis in 1997, steel imports into the US began to rise dramatically. The US trade deficit in the first 11 months of 1998 reached an

⁴⁷⁸ David G. Tarr, 'Costs and benefits to the United States of the 1985 steel import quota program' in Ryuzo Sato and Paul Wachtel (eds), 'Trade friction and economic policy', (Cambridge, Cambridge University Press, 1987), P159-176

For the US-EC steel trade issues see: Kevin Featherstone and Roy H. Ginsberg, 'The United States and the European Union in the 1990s-second edition', (London, Macmillan Press, 1996), 185-188

⁴⁷⁹ Yeager, 'Trade Protection as an International Commodity: The Case of Steel', *The Journal of Economic History*, Vol.40, No.1, *The Tasks of Economic History*, P 33-42

⁴⁸⁰ BBC News, 14. July, 1999, 'Business: The Economy The US arsenal of trade weapons', (http://news.bbc.co.uk/1/hi/business/the_economy/393199.stm)

⁴⁸¹ Jones, 'Politics vs. Economics in World Steel Trade', P91-102

⁴⁸² See: UNCTAD, (iii) Steel and related specialty products, Background note by the UNCTAD secretariat, P6

all-time high of 153 billion dollars.⁴⁸³ The global financial crisis affecting Asia, Russia and parts of Latin America led to shrinking American exports and to a deluge of imports into the still-booming US market.⁴⁸⁴ Among the nations affected by the Asian financial crisis, Japan was hurt more severely than any of the other industrialized countries, mainly due to Japan's strong trade and investment ties in the region. Since the second quarter of 1997, there had been a downturn in Japan's domestic economy. Export demand, mainly to the US, was the only significant source of economic growth.⁴⁸⁵

During 1998, steel producers in Japan, along with Russia and Brazil, captured a large share of the US market. US steel producers accused their rivals of “dumping” and called for the introduction of quotas.⁴⁸⁶ The US government reached agreements with Russia and Brazil on voluntary reductions in steel shipments.⁴⁸⁷ Japan, however, dismissed the idea. Japan claimed that it was America's problem, if its steel industry could not compete internationally. Japan argued that it was the high dollar, not predatory prices, which made Japanese steel competitive. Many industry analysts also pointed out that the success of foreign producers was triggered by the strong dollar, which made their products very cheap. Akira Chihaya, chairman of the Japan Iron and Steel Federation claimed that US mills bought 25 per cent of steel shipped from Japan in 1998 because of a shortage in production capacity.⁴⁸⁸

The EU did not increase its steel exports into the US. On the contrary, according to the UK Steel Association, the EU steel imports had in effect doubled between 1997 and 2001.⁴⁸⁹ Later US pressure on the EU was meant to force the EU to import more steel in order to reduce the pressure of foreign steel imports.

2-1-2. US pressure on Japan for bilateral conflict resolution

⁴⁸³ The Japan Times, 29 January, 1999

⁴⁸⁴ The situation was noted by US Trade Representative Charlene Barshefsky in testimony before a Senate committee in 1999.

⁴⁸⁵ Trade Policy Review of the WTO, on Japan January 1998 noted that Japan's economy had been heavily depending on exports. /

(http://www.wto.org/english/tratop_e/tpr_e/tp69_e.htm)

⁴⁸⁶ BBC News, 13. July, 1999, ‘Business: The Economy US, Russia sign steel deal’, (http://news.bbc.co.uk/1/hi/business/the_economy/393581.stm)

⁴⁸⁷ Russia agreed to limit its exports of steel and other metals to the United States over a five-year period after Washington threatened to introduce quotas and punitive tariffs. The deal was aimed at lifting the threat of Russia being completely excluded from the US market, which could have cost Russia 1.5 billion dollars in export earning over five years. In return, US anti-dumping proceeding against Russian hot-rolled steel was halted.

⁴⁸⁸ The Financial Times, 9 April 1999

⁴⁸⁹ The UK Steel Association, Parliamentary briefing for November 2001, (<http://www.uksteel.org.uk/nw82.htm>)

Facing this import surge the US unilaterally announced in January 1999 that Japan had voluntarily agreed to reduce steel exports. Japan immediately denied the US statement.⁴⁹⁰ US-Japan trade relations further deteriorated when President Bill Clinton, in his State of the Union speech in 1999, indicated his readiness to mount an aggressive defence of the US steel industry and singled out Japan as a prime offender among countries "dumping" steel on the US market.⁴⁹¹ Nobutaka Machimura, Japan's Parliamentary Undersecretary for Foreign Affairs, emphasised Japan's determination to resist US pressure to agree to VERs for steel, as such arrangements violated WTO rules.⁴⁹² The WTO Agreement on Safeguards, Article XIX (Prohibition and Elimination of Certain Measures) clearly stated that "..., a Member shall not seek, take or maintain any VERs, orderly marketing arrangements or any other similar measures on the export or the import side."⁴⁹³ In the past, Japan had concluded a number of VERs with the US. In the GATT era, in most VER cases, exporting countries did not officially announce the conclusion of such VERs. Generally, negotiations for VERs were conducted in private.⁴⁹⁴ These measures were called 'gray area' and had been criticised for their nonconformity with the GATT spirit.⁴⁹⁵

Facing deteriorating relations, the US asked the Japanese government to consider setting up a new economic forum to discuss trade and other matters with the aim of defusing problems, before they caused further friction. Japan welcomed a high-level mechanism to discuss wide-ranging economic issues.⁴⁹⁶ In August 1999, the US proposed formal talks to resolve the protracted dispute over Japanese steel exports to the US. Japan believed that an offer from the US to begin formal, bilateral discussions was based on the

⁴⁹⁰ The Japanese trade ministry's steel division stated that "There is absolutely no truth in the (claim) that we have made a commitment to reduce steel exports to the US." / *The Financial Times*, 9 January 1999

⁴⁹¹ BBC News, 14 July 1999, 'Business: The Economy The US arsenal of trade weapons', (http://news.bbc.co.uk/1/hi/business/the_economy/393199.stm)

⁴⁹² *The Financial Times*, 30 January 1999

⁴⁹³ The Safeguard Agreement was negotiated in large part because GATT Contracting Parties increasingly had been applying a variety of so-called "grey area" measures (Bilateral Voluntary Export Restraints, Orderly Marketing Agreements, and similar measures) to limit imports of certain products. The Agreement now clearly prohibits such measures, and has specific provisions for eliminating those that were in place at the time the WTO Agreement entered into force. / See, Uruguay Round Agreement, Agreement on Safeguards, (http://www.wto.org/english/docs_e/legal_e/25-safeg_e.htm)

⁴⁹⁴ For VERs, see B. Peter Rosendorff, 'Voluntary Export Restraints, Anti-dumping Procedure, and Domestic Politics' in *The American Economic Review*, Vol. 86, No. 3 (American Economic Association, Jun. 1996), P544-561

⁴⁹⁵ Mitsuibussan-boueki-keizai-kenkyuzyo, 'WTO – Nihon keizai ha doukawarunoka', P274-277

⁴⁹⁶ *The Financial Times*, 16 February 1999

misconception that Japan had engaged in unfair trade practices.⁴⁹⁷ Japan made clear that it could not accept any discussions with such prejudice.⁴⁹⁸ Bearing in mind that such bilateral arrangements in the past did not result in favour of Japan, the Japanese government stressed that trade problems in particular should be discussed multilaterally through the World Trade Organisation, rather than bilaterally.⁴⁹⁹

2-1-3. US call for burden sharing on the EU

Further policy measures taken by the US were bound to lead to some relationship between the EU and Japan because they forced both to face challenges from Washington. Without reaching a bilateral agreement with Japan, US frustration was directed against the European Union, one of the largest traders of steel products. There was a view in the US that Europe was not doing its share with respect to absorbing imports, particularly from troubled Asian countries. The Clinton administration therefore called on the European Union for "burden sharing".⁵⁰⁰ The US Secretary of Commerce, William Daley mentioned that the US alone could not absorb all of Asia's exports. He claimed that "We will not be the dumping ground for troubled economies, unless Europe does more, there could be a huge public outcry that is loud enough to rekindle the fires of protectionism." The US was not satisfied with the EU's commitment to sustain a balanced steel trade.

The European Union mentioned emphatically that Europe had no intention of satisfying the US demand. The EU pointed out that European steel imports had grown almost 80 per cent⁵⁰¹ in 1998.⁵⁰² Sir Leon Brittan, Europe's Trade Commissioner, pointed out that although EU imports from Asia were smaller than those by the US, they rose faster in 1999. The EU mentioned that it kept its market open to imports from troubled Asian countries, provided they fulfilled pledges to the IMF to reform and liberalise their economies.⁵⁰³ The EU insisted that the Asian financial crisis hit the EU harder than the US. According to the EU, steel imports into the EU rose by 7 million tonnes, or 43 per cent, in 1998, while exports fell by 4 million tonnes. The EU's balance of trade in steel with third countries fell by 11 million tonnes compared with 1997, while the US balance of trade in

⁴⁹⁷ Masahiko Hosokawa, director of MITI's Americas Division analysed that the US offer to hold the bilateral talk was premised on unfair trade practices by Japan.

⁴⁹⁸ The Financial Times, 18 November 1999

⁴⁹⁹ The Financial Times, 16 February 1999

⁵⁰⁰ The Japan Times, 17 April 1999

⁵⁰¹ According to the Financial Times on 9 January 1999, a spokesman for Sir Leon Brittan, the Trade Commissioner, made a comment that the EU estimated that imports rose by '50 per cent' in 1998.

⁵⁰² BBC News, 21 October 1998, 'Business: The Economy Rodney Smith: Charlene comes to town', (http://news.bbc.co.uk/1/hi/business/the_economy/198212.stm)

⁵⁰³ The Financial Times, 7 November 1998

steel fell by only 9.9 million tonnes.⁵⁰⁴ The EU steel industry was in deep trouble. Demand was down, prices were plummeting. The lack in demand hurt prices.⁵⁰⁵ Facing these problems EU steel makers went through a wave of mergers.⁵⁰⁶

2-1-4. EU and Japanese resistance against US pressure

While putting pressure on Japan toward a bilateral agreement to mitigate its steel exports, the US continued to press the European Union to shoulder more responsibility for reviving global economic growth by removing restrictions on imports from Japan and Russia.⁵⁰⁷ Charlene Barshefsky, US trade representative sought close cooperation on initiatives to liberalise multilateral and transatlantic trade and to discuss trade disputes with the EU.⁵⁰⁸ Her intention reflected concern by the Clinton administration and the will to resist protectionist pressures and maintain support in Congress.⁵⁰⁹

The EU dismissed this criticism and completely ignored the US outcry. In the face of the EU move and a continued flood of steel products, US steel makers started to lobby desperately for support in Congress.⁵¹⁰ These vigorous appeals forced the US government to take Draconian measures towards steel exporters from the following year. US analysts pointed out that placing curbs on Japan, along with Russia, was vital for controlling the surge of imports which were blamed for causing thousands of job losses in the US steel industry.⁵¹¹

Facing tough resistance from the EU and Japan, the US started to exert strong bilateral pressure on some steel exporters which were not WTO members. Since it was not a member of the WTO, Russia finally gave into US pressure and agreed to quotas

⁵⁰⁴ The Financial Times, 13 August 1999

⁵⁰⁵ For example, at the start of 1998, one ton of hot-rolled coil steel sold for 324 dollars in Europe. In 1999, manufacturers were hard pressed to get 230 dollars – a price drop of 29 per cent.

⁵⁰⁶ BBC News, 7 June 1999, 'Business: The Company File Steel industry plays hardball', (http://news.bbc.co.uk/1/hi/business/the_company_file/363051.stm)

⁵⁰⁷ US outcry was due to the fact that since 1997, the EU had agreed restraints with Russia and Ukraine, the biggest exporters of steel products. In that time, the tide of imports from the former Soviet bloc was rising in steel importing countries. Because of the EU agreement with Russia, US imports from Russia doubled to 3 million tonnes in 1997. The US criticized EU agreements with Russia and Ukraine for having caused the diversion of exports to the United States. / The Financial Times, 23 October 1998

⁵⁰⁸ Barshefsky wanted the EU to bring forward from the end of 1999 the deadline for removing curbs which limit sales of Japanese cars, including locally produced models, to about 11 per cent of its market.

⁵⁰⁹ According to Barshefsky, the US purchased twice as much Russian steel as the EU, which restricted imports through quotas. US steelmakers had filed dumping cases against Russian imports. / The Financial Times, 19 October 1998

⁵¹⁰ The Financial Times, 23 October 1998

⁵¹¹ The Financial Times, 23 February 1999

under the threat of duties which would have cut them out of the market altogether.⁵¹² Encouraged by the successful agreement with Russia, in October 2000, the US further warned several countries outside the World Trade Organisation that they must restrain steel exports to the US.⁵¹³ Such a tough US stance with non-WTO members made Japan confirm its policy that trade problems with the US should be discussed through the WTO in order to avoid bilateral pressure from the US.

2-2. US unilateral action

2-2-1. Japan's reaction to Super 301

The EU and Japan's stubborn resistance against US pressure continued, and the US started to resort to tougher trade actions in order to defend the US steel industry. President Clinton threatened to revive Super 301 authority with which he could punish countries which his administration decided were unfair traders. The Super 301 had expired in 1997, but was re-instituted on 31 March 1999. Section 301 (involving 'regular 301', 'super 301' and 'special 301' processes), a provision of the 1974 Trade Act, was the most potent weapon in the US arsenal which authorized not only the investigation of particular goods, but of the trading practices of an entire country.⁵¹⁴ The provisions of the act had been suspended when the WTO was established in 1995.⁵¹⁵

The US revival of Super 301 developed into a serious concern for Japan. It insisted that unilateral sanctions initiated under Super 301 were not acceptable under WTO rules. The US stressed that any action the US took would be consistent with WTO rules and procedures, as strengthening the international trade regime was consistent with US interest.⁵¹⁶ As the US decided to revive the controversial Super 301 procedure, Japan

⁵¹² Russia agreed on 22 February 1999 to suspend its exports of hot-rolled steel to the US for six months, to raise its price and to sharply cut exports in 16 categories, following US threat of big anti-dumping duties. / *The Financial Times*, 23 February 1999

⁵¹³ These included Ukraine, Taiwan and China, which moreover were in advanced talks to become a WTO member. India, which was a WTO member, was also targeted. US steel imports from Ukraine accounted for almost 60 per cent of its exports to the US. The US could not restrict imports from WTO members such as India without violating world trade rules, but was free to do so from countries outside the WTO. / *The Financial Times*, 27 October 2000

⁵¹⁴ For details of Section 301 and its brief history as well as other 301 provisions such as Special 301 and Super 301, see: A. Lynne Puckett and William L. Reynolds, 'Rules, Sanctions and Enforcement under 301: At Odds with the WTO?', *The American Journal of International Law*, Vol.90, No.4, (American Society of International Law, Oct. 1996), P675-689

⁵¹⁵ All formal unilateral actions completed by the US government until 1994 are listed in: Marcus Noland, 'Chasing Phantoms: The Political Economy of USTR' in *International Organization*, Vol. 51, No.3, (the MIT Press, Summer 1997), P368

⁵¹⁶ *The Japan Times*, 29 January, 1999

started market-opening discussions with the US to prevent a trade conflict.

The Iron and Steel Federation of Japan made clear that the industry would take steps toward a complaint with the WTO, if the US imposed sanctions and unilateral restrictions on its steel imports. The chairman of the Federation came to the conclusion that the US steel industry was not hurt by increased imports of Japanese steel, citing "the longer than expected strike" at General Motors in the summer of 1998 as a reason for the decline in domestic steel demand and price drops in the US. The federation was cooperating with the US Department of Commerce and the International Trade Commission in their anti-dumping investigations in response to complaints from the US steel industry. The Iron and Steel Federation of Japan urged Tokyo to file a complaint with the WTO, if Washington resorted to measures such as Super 301 which violated WTO rules. Chihaya, the chairman of the Iron and Steel Federation of Japan pointed out that unilateral import restrictions not only violated WTO rules but also undermined the competitiveness of the US steel mills in the long term.⁵¹⁷ Regarding the domestic situation, he concluded that the steel and iron industry was in a state of overcapacity, and that cut-backs and consolidation were inevitable.⁵¹⁸

As for the Super 301, many analysts, not only those outside the US but also some free-trade advocates within the US viewed these forced negotiations as American bullying. They considered Super 301 as running counter to the multilateral trade regime of the WTO. Michiko Ikeda claimed that if Super 301 was used against a WTO member, it would possibly be illegal under the WTO rules, unless it was used in a field which was not covered by the WTO rules, for instance, practices which might disturb competition, such as Japanese 'Keiretsu.'⁵¹⁹

2-2-2. The EU and unilateral US trade countermeasures

The re-activation of Super 301 by President Clinton, in the context of growing trade tensions, infuriated not only Japan but also the European Union.⁵²⁰ European Union Trade Commissioner, Sir Leon Brittan told the Japanese that Europeans were concerned

⁵¹⁷ The Japan Times, 8 April 1999

⁵¹⁸ Responding to the criticism from Japan, the President of the American Chamber of Commerce in Japan, Glen S. Fukushima claimed that the provision was a "natural part" of US trade policy and not intended to target Japan exclusively. / The Japan Times, Feb. 2, 1999

⁵¹⁹ Ikeda, 'From GATT to the WTO (GATT kara WTO he)', P192

⁵²⁰ The renewal of Super 301 came at a sensitive moment, as the US was seeking authorization from the WTO to retaliate against the EU for alleged failure to comply with the WTO rulings on its banana import arrangements. / The Financial Times, 27 January 1999

about protectionism in the US.⁵²¹ In their view, Super 301 allowed the US government to act as both judge and jury in trade cases.⁵²² In February 1999, the EU made a decision to initiate a procedure against the US on the grounds that US 'fair trade' laws, such as Section 301, were inconsistent with WTO rules.⁵²³ The EU and Japan had repeatedly complained about Section 301, and claimed that it was in violation of the WTO.

Despite its resentment against Super 301, the EU had itself in the past also introduced a general 'unfair trade' provision. Unlike Japan which does not possess any unilateral trade remedies, the EU had introduced, in 1984, the New Commercial Policy Instrument, modelled on US Section 301. The EU had used unilateralist rhetoric in trade relations, for example, in its criticism of domestic regulation in Japan, which limited market access for EU exporters, yet it had not been able to plausibly threaten unilateral measures in the same way as the US.

Therefore, at the conclusion of the Uruguay Round, a number of member governments, led by France, called for the introduction of an EU 'fair trade' instrument with more teeth. The result was the Trade Barriers Regulation (TBR), adopted in December 1994 (TBR replaced the 1984 New Commercial Policy Instrument). This provided the opportunity to act against 'unfair' measures in other countries which inhibited, or prevented, access to third-country markets as well as against 'unfair trade' practices which resulted in, or threatened, material injury to an EU industry. The balance of opinion within the Council of Ministers was against the pursuit of aggressive unilateralism, and hence the TBR was used mainly as a means of identifying potential WTO dispute settlement cases.⁵²⁴ Thus, on unilateral trade remedies, there were differences between the EU and Japan. While the EU exercised such unilateral trade instruments, Japan, in the past, had been targeted by such unilateral measures taken by the US and the EU.

2-2-3. Prohibition of unilateral trade measures under the WTO

The unilateral measures of both the US and the EU were no longer going with the trend of the times. In terms of unilateral trade remedies, such as the TBR or Super 301,

⁵²¹ BBC News, 17. May, 1999, 'Business: The Economy Trade watchdog in trouble', (http://news.bbc.co.uk/1/hi/business/the_economy/346090.stm)

⁵²² BBC News, 14. July, 1999, 'Business: The Economy The US arsenal of trade weapons', (http://news.bbc.co.uk/1/hi/business/the_economy/393199.stm)

⁵²³ 'Foreign Reaction To Reinstitution Of Super 301', FindLaw For Legal Professionals – Japan-US Trade Report Fax, 1996

⁵²⁴ Helen Wallace and William Wallace, 'Policy-Making in the European Union – Fourth Edition', (Oxford, Oxford University Press, 2000), P391, 392

the international institutional context had changed since 1995. The formation of the World Trade Organization greatly inhibited its member countries to use unilateral trade sanctions.⁵²⁵ The creation of the WTO restricted Washington's ability to use Section 301 in order to pry open foreign markets.⁵²⁶ In the GATT era the use of any retaliatory weapon was only challengeable in the GATT, if and when that use was in conflict with the obligations and GATT rules.⁵²⁷ Under the WTO's far stronger dispute settlement mechanism, the US was profoundly constrained in its ability to impose WTO-inconsistent unilateral trade retaliation.⁵²⁸

The EU moved forward on its threat to challenge the mere existence of Section 301 before the WTO. However, the EU's complaint regarding Section 301 was not related to its steel trade with the United States, but originated as part of the US-EU banana dispute.⁵²⁹

On 27 January 2000, the World Trade Organisation adopted a panel ruling that the US could keep its controversial Section 301 trade law as long as it did not take unilateral action against trading partners in violation of WTO rules. The European Union, which had brought the case, decided not to appeal against the panel verdict, which it described as "balanced".⁵³⁰ The panel said that Sections 301-310 of US trade law, which permitted unilateral action against unfair trading practices, were apparently in breach of WTO dispute settlement rules. However, it noted that the US pledged in a formal statement to Congress to abide by the WTO's multilateral procedures, and so far appeared to have done so. The European Union claimed that the report strengthened the WTO system. It required the US not only to respect its existing commitment to avoid unilateral action but to

⁵²⁵ Under Article XXIII of the GATT, it was possible to bring an action against a WTO member, if it was believed that the benefits of membership were nullified, even if there was no violation of the GATT. / H. Wallace & W. Wallace, 'Policy-Making in the European Union – Fourth Edition', P391, 392

⁵²⁶ Previously, the US was ready to retaliate, when target countries did not submit to US demands, aware that denial of access to the lucrative US market could not be successfully challenged in the dysfunctional dispute settlement system of the General Agreements on Tariffs and Trade.

⁵²⁷ The US reinstatement of Super 301 and the threat of action vis-à-vis GATT rules and US obligations under GATT were seen as technically correct, although it was disingenuous. / 'GATT tries to play down US Super 301 action', 4 March 1994, (<http://www.sunsonline.org/trade/process/towards/03040094.htm>)

⁵²⁸ The Japan Times, 17 April 1999

⁵²⁹ 'Foreign Reaction To Reinstitution Of Super 301', FindLaw For Legal Professionals – Japan-US Trade Report Fax, 1996

⁵³⁰ However, a number of developing countries expressed concern at the ruling, saying US legislation should be rewritten. Several developing countries, among them India, Argentina and Hong Kong, complained that the ruling left incompatible legislation in place. / The Financial Times, 28 January 2000

renounce threats of any such action.⁵³¹

The US threat of invoking Section 301 was the first case where the EU and Japan shared the same concern over growing US unilateralism in the steel industry, since world steel traders faced a changing competitive structure of the world steel market after the Asian financial crisis. The case also marked a change in the reactions of the EU and Japan against US bilateral pressure. Facing tough bilateral pressure from the US, the EU and Japan resisted this pressure and were determined to discuss the issue in the WTO.

Despite the January 2000 WTO panel ruling that the US could keep its controversial Section 301 trade law, the US was constrained by its trade partners and the WTO to actually use Section 301. This change forced the US to take more WTO rule abiding trade remedies against foreign imports such as anti-dumping remedies. These anti-dumping remedies are going to be analysed in the next section.

3. Steel trade and anti-dumping measures

3-1. Trade disputes over US anti-dumping measures

3-1-1. Anti-dumping remedies and the GATT/WTO

Anti-dumping duty is one of the few forms of trade restriction permitted under WTO rules. Although it is governed by some WTO-imposed constraints, its practice has been widely criticised as arbitrary and elastic. Therefore, among the instruments of commercial defence, anti-dumping actions are now the most frequently used instrument for 'commercial defence'.⁵³² Article VI of the GATT provides considerable scope for WTO members to apply anti-dumping duties selectively on particular products exported to them, when it is found that these have been dumped. There is no obligation to provide compensation.⁵³³

'Dumping' is the practice of enterprises exporting products at very low prices (below real costs) in order to capture market shares abroad and to eliminate competition. Such practice has been considered to be unfair in international trade. Dumping has the effect that the low price of the imported products may harm the domestic industry which is producing similar products. Although the consumers and industrial users of the product

⁵³¹ The Financial Times, 28 January 2000

⁵³² Marco C.E.J. Bronckers argues the ban on grey area measures in the WTO generated the use of anti-dumping measures by importing countries. See: Marco C.E.J. Bronckers, 'Voluntary Export Restraints and the GATT 1994 Agreement on safeguard' in Jacques H. J. Bourgeois, Frederique Berrod and Eric Gippini Fournier (eds), 'The Uruguay Round Results', (Brussels, European Interuniversity Press, 1995), P275, 276

⁵³³ See, the WTO Uruguay Round Agreement, 'Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994', (http://www.wto.org/english/docs_e/legal_e/19-adp_01_e.htm)

in the importing country may benefit from such low prices, the producer industries usually supported by their labour unions are more vocal for action against dumping.⁵³⁴

In the GATT, the anti-dumping rules were modified during the Kennedy Round (1964-67), when an international anti-dumping code on the implementation of Article VI of the GATT (the article on anti-dumping and CVDs) was successfully negotiated. During the 1980s, Australia, Canada, the EU and the US accounted for about 96 per cent of the anti-dumping / CVD cases filed. The Uruguay Round Agreement on anti-dumping was born to provide more precise rules on the definition of the export prices, the normal value of a product and the conditions of comparing them. It also established more transparent and open procedures to be applied by the national authorities in charge of anti-dumping affairs.⁵³⁵

P. K. M. Tharakan argued that in the past, anti-dumping action was used to force foreign exporters to enter into VERs or to undertake raising prices. In the case of the EU and the US, anti-dumping / CVD actions were basically a flexible tool for preventing imports, whether dumped or not, from causing injury to domestic industry.⁵³⁶ Youichi Nakamura explains that once anti-dumping duties were levied on an imported item, in most of the cases, the item subjected was completely stopped, because the percentage of anti-dumping duties often became huge.⁵³⁷

As more and more countries were introducing anti-dumping measures, in December 1998, Renato Ruggiero, director general of the WTO, noted that the overall number of anti-dumping actions was no higher than the 1992-97 average and was well down on historic peaks.⁵³⁸ However, in a clear reference to the US and the EU, he said anti-dumping use had increased compared with 1995 and 1996, in particular by certain major trading powers and on certain products such as steel.⁵³⁹ Anti-dumping activity was most intense in the steel sector, which accounted for almost 40 per cent of all cases

⁵³⁴ Bhagirath Lal Das, 'The World Trade Organisation – a guide to the framework for international trade', (London, Zed Books Ltd, 1999), P205-224

⁵³⁵ Frederique Berrod, 'The evolution of the rules affecting trade in goods: an introductory note' in Jacques H. J. Bourgeois, Frederique Berrod and Eric Gippini Fournier (eds), 'The Uruguay Round Results', P145

⁵³⁶ P. K. M. Tharakan, 'Political Economy and Contingent Protection', *The Economic Journal*, Vol.105, No.433, (Royal Economic Society, Nov. 1995), P1550-1564

⁵³⁷ Youichi Nakamura, 'WTO ga boueki wo kaeru', (Tokyo, Touyou keizai shinpou sha, 1994), P76-79

⁵³⁸ The comment was based on his assessment of world trade developments over the year to mid-1998 to the WTO's general council.

⁵³⁹ For details of the EU and US anti-dumping policies, see P. A. Messerlin and G. Reed, "Anti-dumping policies in the United States and the European Community", *The Economic Journal*, Vol. 105, No. 433, (Royal Economic Society, Nov. 1995), P1565-1575

opened in 1998.⁵⁴⁰

The US took a particularly aggressive stand on anti-dumping in 1998, for instance by granting expedited procedures for recent suits brought by the domestic steel industry confronted with a flood of imports from Japan and Russia, among others. Anxiety by Washington and Brussels to resist any weakening of their anti-dumping defences had been one reason for a stalemate in discussions over the past two years on possible WTO action relating to competition policy.⁵⁴¹

3-1-2. US invocation of anti-dumping duties

Despite the warning of the WTO director general, the United States started to respond to the import surge of Japanese steel products with fierce anti-dumping actions. Eleven steel import items had been subjected to Washington's dumping investigations since 1997, and the US International Trade Commission ruled against three of the 11 items. In July 1999, Japan aired its concerns to the United States that a series of anti-dumping claims by the US steel industry against steel imports substantially paralysed Japanese exports of most major steel products. Hisamitsu Arai, Vice Minister for International Affairs, told David Aaron, US Undersecretary of Commerce for International Trade that the overuse of anti-dumping suits by the US steel industry was abnormal, even though in 1999, Japanese steel exports to the US declined to levels logged in 1997 before the Asian financial crisis.⁵⁴²

While recognizing that Japanese steel exports to the US declined drastically in 1999, David Aaron, US Undersecretary of Commerce for International Trade insisted that more than 11,000 jobs were lost in the US and two manufacturers went bankrupt in 1998 because of a flood of cheap imports from Japan, Russia and other foreign countries. The US decided to keep a close watch on the level of Japanese steel exports to the US.⁵⁴³ Japan also questioned whether the move by the US Department of Commerce to shorten its investigation period for dumping claims deprived the accused parties of enough time to defend themselves but the US denied this.⁵⁴⁴

3-1-3. The EU and anti-dumping measures

⁵⁴⁰ Many were initiated by developing countries, including Brazil, Indonesia, Mexico and South Africa, some of whose steel exports had been targets of anti-dumping actions by the US and the European Union. / *The Financial Times*, 6 May 1999

⁵⁴¹ *The Financial Times*, 10 December 1998

⁵⁴² *The Japan Times*, July 29 1999

⁵⁴³ *The Japan Times*, July 29 1999

⁵⁴⁴ *The Japan Times*, July 29 1999

Anti-dumping measures were also used by the EC to curb imports from Japan. In the 1980s, the EC had aggressively imposed anti-dumping duties on various Japanese products. The EC-Japan trade imbalance and the EC's structural unemployment and economic depression in the early 1980s added momentum to anti-dumping petitions by Community producers against Japan. The entry into force of the WTO had a great impact on EC/EU trade policy. Contrary to the GATT regime that had tolerated VERs, the WTO Safeguard Agreement provided for the prohibition of new VERs and the progressive elimination of existing VERs (with the exception of Japanese VERs on cars to the EC/EU). Prohibition of VERs in the Euro-Japanese trade would no doubt give weight to anti-dumping and safeguard measures in the EC/EU's arsenal of trade law instruments. Indeed, the EC/EU New Anti-dumping Regulation adopted to implement the WTO Anti-dumping Agreement innovated substantive and procedural rules and, at the same time, gave wide discretion to the anti-dumping authorities.⁵⁴⁵

However, the EU also became the target of the anti-dumping investigation. Up until June 2000, according to WTO notifications, the European Union led the rankings with 49 new anti-dumping investigations, followed by India with 26, Argentina with 23, Australia (18) and Brazil and the US (17 each). The goods from the EU became the main targets of anti-dumping measures. Two-thirds of the 1,229 cases in 1995-99 were directed at poorer nations, headed by China (159) and South Korea (98). The US was the target in 79 cases, followed by Taiwan (60) and Japan (58). UNCTAD claimed there was clear evidence of increased resort to anti-dumping and countervailing measures in sectors such as steel and textiles since 1995, when the WTO banned VERs. At the end of June 2000, in terms of WTO figures, the US had 300 anti-dumping orders and price undertakings in force. The EU came second with 171.⁵⁴⁶

As explained above, since unilateral sanctions or bilateral agreements such as VERs were prohibited under the WTO rules, the anti-dumping act had become a popular remedy to restrict imports, especially for the EU and the US among others. The US took a particularly aggressive stand on anti-dumping, facing a flood of imports from Japan. The US and the EU's inclination toward the use of anti-dumping remedies caused serious concern for Japan. Particularly the US anti-dumping laws targeting Japan's steel exports caused trade conflicts between two economies, and ironically the US anti-dumping laws

⁵⁴⁵ On EC's anti-dumping measures against Japanese products, see: N. Komuro, 'EC Antidumping Measures against Japanese Products', Kobe University, Paper presented for the Third EC-SA-World Conference held at Brussels(European Parliament), 1996, (<http://www.ecsanet.org/conferences/ecsaworld3/komuro.htm>)

⁵⁴⁶ The Financial Times, 7 December 2000

also promoted cooperation between the EU, another heavy user of anti-dumping remedies following the US, and Japan. However, the different positions of the EU and Japan vis-à-vis the US put considerable limitations on any EU-Japan cooperation although both had an interest to efficiently counteract US protectionism. The following sections of this chapter are going to analyse the EU-Japan relationship on US anti-dumping actions.

3-2. The 1916 Anti-dumping Act

3-2-1. US anti-dumping law and EU-Japan

The case of 1916 US Anti-dumping Act is important for EU-Japan relationships, since both the EU and Japan were strongly against the US law. They filed a suit in the WTO DSB, but did so separately. This was due to Japan's expectation that the Clinton-Obuchi summit might provide a breakthrough on this particular issue.

In 1999, a US anti-dumping suit under the 1916 Anti-dumping Act surfaced in the US-Japan steel trade dispute.⁵⁴⁷ The WTO anti-dumping agreement allows governments to impose duties to protect a domestic industry that has suffered from dumping, or the sale of imported goods at unfairly low prices, after due investigation. However, the 1916 law allowed individual firms to file dumping suits with local courts, claiming criminal offence as well as civil liability for compensation that could be as high as three times the damage incurred from dumping. In March 1999, Japan requested the World Trade Organization to rule on the US anti-dumping law, charging that the law was not in compliance with WTO rules.⁵⁴⁸ Japan's WTO appeal was seen as retaliation for growing US pressure on bilateral steel trade.⁵⁴⁹

Although Japan contended that the 1916 Act did not conform to WTO rules on anti-dumping,⁵⁵⁰ Japan was careful with what it requested at the WTO DSB since there were expectations for a positive outcome from the Obuchi-Clinton summit meeting at the White House on 3 May 1999. US-Japan trade disputes over steel and some other sectors, including insurance, flat-glass and telecommunication were expected to be high on the bilateral agenda. Japan chose to refrain from taking any action that could provoke the US Congress, as well as the Clinton administration before the Obuchi-Clinton summit. But

⁵⁴⁷ The US Anti-dumping Act, which had been in force since 1916, provided for a range of civil and criminal penalties against companies and individuals found guilty of dumping including fines, imprisonment and payment of damages.

⁵⁴⁸ Japan's request came after US steel-maker Wheeling-Pittsburgh Steel Corp. used the law to file a lawsuit in Ohio in November 1998 against several foreign firms, including Marubeni Corp., Mitsui & Co., and Itochu Corp. / *The Japan Times*, 11 February 1999

⁵⁴⁹ *The Japan Times*, 11 February 1999

⁵⁵⁰ *The Financial Times*, 29 January 1999

Japan was also playing for time to prepare for a legal battle with the US. Japan was carefully examining the details of the US International Trade Commission judgement and consulting with the Japanese steel companies affected by the rulings.⁵⁵¹

However, Japan was not the only one which resented the US anti-dumping law. The Anti-dumping Act of 1916 was also criticized by the EU. In 1998, the Commission of the European Communities and Japan, after having won no concession during the Obuchi-Clinton summit, separately requested consultations with the US regarding the inconsistency between the sanctions permitted under the 1916 law and those permitted under WTO agreements.⁵⁵² After the failure to resolve the matter, the EU filed a complaint with the WTO over the US Anti-dumping Act of 1916 when an American steel company invoked it to file a suit with a local court in 1996 against a US-based European importer of steel products. The EU's complaint received strong backing from Japan. The WTO's DSB decided early in 1999 to set up a neutral panel to rule on the EU complaint against the American law.⁵⁵³ Japan filed a separate complaint on 11 February 1999. The US immediately expressed disappointment that Japan had followed the EU to the WTO but vowed to vigorously defend the law.⁵⁵⁴

3-2-2. WTO ruling on the US 1916 Anti-dumping Act

As a result of the separate cases brought forward by the EU and Japan, two separate WTO dispute settlement panels stated in final verdicts early in 2000 that the US 1916 Anti-dumping Act violated WTO rules. After the final ruling of the DSB, there was a possibility for the US to appeal the decision to the Appellate Body, the WTO's highest court. However, it is quite rare that the Appellate Body delivers a verdict different from the one handed down by a dispute settlement panel.

Despite the negative prospect, the US appealed the case to the Appellate Body. In July 2000, the WTO Appellate Body met in Geneva for its first and final hearing on the case.⁵⁵⁵ At the end of August 2000, the WTO Appellate Body acknowledged claims from the EU and Japan and ruled that the US must change its 84-year-old anti-dumping law.⁵⁵⁶

Although the US claimed that the 1916 Act was more akin to an antitrust statute

⁵⁵¹ The Japan Times, 15 April 1999

⁵⁵² 'WTO Decision striking down US revenue act of 1916', The American Journal of International Law, Vol.95, No.1, (American Society of International Law, Jan. 2001), P147-149

⁵⁵³ The Japan Times, 10 March 1999

⁵⁵⁴ The Financial Times, 12 February 1999

⁵⁵⁵ The Japan Times, 18 July 2000

⁵⁵⁶ In its original ruling, the WTO asserted that the WTO anti-dumping agreement only allowed member states to impose import duties on goods dumped in their market.

than an anti-dumping statute,⁵⁵⁷ the WTO dismissed the claim.⁵⁵⁸ Accepting the WTO ruling, the US asked the WTO for a ‘reasonable period of time’, i.e. 15 months, for implementation, after consultations with the EU and Japan.⁵⁵⁹ The US argued that it would need until December 2001 to get Congress to make the necessary changes. Both the European Union and Japan pressed for a more accelerated timetable, and in 2000 requested binding arbitration. While Congress in 2000 approved a big change to US tax law to comply with another WTO ruling, legislators were generally reluctant to change US laws to comply with WTO decisions. Although both the EU and Japan were annoyed by the US request for delay, a legislative amendment was particularly difficult in the case of the US anti-dumping law because of the influence of the steel industry.

In February 2001, an independent WTO arbitrator ruled in favour of the EU and Japan and stated that the US must remove a controversial provision of its anti-dumping laws before 26 July 2001. The decision put considerable pressure on the Bush administration, which was forced to seek early congressional action to change the law.⁵⁶⁰

In the case of the US 1916 anti-dumping act, the EU and Japan shared the same concern, since the law negatively affected their steel exports to the US. However, despite this common concern, Japan had shown some hesitation before the Obuchi-Clinton summit, hoping to achieve a bilateral resolution. Japan’s expectation effectively demonstrated the nature of Japan’s US-focused bilateralism.

Although the summit did not resolve the dispute between the US and Japan, Japan’s hesitation prevented EU-Japan cooperation against the US anti-dumping law. Although there was no visible relationship between the EU and Japan, the WTO acknowledged their separate claims and ruled against the US law. In spite of the lack of clear relationship, the case against US 1916 anti-dumping law was seen as a significant

⁵⁵⁷ The United States Mission to the European Union claimed that “Despite its popular name, the 1916 Act was not the anti-dumping law under which the Import Administration of the Department of Commerce applies anti-dumping duties. Instead, it addresses anticompetitive practices and is more akin to an antitrust statute than an anti-dumping statute”. / The United States Mission to the European Union, August 28, 2000, ‘WTO Appellate Body upholds panel ruling against US Revenue Act of 1916’, (<http://www.useu.be/Categories/Antitrust/Aug2800WTOAntidumpingUS1916.html>)

⁵⁵⁸ The Appellate Body argued that the WTO anti-dumping rules were applicable to the 1916 Act and that the Act was inconsistent with these rules, because the civil and criminal penalties provided for in the 1916 Act went beyond the responses which those rules authorized. / “United States Anti-dumping Act of 1916”, (<http://www.ebearing.com/legislation/1916act.htm>)

⁵⁵⁹ For details, see “WTO Arbitrators Decisions – United States – Anti-dumping Act of 1916 – Arbitration under Article 21.3(c) of the Understanding on Rules and Procedures Governing the Settlement of Disputes – Award of the Arbitrator[2001]WTOARB6(28 February 2001)”, (<http://www.worldlii.org/int/cases/WTOARB/2001/6.html>)

⁵⁶⁰ The Financial Times, 1 March 2001

victory for the EU and Japan.⁵⁶¹

3-3. The anti-dumping case on hot-rolled steel

3-3-1. The US anti-dumping act against Japan's hot-rolled steel

One of the steel products which caused a particular outcry during the steel conflict after the Asian financial crisis was hot-rolled steel.⁵⁶² The dispute about the US anti-dumping act against Japanese hot-rolled steel deserves special attention in the context of our research because Japan did not gain any support from the European Union despite the implications of the US anti-dumping action for the EU as well.

The dispute on hot-rolled steel started at the end of the 90s, when a huge amount of Japanese hot-rolled steel was directed to the United States due to its robust economy. US imports of hot-rolled steel from Japan increased more than five times in 1998, and the US bought 10 times more Japanese steel than the European Union did. William Daley, US Commerce Secretary noted that the surge in imports of hot-rolled steel from Japan for 1998 represented a 385 per cent rise over 1997.⁵⁶³ The US became visibly frustrated with these Japanese exports.⁵⁶⁴

In September 1999, the US steel industry first filed a complaint with the US International Trade Commission over alleged dumping by Japanese exporters of hot-rolled steel. Since then, roughly 80 per cent of all Japanese steel exported to the US was subject to anti-dumping measures or investigation. These drastic US measures caused tremendous damage to Japanese steel exports. Together with Japan 24 other economies were also subject to US dumping charges. International Trade and Industry Minister, Takashi Fukaya, announced in a hastily called press conference on 20th October 1999 that Japan had decided to take formal steps also on behalf of those other 24 economies.⁵⁶⁵

⁵⁶¹ Despite the adverse WTO ruling, the US did not repeal the law for more than three years after the ruling. See, EUROPA Trade Issues, 'EU seeks retaliatory and protective measures in US 1916 Anti-dumping Act dispute', Brussels, 22 September 2003, (http://europa.eu.int/comm/trade/issues/respectrules/anti_dumping/pr220903_en.htm)

⁵⁶² See: J. Daniel Stirk, 'United States – Anti-dumping measures on certain hot-rolled steel products from Japan: possibilities and predictions for compliance with the appellate body's report', in 'Law and policy in international business, Vol.33' (2002), P683-716

⁵⁶³ The Financial Times, 29 January 1999

⁵⁶⁴ Meanwhile, three Japanese steel producers filed complaints with a US court against anti-dumping tariffs imposed by the US government on hot-rolled steel imports. Nippon Steel, Kawasaki Steel and NKK filed complaints with the US Court of International Trade, stating that duties ranging from 17.86 per cent to 67.14 per cent were inappropriate. The duties were imposed after the International Trade Commission ruled in June 1999 that imports of Japanese hot-rolled steel products had hurt US industry. / The Financial Times, 1 September 1999

⁵⁶⁵ Japan claimed that the United States overestimated the degree of damage the Japanese imports caused to the US market, by miscalculating the dumping margins. /

3-3-2. Japan's complaint to the WTO

Nearly one month after Fukaya's announcement of filing a complaint, Japan finally brought the case to the WTO on 23 November 1999. There was speculation over the reason why Japan waited nearly one month to take action.⁵⁶⁶ In most of the previous cases where Japan filed complaints with the WTO against one of its trading partners, the country had actually done so only several days or even hours after announcing a decision to take action.

Ahead of the WTO ministerial talks, it was seen that Japan was rallying support from other WTO members on the hot-rolled steel dispute with the US.⁵⁶⁷ To prevent an abuse of anti-dumping measures by its trading partners, especially the US, Japan strongly insisted on putting a thorough review of the WTO's anti-dumping trade provisions on the formal agenda for the new round and tighten the anti-dumping rules. The WTO Ministerial Meeting in Seattle was held for four days starting on 30 November 1999 to officially launch a new round of global trade liberalization negotiations. However, since the US vehemently objected to that idea, Japan was looking for an ally on the anti-dumping issue. Therefore, synchronised with the legal battle in the WTO DSB, Japan was preparing for the Seattle Ministerial Meeting.

Although Japan denied such speculations of rallying support, the anti-dumping case on hot-rolled steel was seen to have some impact on Japan's tough stance on the review of WTO anti-dumping rules. The next section of this chapter is going to analyse the issue of the review of anti-dumping rules. (See: 2-3. Enforcement of WTO anti-dumping rules).

3-3-3. WTO ruling against the US anti-dumping remedy

In accordance with Japan's filing in November 1999 of a complaint with the WTO over the issue, the two governments entered talks on 13 January 2000.⁵⁶⁸ After the talks, Japanese Trade Minister, Fukaya expressed his satisfaction with the talk by making the comment that both sides gained a deeper understanding. However, he withheld Japan's

The Japan Times, 20 October 1999

⁵⁶⁶ The question was raised by an editorial article in the Japan Times on 11th November 1999.

⁵⁶⁷ Japan denied such speculations of rallying support. / The Japan Times, 11 November 1999

⁵⁶⁸ The sessions were being held in accordance with procedural rules for a complaint it filed with the WTO. Under WTO rules, the Japanese and US governments were to enter bilateral talks within 30 days to attempt to settle the dispute. Japan had engaged in bilateral consultations with Washington since 13 January 2000.

decision on further courses of action based on the dialogue.⁵⁶⁹ One month later, Fukaya reversed his position on the outcome of the talks for unknown reasons and suddenly revealed that during the bilateral consultations, both sides had simply restated their position without reaching any kind of settlement.

Subsequently to these failed bilateral talks, in February 2000, Japan decided to ask the WTO to set up a settlement panel to resolve the dispute with the US.⁵⁷⁰ On 20 March 2000, Japan won a WTO panel to investigate US anti-dumping duties on imports of Japanese hot-rolled steel which Japan claimed violated international fair trade rules.⁵⁷¹ The WTO ruling was a hard blow to the US, because the ruling could lead to a review of its anti-dumping laws.⁵⁷²

As compared with other anti-dumping issues on steel, it should be noted that in the case of hot-rolled steel, although it was another tough anti-dumping action taken by the United States, there was no relationship between the EU and Japan. It was reported that Japan intended to gain the support from other WTO members, especially from the EU. However, Japan was left alone against the US use of anti-dumping action and brought the case to the WTO without support from the EU. Although Japan won the case against the United States, it was not reported why the EU remained almost indifferent on the case. The lack of relationship between the EU and Japan on hot-rolled steel makes striking contrast with the US 1916 Anti-dumping Act case where the EU and Japan seemed to share the same concern. The absence of relationship between the EU and Japan on hot-rolled steel may be explained by the fact that US anti-dumping action targeted imports from Japan, and the EU was therefore not a concerned party in this particular case. However, the non-relationship in the hot-rolled steel case casts doubt on the overall EU-Japan relationship on anti-dumping cases with the United States.

3-4. Enforcement of WTO anti-dumping rules

3-4-1. The absence of the EU-Japan cooperation on the issue

Frustrated with a series of anti-dumping charges by the US steel industry, Japan intended to tighten WTO anti-dumping rules to prevent their abuse. Japan acknowledged anti-dumping measures were consistent with WTO rules, but it wanted to revise the measures. Japan was pushing to include the revision in the agenda for the new round of trade liberalization talks to be launched at the Seattle Ministerial Meeting from 30th

⁵⁶⁹ The Japan Times, 21 January 2000

⁵⁷⁰ The Japan Times, 10 February 2000

⁵⁷¹ The Financial Times, 21 March 2000

⁵⁷² The Japan Times, 27 April 2001

November to 3rd December 1999.⁵⁷³ To prevent what it perceived as protectionist practices by WTO members, especially the US, Japan and other Asian countries insisted on including a review of international anti-dumping rules on the new round's agenda. US President Bill Clinton's administration was, however, under strong pressure from the domestic steel industry and labour unions, and vehemently rebutted Japan's demand.⁵⁷⁴

The EU was also concerned about the frequent use of US anti-dumping laws and interested in tightening the WTO anti-dumping rules. However, the EU did not take any proactive action toward the review of anti-dumping rules.⁵⁷⁵ This was due to the fact that the EU was one of the most frequent users of anti-dumping actions, while Japan was mostly the target of such anti-dumping actions.⁵⁷⁶ Consequently, there was still no clear relationship between the EU and Japan on revising anti-dumping rules. Trade ministers from the United States, the European Union, Canada and Japan held two days of talks in Tokyo in May 1999 which centred on preparations for trade liberalization negotiations in Seattle.⁵⁷⁷ Specifically, they discussed the so-called built-in-agenda of service and farming sectors, issues that were being carried over from the Uruguay Round of multilateral trade negotiations. However, priority of the talk was given to a discussion on whether enforcement of anti-dumping measures should be included in the trade negotiations in Seattle.

There were deep differences of opinion, particularly between the US and Japan. Japan still strongly insisted on the need for the WTO to review its existing anti-dumping agreement for the sake of transparency and appropriate practices. But it could not draw a consensus, with the United States being most adamantly opposed.⁵⁷⁸ On this issue, the US and Japan exchanged fierce criticism of each other's position. David Aaron, US Undersecretary of Commerce for International Trade, criticized Japan for preventing the talks by insisting on the need for the WTO to review the enforcement of anti-dumping

⁵⁷³ The Japan Times, 18 November 1999

⁵⁷⁴ The Japan Times, 18 July 2000

⁵⁷⁵ On the revision of the WTO anti-dumping agreement, see: Brink Lindsey and Dan Ikenon, 'Reforming the Antidumping Agreement – a road map for WTO negotiations', (CATO Institute's Centre for Trade Policy Studies, 2002), P2-41

⁵⁷⁶ Anti-dumping activity by the EU was continuing at high level until recently. The EU adopted definitive five-year duties or accepted undertakings in 52 cases in 2000, 12 cases in 2001 and 28 cases in 2002. See; Aubrey Silverstone, 'Anti-dumping rules – Time for Change?' in *Journal of World Trade* 37(6), (Kluwer Law International, 2003), P1074, 1075

⁵⁷⁷ The Quadrilateral Trade Ministers Meeting, the 32nd of its kind since 1982, was chaired by Japanese Trade Minister Kaoru Yosano and attended by Sergio Marchi, Canadian Minister for International Trade; Vice President of the European Commission, the executive body of the EU, Leon Brittan; and US Trade Representative Charlene Barshefsky.

⁵⁷⁸ The Japan Times, 12 May 1999

provisions, while remaining "the greatest dumping country in the world." Hisamitsu Arai, MITI Vice Minister for International Affairs made the point about the growing number of anti-dumping legal cases worldwide which had reached, more than 900 in over 20 countries as of the end of 1998. Putting forward Japan's position, Arai cited the need of some 20 other WTO member states, including developing countries, which emphasize "the importance of strengthening and clarifying the disciplines applicable to the imposition of anti-dumping duties."⁵⁷⁹

At this stage, several countries, including South Korea, Colombia and Egypt, favoured a review of WTO anti-dumping rules in the next round of global trade talks, along with Japan. However, the US had resisted any efforts to include the issue. Ahead of the Seattle meeting, the WTO ruled against the US on its anti-subsidies measures. The ruling came at a delicate time. It was extremely unpopular with the US steel industry. US steel makers also pressed the administration hard not to make concessions in a new trade round which could weaken US anti-dumping or anti-subsidy laws, and were sending a large contingent to Seattle.⁵⁸⁰

Even at this stage, Japan could hardly fathom EU intentions on the issue. The EU stance on the revision of anti-dumping rules was a key for the course of discussion between the US and Japan. Within the Japanese government, there were suspicions that the EU was leaning towards the US stance or that the EU was taking a neutral position.⁵⁸¹ In fact, the EU was also concerned about the increasing use of anti-dumping and protectionist measures by some countries. However, European Commissioner for Trade Pascal Lamy expressed mixed views concerning calls from Japan and other Asian nations to take up anti-dumping issues in the next round. Lamy explained the EU position as "in the middle of the road." It was told by Lamy that the European Union was carefully considering putting anti-dumping on the agenda for the WTO Seattle round to see, if the existing rules were being properly implemented. Lamy stated, "On one side, we'd not like the whole of anti-dumping regulations to be renegotiated, because this would be opening of Pandora's box. But on the other side, we agree that reviewing the way these rules are implemented is something we believe would be in our interest."⁵⁸² Represented by this inarticulate comment of Lamy, the EU's stance on the issue of reviewing anti-dumping rules remained therefore vague. The EU's split position was demonstrated by the fact that it increasingly challenged other countries' dumping laws, notably those of the US, but

⁵⁷⁹ The Japan Times, 1 October 1999

⁵⁸⁰ The Financial Times, 23 November 1999

⁵⁸¹ Murakami, 'WTO – sekaiboueki no yukue to nihon no sentaku', P140-148

⁵⁸² The Japan Times, 5 November 1999

also those of developing countries.⁵⁸³

Despite its indecisive position on the issue of anti-dumping rules, the EU wanted to consolidate its relationship with Japan for the Seattle Ministerial Conference. Lamy urged Fukaya to come along to cement a EU-Japan understanding, adding that the two partners could fight together against protectionist views held by the United States.⁵⁸⁴

3-4-2. The collapse of the Seattle Ministerial Meeting

Despite talks before the Seattle meeting, WTO members stayed divided on their stance on anti-dumping. Japan remained most adamant that anti-dumping rules should be revised. However, thanks to a number of bilateral and multilateral talks, Japan managed to convince the EU to get closer to Japan's stance. The EU became more preoccupied with US protectionism, as the US, ahead of the meeting, toughened its anti-dumping policy against foreign steel imports. In Seattle, participants failed to agree on a specific agenda for the new round, due largely to sharp differences among the industrialized countries over a review of international anti-dumping rules. Therefore, Japan, backed by the EU and others, insisted on putting a review of anti-dumping rules on the agenda for the Doha round to prevent a possible US abuse of the rules.⁵⁸⁵ However, in the face of strong political pressure from the domestic steel industry and labour unions, the US administration of President Bill Clinton rejected the calls from the EU and Japan for a review of the anti-dumping rules in the Doha round.⁵⁸⁶

After the collapse of the Seattle meeting, senior officials from Japan, the United States, Canada and the European Union held secret talks in Ottawa from 21 June 2000 onwards to coordinate policy toward a new round of global trade liberalization negotiations. Although topping the agenda for the Ottawa meeting were issues in all areas, the anti-dumping issue was discussed particularly intensively.⁵⁸⁷ Ahead of the meeting, in May 2000, the European Union and Japan had agreed to work together to persuade the United States to overhaul anti-dumping rules at a new global trade round under the World Trade Organization. With the US opposed to discussing the matter at the new round proving to be a sticking point, the EU and Japan agreed to propose a review of the existing WTO anti-dumping rules. European Trade Commissioner Pascal Lamy asked US Trade Representative Charlene Barshefsky to accept the proposal in a meeting of top

⁵⁸³ China was expected to become their ally as the biggest target of anti-dumping cases, once it joined the WTO. / *The Financial Times*, 6 March 2001

⁵⁸⁴ *The Japan Times*, 26 November 1999

⁵⁸⁵ *The Japan Times*, 27 May 2000

⁵⁸⁶ *The Japan Times*, 27 May 2000

⁵⁸⁷ *The Japan Times*, 27 May 2000

leaders and ministers of the US and the EU in Portugal.⁵⁸⁸ This kind of small meeting was held frequently by some WTO members in order to explore ways to get a new round of global trade talks off the ground.

Some WTO members gathered in Frankfurt on 24 January 2001. This informal sub-Cabinet level conference was originally proposed by Japan and proceeded under Japan's initiative. Among the topics, Japan strongly insisted that anti-dumping should be taken up at the new trade round. The EU and Japan held high-level bilateral talks before the Frankfurt conference. However, the EU and the US did not attend the Frankfurt conference. The US was in transition, as President-elect George W. Bush was preparing to take office on 20 January 2001, succeeding President Bill Clinton. However, the reason of the EU absence was not reported.⁵⁸⁹

In February 2001, after the WTO ruling against the US anti-dumping duties on Japanese hot-rolled steel, US anti-dumping and other trade remedy laws became one of the most sensitive issues in US trade policy. The Bush administration was about to be forced to ask a hostile Congress to change US anti-dumping legislation at the WTO's behest. The issue threatened attempts to re-launch the round in Qatar in November 2001.⁵⁹⁰

Despite US reluctance, the WTO members agreed to discuss the review of anti-dumping rules in the Doha round after all. Since the EU shared the concern about the increasing use of anti-dumping measures taken by developing countries, the US finally compromised on the issue. While the fact that the EU and Japan held high-level bilateral talks on the issue suggests their shared interest, the EU's absence from the Frankfurt conference leaves questions about the intensity of their relationship on this issue.

3-5. The Byrd Amendment law

3-5-1. US anti-dumping law to subsidise domestic steel makers

While the EU and Japan agreed to discuss the review of anti-dumping rules in the WTO, they also thought it necessary to consult each other on the issue of the Byrd Amendment law.⁵⁹¹ The case on the US Byrd Amendment law is particularly important in

⁵⁸⁸ The Japan Times, 28 May 2000

⁵⁸⁹ The Japan Times, 21 January 2001

⁵⁹⁰ The Financial Times, 26 February 2001

⁵⁹¹ M.L. Moveseian (2004) provides a detailed description of the enactment of Byrd Amendment law as well as the development of Byrd Amendment dispute settlement case in the WTO. See, M. L. Movsesian, 'United States: Continued Dumping and Subsidy Offset Act of 2000', *The American Journal of International Law*, Vol. 98, No. 1, (American Society of International Law, Jan. 2004), P150-155

our context, since in this case EU-Japan cooperation was much closer and pro-active. In 2000, the US Byrd Amendment law, officially known as the United States Continued Dumping and Subsidy Offset Act of 2000, gave rise to discussion among major steel traders. The Byrd Amendment allowed anti-dumping tariffs collected by US authorities to be distributed to domestic industries.⁵⁹² Under WTO rules, member economies were allowed to impose anti-dumping duties. However, there was no clause directly banning the practice of offering subsidies to domestic makers from anti-dumping revenues.⁵⁹³ The Byrd Law was enacted amid persistently strong Congressional pressure for tough action to protect the US steel industry against a flood of cheap foreign steel products.⁵⁹⁴ Japan immediately revealed its intention to file a complaint with the WTO, if US President Bill Clinton signed into law a bill that would subsidize American steel makers with dumping tariffs imposed on foreign companies. Japan also announced that it intended to do so jointly with the European Union which was also considering similar actions.

According to this law, domestic companies were to be awarded huge amounts of funds, if foreign products were being dumped below cost in the US market. The EU, which was caught off-guard by the move, warned that the legislation violated World Trade Organisation rules and could trigger another trade war between the world's two largest economies.

High legal costs usually prevented smaller US companies from filing dumping cases. The EU and Japan's common concern was that the US law created an enormous financial incentive to start litigation. The provision could also lead to more cases being adjudicated. Under existing law, a case only proceeded, if supported by a majority of the US industry. Many US companies might agree to support dumping cases simply to be eligible for the windfall.⁵⁹⁵ The chances looked high for the companies in the EU and Japan to be the prime targets of such lawsuits.

The EU and Japan immediately took joint actions. First, Japan's ambassador to the US, Yanai, sent letters protesting the legislation to Senator, Robert Byrd, a West Virginia Democrat and chief sponsor of the bill, and US Trade Representative Charlene Barshefsky.⁵⁹⁶ In addition, jointly with the European Union's ambassador to the United States, he sent a letter to US President Bill Clinton, urging him to veto the bill.⁵⁹⁷ This

⁵⁹² The Japan Times, 23 December 2000

⁵⁹³ The Japan Times, 28 March 2001

⁵⁹⁴ The Japan Times, 28 December 2001

⁵⁹⁵ The Financial Times, 10 October 2000

⁵⁹⁶ The Japan Times, 25 October 2000

⁵⁹⁷ The letter was signed by Japanese Ambassador, Shunji Yanai, Canadian Ambassador, Michael Kergin and EU Ambassador, Gunter Burghardt.

joint action by the EU and Japan was of significant importance since it was rare for ambassadors from different countries and regions to send a joint letter to the US President.⁵⁹⁸

Despite the serious concern from the EU and Japan, President Clinton signed it into law on 28 October 2000, following passage in both the House of Representatives and the Senate. Although Clinton and other administration officials were opposed to the new anti-dumping measures, the President reluctantly enacted it so as to not kill a farm bill which he valued even more.⁵⁹⁹

3-5-2. EU's reluctance to take the case to the WTO

While the EU and Japan showed a strong cooperative stance in protesting the subsidy bill, it was initially a different story when it came to taking the dispute to the WTO. Nearly six weeks after US President Bill Clinton signed the controversial anti-dumping bill on steel trade into law, Japan had still not carried out its strongly aired threat to take the law to the WTO.⁶⁰⁰ This was because the Japanese government hesitated to push the US too hard, fearing negative implications for the entire global trade system.⁶⁰¹ However, Japan was not merely bluffing but trying to take concerted action with other WTO members, especially with the European Union. A senior official at the MITI clearly stated, "we want to take a united front with the 15-nation European Union on this trade case as much as possible." However, the EU was reluctant to take the case to the WTO immediately. According to a MITI official, the EU had already faced many bilateral trade disputes with the US and apparently wanted to take a wait-and-see attitude.⁶⁰²

In reaction to the reserved reaction from the EU, Japan started to consider the timing of filing a complaint with the WTO over the US anti-dumping law without the EU. In spite of the EU's reluctance, Japanese officials were rather optimistic that the new Republican administration of President George W. Bush would move quickly to rescind the controversial law in the Republican-controlled Congress.⁶⁰³ The EU had the same expectation behind its evasive stance on US anti-dumping law. This optimism of the EU and Japan was based on the fact that Clinton had been reluctant to sign the law, so the

⁵⁹⁸ The Japan Times, 27 October 2000

⁵⁹⁹ The Japan Times, 5 December 2000

⁶⁰⁰ The Japan Times, 5 December 2000

⁶⁰¹ The Japan Times, 28 March 2001

⁶⁰² The Japan Times, 5 December 2000

⁶⁰³ The Byrd amendment was pushed by Republicans, although Republican administrations were thought to pursue global trade more enthusiastically than Democratic ones.

Bush administration might be more realistic in its response.⁶⁰⁴ However, there was also speculation that it may be politically difficult for Bush to depart from the Clinton administration's policy, given the fact that US Congress became almost evenly divided between Republicans and Democrats under the Bush administration.⁶⁰⁵ Therefore, Japan kept putting pressure on the US over the anti-dumping law in cooperation with opponents of the law from the US administration and Congress. Japan reiterated its position that the goal of the Japanese government was not to win a legal battle with the US over the new anti-dumping law at the WTO, but to have the law abolished as soon as possible.⁶⁰⁶

3-5-3. EU-Japan joint complaint

Despite the inconsistency of the EU and Japan's position, the EU and Japan finally came to the conclusion of fighting together against the US law. In December 2000, the European Union and Japan filed a joint complaint to the World Trade Organisation over the new US legislation. India, South Korea and Thailand agreed to be joint signatories and other countries were invited to join the initiative or be involved as third parties. Canada, Chile, Brazil and Australia all spoke out against the US law.⁶⁰⁷

In spite of the joint complaints by the EU, Japan and other countries, the Bush administration made it clear that it had no intention of urging Congress to nullify the Byrd law. Earlier in March 2001, US Trade Representative Robert Zoellick went even further by suggesting to a US House of Representatives committee that "safeguard" emergency trade curbs be used on steel imports. The rising US protectionism put the EU and Japan on extra-alert to the US trade policy on steel. The EU and Japan confirmed that they would maintain close contacts with each other over the matter.⁶⁰⁸

The case attracted great attention from all WTO members, because the number of co-complainants was the largest since the dispute settlement mechanism had taken effect in 1996. The EU and Japan sought to bring in as many countries as possible to send a message to the US that countries from diverse areas were clearly opposed to the Byrd Amendment.⁶⁰⁹

3-5-4. The WTO ruling

After filing the complaint with the WTO over the Byrd Law in December 2000,

⁶⁰⁴ The Japan Times, 23 December 2000

⁶⁰⁵ The Japan Times, 12 January 2001

⁶⁰⁶ The Japan Times, 5 December 2000

⁶⁰⁷ The Financial Times, 19 December 2000

⁶⁰⁸ The Japan Times, 28 March 2001

⁶⁰⁹ The Japan Times, 23 December 2000

the EU, Japan and seven other economies held bilateral consultations with the US in early February 2001. Bilateral consultation is the first stage of the WTO dispute settlement procedures. Canada and Mexico, US partners in the North American Free Trade Agreement (NAFTA), later joined the complainants by filing a separate document with the WTO and held separate bilateral consultations with the US in June 2001.⁶¹⁰

Japan intended to be fully prepared for a legal battle at the WTO by carefully examining the implementation rules. While requesting a WTO panel appeared to be the last remaining option, there was still concern among some Japanese officials about a possible negative effect on the entire global trade system by doing so. A senior Foreign Ministry official mentioned that despite the chance of winning the case at the WTO over the Byrd law, Japan needed to be careful in deciding whether to ask for the setting-up of a WTO panel. Japan was concerned that if it drove the US into a corner over steel trade, it might become reluctant about fulfilling commitments it had made in the multilateral arena, even if it would not go so far as to leave the WTO. The EU also shared the same concern with Japan. In fact, when the WTO replaced the GATT in January 1995, some Congressional members had insisted that the US should exit the WTO, if it lost any three consecutive trade cases, calling it the "three strikes-out" principle.⁶¹¹

Despite their concern to put the US into a corner, the EU and Japan eventually decided to bring the case to the WTO with 7 other co-complaints. Bilateral consultations between the US and the 9 complainants including the EU and Japan did not bridge the gap between both sides. Accordingly, in July 2001, the EU and Japan moved on to the second stage of the WTO dispute settlement procedures by requesting the WTO to set up a neutral panel to adjudicate on the case.⁶¹²

The WTO, on 23 August 2001, set up a dispute panel to rule on the complaint by the EU, Japan and seven other WTO members against the Byrd law. The EU and Japan claimed that the unprecedented joint action reflected widespread concern over the law.⁶¹³ On 17 July 2002, the WTO dealt a critical blow against US protection of its steel industry by issuing a preliminary ruling condemning the Byrd law. An interim report by a WTO dispute panel found that the Byrd Amendment violated multilateral rules on anti-dumping

⁶¹⁰ The Japan Times, 28 December 2001

⁶¹¹ The Japan Times, 28 March 2001

⁶¹² The WTO decided to set up a panel in August 2001, and one month later, it decided to let Canada and Mexico join the original nine complainant economies. / The Japan Times, 28 December 2001

⁶¹³ Facing a request from the EU and Japan to set up a neutral panel, the US blocked their first panel request. This was seen as US 'delaying tactics'. Under WTO rules, however, it cannot do so a second time.

and subsidies and called for its repeal. The ruling marked a victory for the EU and Japan which succeeded in rallying support from other affected WTO members. Having created a common front with the largest number of co-complainants in WTO history, the EU and Japan together had achieved a major victory.

Fighting against US protectionism provided a strong motivation for the EU and Japan to maintain cohesion on anti-dumping issues, despite shared concerns about possible negative implications for their relationship with the United States. But looking back at other anti-dumping dispute cases, this cohesion cannot hide the fact that there were also differences between the EU and Japan over their stance towards anti-dumping. This difference stems from the circumstance that Japan had been a target of anti-dumping duties (some of them imposed by the EU), while the EU was one of the main users of the anti-dumping measures. This is due to the structural differences between European and Japanese steel trade. The EU and Japan are the main exporters of steel products, while the EU is also a large importer of them. This structural difference came to the surface again in the case of opposing US safeguards which will be analysed in the following section of this chapter.

4. Steel trade and safeguard measures

4-1. EU-Japan reactions to Section 201 of the 1974 US Trade Act

4-1-1. US safeguard measures

Alongside this EU-Japan victory over these two cases of US anti-dumping measures, there were other protectionist US policies which raised the question whether the EU and Japan would continue their cooperation against their most important ally in so many other policy areas. Further protectionist policies came up because the US steel industry remained stagnant. In August 1999, the US unveiled a "steel action plan" to boost its industry after the surge in cheap steel imports with the onset of the Asian financial crisis.⁶¹⁴ This action plan became a common concern shared by the EU and Japan. The proposed US measures included "safeguard" actions, which could restrict imports of steel wire rod, they put pressure on some countries, particularly Japan, to reduce steel exports to the US, and established a government-backed loan guarantee plan for steel companies. The EU warned the US that the proposed measures by the US could destabilise the world market, and hinted at bringing the case to the WTO.⁶¹⁵ The warning

⁶¹⁴ For details, see: 'Imposition of US Tariffs on steel imports' in *The American Journal of International Law*, Vol. 96, No.4, (American Society of International Law, Oct. 2002), P977, 978

⁶¹⁵ A week after the US government revealed its plan, Sir Leon Brittan, EU Trade

came amid growing criticism of "Section 201 of the US Trade Act," which allowed the US to set import quotas or raise tariffs on imported products, if an increase in imports was deemed to have caused injury to US industry.⁶¹⁶

Import restrictions, such as Section 201 of the US Trade Act of 1974, are called safeguard measures. Safeguard measures are temporary and selective measures, such as increased tariffs, tariff quotas or quantitative restrictions. The WTO allows members to implement a safeguard mechanism to slow imports so that a specific industry can adjust to heightened competition from foreign suppliers.⁶¹⁷ GATT Article XIX, which entitles "Emergency Action on Imports of Particular Products," recognizes a country's right to withdraw or modify concessions granted earlier, or to impose new restrictions, if a product is "being imported in such increased quantities...as to cause or threaten serious injury to domestic producers" and to maintain such restrictions "for such time as may be necessary to prevent or remedy such injury."⁶¹⁸ Exporters have a complementary right under the GATT not to be deprived arbitrarily of access to foreign markets. Under the Uruguay Round trade accord, GATT member countries strengthened safeguard rules by clarifying existing guidelines and tightening timetables.⁶¹⁹ The duration of a safeguard measure is limited to a maximum of eight years.

US safeguard measures known as Section 201 of the US Trade Act of 1974 require the US International Trade Commission⁶²⁰ to investigate complaints formally known as "petitions" filed by domestic industries or workers claiming that they have been injured or are threatened with injury as a consequence of rising imports and to complete any such investigation within six months. The act states that if the US International Trade Commission finds that a domestic industry has been seriously injured or threatened with serious injury, it shall recommend to the President relief measures for the industry in the

Commissioner wrote a letter to Charlene Barshefsky, US trade representative. / *The Financial Times*, 13 August 1999

⁶¹⁶ *The Financial Times*, 13 August 1999

⁶¹⁷ Safeguard actions are known in the United States as "escape clause" actions, and authority to take such actions is provided for in various US laws.

⁶¹⁸ From WTO homepage, General Agreement on Tariffs and Trade 1994, Article XIX: Emergency Action on Imports of Particular Products, (http://www.wto.org/english/res_e/booksp_e/analytic_index_e/gatt1994_07_e.htm#477)

⁶¹⁹ As for the safeguard agreements concluded during the Uruguay Round, see: Thiebaut Flory, 'The Agreement on Safeguards' in Jacques H. J. Bourgeois, Frederique Berrod and Eric Gippini Fournier (eds), 'The Uruguay Round Results', P265-271

⁶²⁰ The US International Trade Commission assessed whether US industries were seriously injured by fairly traded imports and could recommend to the President that relief be provided to those industries to facilitate positive adjustment to import competition. Relief could take the form of increased tariffs or quotas on imports and/or adjustment assistance for the domestic industry. For further details, see: (<http://www.usitc.gov/webabout.htm>)

form of temporary import restrictions (tariffs, quotas, or tariff-rate quotas) or trade adjustment assistance. The President has discretion to follow the US International Trade Commission's recommendations on relief, which normally takes the form of increased duties or quantitative restrictions. Such import relief cannot exceed eight years, including extensions.

4-1-2. EU-Japan anxiety on US move

US safeguard measures under Section 201 of the US Trade Act of 1974 became a concrete issue in March 2002 when they were invoked against the imports of steel products. Prior to the invocation of safeguard tariffs, the EU and Japan kept expressing their strong concerns to the United States. In August 1999, in a letter from Sir Leon Brittan to the US trade representative, the EU had already expressed concern about the prospect of the US applying any measures that could restrict imports of steel wire rod, one of the main categories of steel. The EU warned against pressure from the US on countries such as Japan to reduce steel exports to the US, because it represented a return to the kind of VRAs that had proliferated in the 1970s and 1980s.⁶²¹

On 1 September 1999, following the EU move, Japan also revealed its concern on US safeguard measures by sending a letter to the US in an effort to pre-empt the imposition of tariffs on US imports of Japanese steel.⁶²² The Japanese government claimed that Japanese exports of steel wire rods were not causing injury to US industry, since they were speciality products not manufactured in the US. The letters from the EU and Japan came ahead of a decision expected on September 26 by US President Bill Clinton on whether to impose additional tariffs on imports of steel wire rods from Japan. The Japanese government pointed out that US action raised concerns about further US trade measures that could undermine international efforts to liberalise trade. But the Japanese government went much further than the EU and also asked the US for bilateral consultations under the WTO to resolve the dispute.⁶²³

In spite of the letters from the EU and Japan revealing their concerns about the US

⁶²¹ The EU Commissioner also urged the US President not to sign the Emergency Steel Loan Guarantee Act, which passed through both houses of Congress. This would provide 1 billion dollars loan guarantees to US companies that could not otherwise obtain credit without government backing. According to Sir Leon, the plan would certainly constitute a subsidy under WTO rules, and it could lead to countervailing measures from other countries and result in a damaging escalation of subsidies. / *The Financial Times*, 13 August 1999

⁶²² Two weeks after Sir Leon sent a letter to the US trade representative, Kaoru Yosano, Japan's Minister for International Trade and Industry, wrote to Charlene Barshefsky / *The Financial Times*, 1 September 1999

⁶²³ *The Financial Times*, 1 September 1999

measures, on 18 October 2000, Democratic leaders in US Congress urged the Clinton administration to seek import restraints under Section 201, adding a powerful voice to demands from the US steel industry and the steelworkers' union.⁶²⁴ The industry claimed that unless the administration responded quickly to stem rising imports, several steel companies faced bankruptcy. As explained above, import restraints under Section 201 requires the industry to prove before the International Trade Commission that imports are seriously hurting US producers. However, the industry was asking for immediate curbs on imports even from non-WTO countries.⁶²⁵ Robert LaRussa, the Undersecretary of Commerce for International Trade revealed that the US had urged several countries to restrain steel exports to the US voluntarily.⁶²⁶

It came as a disappointment to the EU and Japan, when on 5 June 2001, President George W. Bush announced that the administration would initiate a safeguard action that could result in import curbs after an eight month investigation and that it would seek international negotiations to cut steel capacity and end market-distorting subsidies.⁶²⁷ The US move was distressing for the EU and Japan, since a safeguard action marked a significant shift of tone in the Bush administration's approach to trade liberalisation policy.⁶²⁸ Bearing in mind that safeguard measures should serve only as an emergency measure, WTO Director General, Supachai shared the same position as the EU and Japan against US safeguard measures.⁶²⁹

4-1-3. US International Trade Commission investigation and EU reaction

The US decision to impose safeguard measures was received very negatively in the EU, since it was a sensitive time for the US and the EU when they were reviving

⁶²⁴ About 200 members of the House of Representatives, including Democratic leader Richard Gephardt, called on the White House to seek import restraints under the Section 201. The resolution followed a letter to President Clinton from the union and chief executives of about 75 US steel companies.

⁶²⁵ Similar request came from a group of 57 lawmakers from the US House of Representatives on 25 October 2000. The lawmakers wrote that imports of several steel products exceeded the 1998 crisis levels. They claimed that the profitability of the steel industry was destroyed for many companies. / The Japan Times, 27 October 2000

⁶²⁶ The Financial Times, 19 October 2000

⁶²⁷ A day after the administration launched actions that could result in curbs on steel imports, Donald Evans, the US Commerce Secretary, promised US steelworkers that the Bush administration was committed to "a lasting solution" to unfair trading practices in the global steel industry.

⁶²⁸ While acknowledging the special role of the US in promoting open trade, Robert Zoellick, the US trade representative clearly stated that if other countries were unwilling to move forward, the US would take care of its own economic interests. / The Financial Times, 7 June 2001

⁶²⁹ The Japan Times, 12 March 2002

efforts to resolve a long dispute over an EU ban on imports of US beef treated with hormones. The two sides were reactivating negotiations to lift 116.8 million dollars in US sanctions imposed on EU exports because of the dispute. The two sides also hoped to manage the political fallout, in case the World Trade Organisation decided that the US foreign sales corporation tax regime still violated trade rules. The EU threatened as much as 2.8 billion pounds retaliation in that dispute.⁶³⁰

In October 2001, an investigation by the US International Trade Commission, initiated by the administration, found that competition from foreign producers was hurting the US steel industry. The finding completely ran counter to Japan's claim and paved the way for trade curbs on as much as 80 per cent of steel imports.⁶³¹ Receiving the result of US International Trade Commission investigation, the Bush administration started to consider whether to invoke Section 201 of the 1974 Trade Act to impose safeguard import restrictions on a wide range of foreign steel products, including some products that had not yet faced anti-dumping duties. Restrictions were expected to raise US manufacturing and construction costs and divert steel imports elsewhere, above all to Europe.⁶³²

The European Union immediately prepared itself to move swiftly to protect its steel market against a surge of imports, in case the US materialised its threat to impose trade restrictions on steel. The EU warned the US that, if Washington imposed curbs, the EU would withdraw immediately from talks in the OECD on cutting worldwide industry capacity and subsidies. The erection of barriers around the world's two largest steel markets risked to create turmoil in the steel sector and setting off an international chain reaction of protectionist measures.

The EU stated clearly that it had no choice but to follow suit to prevent its market being swamped by imports diverted from the US, if the US imposed safeguard measures. The EU began monitoring the steel market in order to watch closely for any sudden increase in imports. This EU move was to calculate what impact a range of possible US import barriers would have on international trade flows. The EU also immediately revealed a plan to challenge any US curbs in the WTO with confidence of winning. However, the EU was concerned that it could take about two years to get such measures removed, during which time the European industry would risk being weakened by a sharp increase in imports.⁶³³

⁶³⁰ The Financial Times, 11 June 2001

⁶³¹ The Financial Times, 24 October 2001

⁶³² The Japan Times, 28 December 2001

⁶³³ The Financial Times, 22 February 2002

4-2. The imposition of US safeguard measures

4-2-1. EU-Japan opposition to US safeguard

On 5 March 2002, Bush announced that his government invoked import restriction measures on imported steel products for three years to protect the domestic steel industry. The US move was a severe blow to its relations with the EU and Japan, the US's two largest economic allies, whose steel producers were expected to be hit hard. It fuelled suspicions, particularly in Europe, that unilateralist impulses, which other governments increasingly discern in US foreign policy, had spread to trade and economic policy. The tough action on steel went beyond what the EU, Japan and other US trade partners had expected.

Safeguard measures are emergency trade measures taken temporarily by a member to provide relief to its domestic industry in the situation of it getting hurt from an increase in imports. Normally, a member is not permitted to restrict imports into its territory or exports from its territory. Only under certain conditions, a member may take recourse to trade measures restricting its imports of a product so as to 'safeguard' its domestic industry. Safeguard measures are sometimes called an 'escape clause' as they enable a member to escape its obligations in specified situations.

The purpose of such a provision in the multilateral trading system is to lighten the burden on the country whose domestic industry is facing acute problems due to imports. The objective is to disperse the burden over all the members to enable the affected member to adjust smoothly to the new situation of international competition in that particular product line. By its very nature, safeguard measures have to be temporary and in support of the adjustment process. Since they are meant to provide temporary protection to the domestic industry to facilitate its adjustment, they are not expected to be used as an instrument of long-term protection.⁶³⁴

On 7 March 2002, the Japan Times reported that Japanese government officials and business leaders reacted with anger to a decision by US President George W. Bush to slap tariffs on imported steel. Japan unveiled its intention to conduct countermeasures after consulting the European Union and South Korea. Under WTO rules member governments are prohibited from taking retaliatory steps against a safeguard measure. Therefore, Japan had two choices; 1.) to ask the US to take countervailing steps by lowering tariffs on other import items, or 2.) to go to the WTO at once. Japan steelmakers faced tariffs up to 30 per cent. In 2001, Japan exported 2.2 million tons of steel to the US,

⁶³⁴ For details of safeguard measures, see: Das, 'The World Trade Organisation – A guide to the Framework for International Trade', P80-97

about 7 per cent of its total steel exports. Japan's steel exports to the US already tumbled to one-third of their peak, due to a spate of US anti-dumping charges. Japanese steelmakers reacted by shifting to exporting items not produced by US rivals, doing so in low volume and in a stable manner, in order to mitigate the impact of US trade restrictions.⁶³⁵

In March 2002, the European Union pledged to launch an immediate complaint with the WTO against new US steel tariffs, which it said represented a clear violation of WTO rules. In a hard-hitting statement, Pascal Lamy, the EU Trade Commissioner, revealed his determination that the EU would take whatever measures necessary to protect its steel industry from an expected surge in imports as steel makers accustomed to exporting to the US searched for alternative markets. The EU, which supplied about one-fifth of US steel imports, was expected to be hardest hit by the US actions. Despite efforts by Pascal Lamy and Robert Zoellick, the US trade representative, to avoid confrontation, EU governments were seen to support the Commission's tough response. According to the Commission, the value of US steel imports fell 23 per cent in 2001, while EU imports were at record levels.

Shortly after President Bush's announcement, the EU, Japan and six other countries requested consultations at the WTO⁶³⁶ and after the consultations ended unsatisfactorily, they requested the establishment of dispute panels.⁶³⁷ The European Commission estimated that EU steel producers could lose exports of about 4 million tonnes to the US market and face imports totalling as much as 16 million tonnes diverted from the US.

4-2-2. International criticism

Negative reaction came not only from the EU and Japan. Russia, the world's fourth biggest steel producer, joined the EU and Japan and called the US move unjustified from a legal or economic point of view. As a retaliatory move, Russia suspended imports of US poultry.⁶³⁸ The IMF also shared the same concern with the EU and Japan and criticised the US for raising trade barriers. The IMF revealed its concern that the US action could hamper its effort to persuade developing countries to reduce their trade

⁶³⁵ The Japan Times, 7 March 2002

⁶³⁶ Six countries were: Brazil, China, New Zealand, Norway, South Korea and Switzerland.

⁶³⁷ 'Imposition of US tariff on steel imports', The American Journal of International Law, Vol.96, No.4, (American Society of International Law, Oct. 2002), P977, 978

⁶³⁸ The Financial Times, 6 March 2002

barriers.⁶³⁹ Criticism on US safeguard measures came also from the US's closest ally in the EU, the United Kingdom. Patricia Hewitt, UK Trade and Industry Secretary, accused the US for levying 30 per cent tariffs on hot-rolled steel and flat-steel products. According to her, the US move led to a real risk that the British and European markets would be flooded with steel products from third countries, mainly in the Far East, that would otherwise have sold to the US.⁶⁴⁰ In March 2002, the UK Prime Minister, Tony Blair revealed his frustration that the US ignored an intensive British lobbying campaign, including a letter and personal telephone call to President Bush. A strong feeling of discontent was found even within the US. Alan Greenspan, the US Federal Reserve chairman gave his rare criticism of the administration in testimony before the Senate banking committee. Greenspan clearly revealed his dissatisfaction with President George W. Bush's decision to impose temporary tariffs on imported steel.⁶⁴¹

The alleged damage for the US market was doubted by the EU and Japan. Japan questioned whether the US was suffering enough to justify the import curbs under international trade rules of the WTO. The EU argued that world trade rules forbid the introduction of defensive tariffs, unless a country had suffered a sudden surge in imports. The European Union claimed that any US restrictions would be illegal, because imports into its market had been falling for several years. US steel imports had fallen steadily since 1999. However, the US claimed its trade restrictions complied with WTO rules, because imports rose strongly for about two years after the 1997 economic crisis in Asia and remained above pre-crisis levels.⁶⁴²

4-3. The EU-Japan challenge in the WTO

4-3-1. Demand for compensation

In March 2002, the EU confirmed that it would coordinate with Japan and other countries including China, South Korea and Brazil in preparing a case against US safeguard measures in the WTO. Japan claimed that it considered bringing the case to the WTO dispute settlement panel. Australia followed the EU and Japan in threatening a WTO challenge. South Korea, the world's sixth largest steel maker, pledged to support efforts by the EU and Japan to fight US tariffs.⁶⁴³

⁶³⁹ The Financial Times, 14 March 2002

⁶⁴⁰ Sir Ken Jackson, General Secretary of the Amicus Engineering Union warned that US tariffs could lead to 9 million tonnes of cheap steel flooding into Europe. He estimated that would cost 18,000 jobs across the European Union and 5,000 in Britain.

⁶⁴¹ The Financial Times, 8 March 2002

⁶⁴² The Financial Times, 22 February 2002

⁶⁴³ The Financial Times, 7 March 2002

While the EU claimed that it was in the EU's long-term interest not to be drawn into a cycle of tit-for-tat retaliation in contravention of the WTO's rules, on 7 March 2002, the EU launched two legal challenges in the WTO aimed at overturning the US steel tariffs.⁶⁴⁴ The European Union revealed a plan to demand that the US compensate it for the cost incurred by its proposed trade restrictions on steel imports. The EU asked the US for immediate compensation in the form of lower tariffs on other products, which could be worth as much as 2 billion dollars (2.3 billion euros) annually. Under Article 8 of the safeguards agreement in the WTO, the EU, Japan and any other countries affected by US measures could demand trade compensation 60 days after the curbs take effect. The article carried a requirement that "members concerned agree on any adequate means of trade compensation for the adverse effects of the measure on their trade." Although the rules had never been tested in practice, if the US refused, the EU was entitled to retaliate automatically by raising its own tariffs on some US exports. That would mark a significant escalation of the dispute, forcing the US to challenge the EU retaliation in the WTO. Japan immediately asked for third-party participation in a dispute settlement case filed by the European Union. Under WTO rules, member countries are entitled to take part in dispute settlement procedures as third parties with observer status, if relevant issues affected their trade policies, even though they are not directly involved in the dispute.⁶⁴⁵

4-3-2. US rejection of EU-Japan demand for compensation

At the same time, Japan filed its own complaint with the WTO against US safeguard. Japan filed a request with the United States to hold bilateral talks with an eye toward trade compensation from the US. Japan estimated the potential losses to its steel makers at 168.94 million dollars. Japan's request was based on Article 12 of the World Trade Organization Agreement on Safeguards, which obligates a WTO member wishing to apply or extend a safeguard measure to provide "adequate opportunity for prior consultations" with concerned parties. During bilateral consultations held in Washington, the two countries failed to narrow their divisions on the issue. The US had already rejected Japan's demand that it scrap tariffs on seven Japanese products, including video cameras and wrist watches, as compensation for the safeguard measure.⁶⁴⁶

The US also rejected EU demands for immediate compensation for the steel curbs in the form of lower barriers to other imports. The US insisted the EU should first prove

⁶⁴⁴ The Japan Times, 20 March 2002

⁶⁴⁵ The Japan Times, 20 March 2002

⁶⁴⁶ The Japan Times, 21 March 2002

its claims in the WTO. The rejection meant the EU must decide whether to escalate the dispute by retaliating against US exports or await the outcome of its separate legal challenge to the steel curbs in the WTO. The European Union decided to take a hard-line. On 12 March 2002, European Union governments gave unanimous backing to the European Commission's uncompromising reaction to US safeguard measures. The 15 EU member states told the Commission to continue its approach to countering the US action. The Commission began the process of consultations in the WTO, which was preliminary to a dispute settlement panel.⁶⁴⁷ The delay of US response to the EU's request for compensation aroused suspicion in the EU that the US was conducting a delaying tactic in the hope that the EU would miss the deadlines under the safeguard measures.

4-4. EU-Japan threat of retaliation

4-4-1. US strategy to isolate the EU

Receiving a negative response from the US, on 15 March 2002, the European Union stepped up its threat to retaliate against the US safeguard measure, unless the Bush administration agreed to EU demands for compensation. Although the EU set no deadline for concluding talks with the US on compensation, the European Commission started to make a list of US goods worth about 2 billion dollars which could face increased EU tariffs as retaliation. The EU tariffs include US steel exports worth about 600 million dollars and textiles. This plan of retaliation by the EU on the sensitive textiles and steel sectors worsened the tense situation.

Facing a tough reaction from the EU, the US hoped to isolate the EU in the dispute over steel but failed to placate Japan and other countries targeted by the action, including Korea, China, Brazil, Australia, New Zealand and Norway, which also demanded US compensation. Japan told the US that it wanted compensation in the form of increased access for Japanese-made consumer products and was prepared to retaliate if the US refused.⁶⁴⁸

While the US and the EU made no progress on Europe's demand for compensation, the US announced that it would negotiate on Japan's request for compensation. Robert Zoellick, US trade representative, announced that the US would enter discussions over a Japanese request for about 160 million dollars in compensation, which would involve the US lowering trade barriers on other products sold by Japan. This position was more conciliatory than before, when the US had said it did not believe such compensation was

⁶⁴⁷ The Financial Times, 13 March 2002

⁶⁴⁸ The Financial Times, 16 March 2002

owed. The offer came, as Japan and South Korea claimed that they would join the European Union in filing a complaint with the WTO over the US steel tariffs. The Japanese government was also threatening to impose retaliatory tariffs on US exports, if the US refused to pay compensation. The US announced its readiness to open the door, as well for negotiations over compensation with other affected parties, including the EU. However, the US mentioned that unlike Japan, the EU took no constructive approach.⁶⁴⁹ Treating the EU and Japan differently, the US tried to divide the grouping led by the EU.

Ironically, immediately after the US softened its stance towards Japan, Japan's Economy, Trade and Industry Minister made the strongest ever comment on EU-Japan cooperation. Japan revealed its plan to work closely with Europe and to welcome the participation of other concerned countries as third parties. Despite the US effort to isolate the EU, Japan intended to maintain or even consolidate the close relationship it had with the EU and other affected nations by the US safeguard.⁶⁵⁰ Takeo Hiranuma called on other steel exporting countries to join the EU-Japan in challenging the US safeguard measures.⁶⁵¹

4-4-2. Escalation and mitigation of transatlantic tensions

Coinciding with the US resistance to compensate, the EU was preparing for retaliation. On 22 March, the European Commission distributed to EU member states a draft list of suggested subjects for retaliation.⁶⁵² EU retaliation was designed to put maximum pressure on the US to withdraw its steel tariffs, while doing minimum harm to European businesses. It included citrus fruit from Florida, steel from the Midwest and textiles from North and South Carolina. It included products for which the EU was not dependent on US imports, but it targeted particular US states to be extra persuasive. The EU believed that President George W. Bush approved punitive tariffs on steel imports to help his political prospects in states such as West Virginia and Pennsylvania. These would be hit by EU retaliation, while targeting citrus would hit Florida, the state that ultimately decided the 2000 election. Florida and Brazil produced 90 per cent of the world's supply of processed orange juice. During its previous disputes with the EU over bananas and

⁶⁴⁹ The Financial Times, 21 March 2002

⁶⁵⁰ Seoul and Tokyo also coordinated their opposition to the tariffs when Junichiro Koizumi, Japanese Prime Minister, visited South Korea for three-days, started on 21 March 2002

⁶⁵¹ The Financial Times, 21 March 2002

⁶⁵² Under World Trade Organisation rules, the EU had to notify its list of US products targeted for potential retaliatory action by 20 May 2002. It then had the right to impose sanctions once a WTO dispute settlement panel had ruled in its favour. / The Financial Times, 23 March 2002

beef produced using hormones, the US targeted those EU states which were the strongest defenders of the EU's policies, hitting countries such as France particularly hard.⁶⁵³

While tensions between the US and the EU were mounting, there were also signs of moderation on both sides as a result of other considerations. Firstly, some EU member states still remained unconvinced of the effect of retaliation, before the WTO ruled on a separate EU legal challenge to the US measures. Some governments, such as Germany and the Nordic countries, expressed concern about the implications of the commission's action, questioning whether unilateral sanctions would really comply with WTO rules. They required clear legal assurances on that point.

Secondly, the Bush administration was under strong pressure from US steel-users to scale back the import restrictions in order to meet EU objections to some extent. The Bush administration was concerned about a rapid rise in the domestic price of many steel products following the imposition of tariffs. Steel users warned Washington that shortages were looming.

Thirdly, while both the US and the EU were obliged to talk tough in order to rally international support, both sides had much to lose, if the steel dispute went out of control. The US and EU decided to prevent this sort of bilateral trade skirmishes caused by new regulations that had blighted transatlantic ties. As a result the US and the EU started to tone down their aggravated trade relations.⁶⁵⁴ Pascal Lamy, EU Trade Commissioner, also had reason to act cautiously. The conflict undermined Lamy's efforts to improve transatlantic trade relations and cooperate more closely with his counterpart, Robert Zoellick. A complete breakdown would destroy ambitions to conclude a successful trade round. Those signals prompted both sides to consider compromise.

4-5. Imposition of EU safeguard measures

4-5-1. The impact of EU safeguard measures on EU-Japan relations

Running parallel with the exchange of arguments between the EU and the US, the EU and Japan were facing a test of the strength of their cooperation. A week after the US imposition of safeguard measures on 20 March 2002, the European Commission

⁶⁵³ The Financial Times, 23 March 2002

⁶⁵⁴ The US and the EU set the new "guidelines on regulatory co-operation" aiming at boosting dialogue between the two at an early stage of the regulatory process, attempt to show up any unintended effects of new laws, publicise proposed rules, and search for alternatives in cases where problems looked likely to arise. In order to ease the transatlantic trade relationship at a time when it was being severely tested by a dispute over steel, the guidelines were negotiated under the so-called Transatlantic Economic Partnership, a US-EU trade initiative launched in 1998 to improve bilateral trade cooperation. / The Financial Times, 13 April 2002

immediately revealed its readiness to impose safeguard import curbs on 15 steel products to prevent a flood of imports from damaging its steel industry.

The Japanese government revealed its concern about the plan by the European Union to join the United States in curbing steel imports. Japan was concerned about the possibility that if every country invoked safeguard measures against each other, it would disturb the market. An abuse would have negative effects on the world's free-trade system. Japan asked the EU to comply with the rules of the WTO, in case the EU took this action.⁶⁵⁵

Despite Japan's concern, on 29 March 2002, the EU invoked the 200-day import curbs on 15 categories of steel products, which meant the imposition of tariffs of between 14.9 and 26 per cent on all imports above set quotas. These safeguard measures were expected to cover imports of around 5.7 million tonnes of steel, accounting for about 40 per cent of EU steel imports. Under the EU plan, quotas were filled on a first-come, first-served basis, not divided between specific exporters, with some developing countries exempted.

The US revealed its plan to file a complaint with the World Trade Organisation against the European Union's decision to introduce these measures. Romano Prodi, European Commission President said the EU action was designed to abide by world trade rules, in contrast to the US measures.⁶⁵⁶ The US was swift to condemn the EU's action, by questioning whether the EU action on safeguards was appropriate given that there had been no time to determine whether there had been an increase in exports that caused injury. The EU believed it already had evidence of increased imports into its market, since President George W. Bush announced tariffs of up to 30 per cent on steel entering the US. The EU normally expected to import around 27 million tonnes of steel annually, but feared that could increase by as much as 15 million tonnes following the partial closure of the US market. Officials stressed the idea was to maintain imports at around current levels. The quotas were set by taking the average of 1999, 2000 and 2001 imports and adding 10 per cent.⁶⁵⁷

Japan expressed concern that the EU import curbs violated WTO rules and may encourage other countries to take similar import restrictions.⁶⁵⁸ Katsusada Hirose, Vice Minister for Trade mentioned that "Economic damage (caused by the EU action) is not so

⁶⁵⁵ Japan's Trade Minister Hiranuma talked to EU Trade Commissioner Pascal Lamy by telephone.

⁶⁵⁶ The Financial Times, 28 May 2002

⁶⁵⁷ The Financial Times, 26 March 2002

⁶⁵⁸ The Japan Times, 27 March 2002

big as that caused by the US action. But we will discuss the issue with the EU since we can't ignore the EU action from the standpoint of the WTO trade rules."⁶⁵⁹ Japan's Trade Minister Hiranuma refrained from commenting on what impact the planned European manoeuvre would have on the EU-Japan alliance.⁶⁶⁰

4-5-2. US tariff exclusion

Facing international criticism, the US suggested its intention to use the exclusion process to try to defuse international anger over the curbs. The US started to consider new requests from foreign steel makers and US importers to exclude hundreds of millions of dollars of steel imports from tariffs. The US was desperately trying to dampen protests over the steel tariffs and weaken European and Japanese efforts to form a broader international coalition to fight the measures in the WTO. For instance, Robert Zoellick, US trade representative, warned China, which said it would press on with a complaint to the WTO, against joining the "running dogs of European imperialism" to oppose the US tariffs.⁶⁶¹

Despite the US suggestion of tariff exclusion of steel imports, Japan started to threaten the US with retaliation. On 11 April 2002, Japan called on the US to withdraw its steel tariffs or face retaliation, if Washington did not compensate it for damage caused to Japanese mills. Robert Zoellick, US trade representative claimed that Japan's steel industry was sheltered, and accused it of dumping its excess capacity on other markets. He pointed out that Japan had about 20 per cent overcapacity, while its domestic prices exceeded those for exports.⁶⁶²

As in Japan, political, public and media pressure was growing in Europe to strike back by linking the steel conflict with other issues such as a dispute over a US corporate tax scheme, in which the EU was threatening sanctions on as much as 4 billion dollars of US exports.⁶⁶³

The European Union's proposal to impose sanctions on US exports brought Brussels and Washington a step closer to their most violent showdown over trade for years. One hundred per cent tariffs totalling 377 million euros were planned to be levied on US exports of these goods to the EU. The commission drew up a longer list of products on which additional tariffs worth up to 626 million euros would be applied, if

⁶⁵⁹ The Japan Times, 9 April 2002

⁶⁶⁰ The Japan Times, 27 March 2002

⁶⁶¹ The Financial Times, 11 April 2002

⁶⁶² The Financial Times, 12 April 2002

⁶⁶³ The Financial Times, 17 April 2002

and when the EU won a WTO dispute settlement case against the US on steel. The US accused the EU of having double standards; by threatening unilateral action while claiming to be operating fully within the rules. The US claimed that the EU must wait until a WTO panel ruled in its favour before taking any counter-measures.⁶⁶⁴

4-5-3. US and EU retaliatory measures

The US warned the EU and Japan that applying sanctions unilaterally would escalate the steel dispute and undermine the multilateral trade system. The US revealed its determination of retaliation, if the European Union went ahead with plans to hit back at US safeguard measures by imposing sanctions on US exports.⁶⁶⁵ Receiving the US threat, the European Commission warned Washington that the US would violate world trade rules, if it carried out the threat to retaliate.

The US believed WTO rules entitled it to retaliate immediately against EU provisional trade safeguards on steel. Washington based its legal case on Article 19 of the General Agreement on Tariffs and Trade safeguards accord, which permitted such retaliation when safeguards caused exporters in other countries damage that was difficult to repair. Brussels claimed that would be hard to prove in the case of US steel producers, because European sales were a very small part of US total output and the EU's safeguards were designed not to reduce but to cap import levels. The US also challenged the EU safeguards in the WTO, saying they did not meet the requirement that they be imposed in critical circumstances.⁶⁶⁶

Facing mounting tensions with the US, Sweden became the first country openly to express doubts about the proposed EU sanctions, which must be approved by EU governments. Gunnar Lund, Sweden's permanent representative to the EU, said that his government was sceptical about retaliating against the US.⁶⁶⁷

Despite the disquiet from some member states, the European Union took a further step towards potential quick-fire retaliation against controversial US steel tariffs. On 7 May 2002, the 15 EU governments unanimously backed European Commission proposals to submit two lists of possible trade sanctions to the WTO. On the same day, the EU submitted its formal request for the establishment of a WTO dispute settlement panel on

⁶⁶⁴ The Financial Times, 20 April 2002

⁶⁶⁵ The Financial Times, 29 April 2002

⁶⁶⁶ The Financial Times, 30 April 2002

⁶⁶⁷ Later, Sweden tried to mitigate its strong tone against EU retaliation maneuver, explaining that the comment from Gunnar Lund was aimed not at European Commission's decision, but at sanction in general.

the steel tariffs.⁶⁶⁸ A week later, the European Union officially notified the World Trade Organisation of two lists of US products, in order to keep open the option of retaliation.⁶⁶⁹

Soon, Japan, along with Norway, joined the European Union in notifying the World Trade Organisation of plans to retaliate against US tariffs on steel imports. The moves marked a further intensification of trade hostilities over US steel policy, which attracted global condemnation. Japan targeted nearly 5 million dollars worth of US steel products on which it might slap 100 per cent tariffs from mid-June 2002. Norway's list targeted 5.6 million dollars in extra duties.⁶⁷⁰ On 22 May 2002, Japan, followed by South Korea, announced that they would join the European Union in calling for a WTO panel to rule on the legality of the US measures. Brazil and New Zealand also filed formal WTO complaints.⁶⁷¹

Trade retaliation against the US safeguard was set at more than 800 million dollars (870 million euros) on US products by WTO members, according to sanction lists lodged by the EU (583 million dollars), Japan (123 million dollars), China (94 million dollars), Norway (6 million dollars) and Switzerland (3 million dollars). If the US tariffs were not withdrawn, sanctions would be imposed automatically after three years, in March 2005.⁶⁷² The EU and Japan also said they might impose tariffs worth 364 million dollars and 5 million dollars respectively on a smaller list of US products in a few weeks under WTO provisions that allowed swift retaliation, if there had been no "absolute increase in imports". The US claimed that early retaliation was unjustified and threatened counter-moves. On retaliation against the US, one of the members of the Japanese delegation revealed that there had been prior consultation between the EU and Japan. When retaliation was discussed, the EU and Japan carefully chose the items for retaliatory tariff-imposition, so as not to harm each other's trade, but impose damage on the US most effectively.⁶⁷³

At this stage, the EU, Japan and ten other countries including South Korea, China and Norway had demanded compensation under the WTO's safeguards agreement.⁶⁷⁴

⁶⁶⁸ The Financial Times, 8 May 2002

⁶⁶⁹ The Financial Times, 15 May 2002

⁶⁷⁰ Japan, South Korea, China, Switzerland and Norway said in April that they intended to follow the EU with panel requests of their own.

⁶⁷¹ On the same day, the US blocked the EU request for the establishment of a panel at the meeting of the WTO's DSB on 22 May 2002.

⁶⁷² Brazil, South Korea, Australia and New Zealand had reserved the right to notify retaliation at any time before the three years were up.

⁶⁷³ Interview was conducted in July 2005 in Geneva Switzerland.

⁶⁷⁴ In a meantime, US safeguard measures spread the same protectionist manoeuvre to other WTO members. China raised tariffs of up to 26 per cent on its steel imports, claiming the temporary move was necessary to end a surge in imports caused by

Although momentum was gathering in the EU and Japan to retaliate, the EU alone suddenly revealed its readiness to delay retaliatory trade sanctions over US steel tariffs.⁶⁷⁵ This EU move was seen as an effort to persuade Washington to ease restrictions on European steel imports. However, the EU clearly stated that the sanctions would be implemented, if the US offer would not satisfy the EU. Despite the sign of EU compromise, the tension between the EU and US was continuing. On the same day when the EU softened its stance, the US took the first formal step in a separate complaint against the EU that could further escalate the dispute. The US asked the WTO to form a dispute settlement panel to hear a complaint that the EU violated trade rules by imposing its own restrictions on steel imports.⁶⁷⁶ A few days later, the European Union was successful in having the WTO set up a panel to rule on US steel tariffs. Six US safeguard measures, including curbs on steel, were examined in the WTO⁶⁷⁷ and were condemned by the EU for allegedly breaching WTO rules.⁶⁷⁸ While the US and the EU had shown willingness to reduce the possibility of mutual retaliation, they finally decided to start the legal battle in the WTO.

After all, the EU was not satisfied with the US offer to exclude European imports from its safeguard tariffs as proposed in bilateral talks. The EU estimated that the 247 product exclusions announced so far covered 330,000 tonnes of EU steel, worth about 230 million dollars out of total EU exports of 2.3 billion dollars affected by the tariffs. The European Commission condemned as "manifestly insufficient" the exemptions so far granted by Washington from its tariffs on steel imports. However, the EU still postponed the decision of whether to retaliate immediately against the US.⁶⁷⁹

After seven successive announcements by the US of exemptions from the duties, in September 2002, the European Commission finally shelved its threat of immediate retaliation against US steel tariffs. The announcement of numerous exemptions from the US tariffs persuaded the EU to hold fire, pending the outcome of a WTO dispute settlement panel on the issue.⁶⁸⁰ This EU decision was based on its confident expectation

diversion from the closed US market. Japan said it was seeking consultations with China on the new tariffs, and South Korea had also expressed disquiet / The Financial Times, 24 May 2002

⁶⁷⁵ The delay followed conciliatory words from US Undersecretary of Commerce, Grant Aldonas, following meetings with senior Commission officials in Brussels.

⁶⁷⁶ The Financial Times, 1 June 2002

⁶⁷⁷ Six US safeguard measures included also curbs on non-steel-related products such as wheat gluten and lamb. / The Financial Times, 4 June 2002

⁶⁷⁸ The Financial Times, 4 June 2002

⁶⁷⁹ The Financial Times, 18 July 2002

⁶⁸⁰ The Financial Times, 26 September 2002

that it would obtain further concession from the US.⁶⁸¹ Simultaneously, the EU decided on a significant reduction of its safeguard measures, applying them to 7 product categories compared with the original 15 categories. As a result, 40 per cent of total EU steel imports was planned to be covered by EU safeguard measures.⁶⁸²

4-5-4. WTO ruling against the US

On 26 March 2003, the WTO ruled that the US violated international trading rules with its imposition of safeguard measures.⁶⁸³ The EU, Japan and six other co-complainants claimed full victory and threatened retaliation. They claimed in a joint statement that the verdict left the US with no other choice but to terminate its WTO-incompatible safeguard measures without delay. Receiving the ruling, the US immediately announced its readiness to appeal.⁶⁸⁴

The European Union announced that it would levy trade sanctions against the US in mid-December 2003, if Washington did not lift its tariffs on steel imports. EU Trade Commissioner, Pascal Lamy claimed that the EU had little choice but to insist on compliance with the WTO rules, as the US did in previous disputes over bananas and beef hormones.⁶⁸⁵ Japan said it was also prepared to levy trade sanctions against the US. The US could face the largest sanctions in the history of the WTO. Pascal Lamy, the European Union Trade Commissioner, said that the EU would slap tariffs of 8 per cent to 30 per cent on 2.2 billion dollars worth of US imports.⁶⁸⁶

US steel makers recognised the tough situation which the Bush administration faced. They told the White House that they would accept an early removal of tariffs on imported steel but remained opposed to the immediate repeal demanded by the European Union and other trading partners.⁶⁸⁷ The concessions was a sharp turn away from the industry's original insistence that the tariffs remain in place for a full three years. The industry hoped the scheme might be sufficient to stave off the EU's and Japan's threats to retaliate by imposing tariffs on US imports. However, the EU viewed any such

⁶⁸¹ Pascal Lamy, the European Union Trade Commissioner, had confidence that the US would grant European steel companies further concessions from punitive US import duties before the end of 2002. The EU decided to wait for the WTO ruling on the legality of the US measures. / *The Financial Times*, 1 October 2002

⁶⁸² *The Financial Times*, 1 October 2002

⁶⁸³ For details, see: Sean D. Murphy, 'WTO decision striking down US steel safeguard measures' in *the American Journal of international law*, Vol. 98, No. 1, (American Society of International Law, Jan. 2004), P179-180

⁶⁸⁴ *The Financial Times*, 27 March 2003

⁶⁸⁵ *The Financial Times*, 5 November 2003

⁶⁸⁶ *The Financial Times*, 11 November 2003

⁶⁸⁷ *The Financial Times*, 19 November 2003

accelerated phase-out of the US tariffs as clearly insufficient, particularly since the EU's case had repeatedly triumphed at the WTO. Commission officials maintained that they were not negotiating with Washington but instead waiting for the US to comply with the WTO's verdict and withdraw the tariffs.⁶⁸⁸

In the meantime, Japan became the first country which sent in a formal notification of retaliation.⁶⁸⁹ In November 2003, Japan threatened to impose 85.2 million dollars (71million euros) in retaliatory tariffs on US imports, in response to the US decision to keep its steel tariffs intact despite a WTO ruling.⁶⁹⁰ Tokyo officially notified the WTO of a list of rebalancing tariffs of up to 30 per cent on US products, including steel products, plastics and coal, after a finance ministry committee approved the list of sanctions.⁶⁹¹ This was the first time Japan threatened retaliatory tariffs against its single largest trading partner.⁶⁹²

In order to avoid retaliation, the US asked the EU and Japan for more time to complete internal consultations. Receiving the US request, Pascal Lamy, the EU Trade Commissioner mentioned that, apart from the steel tariffs, the US record of compliance with WTO rulings had been relatively good. Based on this view, the US finally reached a settlement with Japan and the EU, after the EU, Japan and six other countries gave the US extra days to comply with the WTO ruling. By doing so, the EU and Japan played down the fear that the confrontation over safeguard issues would develop into a sharp deterioration in relations with the US.⁶⁹³

The WTO ruling against the US safeguard was another victory for the EU and Japan, which played a central role among the economies affected by the US safeguard measures. After all, the case of safeguard provided very important opportunities for the EU and Japan to work together for a common goal, but it also showed the fragility and incompleteness of their cooperation. This fragility stems from the structural differences in their steel trade. Unlike Japan - a leading steel exporter- , the EU is both a big steel importer and exporter and had therefore felt compelled to invoke its own safeguard measure to protect its steel market.

⁶⁸⁸ The Financial Times, 19 November 2003

⁶⁸⁹ The Financial Times, 28 November 2003

⁶⁹⁰ The amount of the retaliatory tariffs, at 85 million dollars, was equivalent to the estimated losses suffered by Japanese steel makers.

⁶⁹¹ The highest tariffs Japan was set to impose on US goods, at 30 per cent, were on intermediate goods such as petroleum, gold and steel. The lowest tariffs, at 5 per cent, were set to be imposed on consumer goods, such as handbags, clothing and linens.

⁶⁹² The Financial Times, 27 November 2003

⁶⁹³ The Financial Times, 28 November 2003

5. WTO Dispute Settlement System

As we have seen in this chapter, steel trade issues are closely related to the increased use of US protectionist measures and to legal battles in the WTO. Therefore, this part of chapter is devoted to analyse the function of the WTO, particularly its dispute settlement system, and to see how it affected the EU-Japan relationship. This steel chapter is a good example to illustrate the EU's and Japan's involvement in multilateral resolutions of trade conflicts. Therefore, we will go beyond the steel trade issue and consider the role of the WTO, particularly the DSB for the EU and Japan.

5-1. Increased use of protectionist measures by the US

A factor which promoted EU-Japan relationships on various steel trade issues has been the growing protectionism in the United States, especially increased resort to measures involving legal procedures for determining when firms have exported 'unfairly' by selling below cost (dumping) or receiving government subsidies. These measures include remedies funded by AD or CVDs. The imposition of these duties constitutes a unilateral retrogression from WTO rules. As AD and CVD procedures have increasingly been used, analysts have sought to find ways of strengthening the rules to avoid protectionism.⁶⁹⁴

In theory, a case can be made for AD and CVD when the exporting firm intends to use predatory pricing to obtain monopoly control in a given market. In reality, however, the test for AD and CVD cases is much weaker. In the United States, for example, a foreign firm can be found to be dumping even if it is selling well above marginal cost or if it fails to provide adequate information in the time stipulated by the American authorities. Even different timing of the recording of sales in the home and the foreign market could result in a finding of dumping when sales prices were, in fact, identical. The harassment value of an AD or CVD suit may be considerable for the foreign firm against which the complaint is filed, as is evidenced by the number of times countries have agreed to VERs to avoid AD or CVD proceedings and penalties.⁶⁹⁵

In addition to administered protection, the tendency to negotiate bilaterally has increased, again especially by the United States. Since the mid-1980s, US trade policy become increasingly aggressive and bilateral. Even if bilateralism were confined to the United States, there would be cause for concern as such dealings further undermine support for open multilateralism, instead moving toward Regional Preferential

⁶⁹⁴ Kruger, 'WTO as an international organisation', P23

⁶⁹⁵ Kruger, 'WTO as an international organisation', P8

Arrangements or other mechanisms for protecting one's producers from the vagaries of administered protection and bilateral pressures.⁶⁹⁶

A number of aspects of US trade policy seemed to indicate a lack of commitment to the multilateral system. The United States exerted not only bilateral pressures on its key trading partners such as Japan without resort to the multilateral trading system, but it also threatened to adopt measures such as Super 301 which violate WTO principles.⁶⁹⁷

5-2. Reinforced Dispute Settlement System in the WTO

Our research in this chapter revealed the fact that the establishment of the WTO, especially the reinforced Dispute Settlement System, promoted EU-Japan relationships by providing an arena for them. The WTO was assigned responsibilities additional to those earlier carried out by the GATT. There are also added functions in the WTO which were a significant improvement of the GATT trading system.

In 1945, when the other Breton Woods institutions were established, world government leaders determined that it would be necessary to create another institution specialising in international trade, the International Trade Organisation (ITO). However, the ITO did not come into force because parliaments, particularly the US Congress, would not approve it in the late 1940s. Therefore, its substitute, the GATT, remained merely a multilateral trade and tariff agreement. For this reason, although the GATT trade negotiations were remarkably successful, it contained some defects in its function. Among the defects, the weakness of Dispute Settlement System was notable.

The very success of the multilateral tariff negotiations conducted under the aegis of the GATT made the world become more interdependent at an unprecedented rate. That interdependence generated a number of new challenges for the international trading system as well as a number of trade disputes. In response to the increase in trade conflicts, the Uruguay Round resulted in a new treaty text on dispute settlement, the 'Dispute Settlement Understanding' (DSU). For the first time, contracting parties obtained a substantial binding treaty text with respect to dispute settlement for the newly established WTO. Thus, the creation of the WTO led to significant and institutional innovations that allowed the disputes settlement system to gain credibility, predictability and legitimacy in the global trading system.

John H. Jackson points out that the major change in the WTO Dispute Settlement System is the elimination of 'blocking' of a final panel report. Blocking was a major

⁶⁹⁶ Kruger, 'WTO as an international organisation', P9

⁶⁹⁷ Kruger, 'WTO as an international organisation', P19

defect of the previous system in the GATT, which is no longer permitted in the WTO.⁶⁹⁸ In the past, it was possible for any Contracting Party to the GATT to frustrate dispute settlement by blocking either the establishment of a panel or the adoption of a panel report.⁶⁹⁹ Thus, the DSU made the establishment of a panel more ‘automatic’ in the event of a dispute, whereby reports of a dispute settlement panel and the appellate panel will almost always become binding.

Saadia M. Pekkanen argues that among the general improvements in the WTO Dispute Settlement System, the speed of dispute settlement is a major advancement.⁷⁰⁰ In the WTO dispute settlement system, unless the members of a dispute agree otherwise, the rules automatically preset the entire period of a dispute, from the date of establishment of a panel to the adoption of the reports, generally to nine months if there is no appeal, and to twelve months if there is one. This emphasis on speed is decidedly better than having the dispute drag on interminably with no end in sight, which was often the case in trade disputes involving the United States, Japan and the EU under the old GATT.

As we have seen in this chapter and also in Chapter 2, the EU and Japan effectively used the improved Dispute Settlement System in the WTO in order to resolve trade frictions between them, as well as trade disputes with the United States. Obviously, not only the common international trade rules of the WTO but also the reinforced mechanism of Dispute Settlement System encouraged the EU-Japan resort to the multilateral resolution of trade conflict.

5-3. The EU and the DSB

Although the EU cooperated with Japan within the WTO on numerous occasions, trade imbalances dominated when it came to their bilateral relationship and forced the EU to share the same concern with the US. The EU reacted with anti-dumping procedures and other policies to prevent excessive imports from Japan, and it emphasised Japan's closed market to European products and services as one of the most significant problems between them. In this respect, European and American criticisms of Japanese economic practices were often similar, accusing Japan that its market was to a very high extent

⁶⁹⁸ John H. Jackson, ‘Effective Dispute Settlement Procedures’ in Anne O. Krueger (eds), ‘the WTO as an international organisation’, (Chicago, the University of Chicago Press, 1998), P163, 164

⁶⁹⁹ Woolcock, ‘European Trade Policy’ in Helen Wallace and William Wallace, ‘Policy-Making in the European Union’ Fourth Edition, P387

⁷⁰⁰ Saadia M. Pekkanen, ‘Sword and Shield – the WTO Dispute Settlement System and Japan’ in Ulrike Schade and William Grimes (eds), ‘Japan’s managed globalisation’, (New York, M.E. Sharpe, 2003), P81

protected against imports by the structure of the Japanese economy and society as well as by the government.

Despite the fact that the Europeans shared interest with the US in terms of opening the Japanese market, the Europeans were also increasingly concerned about US protectionism.⁷⁰¹ For instance, on automobiles, the Europeans criticised the US for its pressure of setting numerical targets for the purchase of US vehicle parts by Japanese carmakers, since such import increases of US products negatively affected European exports to the Japanese market. Therefore, the Europeans constantly expressed concern and dissatisfaction with US pressure on Japan for a results-oriented approach as well as US unilateral measures such as Super 301.

Behind the European concern was the realisation that it had less influence on Japanese trade policy compared with the US. For this reason, although Europe considerably depended on the use of bilateral measures in order to cope with Japanese trade surpluses, there was also a strong desire on their part to strengthen multilateral trade rules to confine US protectionist pressure on Japan. Concerns regarding US pressure on Japan led not only to the motivation to support the creation of the WTO but also to forging closer links between the EU and Japan in view of their shared interests.⁷⁰²

This indicates that in spite of trade frictions, the EU and Japan maintained a relatively good relationship, and they shared the same concern about US pressure. The EU's concern about US pressure in the steel trade dispute is remarkable and became a platform for EU-Japan cooperation on steel trade (See 4-4 of this chapter). As in the case of steel, the EU utilised the binding rules of the WTO Dispute Settlement System. This was in contrast to the EU's attitude towards the previous GATT Dispute Settlement System which the Europeans regarded as a political process. The EU's acceptance and utilization of a compulsory and binding legal system of Dispute Settlement System was a drastic change in the EU's trade policy.⁷⁰³

5-4. Japan and the DSB

An important factor which promoted Japan's positive commitment in the WTO is the drastic change in Japan's trade policy. Facing result-based trade policies used by

⁷⁰¹ Gregory C. Shaffer, 'Defending Interests – Public-private partnerships in WTO litigation', (Washington DC, Brookings Institution Press, 2003), P102

⁷⁰² Stephen Woolcock, 'Market Access Issues in EC-US Relations –Trading Partners or Trading Blows?', (Paris, Royal Institute of International Affairs, 1991), P22. P23

⁷⁰³ Pieter-Jan Kuyper, 'The new WTO Dispute Settlement System: the impact on the community' in Jacques H. J. Bourgeois, Frederique Berrod and Eric Gippini Fournier (eds), 'The Uruguay Round Results', (Brussels, European Interuniversity Press, P92

Europe and the US, Japan realised that full compliance with the GATT rules could prevent other countries' use of GATT-incompatible trade measures aimed at Japanese export strategy and Japanese advantage related to its political economic system which were not regulated by the GATT. Japan's strategy to comply with GATT was a result of the Japanese experience as the passive partner in an international trade system where the rules were set by the US and Europe.⁷⁰⁴

From its accession to the GATT in 1955 until around the end of the Uruguay Round in 1994, Japan studiously tried to avoid using the GATT machinery to resolve its trade problems. While the GATT dispute settlement system was in effect, a total of twenty-three complaints were recorded against Japan. Japan, however, registered a mere five complaints in return across the same period of time.

As Saadia M. Pekkanen argues, Japan simply avoided legal embroilment in the GATT Dispute Settlement System, whether as complaint or defendant.⁷⁰⁵ Instead, Japan preferred to reach bilateral settlements with its trade partners behind the scenes in a nonconfrontational manner. Pekkanen named two main reasons for Japan's reluctance to use the GATT dispute settlement system: 1.) Japan wished to avoid drawing attention to its many protectionist trade measures and policies then in force; 2.) There was a perception within Japan that the GATT was biased against Japan, and it would not render fair rulings in Japan's favour.

However, Japan's perception and attitude towards the GATT was changed by some successful GATT dispute settlements in favour of Japan, such as the case with the EC on anti-dumping or anti-circumvention. Such favourable GATT rulings for Japan reinforced emerging domestic options and perceptions in favour of the use of international legal rules to handle trade disputes.

In her work 'Sword and Shield', Saadia M. Pekkanen argues that like most other countries after 1995, Japan moved increasingly toward the use of the legal rules of the WTO as a means of resolving contentious trade conflicts and concerns.⁷⁰⁶ By 1995, the Japanese trade policy establishment was fully geared up to use the WTO rules as a functional strategy, which allows Japan to use the legal rules both as sword with which to challenge the measures and practices of its trade partners, and as a shield for domestic measures and practices. Anti-dumping cases with the US on the steel trade, which we

⁷⁰⁴ Woolcock and Yamane, 'RIIA special paper, EC-Japanese trade relations: what are the rules of the game?', P32-37

⁷⁰⁵ Pekkanen, 'Sword and Shield – the WTO Dispute Settlement System and Japan', P83

⁷⁰⁶ Pekkanen, 'Sword and Shield – the WTO Dispute Settlement System and Japan', P77-97

have seen in Chapter 4, were mentioned by Pekkanen as a good example of Japan's use of the WTO as a sword.

In invoking the dispute settlement processes at the WTO, Japan essentially used an entirely legitimate set of legal tactics to ward off foreign pressures and to try to preserve its domestic measures to the extent possible. The emphasis of Japan's trade diplomacy was important in allowing Japan to confront its trade partners on an equal legal footing. Japan's trade strategy made its trade partners perceive that the most important policy implication in dealing with Japan would be largely a matter of playing by the rules of the WTO.

However, the multilateral trading system is not completely protected against aggressive bilateral trade policy.⁷⁰⁷ Japan realises the fact that it alone cannot resist US protectionist and bilateral pressure. In order to restrain increasing protectionist pressure in the US, it is indispensable to form a coalition with other countries which share the same interests.

Besides, standing on the same side as the EU rules out the worst case that the EU and US team up against Japan. For example, the EU vehemently demanded to join the US-Japan semiconductor agreement in ministerial meetings after gaining an informal consent from the US.⁷⁰⁸ In order to avoid such a worst case, it appears to be crucial for Japan to keep focusing on the common interest with the EU and keep it on the same side. In the past, when Japan had serious trade frictions with the Europeans, Japan used the tactic to dilute the Community's authority and cohesion by insisting on including the United States in trade talks.⁷⁰⁹ This suggests that the current EU-Japan cooperation in the WTO might be a Japanese tactic to include the EU in trade talks between Japan and the US, in the expectation of using the EU's opposition against US protectionism for its own benefit.

Conclusions

This chapter investigated EU-Japan relationships on steel trade by examining their reactions to various steel-related trade disputes with the United States. Following agricultural trade, steel trade is the most crucial for the EU and Japan, due to the size of their steel trade and the domestic importance of steel industry. Trade tensions caused by

⁷⁰⁷ Horst Siebert, 'What does globalisation mean for the world trading system?' in the WTO Secretariat, 'From GATT to the WTO: the Multilateral Trading System in the New Millennium, (Hague, Kluwer Law International, 2000), P144

⁷⁰⁸ Murakami, 'WTO – Sekaiboueki no yukue to Nihon no sentaku', P149

⁷⁰⁹ Nester, 'European Power and The Japanese Challenge', P251, 252

steel trade had been looming for a long time, as steel production was hit by overcapacity. It became a common agenda for many steel-trading economies to promote their exports, while granting protection to their domestic steel industry from fierce international competition.

In steel issue, there is a significant structural difference between the EU and Japan. The difference is somehow the exact opposite from their structural difference in agricultural issue. While Japan's main interest was to promote its steel exports, the EU's prime interest was protecting its internal steel market. Like agricultural issues, both the EU and Japan are keen on protecting or promoting steel industries.

US protectionism on steel imports framed to a large extent the degree of relationship between the EU and Japan. The EU and Japan shared the same concern over the US threat to invoke unilateral trade remedies such as Section 301, as well as US bilateral pressure. Against US protectionist remedies, the EU and Japan responded by bringing the case into the WTO. The WTO dispute settlement system provided an arena for concerned economies to solve disputes in a multilateral context.

Once, a case is brought into the WTO, a dispute settlement occurs along established judicial procedures without leaving any space for political influence from members. This system helped the EU and Japan to avoid to some degree bilateral tensions with the US throughout the dispute settlement procedure. The process, as Stephen Gill explains with "new constitutionalism", places restraints on the democratic control of public and private organisation and institutions.⁷¹⁰ These restraints would complement the discipline of market forces to constrain the policy autonomy of governments. This particular function of the WTO will be analyzed later in the main conclusion.

⁷¹⁰ Stephen Gill (edt.), "Gramsci, Historical Materialism and international Relations", (Cambridge University Press, 1993), P10, 11

Chapter 5
Conclusion

1. Introduction

In the previous chapters, we have investigated the relationship between the EU and Japan in the WTO. Because of the nature of WTO's function, which deals mainly with member states (with exception of the EU), the "state" remains as a main actor. However, it became clear that behind their relationship, various social forces significantly influenced the action of the EU and Japan. In this chapter, as a conclusion, we will look closely at social forces and investigate how social forces influenced the position of the EU and Japan, as well as the WTO. Besides this, we will also analyse how the function of the WTO has influenced the EU and Japan, and their relationship.

This thesis raised the question about liberal trade theory and its serious gap between theory and actual practices, and suggested an alternative approach to structural issues of the state-centric approach to world politics. While we consulted neo-liberal institutionalist theory to investigate the role of the WTO and its influence upon the EU-Japan relationship, we also carefully observed the relationship of various social forces within the EU and Japan from a neo-Gramscian perspective.

The Neo-liberal institutionalist approach focuses on the role of the institution and its influence upon states. Since the WTO deals only with states, such a neo-liberal institutionalist approach was useful. While the influence of the institutions on state actors is important, how the state actors and various social forces within the state influence the institution and shape world politics is an equally important research topic, which has not been thoroughly researched yet.

Therefore, in an attempt to complement such shortcomings of the neo-liberal institutionalist theory, from a neo-Gramscian perspective, we tried to direct attention to concentrating solely on state dominance. The conceptual framework developed by neo-Gramscian perspectives rethinks prevalent ontological assumptions in IR due to a theory of hegemony that focuses on social-class forces engendered by changes in the social relations of production, forms of state and world order.⁷¹¹

2. Summary and the examination of hypotheses

To summarise, this thesis introduced an alternative approach to structural issues of hegemony and world order to that in mainstream debates in IR. Notably, a case was made for a critical theory of hegemony that directs attention to relations between social interests in the struggle for consensual leadership rather than concentrating solely on state dominance.

⁷¹¹ Morton, 'Unravelling Gramsci', P135

Hegemony here is understood as "the articulation and justification of a particular set of interests as general interests, appears as an expression of broadly based consent, manifested in the acceptance of ideas and supported by material resources and institutions, which is initially established by social-class forces occupying a leading role within a state".⁷¹² This concept of hegemony is a clear contrast to the conventional IR theory, which reduces hegemony to a single dimension of dominance based on the economic and military capabilities of states. Hegemony is therefore a form of dominance, but it refers more to a consensual order, so that 'dominance by a powerful state may be a necessary but not a sufficient condition of hegemony. If hegemony is understood as an 'opinion-moulding activity', rather than brute force or dominance, then, consideration has to turn to how a hegemonic social or world order is based on values and understanding that permeate the nature of that order.⁷¹³

There are clearly a variety of neo-Gramscian perspectives dealing with a diversity of issues related to the analysis of hegemony/supremacy in the global political economy. Various neo-Gramscian perspectives provide an alternative critical theory route to hegemony by focusing on social classes in the social relations of production, forms of state and world order.⁷¹⁴

In the introduction, we have set the following hypothesis: By creating the conditions for the hegemony of transnational capital, utilising and strengthening the system or function of the WTO, social forces within the EU and Japan joined the forces beyond national boundaries and attempted to create international rules and norms in favour of their interests. In other words, depending on trade issues, various social forces within the EU and Japan, with the same or similar interests, have effectively utilised the international organisation and significantly contributed to the creation of general conditions of hegemony by influencing the trade policy of each government (See Table - 11).

Our empirical research shows that the creation of the WTO facilitated cooperation between social forces in different countries by moulding consensus in the international level, although the question remains, as to if the creation of the institution contributed to the creation of new hegemony (or supremacy) in world economy. We have also witnessed that once such consensus is made in the international level within an international organisation, new international rules or norms may even override domestic

⁷¹² Morton, 'Unravelling Gramsci', P113

⁷¹³ Morton, 'Unravelling Gramsci', P113, 114

⁷¹⁴ R.W. Cox, 'Production, Power and World Order: Social Forces in the Making of History', (New York, Columbia University Press, 1981), P126-155

rules and will start functioning as a global standard.

Table-11: Main social forces in our empirical research

Before the establishment of the WTO	Automotive industry, whisky makers, Keiretsu group, MOFA, MITI, MOFF, etc.
Agricultural issue in the WTO	Agricultural industry, farm lobby, farmers union, the Ministry of agriculture in Japan, etc.
Steel issue in the WTO	Steel industries, US Congress, the Clinton administration, US International Trade Commission, the European Commission, the Iron and steel federation in Japan, MITI, etc.

The agricultural case illustrates how social forces have a serious effect on a country's national trade policy. For the EU and Japan, the domestic importance of the agricultural sector is marginal in the overall economy of both sides. However, this relatively small sector prevented both economies from playing a more pro-active role in farm liberalisation talks in the WTO. Social forces, such as the agricultural industry and farm lobbies fully utilised their political clout to the national agricultural trade policy. National trade policies heavily influenced by particular social forces may face the necessity to find like-minded WTO members at agricultural talks in order to achieve their goals in a multilateral level. To form an ally is necessary in the multilateral level, since during the Uruguay Round, the EU and Japan needed to make considerable concessions due to the fact that a solid ally of the US and Carins Group showed a clear cooperation and managed to put mounting pressure on both the EU and Japan.

In the process of forming a group or ally in the multilateral level, social forces often overcome the structural differences in the sector in order to achieve the highest common factor. For example, Japan's main interest in agriculture was to protect its agricultural market, while the EU's main goal was to promote its agricultural export. To achieve their goals, both the EU and Japan, social forces in the agricultural sector managed to obscure their structural differences and created a united front under the common goal against farm liberalisation talks.

The steel case showed the detailed process in which the EU and Japan utilised the WTO as an international organisation and its judicial function. A series of judicial procedures on steel products are again largely motivated by domestic social forces,

namely the steel industry. Like the agricultural industry, though the steel sector plays a marginal role in terms of world trade, domestic politicians cannot ignore the political influence of the steel sector. The steel case shows that the creation of the WTO facilitated cooperation between social forces in different countries by moulding consensus in the international level. Social forces in this case are mainly steel industries, trade representatives and politicians. Severe outcry from domestic steel makers and heavy government involvement in the steel industries made the steel case politically important also in the multilateral level.

Both the EU and Japan, in invoking the dispute settlement processes at the WTO, used an entirely legitimate set of legal tactics to ward off foreign pressure (mainly pressure from the United States). Utilizing the WTO's dispute settlement system was an important change particularly in Japan's trade diplomacy, which in the past often solved trade frictions with the United States bilaterally. The emphasis of trade diplomacy of utilising an international organisation as a mean of solving conflicts allows the EU and Japan to confront its trade partners on an equal legal footing. Such foreign trade policy sends their trade partners a strong message that the most important policy implication to deal with the EU and Japan is to take a legal action in WTO's dispute settlement system.

Such legal procedure in the WTO also facilitated the cooperation between social forces in the EU and Japan, since the WTO's judicial procedure allows other members to take part in a dispute as a third party. This rule allowed social forces within the EU and Japan to coordinate their strategy and get involved in each other's trade disputes. In fact, after the successive WTO ruling against the US anti-dumping duties, the EU and Japan seemed to gain more confidence with their strategy of utilising the WTO and moulding international opinion by rallying support from like-minded economies.

Like the agricultural or steel industry, non-state actors such as interest groups and multilateral cooperation are becoming increasingly influential as social forces. Such social forces have effectively utilised the international organisation and significantly contributed to the creation of general conditions of hegemony by influencing the trade policy of each government. Multilateral trade rules in the WTO and its judicial system became an impetus and common ground for consent among various social forces in the multilateral level. Robert. W. Cox defined hegemony as: "the articulation and justification of a particular set of interests as general interests, appears as an expression of broadly based consent, manifested in the acceptance of ideas and supported by material resources and institutions, which is initially established by social-class forces occupying a leading

role within a state".⁷¹⁵ As he asserts, if hegemony is understood as an 'opinion-moulding activity', rather than brute force or dominance, what we have witnessed in WTO trade negotiations could be considered as a form of hegemony created by social forces utilising the international organisation. Social forces which succeeded to influence their national government and later regional and multilateral trade rules could be considered as the main actors which created hegemony as consensual order. If so, the findings in this theory effectively supports my hypothesis: By creating the conditions for the hegemony of transnational capital, utilising and strengthening the system or function of the WTO, social forces within the EU and Japan joined the forces beyond national boundaries and attempted to create international rules and norms in favour of their interests.

3. Three level approach

As Linda Weiss and John M. Hobson assert, cooperative combining of social energies is the core of state strength.⁷¹⁶ Collaborative linkage is what gives states an unusual capacity for effective intervention, particularly in the context of a highly integrated world economy. At the same time, states face strong opposition from some social forces domestically. What we have witnessed in agriculture and steel issues support this theory. Politically powerful agricultural and steel industries actively participated in various forms to shape national policy in favour of their interest. However, the attempt to reflect their interest on national policy is merely the first step for the industries. The final goal of the industries is for their government to make their national policies prevail globally in order to achieve international agreements in international institutions which will provide a favourable condition for themselves. Therefore, for the creation of hegemony of social class forces, the role of the institution is indispensable.

Besides, international institutions help countries overcome domestic opposition and conclude mutually beneficial agreements with the other countries in the world. The WTO has independent jurisdiction, its rules and rulings are binding on all members, and it has the power to impose sanctions, to overrule state and local powers, and to override national regulatory powers. As the WTO is the supranational institution with an enforcement capacity on its members, its decision has a direct impact on domestic social forces within states. In this sense, the state is not unquestioningly taken as a distinct

⁷¹⁵ R.W. Cox, 'Social Forces, States and World Orders: Beyond International Relations Theory', *Millenium Journal of International Studies* Vol.10 (2) (London, London School of Economics, 1981), P139

⁷¹⁶ Linda Weiss & John M. Hobson, 'States and Economic Development', (Polity Press, Cambridge), P170

institutional category, or thing in itself, but conceived as a form of social relations through which capitalism and hegemony are expressed. Therefore, state should be understood, not just as the apparatus of government operating within the 'public' sphere (government, political parties, military) but also as part of the 'private' sphere of civil society (church, media, education) through which hegemony functions. Hegemony is created by various social forces within the state, and once hegemony has been consolidated domestically it may expand beyond a particular social order to move outward on a world scale and insert itself through the world order. By doing so it can connect social class forces across different countries.⁷¹⁷

For example, in the liquor tax dispute between the EU and Japan, Japanese whisky producers maintained a cooperative stance with a Scottish whisky maker, as well as the EU, in order to demand the Japanese government to change its liquor tax system (see Chapter 2). In another example, Japanese business groups, such as Keidanren (the Federation of Economic Organisations) also have regular contact with their European counterparts and with European officials, while the European Business Community in Tokyo lobbies actively among Japanese decision-makers. According to Atsuko Abe, such activities by private actors influence, or sometimes even replace, government-level decisions as resolutions for economic conflicts. Therefore, diversity of actors with different interests is an important element in deciding a country's foreign trade policy. Making matters more complicated, the agenda of WTO trade negotiations is broadening, bringing in new actors, such as Non-Governmental Organisations (NGOs).⁷¹⁸

The complexity of the issue concerning diversified actors is even more conspicuous with the EU. The EU is a composite player, consisting of twenty five countries (as of May 2004) with various interests on various topics. Therefore, it is very difficult for the EU to coordinate its foreign trade policy. Between the member states, there are fundamental differences in trade culture, ranging from protectionism to free trade.⁷¹⁹ Such disunity of the EC/EU was utilised in the past by Japan to deal with some of the trade problems with the EC/EU. Within the framework of bilateral trade relations, Japan often undermined the EC/EU by negotiating with European countries separately. For example, Japanese car makers established a friendly relationship with the British government through their direct investment in the UK. This helped the Japanese

⁷¹⁷ Morton, 'Unravelling Gramsci', P120, 121

⁷¹⁸ Woolcock, 'European Trade Policy', P373

⁷¹⁹ Michael Smith, 'The European Union' in Brian Hocking and Steven McGuire (ed.), 'Trade Politics, International, Domestic and Regional Perspectives', (London, Routledge, 1999), P276-278

transplant cars to be excluded from the formal agreement between the Japanese government and the EC. Members of the EC reacted differently towards Japan's trade policy. Japan utilised the 'divide and conquer' strategy to deal with a non-unified EC (see Chapter 2).

The WTO is essentially not concerned with the behaviour of private businesses. It deals only with the actions of governments, establishing disciplines on trade-policy instruments such as tariffs, quotas, subsidies, or state-trading. The WTO is a regulator of the regulatory actions of governments that affect trade and the conditions of competition facing imported products on domestic markets.⁷²⁰ This is also the same with the WTO Dispute Settlement Body. As the WTO represents an inter-governmental agreement, private parties do not have legal standing before the WTO DSB. The private sector must go through its government.⁷²¹

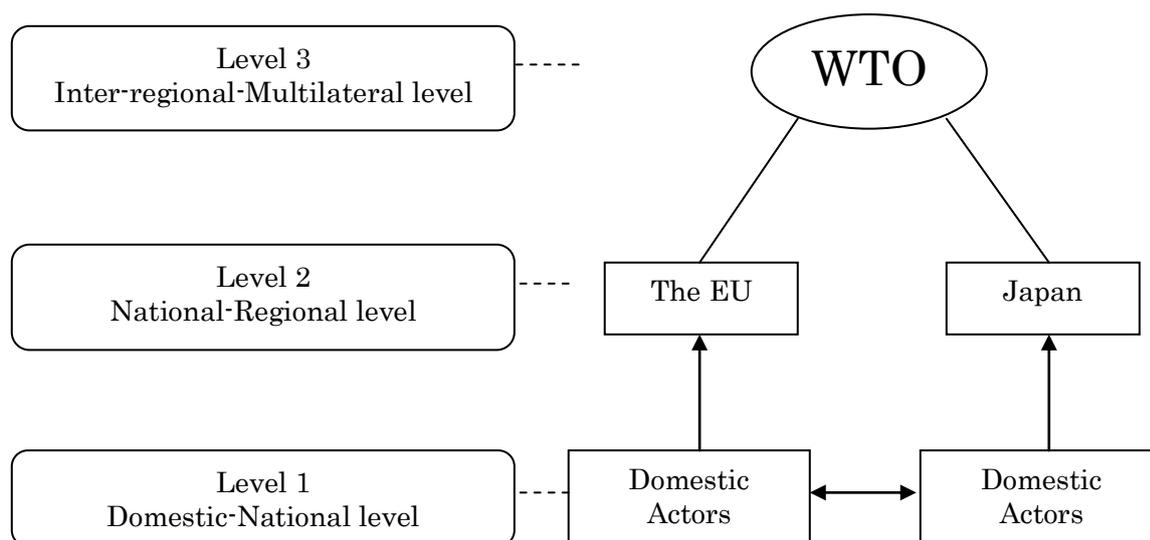
Within the EU, individual EU member states do no longer have sovereignty over trade policy. This has been delegated to the Commission of the European Communities. Therefore, although each EU member state is also a member of the WTO, the European Commission now formally represents the Community and has the responsibility for conducting negotiations and administering trade policy instruments.⁷²² However, from time to time, members of the European Union have different opinions over various issues. It is therefore crucial for us to look at the differences among EU member countries, in case such differences become an important element in terms of the EU-Japan relationship. In this sense, Putnam's two level approach is not sufficient and should be developed into a three level approach.

⁷²⁰ Hoekman and Kostecki, 'The Political Economy of the World Trading System', P12

⁷²¹ Hoekman and Kostecki, 'The Political Economy of the World Trading System', P31

⁷²² Smith, 'The European Union', P276-289

Table-12: Framework for Three Levels of Analysis



In this regard, Taeyoul Paek’s work provides a very useful method for analysing our objectives. In his work, ‘The WTO Ruling on the Dispute between Kodak and Fujifilm’, Paek attempted to analyse the conflicts between the US and Japan in the Fuji-Kodak case disputed in the WTO.⁷²³ His objective was to analyse the influence of private sectors, such as Fuji-Kodak in the context of the international organisation. In order to analyse the issue, he employed an approach which he called ‘Three Levels of Analysis’ (See Table 11).

His approach is unique in the way he tries to analyse the role of the international organisation as well as the influence of diversified domestic actors. Because of our purpose, it is therefore reasonable to employ the three level approach which goes beyond the analysis on bilateral relations between the EU and Japan and deals with domestic actors within the EU and Japan as well as the role of the WTO.

With the three levels of approach, we will first see how domestic actors are involved in the decision making of Japan and individual EU member countries. (Level 1). Second, how the EU manages to integrate various trade policies of each EU member country into the trade policy as the European Union. (Level 2). And finally, how the EU and Japan coordinate their trade policies towards WTO trade negotiations (Level 3). The approach will show more clearly, for instance, disarray within the EU, which might have

⁷²³ Taeyoul Paek, ‘The WTO Ruling on the Dispute between Kodak and Fujifilm: Three Levels of Analysis’, in *Journal of Asia-Pacific Affairs*, Volume 3, No 1.(Seoul, Asia-Pacific Research Centre Hanyang University, August 2001), P78-102

a significant influence upon the EU-Japan relationship in the WTO.

Analysing what social forces have the most influence over making national trade policy or later over multilateral trade rules is a significant task. For example, in the agricultural case, Japanese rice producers or farm lobbies such as Nokyo first utilised their political influence on domestic politicians (particularly on Liberal Democratic Party) which depend on votes from agricultural industries. As a result, national trade policy became considerably protective in agriculture (Level 1). EU member countries also take the same process to create agricultural trade policies on the domestic-national level. Recipients of CAP such as France or Poland maintain their national agricultural policy supportive for agricultural subsidies and negotiate their stances with contributors of CAP such as Germany. Through internal negotiations within the EU, the EU's agricultural trade policy has been decided on national-regional level (Level 2). In the WTO, the EU, Japan and other member countries with protectionist agricultural trade policy coordinate their stances on farm trade liberalisation talks in the WTO and create a united front on an inter-regional-multilateral level (Level 3). The EU and Japan fully utilised their influence as major WTO players and negotiated against food exporting countries such as the US, Carins Group, and effectively succeeded to reflect their interests in multilateral trade rules.

In sum, each social force first works on influencing their political clout on their politicians to create national agricultural policy. Once their interest has been reflected in their national agricultural policy, WTO members find other likeminded members to consolidate their position in trade talks on the inter-regional or multilateral level. As a result, even members with completely different industrial structure (such as Japan as food importing country and the EU as food exporting countries) could cooperate on an inter-regional-multilateral level.

In the above process of Level 1, 2 and 3, there is a variance in the patterns of influence on each level. In case of the EU, protectionist agricultural policy could be weakened, when the EU members internally discuss their Common Agricultural Policy, since within the EU members, there are countries which are not keen on maintaining costly agricultural subsidies. However, once their anti-farm liberalisation stance is adopted on the national-regional level, it will not be so difficult to find other WTO members which need to protect their domestic agricultural sector. Once like-minded countries create groups (such as Carins Group) or make a common strategy (such as "Multifunctionality of agriculture") for multilateral trade talks, the interests of each social force will be strengthened and amplified on the inter-regional-multilateral level. Thus, through the process of Level 1, 2 and 3, the interest of social force could become a global

standard.

4. New constitutionalism

As referred to in the introduction chapter, on the role of international organisations, Stephen Gill developed his theory of new constitutionalism. He uses the term 'supremacy' instead of hegemony for the case when a situation of hegemony is not apparent.⁷²⁴ According to him, the politics of supremacy are organised through two key processes; the new constitutionalism of disciplinary neoliberalism and the concomitant spread of market civilisation. Gill argues that new constitutionalism involves the narrowing of the social basis of popular participation within the world order of disciplinary neoliberalism. It involves the hollowing out of democracy and the affirmation, in matters of political economy, of a set of macro-economic policies such as market efficiency, discipline and confidence, policy credibility, and competitiveness. It is the move towards construction of legal or constitutional devices to remove or substantially insulate the new economic institutions from popular scrutiny or democratic accountability.

In this sense, the WTO has significantly contributed to the mechanism of surveillance and has supported the market civilisation of new constitutionalism in mutual surveillance. Through our empirical research, we have seen that the WTO, as an international organisation effectively provided rules, norms and surveillance system in trade and, as a result, contributed to the condition where various social forces interact with each other. We have witnessed that various social forces influenced the trade policies of the EU and Japan and attempted to achieve their goals at the international level. In this sense, the outcome of our empirical research supports Gill's new constitutionalism and our hypotheses that: depending on trade issues, various social forces within the EU and Japan, with the same or similar interests, have effectively utilised the international organisation and significantly contributed to the creation of general conditions of hegemony by influencing the trade policy of each government.

The WTO's surveillance mechanism with its DSB has successfully contributed to the constitutionalisation or legalisation of world trade system. However, what we need to stress from the outcome of our research is that the market civilisation of new constitutionalism is in danger of collapse, if member countries and the social forces within states stop supporting its legalised system and lose faith in further trade liberalisation. As with agriculture or steel, when, in the process of rule-making and

⁷²⁴ Stephen Gill, 'Gramsci, Historical Materialism and International Relations', (Cambridge University Press, 1993), P127, 128

legalisation of world trade, trade negotiations start to cover sensitive topics for key domestic industries, WTO member countries begin to pay more attention to the social forces in order to build a consensus domestically. When domestic social forces wish to stall trade liberalisation, it will significantly affect the country's policy for further trade negotiation.⁷²⁵

In recent years, we have been witnessing that, due to the delay in WTO trade liberalisation talks, some members have shifted their attention from the WTO to bilateral trade agreements, such as FTA. The multilateral trade system under the new constitutionalism and its role of maintaining market efficiency, discipline and confidence in world trade will be lost, if members lose faith in the multilateral trade system and opt for bilateral trade agreements. Adding to agriculture and steel, now the WTO is dealing with a number of cumbersome and challenging tasks. Therefore, on the EU-Japan relationship in the WTO, analysis can be pushed into further theoretical and empirical areas by addressing a number of other trade issues.⁷²⁶ In the WTO, where states still remain the main actor, non-state actors are increasingly becoming influential. I believe that the neo-Gramscian perspective is an effective tool for the analysis of hegemony created by various social forces. Particularly investigating the social forces in the leading members of the WTO such as the EU, Japan the US, it will be interesting to analyse what social force will create the new dominance, how hegemony/supremacy will be shaped by them, and how new constitutionalism of multilateral trade system will be maintained.

⁷²⁵ Robert Gilpin, 'The Political Economy of International Relations', (New Jersey, Princeton University Press, 1987), P171-P230

⁷²⁶ Morton, 'Unravelling Gramsci', P134, 135

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