

# U.S.-JAPANESE TRADE RELATIONS

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HEARING  
BEFORE THE  
JOINT ECONOMIC COMMITTEE  
CONGRESS OF THE UNITED STATES  
NINETY-SIXTH CONGRESS  
FIRST SESSION

—————  
OCTOBER 10, 1979  
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Printed for the use of the Joint Economic Committee



U.S. GOVERNMENT PRINTING OFFICE  
WASHINGTON : 1980

55-568

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For sale by the Superintendent of Documents, U.S. Government Printing Office  
Washington, D.C. 20402

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# CONTENTS

## WITNESSES AND STATEMENTS

WEDNESDAY, OCTOBER 10, 1979

Bentsen, Hon. Lloyd, chairman of the Joint Economic Committee: Opening statement-----	Page 1
Staats, Hon. Elmer B., Comptroller General of the United States, accompanied by John E. Milgate, Associate Director, International Division; Eleanor M. Hadley, Group Director, International Division; and Peggy Truver, Supervisory Auditor and Economist, International Division-----	3
Sevin L. J., chairman of the board and chief executive officer, Mostek Corp., Carrollton, Tex., on behalf of the Semiconductor Industry Association-----	15
Wolff, Alan Wm., former Deputy Special Representative, Office of the Special Representative for Trade Negotiations; currently with the law firm of Verner, Liipfert, Bernhard & McPherson, Washington, D.C.-----	26
Tanaka, H. William, partner, law firm of Tanaka, Walders & Ritger, Washington, D.C.-----	35

## SUBMISSIONS FOR THE RECORD

WEDNESDAY, OCTOBER 10, 1979

Bentsen, Hon. Lloyd: Chart reflecting U.S. trade balance with Japan-----	2
Committee To Preserve American Color Television (COMPACT): Letter to Senator Bentsen from Jacob Clayman and Allen W. Dawson, cochairmen, COMPACT, dated November 21, 1979, regarding the section on color television in the GAO report entitled "United States-Japanese Trade: Issues and Problems"-----	76
Sevin, L. J.:	
Prepared statement-----	17
Response to additional written questions posed by Senator Bentsen--	61
Staats, Hon. Elmer B., et al.:	
Prepared statement-----	7
Letter to Senator Bentsen, dated November 30, 1979, supplementing his testimony regarding the availability of comparative international statistics on productivity levels-----	14
General Accounting Office's recommendations on export promotion and related trade issues-----	56
Response to additional written questions posed by Senator Bentsen--	59
Tanaka, H. William:	
Prepared statement-----	38
Response to additional written questions posed by Senator Bentsen--	67
Wolf, Alan Wm.:	
Prepared statement-----	29
Response to additional written questions posed by Senator Bentsen--	65

# U.S.-JAPANESE TRADE RELATIONS

WEDNESDAY, OCTOBER 10, 1979

CONGRESS OF THE UNITED STATES,  
JOINT ECONOMIC COMMITTEE,  
*Washington, D.C.*

The committee met, pursuant to notice, at 10:05 a.m., in room 6226, Dirksen Senate Office Building, Hon. Lloyd Bentsen (chairman of the committee) presiding.

Present: Senators Bentsen and Jepsen.

Also present: John M. Albertine, executive director; Richard F. Kaufman, assistant director-general counsel; Kent H. Hughes and George R. Tyler, professional staff members; Mark Borchelt, administrative assistant; Katie MacArthur, press assistant; and Stephen J. Entin, minority professional staff member.

## OPENING STATEMENT OF SENATOR BENTSEN, CHAIRMAN

Senator BENTSEN. Comptroller General Staats, let me first say I'm very pleased—and I speak on behalf of members of the Joint Economic Committee—for the very extensive study you've made of Japanese-American trade. I think it's going to be a lot of help to us. It tells us something about the inability of the United States to export and penetrate the Japanese market. It also contains some warning signals about our trading future. I think it also shows that it's not just a question of protectionism in Japan, but also a lot of things that we, as exporters, have to do to build up our export trade, whether with Japan or other countries.

As I look at these figures on the chart—you might say this is the black and white of it—it shows where we were in 1958 as opposed to 1979. It shows that we had a modest trade surplus until we reached 1965, and then our trade went into a deficit with Japan. It finally reached a deficit of approximately \$12 billion in 1978.

We see some encouragement now, in 1979. We have about a \$2 billion improvement, as I recall, for the first 6 months of 1979. I think part of that was because of the tough trading done by Ambassador Strauss, Ambassador Wolff, and the Congress.

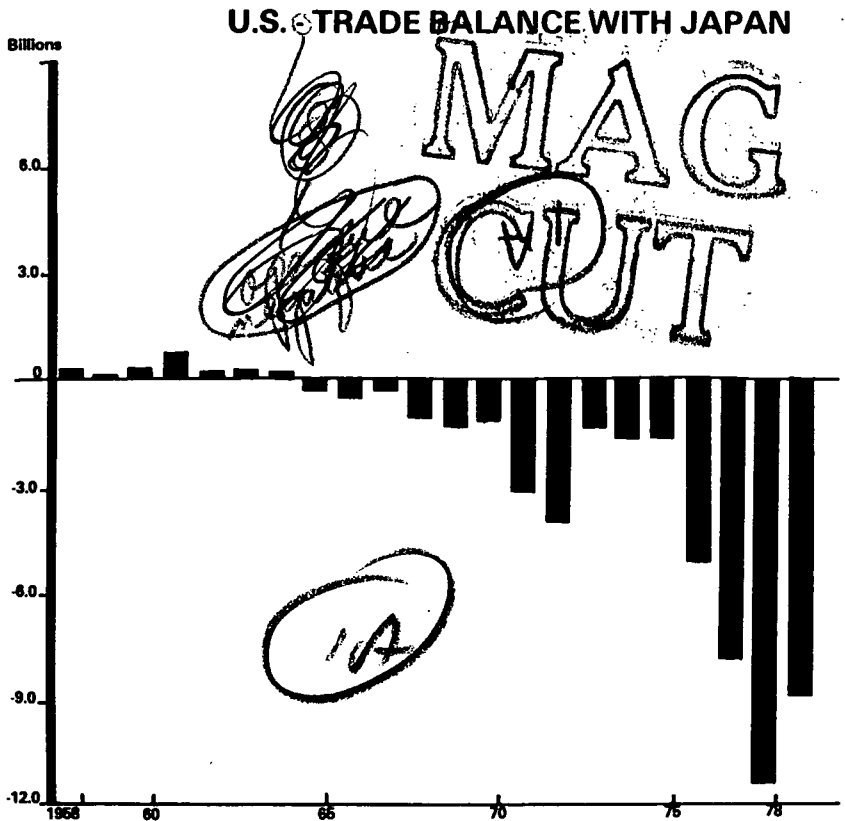
But I see plenty of cause for concern about the future. The August trade deficit with Japan widened substantially, to over \$700 million. The gap reflects an increase in automobile imports and a decline in U.S. exports to Japan.

The Japanese Government is determined to enter the high technology future; isn't it, Mr. Sevin? The semiconductor industry is a good case in point. In 1974, Japan exported only 5 percent of its semiconductors. Last year the figure was 20 percent.

But there's another aspect of the GAO report that suggests some lessons for the United States. The Japanese emphasis on investment, the use of accelerated depreciation to foster industrial growth, and the conscious development of an export strategy, are all areas that we must emulate in improving America's economic performance.

I look at the difference, for example, in the personal savings rate in Japan, and what it is here in the United States. As I recall, in the first quarter of this year the rate was about 4.6 percent for us and in the area of 22 percent for the Japanese. And that has meant a higher rate of capital formation for them.

[The chart referred to in Senator Bentsen's opening statement follows:]



Senator BENTSEN. So I'm very pleased to have you this morning. Following your testimony, we have other members of the panel who have now moved up to the table. Mr. William Tanaka, a prominent Washington trade attorney, Mr. Alan Wolff, former Deputy Special Trade Representative and Mr. Sevin of Mostek. Will you proceed, Mr. Staats.

**STATEMENT OF HON. ELMER B. STAATS, COMPTROLLER GENERAL OF THE UNITED STATES, ACCOMPANIED BY JOHN E. MILGATE, ASSOCIATE DIRECTOR, INTERNATIONAL DIVISION; ELEANOR M. HADLEY, GROUP DIRECTOR, INTERNATIONAL DIVISION; AND PEGGY TRUVER, SUPERVISORY AUDITOR AND ECONOMIST, INTERNATIONAL DIVISION**

Mr. STAATS. Thank you, Mr. Chairman. We have a longer prepared statement which has been distributed, of some 21 pages, but in view of your interest in having an abbreviated statement we have a shorter statement which is available to you, and I will read that statement, and then will be prepared to participate in the panel and answer any questions that you have.

This study, as you've already indicated, was undertaken at your request. We looked at two different matters. First, a comparative analysis of the United States-Japanese trade policy. Second, the experience of firms that have been successful in penetrating Japanese markets, and other firms that have encountered only frustration.

The steadily increasing deficit in U.S. trade with Japan—

Senator BENTSEN. Would you hold just a minute. Is that microphone on, because we have a large audience and what you have to say—

Mr. STAATS. The steadily increasing deficit in U.S. trade with Japan between 1976 and 1978 resulted in widespread concern in the United States. In 1978, the deficit increased to \$11.6 billion, amounting to 2½ times that of 1976. Currently it is estimated that the United States-Japan bilateral deficit in 1979 may be about \$9 billion.

In comparing United States and Japanese export policies, GAO finds the sharpest contrast in the different approach toward the identification of what is a suitable export industry. Japan's commercial policy rests in identifying industries with strong export potential, and providing them with support. In the United States, there is no analysis of export potential among industries. Before promoting an export industry, Japan asks, Do the products of this industry have a high value-added content? Will demand for this produce rise with rising income?

These questions are not asked in the United States. Japan encourages its strong industries. The United States protects its weak ones. Japan's primary technique for encouraging industry with strong trade potential has been accelerated depreciation, with great emphasis on modern plant and equipment. The United States has no statistics on the average age of plant and equipment by industry, and how these statistics compare with other countries. The United States gives an investment credit to all manufacturers alike. Japan favors certain industries over others, with a view to supporting industries important to the performance of the economy.

At the present time, for example, the computer industry is receiving the greatest government benefits.

We selected seven industries to identify factors that are favorable and unfavorable to marketing in Japan. The firms selected for study were drawn from the following industries: Computers, automotive, telecommunications, color television, machine tools, logs

and lumber, and soybeans. Our study of the seven U.S. industries reveals that problems encountered in penetrating the Japanese market are both United States and Japanese in origin.

On the Japanese side, our study reveals that past Japanese Government policies, tariff and nontariff barriers, Government assistance presently given to certain key industries and the structure of the Japanese market affect the ability of U.S. producers to enter the market. On the U.S. side, we believe that U.S. corporate strategy and the domestic market orientation of U.S. industry have inhibited the success of U.S. producers in the Japanese market.

Some of the difficulties which the U.S. firms face today in their attempts to penetrate the Japanese market are the result of past Japanese policies. Although in the recent past, the Japanese have been willing to remove many tariff and nontariff barriers, this has often occurred only after targeted industries have become firmly entrenched in the domestic market and highly competitive in international markets.

For example, I might say here, between 1959 and 1969, the auto production in Japan grew some eighteenfold, with exports increasing from 7.3 percent to 18.4 percent of the total production. By 1977, this had increased to 50 percent of total automotive production going into exports.

Japan, with systematic and coordinated industrial trade policies, has in several instances been overzealous in its protection of its "growth" or "target" sectors. Not only has the Japanese Government afforded these sectors protection from foreign competition, but it has also provided targeted sectors with special tax incentives, R. & D. subsidies, development loan programs, market guarantee programs, oversea market development programs, promotion of cooperative Japanese industry relationships and so on. The three areas in particular where this has happened, of course, have been the computer industry, the machine tool industry, and the telecommunications industry.

Now, turning to NTT, we believe that at this point it would be useful to discuss the Japanese telecommunications industry. Unlike any of the other examples presented in our case studies, the telecommunications market is virtually closed to foreign and in fact domestic manufacturers not members of the NTT family. Primary among the barriers impeding U.S. entry into the market is the lack of clear definition between central office and interconnect markets and NTT's policy regarding equipment and installation approval.

Additionally, although most nations prefer domestic suppliers in granting contracts for telecommunications equipment, NTT's use of sole-source procurement—in other words, procuring from its family members rather than competitive sealed bids or negotiated contracts—has further circumscribed foreign entrance to the market. Despite the negotiation of the Government procurement code and a bilateral mutual reciprocity agreement, we do not anticipate a substantial decline in the bilateral telecommunications trade deficit.

Even if access to Government procurement were to be denied to the Japanese suppliers, the Japanese would still have an immense opportunity in the private U.S. market. However, the U.S. suppliers do not have similar access to the Japanese market, because of the procedural and structural problems discussed above, and in greater detail in our report.

While the telecommunications market remains a conspicuous exception to Japan's recent liberalization of trade barriers, some other U.S. industries face markets which, for structural reasons, are difficult to penetrate. For example, U.S. manufacturers of color television receivers note many problems in entering the Japanese distribution system. Japanese retail and servicing facilities are generally owned or controlled by the major manufacturers. Exclusive distributorships are heavily, if not totally, financed and supported by CTR manufacturers. As a result, these distributors normally do not carry foreign brands because they fear losing their franchises with their normal suppliers. U.S. electrical and electronic product manufacturers, therefore, must rely on a Japanese firm with an established distributor chain for the sale of their products. Similarly, U.S. auto manufacturers state that they are unable under Japan's exclusive dealership to market through the dealer networks of the major Japanese auto manufacturers. This system is currently under investigation by Japan's Fair Trade Commission.

As suggested by our case studies, in addition to causing these marketing problems, the Japanese distribution system is responsible for adding costs to U.S. products in the Japanese market. In our automobile case study, the manufacturer pointed out that these distributorships are the single most significant element in increasing the cost of an American car in Japan.

As indicated earlier, many Japanese tariffs have been reduced; however, a number of nontariff barriers exist, which impede access to the Japanese market. Perhaps the most significant of these are the approval system required to meet safety, electrical, and engineering standards in order to sell in Japan.

For example, here I might add that the Japanese have a self-certification system with respect to the environmental and safety and other requirements, whereas the U.S. auto going into Japan has to go through an individual inspection, automobile by automobile, requiring in some cases up to 19 different changes. We point this out in greater detail in our prepared statement, and more fully, even, in our report.

While Japanese market structure and Government policies have made it difficult for a number of U.S. firms to successfully compete in the Japanese market, U.S. corporate strategy and the domestic market orientation of U.S. industry have also contributed to this lack of competitiveness.

For instance, the strength of the American auto industry is in large cars, which were in high demand in the domestic market. Exporting large cars, the U.S. industry was able to capture only a portion of the small luxury car market in Japan. Because U.S. producers were not able to achieve volume sales, they were reluctant to make changes in their vehicles which required expensive retooling, for example, a shift from left-hand to right-hand drive vehicles, although the Japanese make such modifications to their export vehicles. They are able to do so because of the high volume of sales in the United States and the fact that only a few other countries, such as the United Kingdom, use right-hand drive vehicles. Thus, since left-hand drive is used overwhelmingly worldwide, Japan was converting to compete in the world market, whereas the U.S. producers would be converting essentially for the Japanese and the United Kingdom market.



Apart from not adapting their products to meet the needs of the Japanese market, some U.S. industries have been criticized for not providing adequate after-sales servicing and technical assistance. Japanese machine tool importers claim that U.S. machine tool firms have a poor record in followup servicing, particularly in the area of numerically controlled machine tools. They also cite the long delivery time of U.S. machine tools, as compared with Japanese tools, as problematic.

Japanese distributors of U.S. electrical and electronic products stated that there was a lack of enthusiasm on the U.S. side for export. They stated that often there was very little effort to conform products to meet Japanese design and safety specifications, and a lack of coordination between the domestic and export model changes in design and feature. Japanese firms complained that model changes are often made in accordance with U.S. market trends, without any concern or focus on the needs and demands of the Japanese market. Furthermore, Japanese companies pointed out that U.S. firms made little followup efforts in their sales, for example, meeting with distributors, providing technical and sales assistance and so on.

While we found that U.S. manufacturers in our selected case studies face a variety of difficulties in their attempts to penetrate the Japanese market, U.S. agriculture and raw material sectors have been extremely successful. In 1978, 35 percent of our exports to Japan were agricultural products, compared to 21 percent of our exports to the world. Because Japan must import many agricultural goods and raw materials, there are few major trade barriers hindering U.S. exports of such products as soybeans and logs.

I'll go on now to the summary, Mr. Chairman. We believe that the trade imbalance between the United States and Japan has been caused by a mix of several elements:

- A weakening in U.S. manufacturing productivity and competitiveness;

- A trade policy that is import rather than export oriented;

- And Japanese tariff and nontariff barriers.

Our study has revealed a number of factors such as low savings and investment rates, a decline in R. & D. expenditures relative to GNP, a disparity in the quality of manufacture for certain products compared with the Japanese, and problems in labor-management relations which contribute to a weakening in U.S. productivity and competitiveness in international markets. As we point out in chapter 9 of our report, it is alarming to note that in the past several years the United States has had the lowest rate of savings and capital formation of any major industrialized country. By contrast, Japan has had the highest rate. Savings in the U.S. economy are proportionately one-third of those in Japan, and proportional to its GNP, Japan has been putting up new plant and equipment and infrastructure at double the rate of the United States. In 1978, although the American economy was close to double the Japanese economy, the level of investment was almost equal, \$148 billion in the United States compared to \$144 billion in Japan.

Similarly, in recent years, the United States has been spending a smaller proportion of GNP on R. & D. than was true earlier. As our relative expenditures on R. & D. have been falling, Japan's relative expenditures have been rising. Moreover, the record of quality manufacture between the two countries is disparate. In product after product, Japan's defect ratio is lower than that of the United States.

The foregoing factors combine to produce quite different levels of productivity in the American and Japanese economies. Japan's average annual increase in productivity was 3.4 times that of the United States between 1960 and 1977. Between 1970 and 1977, Japan's annual gains were 1.8 of those of the United States. In fact, between 1970 and 1977, with the exception of the United Kingdom, the U.S. average annual change in productivity was the lowest of any other major industrialized country, and as you know, for this year it is a negative 3 percent.

Although U.S. exports have had a sharp price advantage in the last 2 years vis-a-vis Japanese goods, due to currency realignment, American goods have been handicapped by the greater inflation in the American economy as compared to the Japanese economy. That the U.S. price advantage has not been translated into increased exports to the extent that might be anticipated is, no doubt, a reflection that although the price is an important determinant of international competitiveness, other factors such as product quality, after sales servicing, financing, Government decisions, other nonmonetary factors, artificial trade restrictions and so on, also affect U.S. industry's ability to compete in foreign markets.

U.S. industry has traditionally focused its attention on the domestic market because of the size and wealth of this market. Japan, on the other hand, because of its need for raw materials and many agricultural products, has had a keen awareness of the importance of exports. It is not surprising, then, that Japan's trade policy focuses on identifying and providing support to industries with strong export potential, whereas U.S. policy has focused on protecting industries from injurious imports.

Thus, Japan's trade policy is anticipatory, while U.S. trade policy is reactive. Finally, the United States-Japan trade balance has been affected by tariff and nontariff restrictions. Previously, Japanese tariffs, investment restrictions and import quotas afforded Japanese industries protection from import competition until these industries were well entrenched in the domestic market and successfully competing in foreign markets. Since the early 1970's, these barriers have largely come down; however, attitudes and perceptions on both sides have not changed as rapidly. Moreover, our case studies reveal that the Japanese distribution system of design and safety standards present recurring problems for American producers selling in Japan. Although there are various factors affecting U.S. sales to Japan, including the domestic market orientation of U.S. industry, efforts should be made to overcome the above-mentioned inequities in bilateral trade. Additionally, U.S. industry must be encouraged to address the underlying economic factors discussed above, which will affect its international competitiveness. This completes our statement, Mr. Chairman.

And thank you very much.

[The prepared statement of Mr. Staats follows:]

PREPARED STATEMENT OF HON. ELMER B. STAATS

Mr. Chairman and members of the committee, we are pleased to be with you today to discuss our recent report, "United States-Japan Trade: Issues and Problems." Our work was performed at your request for GAO to undertake (1) a comparative analysis of United States and Japanese trade policy and (2)

a study of the experience of firms that have been successful in penetrating Japanese markets and other firms that have encountered only frustration.

The steadily increasing deficit in U.S. trade with Japan between 1976 and 1978 resulted in widespread concerns in the United States. In 1978, the deficit reached \$11.6 billion, amounting to two and half times that of 1976. Currently, it is estimated that the United States-Japan bilateral deficit in 1979 may be about \$9 billion.

#### TRADE POLICIES CONTRASTED

In comparing United States and Japanese export policies, GAO finds the sharpest contrast in the different approach toward the identification of what is a suitable export industry. Japan's commercial policy rests on identifying industries with strong export potential and providing them with support. In the United States, there is no analysis of export potential among industries. Before targeting an "export industry," Japan asks "Do the products of this industry have a high value-added content? Will the demand for this product rise with rising income?" These questions are not asked in the United States. Japan encourages its strong industries; the United States protects its weak ones.

GAO found significant differences in "export consciousness" between the two countries. Japanese "think" foreign trade, as early as the fifth grade, school children are introduced to its importance for their country. Americans come from a quite different background—a richly endowed economy, continental in breadth, for which in the past, foreign trade has been a minor element.

This study confirmed that the United States must heighten its "export consciousness" which, among other things, means studying other nations' preferences and designing products accordingly.

Japan's foreign trade administration is more focused than that of the United States, because, lacking raw materials and land sufficient to feed itself, virtually the only goods Japan has to sell to the world are manufactured goods. The United States, by contrast, sells manufactured goods, agricultural products, and crude materials, each with its own trade administration.

Japan's primary technique for encouraging industries with strong trade potential has been accelerated depreciation, with great emphasis on modern plant and equipment. The United States has no statistics on the average age of plant and equipment by industry and how these statistics compare with other countries. The United States extends investment credit to all manufacturers alike; Japan favors certain industries over others, with a view to supporting industries important to the performance of the economy. At the present time, for example, the computer industry is receiving the greatest government benefits.

There is an important time frame difference between Japan and the United States in trade policy. Japan anticipates. Its conception of "early warning" rests on economic projections 5 to 10 years or more in the future. Because Japan perceives increasing pressure from newly industrializing countries in textiles, consumer electronic products and the like, the government feels compelled to encourage industry to move into more sophisticated types of manufacture. The United States reacts. Its conception of "early warning" is based on import statistics of the goods which arrive.

We selected seven case studies to illustrate the wide range of problems in different industries and to identify factors that are favorable to marketing in Japan. The firms and trade selected for study were drawn from the following industries: Computers, automotive, telecommunications, color television, machine tools, logs and lumber, and soybeans.

Our study of the seven U.S. industries reveals that problems encountered in penetrating the Japanese market are both U.S. and Japanese in origin. On the Japanese side, our study reveals that past Japanese Government policies, tariff and non-tariff barriers, government assistance presently given to certain key industries, and the structure of the Japanese market affect the ability of U.S. producers to enter the market. On the U.S. side, we believe that U.S. corporate strategy and the domestic market orientation of U.S. industry have inhibited the success of U.S. producers in the Japanese market.

#### PAST JAPANESE GOVERNMENT POLICIES AND THEIR IMPACT

Some of the difficulties which U.S. firms face today in their attempts to penetrate the Japanese market are the result of past Japanese policies. Although, in the recent past, the Japanese have been willing to remove many tariff and non-tariff barriers, this has often occurred only after "targeted" industries have

become firmly entrenched in the domestic market and highly competitive in international markets. For example, after 1971, Japan's auto industry was no longer closed to foreigners as it had been since the early postwar years. Until 1971, the Japanese Government, in an attempt to aid the development of the auto industry, did so by excluding imports and foreign investment (with the exception of licensing foreign technology), by granting the industry preferred status for receipt of foreign exchange allocations, and by granting special tax concessions to the industry. As a result of these favorable policies, Japan's domestic auto production expanded eighteenfold between 1959 and 1969 with exports growing gradually from 7.3 to 18.4 percent of production. By the time Japan began reducing import and investment barriers, exports had taken on increasing significance in the continued growth and health of the industry accounting for over 50 percent of production by 1977.

Another case in point is that of the color television industry. Again, as we have discussed at length in our report, the Japanese industry was protected by tariff and non-tariff barriers which effectively prevented the entrance of foreign competition. As noted in the case of the auto industry, Japan has been willing in the recent past to lower or do away with barriers such as foreign exchange allocations, investment restrictions, import quota systems and high tariffs. However, these reductions for the most part did not occur until the beginning of the 1970's when the Japanese industry was well established domestically and enjoying growth in international sales.

#### JAPANESE GOVERNMENT ASSISTANCE

Japan, with its systematic and coordinated industrial growth and trade policies, has in several instances been over-zealous in its protection of its "growth" or "target" sectors. Not only has the Japanese Government afforded these sectors protection from foreign competition, but it has also provided targeted sectors with special tax incentives, R&D subsidies, development loan programs, market guarantees programs, overseas market development programs, promotion of cooperative Japanese industry relationships, etc. Excellent examples of targeted industries receiving such aid are the Japanese computer, machine tool, and telecommunications industries. The Japanese computer industry has been the recipient of a number of direct subsidies such as the very-large integration program (VLSI) whereby the government subsidized 50 percent of selected private companies' R&D for fourth generation computers. Additionally, for research purposes, the Japanese industry has been divided into three groups—Fujitsu-Hitachi, Nippon Electric (NEC)-Toshiba, and Mitsubishi-Oki.

In addition to industry research groups, close business government relations have also enhanced development of Japanese industry. This is true in the machine tool and telecommunications industries. Japanese machine tool builders have been encouraged to develop, as a 6-year national project, a flexible computer controlled machining system. Similarly, Nippon Telephone and Telegraph (NTT), the government regulator/operator of Japan's telecommunications network, encourages a variety of telecommunications, technology and service-related R&D through direct and indirect subsidies and joint R&D efforts with its four family members.

The Japanese Government, in an effort to encourage and direct the development of key industrial sectors, has enacted a number of tax incentives and concessions for research and development, marketing, etc. Perhaps the most significant of these are accelerated depreciation allowances which allow targeted industries to write off as much as 50 percent of the costs of plant and equipment in the first year. Furthermore, the Japanese Government either itself or through specially-created agencies has provided guaranteed markets or strong incentives for Japanese purchases of targeted industry products. For example, the Information-Technology Promotion Agency created in October 1979, was established to, among other things, purchase any software package having a high degree of public interest. In some instances, special depreciation allowances have been enacted for end-users to encourage the purchase of sophisticated equipment.

#### NTT: AN EXCEPTION TO LIBERALIZATION

We believe, that at this point, it would be useful to discuss the Japanese telecommunications industry. This industry obviously benefits from many of the tax incentives and R&D subsidies enjoyed by the computer industry given the increasing computerization of telecommunications systems. In fact, the primary

firms involved in the development of computer hardware, software and peripheral technology are also members of NTT's family. However, unlike any of the other examples presented in our case studies, the telecommunications market is virtually closed to foreign and, in fact, domestic manufacturers not members of the NTT family. Primary among the barriers impeding U.S. entrance in the market is the lack of clear definition between central office and interconnect markets and NTT's policies regarding equipment and installation approval. Additionally, although most nations prefer domestic suppliers in granting contracts for telecommunications equipment, NTT's use of sole-source procurement—in other words, procuring from its family members—rather than competitive sealed bids or negotiated contracts has further circumscribed foreign entrance to the market. Despite the negotiation of the government procurement code and a bilateral mutual reciprocity agreement, we do not anticipate a substantial decline in the bilateral telecommunications trade deficit.

Even if access to government procurement were to be denied to the Japanese suppliers, the Japanese would still have an immense opportunity in the private U.S. market. However, the U.S. suppliers do not have similar access to the Japanese market because of the procedural and structural problems discussed above and in greater detail in our report.

#### THE JAPANESE DISTRIBUTION SYSTEM

While the telecommunications market remains a conspicuous exception to Japan's recent liberalization of trade barriers, some other U.S. industries face markets which for structural reasons are difficult to penetrate. For example, U.S. manufacturers of color television receivers (CTRs) note many problems in entering the Japanese distribution system. Japanese retail and servicing facilities are generally owned or controlled by the major manufacturers. Exclusive distributorships are heavily, if not totally, financed and supported by CTR manufacturers. As a result, these distributors normally do not carry foreign brands because they fear losing their franchises with their normal suppliers. U.S. electrical and electronic product manufacturers, therefore, must rely on a Japanese firm with an established distributor chain for the sale of their products. Similarly, U.S. auto manufacturers state that they are unable, under Japan's exclusive dealerships, to market through the dealer networks of the major Japanese auto manufacturers. This system is currently under investigation by Japan's Fair Trade Commission.

As suggested by our case studies, in addition to causing these marketing problems, the Japanese distribution system is responsible for adding costs to U.S. products in the Japanese market. For example, in our automobile case study, the manufacturer (case participant) pointed out that these distributorships are the single most significant element in increasing the cost of an American car in Japan. It should be noted that the distribution system similarly applies to Japanese manufactured automobiles. Car dealer incentives and profit margins account for an increase of \$950, \$1,925 and \$2,600, for subcompact, small sporty and compact cars, respectively. Similarly, our soybean case participant stated that the distribution system contributed to increased costs of soybeans, although not to the extent that U.S. exports become noncompetitive with substitutes.

#### STANDARDS AND APPROVAL SYSTEMS

As indicated earlier, many Japanese tariffs have been reduced; however, a number of non-tariff barriers exist which impede access to the Japanese market. Perhaps the most significant of these are the approval systems required to meet safety, electrical, and engineering standards in order to sell in Japan. For example, in our auto case study, we note that the approval process for foreign automobiles is more complicated and time-consuming than that for Japanese automobiles. While Japanese auto manufacturers are able to "self-certify" that an automobile meets standards once the type of vehicle has been approved; U.S. auto manufacturers, even after obtaining approval for a type of vehicle, must submit each auto to be sold for further inspection in order to obtain approval.

Our case participant described no less than 19 changes—some relatively minor, others significant in terms of work required and costs incurred—made to U.S. vehicles to meet Japanese standards. Similarly, our consumer electronic case participant noted that stringent design specifications, quality control and safety standards have created problems for them in the Japanese market.

In the case of telecommunications, U.S. producers also face similar problems. A significant factor inhibiting U.S. entrance into the market is NTT's type and case or installation approval. Although general specifications are publicly announced by NTT, detailed specifications are generally not publicly disclosed on the grounds that they are proprietary to NTT or to the company which developed the product. Given the close relationship between NTT and its "family" which presumably is aware of unannounced specifications, foreign firms are seriously disadvantaged in this market. Not only do these approvals require a significant amount of time to obtain, but they require an extensive amount of documentation from the manufacturer as well. Moreover, NTT requires that equipment and manufacturing facilities be inspected for quality control. However, NTT has reportedly never made such overseas inspections.

It should be recognized that, in some instances, regulations have been relaxed. Japan deferred for 3 years until 1980, its stringent 1978 automobile exhaust standards and has simplified its emission testing procedures for U.S. items considered equivalent to those of Japan. In addition to suspending its emission standards on foreign cars temporarily, the government in 1977, began sending examiners to the United States. These examiners perform safety and emission testing on-site which will reduce the cost and time required for meeting approval. Similarly, recent changes in Japanese import regulations have had a positive effect on U.S. lumber exports. While the Japanese do not recognize lumber grading marks stamped outside Japan, reinspection regulations have recently been relaxed. Additionally, in June 1978, Japan revised its grading standards to match more closely those of the United States in order to alleviate lumber quality classification problems.

#### U.S. CORPORATE STRATEGY AND DOMESTIC MARKET ORIENTATION

While Japanese market structure and government policies have made it difficult for a number of U.S. firms to successfully compete in the Japanese market, U.S. corporate strategy and the domestic market orientation of U.S. industry have also contributed to this lack of competitiveness. For instance, the strength of the American auto industry is in large cars which were in high demand in the domestic market. Exporting large cars, the U.S. industry was able to capture only a portion of the small luxury car market in Japan. Because U.S. producers were not able to achieve volume sales, they were reluctant to make changes in their vehicles which required expensive retooling—for example, a shift from left-hand to right-hand drive vehicles. Although the Japanese make such modifications to their export vehicles, they are able to do so because of the high volume of sales in the United States and the fact that only a few other countries such as the United Kingdom use right-hand drive vehicles. Thus, since left-hand drive is used overwhelmingly worldwide, Japan was converting to compete in the world market whereas the U.S. producers would be converting essentially for the Japanese and U.K. markets.

In the case of lumber, U.S. mills have been reluctant to convert to produce Japanese sizes as they want to be ready to meet the demands of the vast U.S. housing market. Rather than produce lumber suitable for the traditional Japanese housing market, U.S. mills prefer to export U.S.-sized lumber. Thus, they have been able to capture only a small portion of the Japanese lumber market. U.S. producers would rather that the Japanese change their housing construction methods in order to use U.S.-sized lumber, than change U.S. lumber sizes to meet Japanese requirements.

Similarly, our TV case participant, noted in a 1970 letter to a potential Japanese distributor that making required modifications for safety and design standards would not be economically feasible. The U.S. firm, after weighing the expense of gearing production for these changes against potential sales volume, determined that such costly modifications would not be cost effective.

Apart from not adapting their products to meet the needs of the Japanese market, some U.S. industries have been criticized for not providing adequate after-sales servicing and technical assistance. Japanese machine tool importers claim that U.S. machine tool firms have a poor record in follow-up servicing, particularly in the area of numerically controlled machine tools. They also cite the long delivery time of U.S. machine tools as compared with Japanese machine tools as problematic.

Japanese distributors of U.S. electrical and electronic products stated that there was a lack of enthusiasm on the U.S. side for export. They stated that

often there was very little effort to conform products to meet Japanese design and safety specifications, and lack of coordination between domestic and export model changes in design and feature. Japanese firms complained that model changes are often made in accordance with U.S. market trends without any concern or focus on the needs and demands of the Japanese market. Furthermore, Japanese companies pointed out that U.S. firms make little follow-up effort in their sales, for example, meeting with distributors, providing technical and sales assistance, and so on.

#### UNITED STATES-JAPAN AGRICULTURAL TRADE

While we found that U.S. manufacturers in our selected case studies face a variety of difficulties in their attempts to penetrate the Japanese market, the U.S. agricultural and raw materials sectors have been extremely successful. In 1978, 35 percent of our exports to Japan were agricultural products, compared to 21 percent of our exports to the world. Because Japan must import many agricultural goods and raw materials, there are few, major trade barriers hindering U.S. exports of such products as soybeans and logs.

Logs, not lumber, dominate Japan's wood products imports from the United States. However, this has been the result of both the desire of the Japanese to protect their sawmill industry, as well as the reluctance on the part of U.S. mills to cut lumber suitable for the present Japanese housing market. We found disagreement among members of the U.S. wood products industry as to whether the United States should attempt to export more lumber (and other value-added products such as plywood) rather than logs, or if the United States should be exporting logs at all. During upturns in the U.S. housing market, Japanese demand for U.S. forest products is viewed as competition which forces up the price and restricts the supply of U.S. lumber. This attitude has led to both formal and informal log export controls. Thus, in this instance, balance-of-trade considerations are in conflict with domestic concerns.

There is an additional feature of U.S.-Japan trade revealed in our case studies which we believe is noteworthy. Even as U.S. producers pay more attention to the needs and demands of the Japanese market and consumer, some U.S. producers see their best opportunity in competing with Japanese products in the American market. The U.S. auto industry, for example, is now working hard to produce smaller cars, and sees the trade challenge more in terms of reducing Japan's share of the U.S. market than in U.S. gains in the Japanese market.

#### SUMMARY

GAO believes that the trade imbalance between the United States and Japan has been caused by a mix of several elements:

- A weakening in U.S. manufacturing productivity and competitiveness;
- A trade policy that is import rather than export oriented; and
- Japanese tariff and non-tariff barriers.

#### PRODUCTIVITY AND COMPETITIVENESS

Our study has revealed a number of factors such as a low savings and investment rates, a decline in R&D expenditures relative to GNP, a disparity in the quality of manufacture for certain products compared with the Japanese and problems in labor-management relations which contribute to a weakening in U.S. productivity and competitiveness in international markets. As we point out in Chapter 9 of our report, it is alarming to note that in the past several years the United States has had the lowest rate of savings and capital formation of any major industrialized country. By contrast, Japan has had the highest rate. Savings in the U.S. economy are proportionally one-third those in Japan, and proportional to its GNP, Japan has been putting up new plant and equipment and infrastructure at double the rate of the United States. In 1978, although the American economy was close to double the Japanese economy, investment levels in equipment were almost equal—\$148 billion in the United States compared to \$144 billion in Japan.

Similarly, in recent years the United States has been spending a smaller proportion of GNP on R&D than was true earlier. As our relative expenditures on R&D have been falling, Japan's relative expenditures have been rising. Moreover, the record of quality manufacture between the two countries is disparate. In product after product, Japan's defect ratio is lower than that in the United States.

GAO believes the United States must pay greater attention to new plant and equipment. For most of the years, 1970-78, Japan's ratio of gross fixed investment (exclusive of residential construction) to gross domestic product has been double that of the United States. Not only has Japan's ratio of personal savings to disposal personal income in this period been roughly three times that of the United States, but the United States has proportionately been investing far higher amounts outside its borders.

Another important element in Japan's international competitiveness is its employment system which grants job security to the elite of the labor movement, with the result that relatively, Japan experiences far less time lost to strikes than the United States.

The foregoing factors combine to produce quite different levels of productivity in the American and Japanese economies. Japan's average annual increase in productivity was 3.4 times that of the United States between 1960-77, and between 1970-77, Japan's annual gains were 1.8 those of the United States. In fact, between 1970-77, with the exception of the United Kingdom, the U.S. average annual change in productivity was the lowest of any other major industrialized country.

Although U.S. exports have had a sharp price advantage in the last 2 years vis-a-vis Japanese goods due to currency realignment, American goods have been handicapped by the greater inflation in the American economy as compared to the Japanese economy. That the U.S. price advantage has not been translated into increased exports to the extent that might be anticipated is no doubt a reflection that, although price is an important determinant of international competitiveness, other factors such as product quality, after-sales servicing, financing, government decisions, other non-monetary factors, artificial trade restrictions, and so on, also affect U.S. industries ability to compete in foreign markets.

#### TRADE POLICY

U.S. industry has traditionally focused its attention on the domestic market because of the size and wealth of this market. Japan, on the other hand, because of its need for raw materials and many agricultural products, has had a keen awareness of the importance of exports. It is not surprising, then, that Japan's trade policy focuses on identifying and providing support to industries with strong export potential, whereas, U.S. policy has focused on protecting industries from injurious imports. Thus, Japan's trade policy is anticipatory, while U.S. policy is reactive.

#### TARIFF AND NONTARIFF BARRIERS

Finally, the U.S.-Japan trade balance has been affected by tariff and nontariff restrictions. Previously, Japanese tariffs, investment restrictions, and import quotas afforded Japanese industries protection from import competition until these industries were well entrenched in the domestic market and successfully competing in foreign markets. Since the early 1970's, these barriers have largely come down; however, attitudes and perceptions on both sides have not changed as rapidly. Moreover, our case studies reveal that the Japanese distribution system and design and safety standards present recurring problems for American producers selling in Japan. Although there are various factors affecting U.S. sales to Japan including the domestic market orientation of U.S. industry, efforts should be made to overcome the above-mentioned inequities in bilateral trade. Additionally, U.S. industry must be encouraged to address the underlying economic factors discussed above which also affect its international competitiveness.

Senator BENTSEN. Mr. Staats, you have brought forth some very dry numbers, but I must say that what you have presented show that fighting Japanese protectionism is not enough. We need the kind of progressive and aggressive policies in this country that will modernize this country's plant and equipment. We must put more stress on productivity and capital formation.

How does the relative productivity of the two countries stand now on output per man-hour? I know the trend lines are extremely disturbing, but how do the two countries stand on output per man-hour?



Mr. STAATS. I have the figure for our own situation. It's a negative 3 percent so far this year.

Senator BENTSEN. That's in the so-called increased productivity. I am asking for the total productivity per man-hour, just a present day snapshot.

Mr. STAATS. I misunderstood your question.

Ms. HADLEY. Astonishingly enough, Senator Bentsen, we have no official statistics from industry on this point. The Labor Department does not compile them. We sought them because we wanted to make comparison of existing level with existing level. There are no official U.S. statistics on this point, and we certainly feel we should have this information.

Senator BENTSEN. We should. And I have been using some numbers. I was asking you this question because I thought there was an answer. [Laughter.]

You do surprise me with that. I had better go back and check the source of the numbers I have been given. I was under the impression that the output per man-hour might be a little to our advantage yet. I know it very definitely was, but I also know the trend lines are very much the other way.

Did you say that the Bureau of Labor Statistics doesn't have those?

Ms. HADLEY. It does not compile such statistics, though, as you observed, any number of people keep making these comparisons. A very prominent speaker a few weeks ago, in a briefing at the Department of State, was making level comparisons, and I asked him where he got his figures, and it was rather astonishing to him to learn that there are no official U.S. statistics on this.

Senator BENTSEN. I had better look back at some of my speeches. [Laughter.]

[The following information was subsequently supplied for the record:]

COMPTROLLER GENERAL OF THE UNITED STATES,  
Washington, D.C., November 30, 1979.

B-162222

HON. LLOYD BENTSEN,  
Chairman, Joint Economic Committee,  
Congress of the United States.

DEAR MR. CHAIRMAN: During our October 10 testimony on United States-Japan trade, we discussed the availability of comparative international statistics on productivity levels. After further checking, given the importance of the productivity issue before the American people, it occurred to me that it would be useful to drop you a followup note on the point.

As you later brought out at the hearing, the Bureau of Labor Statistics does publish total aggregate international comparisons of the level of productivity and it publishes international comparisons of the level for manufacturing as a whole, but the point we were making is that it does not publish industry comparisons with the exception (as was subsequently learned) of the iron and steel industry.

In international trade in manufactured goods, competitive pressures are felt at the industry level. I would like to suggest that a useful public purpose would be served if the American public was provided with international comparisons of productivity levels industry by industry.

Sincerely yours,

ELMER B. STAATS,  
Comptroller General of the United States.

Senator BENTSEN. I have a Finance Committee meeting with rather sticky problems involved, so why don't we go through these presentations.

Mr. Sevin, would you go ahead. I have got a lot of questions I want to ask you.

Mr. STAATS. Mr. Chairman, if we don't have time to reach all your questions today, we will be very happy to respond in writing for the record.

Senator BENTSEN. I will send you a number of written questions. I really think this study is terribly important to put things in perspective between the two countries. We get an awful lot of rhetoric on both sides of that ocean, and here you have rather evenhandedly, from what I have seen thus far, surveyed the problem. I think it will be very important and helpful to the people of this country to try to understand our current economic dilemma.

Mr. Sevin.

**STATEMENT OF L. J. SEVIN, CHAIRMAN OF THE BOARD AND CHIEF EXECUTIVE OFFICER, MOSTEK CORP., CARROLLTON, TEX., ON BEHALF OF THE SEMICONDUCTOR INDUSTRY ASSOCIATION**

Mr. SEVIN. My name is L. J. Sevin. I am chairman of the board and chief executive officer of Mostek Corp., in Carrollton, Tex. Our company, which manufactures integrated circuits, has over 6,000 employees and enjoys annualized sales in excess of \$200 million.

I appear today on behalf of the Semiconductor Industry Association, a trade association of 33 United States-based manufacturers of semiconductors. I am honored to be invited to testify before this committee. Rather than read my entire statement, I will summarize it briefly and submit the full text of my prepared statement for the record.

My goal is to focus on what we see as the real problem of United States-Japan trade. The problem, we agree, is structural: The Japanese target industry system, which places the Japanese Government, with its limitless financial resources, behind a particular Japanese industry which is targeted for growth. Our present trade laws and treaties, including the MTN legislation, do not deal with such economic structures, and private American companies are hardly in a position to negotiate directly with the Government of Japan for structural changes, and, of course, we don't expect the Japanese to change their economic system.

We ask, however, that our Government negotiate at the highest levels with the Japanese Government to achieve a solution which moderates the disruptive international effects in the Japanese target industry practices. If negotiations are not successful, legislation may be necessary. But we do not intend to sit idly and watch the destruction of our industry.

Mr. Chairman, the American semiconductor industry stands exposed to the same Japanese target industry strategy which decimated the American color TV and steel industries. These targeting practices have also burdened U.S. commerce and a number of other industries. The successes of Japanese target industry strategies are well documented by the GAO report. As we all know, very little has been done by our Government so far to prevent these threats to our industries from becoming a reality.

The GAO report on United States-Japan trade problems does not focus specifically on trade in semiconductors. However, the Japanese Government's effort to develop a Japanese-owned computer industry has had dramatic impact on our industry. Modern semiconductor capability is absolutely essential to Japan's development of state-of-the-art computers.

As documented on page 177 in the GAO report, the Government of Japan, principally the Minister of International Trade and Industry, decided in the mid-1960's that Japanese industry should shift away from heavy industries, such as shipbuilding and chemicals, and move into clean, knowledge-intensive, high-value-added industries, such as integrated circuits and computers.

This decision was based, in part, on Japan's problems with pollution, raw material dependence, and rapidly rising costs. This evolution was not the result of free market forces or Japanese private sector innovation. It reflects a political decision as to the desirable course for Japan's future economic development. The development of exports by Japanese-owned firms and discrimination in Japan against foreign-owned enterprises has been a key tenet of Japanese economic planning.

The Japanese Government plans for its computers are aimed not only at such competitors as IBM, but also at smaller foreign-owned semiconductor, computer, and telecommunications companies. When Japan accelerated its target industry program for computers in 1960, it already had a fairly highly developed computer industry. IBM actually manufactured computers in Japan, and was supplying the Japanese market. Japan thus did not seem to want a computer industry; it wanted a Japanese-owned computer industry. The Government of Japan successfully targeted a large multinational company by "growing" a large Japanese-owned set of competitors. As a result, IBM's market share in Japan has declined to less than 30 percent in 1976, and it's much smaller than its share of market in the free market economies. If a company with the resources of IBM cannot protect its market position against Japanese targeting, the chances for successful penetration of the Japanese market by smaller U.S. semiconductor companies appear remote.

Japanese Government discrimination in favor of Japanese-owned firms must cease if the Japanese market is to be opened to international trade. As one might predict from their flood of exports in other target industries, the Japanese have accelerated exports and state-of-the-art integrated circuits to the United States. The principal product that the Japanese have exported to gain a significant portion of the U.S. semiconductor market is the 16,000-bit random access memory, otherwise known as the "16K RAM." It is the most advanced semiconductor memory component now in quantity production.

Many of these exports have been priced substantially below the going price in the American market. The market penetration motives are apparent when you consider that the Japanese-owned companies could sell the same 16K RAM products for a 25- to 50-percent higher return in their own market.

This phenomenon is illustrated in a table, which I am submitting with my prepared statement, which shows that Japanese companies lost \$500,000 on five selected contracts during 1979, by electing to sell here rather than in Japan. I ought to know this. My company, Mostek, was

an early leader in products such as the 16K RAM, and it is still very dependent on it for its success. I know what it's like to live and operate right in the middle of the bull's-eye of Japan's newest target.

The Japanese pricing strategy worked during 1978 and 1979. The Japanese-owned semiconductor firms have captured approximately 42 percent of the 16K RAM market in the United States. Now, the Japanese have argued that they solve trade problems by their investments in the United States. From purely a trade statistics viewpoint, this argument might have limited merit. Surprisingly, the GAO report seems to endorse this solution. This committee might study whether the U.S. investments by Japanese undermine the earning power of U.S. firms, making them less competitive in the United States and in world markets. For example, the return on color television operations for American producers dropped steadily from 8.7 percent of sales in 1971 to 3.7 percent, 2.8 percent, and 1½ percent, respectively, in 1976, 1977, and 1978. This was the period when Japanese firms shifted from imports to assembly of color television in the United States.

Now a return of 1½ percent on sales is hardly conducive to capital formation in free capital markets. And U.S. television firms, as a result, are in trouble. Television is no longer a growth industry; 1½ percent also approximates the average return by Japanese semiconductor firms. If Japanese firms selling from their U.S.-based plants force such low returns on American semiconductor companies, the American industry will lose its growth potential and its ability to raise capital.

All during the period when Japanese banks stand ready to supply capital funds for more Japanese-owned plants.

Our present laws may be inadequate to deal with this problem. Perhaps legislation is needed which will tax U.S. operations of foreign-owned firms in an amount necessary to offset the advantages which they derived from their governments. We recommend that such legislation be seriously considered.

Our suggested remedies to trade problems with Japan fall into four basic categories:

One, tax incentives designed to keep U.S. industry on a parity with the Japanese;

Two, on combating disruptive imports by the Japanese;

Three, better access to Japanese markets; and

Four, on the control of investments in the United States.

I am told that my 10 minutes is up. So, I will tell you that those are our recommendations, which are explained more fully in my prepared statement. I hope the committee considers them seriously as we have submitted them in written form. I recognize that they are extremely broad in character, and that implementation would involve much effort by many elements of Congress and the executive branch. We want very much to encourage this kind of active dialog which would lead to U.S.-Japan trade problems, and we are prepared to continue to assist you in every possible way.

Thank you.

[The prepared statement of Mr. Sevin follows:]

PREPARED STATEMENT OF L. J. SEVIN

My name is L. J. Sevin. I am Chairman of the Board and Chief Executive Officer of Mostek Corporation of Carrollton, Texas. Our company, which manu-

factures integrated circuits, has over 6,000 employees and enjoys annualized sales in excess of \$200 million.

I appear today on behalf of the Semiconductor Industry Association (SIA), a trade association of thirty-three U.S.-based manufacturers of semiconductors. With me today are Warren Davis, Director of Research of the Semiconductor Industry Association; and Peter B. Archie, of Peabody, Rivlin, Lambert & Meyers, our Washington counsel.

Mr. Chairman, I am particularly pleased to have the opportunity to discuss the United States semiconductor industry in the context of the Government Accounting Office study of trade problems between the United States and Japan.<sup>1</sup> Our interest in the subject of today's hearings is based on the concern of many SIA members about the international trade practices of the Japanese-owned semiconductor firms.

My goal today is to focus on what I perceive as the real problem with United States-Japan trade. The trade problems with Japan are structural: the Japanese target industry system which places the Japanese government, with its limitless financial resources, behind a particular Japanese-owned industry which is targeted for growth. Our present trade laws and treaties, including the MTN legislation, do not adequately deal with such economic structures, and private U.S. companies are hardly in a position to negotiate directly with the government of Japan for structural changes. Of course we don't expect the Japanese to revamp their economic system. We ask, however, that our government negotiate at the highest levels with the Japanese government to achieve a solution which moderates the disruptive international effects of the Japanese target industry practices and which removes structural barriers to the Japanese market and neutralizes the Japanese advantages in international trade. If negotiations are not successful, legislation may be necessary. We do not intend to sit idly and watch the destruction of our industry.

## I

### BACKGROUND

The U.S. semiconductor industry is a leader in a growing world industry which is expected to reach annual sales of \$10 billion in 1982 and perhaps \$20 billion by the late 1980's. Even more important, semiconductors serve advanced electronics equipment markets which are expected to total \$200 billion of annual sales by the late 1980's.

One of my colleagues in the SIA recently testified before the International Trade Commission that semiconductors are the "crude oil" of the advanced electronics systems.<sup>2</sup> The strength of all industrialized nations, Jerry Sanders urged, will largely depend on semiconductors by the end of this century. His conclusion, which I share with you today, is that the effectiveness of the United States government in coming to grips with contemporary problems of international competition will determine whether our country is a net importer or exporter of the "crude oil" for tomorrow's advanced computer and telecommunication systems. If Japanese targeting continues to be successful, the United States could become a net importer of another vital commodity. Now is the time to avoid a crisis with ramifications potentially as important as the present energy crisis. We endorse the conclusion of the GAO study<sup>3</sup> that U.S. policy has been "reactive," not "anticipatory." Now is the time to anticipate the threat to our high technology industries, and now is the time for our government to act.

Mr. Chairman, the U.S. semiconductor industry stands exposed to the same Japanese target industry strategy which decimated the U.S. color TV and steel industries. These targeting practices have also burdened United States commerce in a number of other industries. The successes of the Japanese target industry strategies are well documented by the GAO Report.<sup>4</sup> As we all know, very little has been done by our government to prevent the Japanese threats to our industries from becoming harsh realities.

The GAO Report on United States-Japan trade problems did not focus specifically on trade in semiconductors. However, the Japanese government's effort to

<sup>1</sup> Report by the Comptroller General of the United States, "United States-Japan Trade: Issues and Problems (Sept. 21, 1979)" (hereinafter cited as the "GAO Report").

<sup>2</sup> Statement of W. J. Sanders, President, Advanced Micro Devices, before the International Trade Commission, May 30, 1979.

<sup>3</sup> GAO Study, "Conclusion," p. 191.

<sup>4</sup> See, for example, GAO report, ch. 5, "Color Television."

develop a Japanese-owned computer industry<sup>5</sup> has a dramatic impact on our industry: Modern semiconductor capability is absolutely essential to Japan's development of state-of-the-art computers. Accordingly, the governmental benefits conferred on the Japanese-owned computer firms which are documented in the GAO report include substantial research and financial aid which was focused directly on Japanese semiconductor development. More specifically, the Japanese legislation which targeted the computer industry identified semiconductors as a key element in the target industry program.<sup>6</sup> Further, protection of the Japanese telecommunications industry<sup>7</sup> forecloses our companies from sales to a significant Japanese consumer of semiconductors.

As a result of its unique products and diligent marketing efforts over the three decades of its existence, the American semiconductor industry has achieved and sustained a 60 percent share of worldwide consumption of semiconductors. Furthermore, American product technology and process technology pervade the world. Make no mistake about it, at this time, transistors and integrated circuits manufactured by foreign competitors such as Philips, GEC, Siemens, Nippon Electric and Hitachi are basically American designs which are produced on specialized equipment of American manufacture.

A classic example of American ingenuity and pioneering spirit? Perhaps. But all of this is changing fast.

## II

### THE PROBLEM

Much of the dynamics of the U.S. semiconductor industry has come not from the established firms, but from entrepreneurial ventures in which employees spin off from the major electronics firms to exploit a technology or product which has been overlooked by the majors. Many of these enterprises, financed by private funds raised in free capital markets, have been so remarkably successful that they have shaken the conventional wisdom in the large companies, causing them to revitalize their research and market strategies. The results of free enterprise have been phenomenal technological advances and rapidly growing small companies.

Rather than develop small innovative growth companies, over the past twenty-five years several large Japanese companies have imported semiconductor technology, notably from Western Electric, Texas Instruments, and Fairchild Camera and Instrument. This was part of the overall acquisition of Western technology in all disciplines, orchestrated by the Japanese government, and purchased at bargain prices.<sup>8</sup> In 1977, for example, Japan's technology imports were \$1,027 million and its technology exports were only \$233 million.

But until the early 1970's, the progress of the Japanese electronics industry was slow and focused principally on consumer electronics, leaving the more advanced sectors such as data processing and telecommunications to the Americans.

As documented on page 177 of the GAO Report, the Government of Japan, principally the Ministry of International Trade and Industry (MITI), decided in the mid 1960s that Japanese industry should shift away from heavy industries such as shipbuilding and chemicals and move into the "clean, knowledge-intensive," high-value-added industries such as integrated circuits and computers. This decision was based in part on Japan's problems with pollution, raw material dependence, and rapidly rising costs. This evolution was not the result of free market forces or Japanese private sector innovation, but reflects a political decision as to the desirable course of Japan's economic development.

The core problem in our trade relations is accurately identified by the GAO Report—the pervasive economic planning by the government of Japan. Countries in Western Europe and emerging nations such as South Korea also engage in planning, but the real threat, at present, is from Japan. One result of the planning has been to give the Japanese-owned companies competitive advantages in export markets which not only burden U.S. commerce in general, but have severely crippled or destroyed several U.S. industries.

Development of exports by Japanese-owned firms, concurrent with discrimination in Japan against foreign-owned enterprises, has been a key tenet of Japanese

<sup>5</sup> GAO report, ch. 2.

<sup>6</sup> See GAO report, ch. 2, pp. 26–30, and, in particular, the description of the "VLSI" program at p. 29.

<sup>7</sup> GAO report, ch. 4.

<sup>8</sup> See, e.g., Abegglen & Hout, "Facing Up to the Trade Gap With Japan," *Foreign Affairs*, fall, 1978, pp. 146, 160.

economic planning. The Japanese government's "plans" for the computer industry are aimed not only at such competitors as IBM, but also at smaller foreign-owned semiconductor, computer and telecommunications companies. When Japan accelerated its target industry program for computers in the 1960s, it already had a highly developed computer industry. IBM actually manufactured computers in Japan and was adequately supplying the Japanese market. Japan thus did not want a computer industry: It wanted a Japanese-owned computer industry. The government of Japan successfully targeted a large multinational company by "growing"<sup>9</sup> large Japanese-owned competitors. As a result of the Japanese targeting, IBM's market share in Japan had declined to less than 30 percent in 1976 and is much smaller than its share in free market economies, which range from 60 to 75 percent.<sup>10</sup> If a company with the resources of IBM cannot protect its market position against Japanese targeting, the chance for successful penetration by small U.S. semiconductor companies appears remote. Government-backed discrimination in favor of Japanese-owned firms must cease if the Japanese market is to be opened to international trade.

Japan's economic planning has swiftly shifted the U.S. semiconductor industry's position from worldwide predominance to one of severe jeopardy. One industry observer, British consultant I. M. MacIntosh, concluded in a recent analysis that, as a result of intervention by foreign governments, the United States' preeminence in integrated circuits is diminishing and that the Japanese will reach parity in the medium term, followed perhaps some years later by the Europeans.<sup>11</sup>

As the GAO study relates, the government of Japan has channelled research funds to specifically favored Japanese-owned firms and groups of firms. Electronics industry development laws provided exemptions from the Japanese anti-trust laws, and group research was conducted which avoided duplication and thus yielded a high return for research expenditures. Some of these companies have arranged themselves into zaibatsu-like groupings with commercial banks in the center. The banks, as is the tradition in Japan, have provided up to 80 percent of the capital to their related companies in the form of short-term and medium-term loans. Standing behind the commercial banks are the Bank of Japan and the Ministry of Finance; the loans therefore appear to be de facto guaranteed. Indeed, only some form of a guarantee can explain the high debt-equity ratios of the Japanese companies. In any event, the growth of the Japanese semiconductor industry certainly was not financed by the free market capital formation process. Quite the contrary. In addition, the selected Japanese-owned semiconductor firms enjoy outright government grants of \$60 million or more per year and participate in the NTT laboratory research<sup>12</sup> and may receive the benefits of government research labs, as well.

The Japanese companies have very efficiently pursued collaborative research on advanced integrated circuit technology which would be in violation of anti-trust laws in the United States. Further, while U.S. patents are a matter of public record, key Japanese research is carefully shielded from disclosure to foreigners on the basis that government funds contributed to the research. The companies have aggressively built and then expanded modern factories employing state-of-the-art equipment. For example, when an American equipment manufacturer announced, three years ago, a new \$1 million computer-based electron beam mask-making system, three of the first five units were purchased by the Japanese.

While government-directed funds have financed the Japanese industry, free market capital formation in the United States has not kept pace with the rapid growth of the semiconductor industry. U.S. firms have experienced difficulties raising sufficient funds in the American capital markets to modernize and expand their companies at the pace required to meet worldwide demand. As a consequence, some U.S. companies have sought foreign sources of capital and others have been acquired outright by foreign companies or allowed foreign firms to take substantial equity positions in their firms. Notable examples of foreign acquisitions of U.S. firms are Philips/Sigmetics, Schlumberger/Fairchild and Nippon Electric/Electronic Arrays. Examples of minority equity investments by foreign firms in U.S. companies are Siemens/Advanced Micro Devices, Bosch/American Micro Systems and Northern Telecommunications/Intersil.

<sup>9</sup> See GAO report—"Japan Grows Key Industries," p. 176.

<sup>10</sup> See GAO report, ch. 2, "Computers," p. 22, chart 2.

<sup>11</sup> The Integrated Circuit Industry to 1985," MacIntosh Consultants Co., Ltd.

<sup>12</sup> See GAO report—"Telecommunications," p. 66.

The American semiconductor industry does not contest the decision by the Japanese to compete with the U.S. firms, but we do contest the scope of support by the Japanese government and the tactics being employed by the Japanese companies. In a free market, the U.S. semiconductor companies are competitive with any private companies in the world. We question, however, whether the Japanese semiconductor firms fairly fit the description of private enterprise. Rather, when we look closely at the Japanese companies, we feel that we are competing with the central Treasury of the Japanese government. The GAO Report suggests that our analysis is not entirely wrong.<sup>13</sup> Specifically, we support the criticism in the Report that Japan has not allowed free market forces full play in development of its targeted industries.

### III

#### PENETRATION OF THE U.S. MARKET

The Japanese, as one might predict from their flood of exports in other targeted industries, have accelerated exports of state-of-the-art integrated circuits to the United States. Moreover, many of these exports have been priced substantially below the going price in the U.S. market. Their market penetration motives are apparent when you consider that the Japanese-owned companies could sell the same 16K RAM products for a 25-50 percent higher return in Japan. This phenomenon is illustrated in Table 1, attached, which shows that the Japanese companies lost \$500,000 on five contracts during 1979 by electing to sell in the United States rather than in Japan. The Japanese loss on all U.S. sales was doubtlessly much larger. This is a small part of the sacrifice the Japanese made to buy a share of the U.S. semiconductor market.

The principal product that the Japanese have exported to gain a significant portion in the United States semiconductor market is the 16K RAM (the 16,000 bit Random Access Memory), which is the most advanced semiconductor computer memory device in volume production. In two years and by pricing their way into a capacity-limited seller's market, three large Japanese-owned companies—Nippon Electric, Hitachi, and Fujitsu—have severely disrupted the U.S. market.

I ought to know. My company, Mostek Corporation, was an early leader in products such as the 4K RAM and 16K RAM, and is still dependent on these products for its success. I know what it's like to live and operate right in the middle of the bull's-eye on Japan's newest target.

Even in the face of strong demand, Mostek and other U.S. semiconductor producers have typically reduced their prices along the learning curve. Beginning in 1978 when Japanese imports began to flood the United States 16K RAM market, Japanese products were priced approximately twenty to thirty percent below the U.S. price, even though the Japanese were not as far down the learning curve. Initially U.S. companies were forced to drop their prices to meet the Japanese but, as demand remained strong in late 1978 and early 1979, a two-tier price structure began to develop with the Japanese products typically selling in the United States at 20 percent or more below the prices charged by U.S. companies. Nonetheless, the low Japanese prices forced the U.S. companies to keep prices lower than normal.

The Japanese pricing strategy worked during 1978 and 1979. The Japanese-owned semiconductor firms have captured approximately 42 percent of the 16K RAM market in the United States—which is ahead of the target market share of 25 percent<sup>14</sup> which Nippon Electric Company announced two years ago when the Japanese market share was quite small. Japanese targeting practices must thus be regarded as a real threat to United States semiconductor markets.

One might argue that U.S. consumers benefit from these bargain prices. But we must realistically ask how long such bargain prices last. Middle Eastern oil was a bargain until the United States became dependent upon it, then the prices escalated. Similarly, sooner or later the Japanese losses on high density memory products (such as those shown on Table 1) will be recouped. We respectfully submit that it is foolish to assume that the Japanese semiconductor companies plan to confer any long run benefits on consumers in the United States.

<sup>13</sup> See GAO report, pp. 176-77.

<sup>14</sup> A leading Japanese semiconductor executive, quoted in *Electronics*, June 9, 1977, p. 103.



The Japanese pricing has already caused several U.S. companies to abandon the 16K RAM market. In 1978, faced with low priced Japanese imports, several American semiconductor companies substantially reduced or even abandoned 16K RAM production and shifted their plants to products which the Japanese could not manufacture. However, having driven several companies out of the market, the Japanese now argue that the U.S. semiconductor firms cannot meet domestic demand. The answer is that the U.S. firms simply do not have captive sources of capital such as the Bank of Japan and the Japan Development Bank and must maintain current earnings in order to expand capacity and finance research. Funding is simply unavailable in the U.S. to finance a prolonged price war.

Let us examine one further implication of the sudden surge of 16K RAM imports.

High density memory products such as the 16K RAM serve a high volume mass market. The other leading integrated circuit product, the microprocessor, a high density logic circuit, is produced in relatively small quantities to custom design of specific customers. The RAM volume finances the supporting research required for development of further integrated circuit products and permits amortization of the R&D expense over the high volume. If the 16K RAM market, or the successor 64K RAM market, were lost to predatory Japanese competition, the American semiconductor industry would suffer not only in RAMs, but in all integrated circuit product lines. Without the cash flow from the high volume products, the U.S. firms would be hard pressed to remain competitive technologically and the United States could become a net importer of state-of-the-art circuits.

#### *Restricted Access to the Japanese Markets*

While Japanese companies invade the U.S. market, our hands are tied in Japan.

An important part of Japanese government policy has been to shelter their home markets for semiconductors, integrated circuits and other manufactured products. They do this through a complex set of barriers which are contrary to all notions of free trade. As a consequence, foreign penetration of the total Japanese semiconductor market has been limited by an apparent de facto quota of 10 percent of Japanese consumption and American imports of integrated circuits have been limited by a de facto quota of approximately 20 percent of Japanese consumption. These numbers compare to 60 percent and 75 percent American share of the European semiconductor and integrated circuit markets, respectively. The reasons for the disparity are directly attributable to the fact that the Japanese government wants neither foreign investment nor imports of manufactured goods, particularly products of high technology industries.

#### *Exclusion of Direct Investments*

The table of capital inflows into Japan in the GAO Report shows that the levels of foreign investment in Japan have been significantly lower than those in other developed countries.<sup>15</sup> Certainly the Japanese market should be attractive to many investors. Why, then, is foreign investment so low? The answer lies with the restrictive governmental policies.

As a practical matter, acquisitions in Japan are limited to bankrupt companies which the government hopes to salvage. Japanese law requires a unanimous vote of the Board of Directors of an acquisition target firm which makes acquisitions by foreigners practically impossible unless the Japanese government consents. Similar restrictions do not exist in the United States and the major Japanese semiconductor firms are exercising their privilege under our laws to acquire U.S. firms (Nippon Electric-Electronic Arrays) or take equity positions in American high technology companies (Fujitsu-Amdahl). Acquisitions and joint ventures are also freely permitted in Western Europe and this strategy is being employed by both American and Japanese firms to strengthen their toehold in Europe. Once again, Japan simply does not play by the rules which govern trade and investment in advanced economies. Participation in target industry development programs is restricted to indigenous firms. Foreigners are excluded.

Texas Instruments (TI) is the only American semiconductor company which has successfully established manufacturing facilities in Japan. TI virtually

<sup>15</sup> GAO report, ch. 9, table 4, p. 163.

"shot their way in" in 1968, by threatening to file for an injunction against imports into the U.S. of most Japanese integrated circuits for alleged patent infringement unless the government of Japan allowed TI to establish a plant in Japan. To "comply" with investment laws, Japan selected Sony Corporation as a cosmetic joint venture partner for TI. In due course, TI commenced production and later bought out its partner, which was never active in management of the joint enterprise. Over the past decade, TI has expanded its facilities in Japan. Further, as Boston Consulting Group's Tokyo manager James C. Abegglen states " \* \* \* investment in Japan is a powerful stimulant to export sales to Japan".<sup>16</sup> Thus, by denying other U.S. firms the right to acquire local companies and invest locally, Japan tends to stifle imports, as well. All according to plan.

#### *Unsuccessful Joint Ventures*

During the 1970's, other large American electronics firms attempted to establish manufacturing operations in Japan but lacked a bargaining chip like Texas Instruments. Motorola entered into a joint venture with Alps and constructed a factory in Honshu; Fairchild entered into a joint venture with TDK with intentions to vertically integrate backwards from semiconductor distribution to final assembly and eventually to wafer fabrication. Both ventures were unsuccessful and were dissolved. In recent years, we are told, the Japanese foreign direct investment law has been "liberalized" to permit wholly-owned manufacturing ventures to be formed. If foreign investment in Japan is the test of liberalization, the policy has failed. As the GAO Report indicates, foreign investment continues to decline in Japan.<sup>17</sup>

Like Motorola and Fairchild, other investment overtures by American companies have been frustrated. The reasons are bureaucratic delays in obtaining licenses and permits, unavailability of skilled labor, and the total absence of Government of Japan financial or tax incentives to foreign investors. While Japanese firms entering the U.S. market hire away the best personnel from U.S. semiconductor companies, the Japanese government appears to foster the attitude among Japanese citizens that employment by alien firms is undesirable. It thus takes a considerable time for a foreign-owned de novo manufacturing or sales facility in Japan to hire and train a staff and to become effective and profitable. For example, after an intensive one year search, one U.S. semiconductor company was able to hire a native Japanese semiconductor salesman, but only from another U.S.-owned company. Obviously such personnel practices, which have no counterpart in either the United States or Western Europe, give the entrenched Japanese-owned companies significant advantages in their home market. Affirmative action is clearly needed to assure equal treatment of all investors in Japan. The signal is clear. The Japanese government does not want foreign investment in Japan, particularly in target industries.

In contrast to the barriers to foreign investment in Japan, Japanese companies are taking advantage of U.S. Federal, State, and local investment incentives such as industrial revenue bonds and training subsidies to build factories in areas such as San Diego, Memphis, and Dallas, to mention just a few locations. Also, Japanese companies receive liberal investment incentives from the governments of the European Economic Community. Examples include the Nippon Electric investment in Ireland (tax holidays, cash grants, training subsidies), and Hitachi/NEC in the United Kingdom where the British National Enterprise Board allows foreign as well as domestic high technology ventures to draw on liberal grants and subsidies.

Most governments of "free" countries with developed economies are indifferent to the nationality of shareholders and welcome all investors, nationals and aliens alike, and offer financial incentives on equal terms. Japan stands alone in its discriminatory policies.

#### *Japanese Restrictions Against Semiconductor Imports*

The Japanese systematically restrict imports of American semiconductors and particularly large scale integrated circuits. They do so in several ways which we will briefly discuss:

<sup>16</sup> Abegglen & Hout, "Facing Up to the Trade Gap With Japan," Foreign Affairs, fall, 1978, p. 163.

<sup>17</sup> GAO report, ch. 9, table 4, p. 163.

By maintaining high tariffs :

By frustrating attempts of American companies from quoting on new orders; and

By practicing customs harassment.

Let us deal with these barriers one by one (including contrasting conditions in Japan to those in the United States and other advanced nations) :

The published Japanese customs duty on integrated circuits is 15 percent, and the applied rate is 12 percent. The government of Japan agreed at the Multilateral Trade Negotiations (MTN) in Geneva to reduce these tariffs to 4.2 percent, in stages over the next eight years. The United States' duty on semiconductors is 6 percent and will also drop to 4.2 percent over the same staging period. Efforts to accelerate the staging of the reduction were strongly resisted by the Japanese and hence were unsuccessful. Eight years in our industry can be a lifetime of a product. Eight years ago, for example, the 16K RAM was unavailable commercially.

The actual tariff can be higher than 12 percent, as American semiconductor firms are subjected to arbitrary tariff "uplifts," surcharges applied to invoice values of up to 10-15 percent on imports into Japan between related companies. Uplifts are to be eliminated under the MTN customs valuation code, and we hope that implementation by the Japanese will be prompt and consistent with the spirit of the Geneva accords.

In addition to high tariffs, the American companies encounter a myriad of barriers in gaining access to specifications necessary to quote on Japanese business.<sup>18</sup> This trait is unusual because Japanese firms pride themselves on flexibility in customer-supplier relationships.

Further, U.S. firms frequently cannot obtain duty rebates if they desire to re-export goods from Japan or can obtain such rebates only after extreme difficulty.

American semiconductor companies are not certified by the Japanese government for sales of integrated circuit products to a key Japanese telecommunications customer—Nippon Telephone and Telegraph.<sup>19</sup> One excuse given is that the U.S. firms have not participated in the government-sponsored research and development programs in the NTT labs. It is true that U.S. firms do not participate, because foreign companies are permanently excluded from participation. The participating Japanese companies, however, while unable to purchase integrated circuits ("ICs") for sale to NTT, do purchase some American IC components for telecommunications systems being exported to foreign suppliers. This dichotomy leads to twin production lines in the Japanese plants—one inserting American ICs into the printed circuit boards for the export market; the other using indigenous parts.

The Japanese have vociferously defended their protectionist policies. For example, we hear a litany of excuses why the Japanese do not import more U.S. goods, which include: out-of-date and inefficient U.S. factories; declining U.S. labor productivity; poor U.S. quality and lack of quality control; and the U.S. has forfeited export opportunities.

These arguments simply do not apply to the U.S. semiconductor industry. Our labor productivity is extremely high. Objective tests show that our quality is unsurpassed. And our export effort has been remarkably successful—everywhere, that is, except Japan, where the governmental policies frustrate meaningful import competition.

To sum up, in my view anyone who applies the traditional Japanese arguments to the U.S. semiconductor industry simply does not know the history of our industry. We have not been "reluctant exporters." We have, however, been stonewalled in Japan.

## V

### JAPANESE INVESTMENT IN THE UNITED STATES

The Japanese have argued that they solve trade problems by their investments in the United States. From purely a trade statistics viewpoint, this argument perhaps has limited merit. Surprisingly, the GAO Report seems to endorse

<sup>18</sup> GAO report, ch. 4, "Telecommunications," p. 74 ("detailed specifications are generally not publicly discussed" by NTT).

<sup>19</sup> Barriers to sales to Nippon Telephone & Telegraph are documented in the GAO report at pp. 74-76.

this solution.<sup>20</sup> This Committee might study whether U.S. investments by the Japanese undermine the earning power of U.S.-owned firms, making them less competitive both in the United States and in world markets. For example, the return on color television operations for U.S. producers dropped steadily from 8.7 percent of sales in 1971 to 3.7 percent, 2.8 percent and 1.5 percent, respectively, in 1976, 1977 and 1978.<sup>21</sup> This was the period when Japanese firms shifted from imports to U.S. assembly of color televisions. A return of 1.5 percent on sales is hardly conducive to capital formation in free capital markets and the U.S. television firms are not prospering. Television is no longer a growth industry.

1.5 percent also approximates the average return by Japanese semiconductor firms. If Japanese firms, selling from their U.S.-based plants, force such low returns on the U.S. semiconductor companies, the U.S. industry will lose its growth potential and its ability to raise capital, all during a period when the Japanese banks stand ready to supply capital funds for more Japanese-owned plants.

## VI

### THE REMEDY

Our suggested remedies fall into four basic categories:

- (1) Tax incentives designed to keep the U.S. industry on a parity with the Japanese.
- (2) Meaningful remedies for disruptive imports by the Japanese.
- (3) Access to the Japanese market.
- (4) Investments by the Japanese in the United States.

#### (1) *Tax Incentives*

Congress should establish a policy for the United States which provides incentives and other stimuli for those industrial sectors which we can reasonably expect to contribute disproportionately to the productivity, research strength, and trade strength of the national economy. Integrated circuits and computers would place high in this list. The incentives would relate to such parameters as innovation, exports, value added, employment (both qualitative and quantitative) and would stimulate intensified R&D and capital investment in the leading industries.

Specifically, we recommend the following:

Tax credits for year-to-year increases in research expenditures by fast growth, high technology firms;

Rollover provisions—capital gains tax deferral for reinvestment in new securities issues;

Liberalized depreciation, the net effect of which would be a three year write-off of equipment with a commensurate investment tax credit period;

Jointly funded cooperative research on university campuses in high technology areas; and

Tax credits for corporate contributions to universities, not to exceed 10 percent of total R&D expenditures by the corporation.

#### (2) *Japanese Imports*

If the Japanese government persists in disrupting free market forces, our government must apply an equivalency standard to limit Japanese-owned semiconductor penetration of the U.S. market. This standard should be applied on a product-by-product basis and tied to the equivalent of U.S. penetration of the Japanese market.

#### (3) *Access to Japanese Market*

Our government should negotiate with Japan for immediate implementation of the MTN tariff cuts, inclusion of NTT under the Government Procurement Code, and strict enforcement of the other nontariff barrier codes.

Japan must immediately eliminate all discrimination against foreign-owned companies with respect to equal access to financing, research and employment.

The Japanese must also cease all restrictive patent practices and must allow foreign-owned companies to acquire Japanese semiconductor patents as freely and openly as Japanese acquire American patents.

<sup>20</sup> GAO report, ch. 5, "Color Television."

<sup>21</sup> Source: ITC data.

## (4) Japanese Investment in the United States

Congress should consider legislation which would tax U.S. operations of foreign-owned firms in an amount necessary to offset the advantages which they derive from foreign governments. If Japanese trade practices conducted from plants within our borders disrupt our markets or threaten the U.S.-based industry, appropriate steps must be taken to correct the situation.

TABLE I.—SELECTED 16K RAM SALES IN JAPAN BY A UNITED STATES COMPANY DURING 1979

[Landed price in Japan of United States 16K RAM's and total loss by Japanese semiconductor companies on 5 sample contracts due to sell in the United States rather than in Japan]

Japanese customer <sup>1</sup>	16K RAM (type)	Contract quantity	Landed price in Japan of United States 16K RAM (per unit)			Landed price in Japan	Japanese price in United States for same product <sup>2</sup>	Japanese loss on exports	
			United States f.o.b. price	Freight and duty	Trading company commission			Unit	Total
A.....	4116 N-4	20,000	\$5.75	\$0.86	\$0.86	\$7.47	\$4.85	\$2.62	\$52,400
B.....	4116 N-4	30,000	5.50	.83	.83	7.16	4.85	2.31	69,300
C.....	4116 J-2	60,000	6.75	1.01	.34	8.10	5.40	2.70	162,000
C.....	4116 J-3	60,000	5.75	.86	.29	6.90	5.10	1.80	103,000
D.....	4116 J-3	60,000	5.95	.89	.30	7.14	5.10	2.04	122,400
Total.....									514,100

<sup>1</sup> Customers C and D also manufacture semiconductors.

<sup>2</sup> Does not reflect deductions for costs of freight and duty which were also absorbed by the Japanese companies.

Source: Mostek Corp.

Senator BENTSEN. Mr. Sevin, I have read that you have sold your company. It makes me happy for you and, I suppose, your bankers. But it also makes me a little sad because I have known you for a long time as a pioneer in the semiconductor business and a leader in that field of competitiveness that is part of the American system at its best.

I can't help but wonder if what you have just stated wasn't a part of your decision. You don't have to comment on that if you don't want to.

Mr. SEVIN. We did sell our stockholders company, yes. We have traded a number of public stockholders for one large stockholder, although this should not and will not make any difference in the way we operate our company. It will not make any real difference in the problems we have of capital formation. After all, United Technologies is not a charitable institution.

Senator BENTSEN. I understand.

I have some other questions later, but I would like to call on Mr. Wolf now.

**STATEMENT OF ALAN WM. WOLFF, FORMER DEPUTY SPECIAL REPRESENTATIVE, OFFICE OF THE SPECIAL REPRESENTATIVE FOR TRADE NEGOTIATIONS; CURRENTLY WITH THE LAW FIRM OF VERNER, LIPIFERT, BERNHARD & McPHERSON, WASHINGTON, D.C.**

Mr. WOLFF. Thank you, Mr. Chairman. It's good to be back appearing before you.

I congratulate you on the idea of having the GAO here on the study that has been produced. I congratulate Mr. Staats on what I think is a very fine job in an area that really needs a lot of work. It's some-

thing that should not be a one-time effort, but a continuing review should take place of trade relations and key issues with Japan.

One problem that we have in this country is a lack of a long attention span for our trade problems with Japan. It has become apparent that we're almost entirely dependent upon Texans for our progress in trade relations. [Laughter.]

Senator BENTSEN. That's not all bad.

Mr. WOLFF. We have John Connally, who pointed a few things out to us in the early 1970's, and Bob Strauss, and you've had a long-term interest in this subject.

In my service with the Carter administration as Deputy Special Trade Representative, Japan ranked among my key concerns, one of the critical issues that was within my responsibility. And we made some very concrete progress in a number of very contentious areas. And I regard those successes as important, not just because they resulted in additional opportunities for American businessmen in the Japanese market, but because they contributed substantially to the strengthening of overall relations between the two countries. But I'd stress that these were only a beginning, really, on a very long and difficult road.

Our policy outlook was that we couldn't paper over differences in the trade area with Japan; that it would undermine our long-term relationship to do so; and that being very firm and pursuing solutions very strenuously is in the long-term interests of Japan and the United States in terms of our political as well as economic interests.

I regard the Strauss-Yoshida joint statement of January 1978 as an important step forward in that process of coming to grips with the problems we face, as well as the key things that were accomplished in the Multilateral Trade Negotiations: The cut in tariffs, the agricultural concessions, and in particular the nontariff barrier agreements.

I'd say that one of the things that the GAO points out in its report is that the Japanese have maintained protection for a long time in various industrial sectors, and this is true. And then the liberalization comes once the industry is relatively strong, which is a good strategy from perhaps a national point of view of Japan. But it leads to less credit being given than the Japanese might expect.

The Japanese came here in December 1977 and they announced that they were going to eliminate the tariff on cars, which is something we had asked them to do for years, and they wondered why there was no great positive congratulatory outcry in this country in their favor. And the reason is it was too late. The Japanese market had developed behind a series of protective devices, and when the tariff came off there was no congratulations to be heard on our side.

I think that the significance of the MTN really comes in the nontariff barrier areas. There are extremely difficult problems, you know, in the past in the product standards area, testing certification, both in agriculture, citrus; years of problems in trying to get use of our fungicides approved. The Pacific Northwest still has a problem with cherries in their shipments. Automobiles still have some problems in testing.

The standards code should help resolve some of those problems. And the Government procurement code, I think, will help open up some new business, although that is going to be a struggle.

But the tools are there, new tools are there, and I think they ought to be used.

The danger I see currently is that the pressure may be off to a large degree to come to grips with the problems that I still see before us. The Japanese current account surplus which was an astounding \$17 billion a year ago, has turned around to what may be a \$3 billion to \$5 billion deficit this year. And their global trade surplus is substantially eroded. There is still a \$9 billion surplus of the Japanese with us. But globally, the Japanese are posing less of a source of disruption to the world economy than they were earlier.

This could lead to complacency with respect to the opening of the Japanese market, and I think that would be a terrible error for you as officials, as well as for Japanese Government officials.

First of all, it was stated that the appreciation of the yen was a cure to the problem, but it overstated the trade surplus. Now, the depreciation of the yen last year, going from the high of 175 to the dollar to this morning, about 228 yen to the dollar, means that the turnaround is overstated. And the solution seems to be at hand. But I don't think it is.

Japanese goods are going to be increasingly competitive because of the one-quarter depreciation of the yen in the last year. And while we applaud a strong dollar for global reasons, for reasons of the global economy, the exchange rate is not going to be the long-term solution with Japan. We look to have it solve more of our problems than it can. With Japan so completely dependent on energy imports, the yen may well remain weak for a good deal of time to come, and that means that exports will be highly competitive.

And also, of course, our rate of inflation is high. While the Japanese rate of inflation is increasing, there's been a gap there, too. So the real currency changes, as far as the normal kinds of changes, are much less than people may feel exist.

We still face problems that can't be cured by exchange rate changes in our trade relations with Japan: The problems in the distribution system that Mr. Staats has alluded to, the inability of foreign retailers to invest in the Japanese distribution system very easily. Not only is wholly owned investment discouraged, but joint ventures are also difficult for retailers, for manufacturers and for distributors as well. And investment is closely linked to trade.

If we don't have a major presence in Japan, the sale of industrial intermediates as well as consumer goods is inhibited.

There are also a number of other factors that aren't susceptible to exchange rate changes: The closeness of the various sectors of the Japanese economy, the closeness of government to industry.

One of the things that the GAO really points up is that we do not have an industrial policy in this country. Consciously, we don't have an industrial policy. We don't favor the steel industry over the shoe industry, or textiles over semiconductors. We have a *laissez faire* policy and others don't. And we're going to have to come to grips with the fact that we don't have conscious planning of that kind.

I see a resurgence of problems in terms not only of our export opportunities in Japan, but also the presence of a disruptive influence in our market. If I were a Japanese policymaker, I might be getting concerned about the global position of Japan, the erosion of the trade

surplus, and the substantial deficit, and I might consider taking off the export surveillance which has been in place for a number of products—special surveillance on automobiles, steel, ships, and television sets, and regular surveillance on motorcycles, washers, and cameras—I think that would be enough.

I think that the inundation of this market that took place in color television sets could be repeated, and not only should the Japanese be vigilant of excessive competitive problems in our economy, but our own policymakers must be. In areas like computers, color televisions, copiers, commercial aircraft, and semiconductors. So, while Government efforts have been, I think, inadequate, as Mr. Sevin has said, I think the private sector has tools on the trade agreement side and those really ought to be examined closely by the private industries that have to compete with current Japanese competition and future competition.

My prepared statement has a number of other suggestions that may be useful both for you as policymakers and for the Japanese Government.

Thank you.

[The prepared statement of Mr. Wolff follows:]

PREPARED STATEMENT OF ALAN WM. WOLFF

Mr. Chairman, I very much appreciate the opportunity to appear before you today on the subject of United States economic relations with Japan.

In my service with the Carter Administration as Deputy Special Representative for Trade Negotiations to Robert S. Strauss, trade problems with Japan ranked among the most critical issues within my responsibility. I count among the successes that Bob Strauss and I and our office enjoyed during these years making some concrete progress on a number of very contentious issues that divided Japanese and American policy makers. I regard the successes that we have had as important, not just because they resulted in additional opportunities for American businessmen in the Japanese market, but because they contributed substantially to the strengthening of overall relations between the two countries.

The agencies of the U.S. Government are rarely united in any common policy or common approach to a problem. This is to be expected in a pluralistic society with widely differing points of view on any given subject. But with respect to our trading relations with Japan there was a remarkable coalescence of views that lasted for a few years, and was expressed through the work of Assistant Secretary's Group on Japan that I chaired.

Essentially, the consensus view was that harmonious long-term political and economic relations between the United States and Japan depended on the continuing process of the liberalization of the Japanese market. Of particular economic and political importance was the increase of imports of manufactured goods into Japan. The tools to achieve this objective were a combination of macroeconomic and microeconomic policies and measures: the upward float of the yen, expansionary Japanese domestic economic policies, and a number of concrete actions taken by the Japanese government to remove trade restrictions and increase imports.

The amount of attention given to our relations with Japan was very substantial, in the press, in the Congress, and in the Executive Branch. Delegations of Japanese government officials, legislators, and businessmen visited the United States frequently. As the Japanese current account and trade surplus grew to enormous proportions, substantial progress was made. This prevented, during a very difficult time, an overreaction either in the United States in the form of closing our market to Japanese goods, or in Japan where there was increasing resentment against what was seen as overbearing United States pressure.

Instead of an open break, an accord was reached in the Strauss-Ushiba joint statement of January 1978. I know of no parallels in history to the agreement reached in that document. Its importance lay not so much in the specific imports that were to be increased, such as beef and citrus, but for the direction set for



U.S. and Japanese trade policies: toward the expansion of trade rather than the Japanese opting for status quo and the United States and Europe reacting by closing their markets to Japanese goods.

There followed substantial agreements in the Tokyo Round of Multilateral Trade Negotiations concluded in April in Geneva, Switzerland.

Japanese Industrial Tariffs will be cut by over 40 percent from applied rates, by over 60 percent from official GATT bound rates. Thus Japanese tariffs will be as low or lower than those on United States dutiable trade, ending a long source of friction between our two countries.

In agriculture, Japan made offers covering \$1.3 billion in U.S. exports covering almost every request made by the United States for concessions from Japan. Japan also enlarged its citrus and beef quotas, which is the beginning of what can be very valuable markets for these two commodities in Japan. Both of these areas will be the subject for further negotiations with the Japanese within the next few years.

With respect to nontariff barriers, Japan will sign all of the codes of conduct agreed to in the Multilateral Trade Negotiations.

Of great importance is this last point. The Products Standards Code, the Customs Valuation Code, the Government Procurement Code, and the Aircraft Agreement can provide the rules and procedures to achieve solutions to some of the most difficult trade problems that have aggravated relations between the two countries. Further negotiations are in progress to assure that telecommunications equipment, in which the United States has a comparative advantage, will be able to compete freely for the Japanese government procurement market. In early June of this year, the Japanese agreed with Ambassador Strauss to afford the United States reciprocity in this area. Specific progress has also been made with respect to a number of products standards issues, and the outlook is good for further progress to be made.

With significant progress made in the Multilateral Trade Negotiations, the results of which will be primarily felt over an extended period of time, there also occurred significant improvement as the result of short run economic policies and measures. According to Japanese figures on a customs clearance basis, in August Japan had a trade deficit of \$1.65 billion. This figure reflected a 46 percent increase in imports when compared with the previous August, with only a 3 percent gain in exports (in dollar terms). According to recent projections, Japan will go from a surplus position of \$17 billion for its current account to a \$3-5 billion deficit this year, if not more. Japanese trade surpluses of prior years would also be substantially eroded. While Japan would still have a substantial trade surplus with the United States (perhaps around \$9 billion this year), it can no longer be easily argued that Japan is continuing to impose a burden upon the world economy to the extent it did when it was accumulating a trade surplus of \$24 billion and a current account surplus of \$17 billion, with a world in debt to OPEC.

In the face of this dramatic change in circumstances, it is not surprising that the level of the public and government attention that has been devoted to U.S. trade relations with Japan has dropped off substantially. The extreme sense of urgency that characterized the last few years has been succeeded by a sense of complacency.

The purpose of my outlining the progress that has been made is two-fold. First, Japanese policymakers deserve credit for the move toward greater openness that they launched. Secondly, and of equal importance, the complacency that the program to date appears to be generating carries with it significant risks for the United States and Japan. It could lead to an increase in misunderstandings and tensions in the months and years ahead, squandering the good will which has been painfully accumulated over the last 18 months.

It was suggested to me last week that U.S. trade policy ought to have more consistency and that we ought not to make progress in our relations with Japan dependent upon the appearance upon the scene of Texans. While I admire the two Texans under which I have served, John Connally at the Treasury and Bob Strauss as Special Trade Representative, I would agree that more consistency is needed in the attention that we give to our trade relations with Japan. The temptation to optimism that exists today also existed in September 1973 when our negotiators pointed to specific measures that the Japanese government had taken to liberalize a number of imports, and the substantial change in the trade balance of Japan that occurred then. We have more recently gone through a period of more extensive efforts, and have seen even greater movement towards balance with Japan. What followed the 1971 and 1972 negotiations was a relaxation of

tensions and a turning of attention by policymakers in both capitals to other problems. One can sense a similar drift in the attention of officials in Washington and Tokyo now.

Has there been a fundamental change? I believe that there has but it has been a change that is only at its beginning. The first steps have been taken, but as with the Multilateral Trade Negotiations recently concluded, almost all the benefits are dependent upon follow-through.

The startling turnaround in the figures of Japan's overall trade balance and its current account balance has a lot to do with the increase in the price of oil as well as the sharp appreciation of the yen (peaking last October at 175/dollar) and then its sharp depreciation since that time. The J-curve effect swelled the Japanese surplus figure even as the rate in growth of exports was diminishing due to the higher priced yen. Now the yen is one-quarter cheaper than it was a year ago and one can expect Japanese exports to become increasingly competitive and imports to become increasingly dear. The same effect (the appreciation of the yen) which artificially swelled the trade surplus of last year while it in fact contained part of the basis of the cure, is now working perversely in the other direction—the yen/dollar exchange rate originally overstated the problem. Now it overstates the extent to which there has been a cure.

Exchange rates no longer contain (if they ever did) as much of the solution to trade problems as was once thought. While floating exchange rates normally should correct for the normal trade imbalances among nations, they cannot by themselves correct imbalances between two countries which are both substantial net oil importers. Japan is almost entirely dependent for energy on imports. This causes an imbalance in the Japanese trade position which is difficult to overcome even though this was done once in the mid-1970's. Indeed Japanese commentators are wondering whether it can be done again. The result of the concern that the Japanese economy may not be equal to the task is a low yen value. This energy-related depreciation of the yen causes, in the view of a number of economists, the Japanese yen to be under-valued. This means that the normal corrective of the exchange rate (never necessarily a corrective in a bilateral trade imbalance) is even less so now between Japan and the United States.

It is not just OPEC's presence that makes the exchange rate inadequate as a corrective, there is also the lack of price sensitivity of many goods traded between the United States and Japan. Many U.S. exports to Japan will not be increased by a lower price. Wheat, soybeans, large commercial jet aircraft, and high technology goods which the United States supplies to Japan are not supplied in substantially increased quantities with a decline in price caused by a depreciating dollar. Japanese exports to the United States, on the other hand, have endured substantial dollar price increases due to appreciation of the yen without faltering. This is due in part to brand recognition and quality as well as the demand for goods which were not readily available in sufficient quantity in the United States, such as small cars.

Another factor which must be considered is the real as opposed to nominal appreciation of the yen. I do not have the current figures, but I would assume given the recent depreciation of the yen over the last 12 months that the real appreciation of the yen in recent years is very slight indeed, netting out the relative rates of inflation in Japan and the United States.

There are also other problems which are beyond the reach of exchange rate changes and price competitiveness. These are the areas of the Japanese economy that are protected from external competition by a variety of nontariff barriers. In the agricultural area, although Japan is in fact the best customer for agricultural exports that the United States has (amounting to some \$5 billion in the current year), resale price maintenance for food, in particular wheat, inhibits sales of imported products in Japan. With respect to imports of consumer goods, there continues to be the very substantial problem of a very complicated distribution system which marks up goods to the consumer to the point where they cease to be attractive in quantity. This may in fact be exacerbated by the adoption in 1980 of a general excise tax. It is widely accepted that the adoption of a tax on consumption with rebate of the tax at the border on exports will have an export incentive and import inhibiting effect when the tax is adopted, particularly if the tax substitutes for other forms of revenue. Thus at a time when the Japanese market is already considered to be resistant to imports of consumer goods, the introduction of a general consumption tax could run counter to positive adjustment in the Japanese economy.

The difficulties of the distribution system for consumer goods are reinforced by the inability of foreign retailers to invest in the Japanese distribution sys-

tem. Not only is wholly-owned investment discouraged, but joint-ventures are also difficult both for retailers (as well as for manufacturers and distributors). Thus, investment is closely linked to trade, and the inability to invest results in far lessened ability to export to Japan, whether the product is a consumer good, or an industrial intermediate.

Lastly, there is the closeness of the various sectors of the Japanese economy, about which American businessmen, legislators, and negotiators speak with what must be viewed in Japan as paranoia. There is, nevertheless, in Japan, however, a distinctly Buy Japan policy, which is changing very slowly, and this change must accelerate if a protectionist reaction abroad is to be avoided.

Insofar as exports to the United States are concerned, the outlook for Japanese performance in this market is good. The exports of automobiles, which have been leading Japanese exports, remain very strong, selling at a premium. This is due to American demand. Exports of steel, which dropped by 28 percent compared with the first half of 1978, were slowed by the trigger price mechanism. However the average price of steel in the United States is increasing, and due to the depreciation of the yen and its effect on the trigger price mechanism, it is conceivable that an increase in steel tonnage imported from Japan could be seen in the latter part of this year and early next year.

In the new areas of competition, the experience of color television imports into this market could be repeated. The rapid expansion of the presence of color television exports to the United States was in part due to very keen competition among Japanese firms themselves to establish themselves in this market. This could be repeated with copying-machines and computers as well as other new products. The press stories about Japanese plans for this market are numerous in these products, particularly with respect to computers. At the same time there are press reports that MITI has terminated the "special surveillance products list" (automobiles, steel, ships, and television sets) as well as the "surveillance products list" (involving motorcycles, copiers, watches and cameras) which were designed to limit exports in the first case, and export growth in the latter case. I understand that this is not the case. Removal of guidance in favor of the Japanese Government monitoring export trends may not be effective in preventing the build-up of antagonisms caused by a sudden rush of exports as in the past.

#### CONCLUSION

The problems that afflict U.S. trade relations with Japan are not new nor are they easily resolved. An important start has been made in the Multilateral Trade Negotiations as well as in the bilateral negotiations that have been held in the last few years. The problems have not disappeared although they have been recently somewhat eclipsed by the (probably temporary) disappearance of the Japanese global surplus. The bilateral deficit with the United States remains quite large.

There are a variety of prescriptions to continue the process of achieving balance, in large part, through an opening of the Japanese market. While the focus of my remarks has been the problems U.S. exporters meet in the Japanese market, a more complete picture would require a review of the absolutely fundamental changes needed in this country. This has been the subject of the hearings before this Committee. For U.S. exporters to be competitive, the rate of inflation in the United States must be brought within reasonable limits. Productivity and the rate of innovation must be expanded substantially. U.S. export efforts must be increased dramatically. I have not given these points emphasis in these remarks because the context is particularly United States-Japanese trading relations, however, demand for United States exports will not increase abroad if we do not make early and significant progress in these areas.

Upon leaving the government I made a number of recommendations which, upon review, I still feel are very important to the preservation of long-term political and economic relations of the closest kind between the United States and Japan:

#### I. MTN IMPLEMENTATION

(1) Implement the MTN quickly and thoroughly. Other countries, including Japan, have no hesitancy in telling us how to write our legislation, we should have no reluctance to do the same for them. It is not enough for a country to say that a code will be adopted as domestic law. There are many provisions in the code which are not self-executing. The codes embody many common law

and administrative practice concepts that are not as familiar to other legal systems as they are to our own. These include transparency in administration, the opportunity to be heard, and the right to appeal. We must be sure that these are adopted abroad, both in Japan and elsewhere, both in letter and in spirit.

(2) Build a close relationship with U.S. exporters so that we know how the codes are being applied to individual transactions. A good start has been made in developing a close relationship between the Executive Branch and the private sector in the advisory process developed for the MTN. This should be adapted for use in the post-MTN period. Close Congressional consultations with the Committees of Congress having a direct interest in the implementation of the MTN should also be improved.

(3) The United States Government should be quick and firm in taking action should there be any shortfalls in implementation. The United States Government should make it widely known that it will take up cases and invoke the dispute settlement procedures in the codes. But also, that we will respect the rules ourselves, and only bring legitimate cases—not bringing cases because our Government is unwilling to tell any powerful interest group in this country that it does not have a valid case.

(4) Private interests should be told that section 301 of the Trade Act is meant to be used. The amendments in section 301 in the implementing legislation are a powerful tool for private parties to make the international rules work. Private parties must, however, use discretion in bringing cases, and try to avoid using the procedures as harassment rather than as a legitimate means to obtain legitimate ends. Unfortunately, Americans have a world-wide reputation of being litigious. It would be very unfortunate if the code procedures broke down through excessive and inappropriate use of the dispute settlement process. What is required is that case law be built, that the codes be flushed out and given additional meaning.

Cases should not be allowed to become foreign policy issues. It may be that cases generate hostility, but in my experience reluctance to press U.S. interests at an early stage allows political pressures to be built up which make the settlement of issues ultimately more difficult. The U.S. trade agreements program operates well only if it has a broad domestic constituency. This was demonstrated very clearly when the Trade Act passed by an overwhelming margin in both the House and the Senate a few months ago.

## II. U.S. GOVERNMENT ORGANIZATION

(1) We must reorganize the Executive Branch quickly and effectively so that it can carry out an active implementation policy. The President's Plan deserves prompt support and should be put into place quickly. It is not that anyone who has given a good deal of thought to the trade area could not come up with a different plan which he would no doubt think would be better, but there is no consensus beyond that represented by the President's Plan. It should be adopted in the very early future. It will help assure that trade policy is articulated through one person in the United States Government (the U.S. Trade Representative). It will make substantial progress toward assuring that a maximum effort is made at interagency coordination of policies that affect our trade interests. It will consolidate a number of the trade functions of the government. It will strengthen the analytical abilities of the Commerce Department.

The President's Plan does increase foreign representation of our commercial interests abroad, and hopefully make it more effective through the transfer of the Commercial Officer positions from the Department of State to the Department of Commerce. I would hope that this will evolve into a career U.S. Commercial Service which will be able to work hand-in-hand with businessmen in bringing down foreign barriers abroad.

The plan is as yet silent on what will be done where a more effective presence is needed in foreign capitals. We happen to have a number of superb foreign service officers representing U.S. commercial interests abroad. One of the finest, has recently been posted to Tokyo. That blunts one of my suggestions which is to establish a strong and able presence in major foreign capitals to advance the commercial interests as well as the foreign policy interests of the United States. It is nevertheless my feeling that in Tokyo a more substantial U.S. Government effort concerned with our trade interests is needed. It could be in the form of additional resources provided to the Economic Minister of the U.S. Embassy. The problems are so large, and so many, that I feel that additional resources

are warranted. I am going to Tokyo as well as number of other capitals in the Far East early next week, and I would be happy to supplement these views for the record after being able to talk to our people in the field directly after gaining a current assessment.

(2) We must also greatly improve the administration of our unfair practice remedies. It is one thing to make the remedies faster, this can be an improvement for both foreign exporter and U.S. producer alike. However, the administration of the unfair trade practice laws must be more than prompt, they must be administered with reason and intelligence. By and large, American producers do not seek the exclusion of foreign competition from the American market, and what is so often labeled "protectionism" is simply a desire to avoid the excesses of competition that are in fact unfair.

### III. U.S. POLICIES AFFECTING EXPORTS

There are a wide variety of steps that can be taken to assist, or not to hinder, U.S. exports to Japan as well as to other markets.

(a) Make sure that our tax and antitrust laws as well as other potential export disincentives, do not unnecessarily impede exports. For example, the creation of U.S. trading companies (particularly to represent smaller businesses) should be explored.

(b) Adopt domestic economic and tax policies that foster an increase in productivity, an increase in research and development to maintain our technological edge, and reduce the rate of inflation so that price competitiveness is enhanced.

(c) We should be training Japanese area specialists who are also businessmen. Ambassador Mansfield has suggested the earmarking of profits for sponsoring internships for U.S. business executives in Japan. Congressman Sam Gibbons has suggested that the government underwrite or at least encourage business schools in this country to have area and language studies that concentrate particularly on Japan. Clearly we need a substantially increased body of American business representatives in Tokyo who speak Japanese and understand that market.

(d) We must continue to welcome Japanese investment in the United States for new manufacturing facilities which can contribute importantly both politically and economically to our bilateral relations.

### IV. JAPANESE GOVERNMENT POLICIES

There are a number of policies that have been addressed above. In particular, attention should be addressed to:

(a) Fostering changes in the distribution system to remove current barriers to the flow of imports into Japan; e.g. by allowing the free expansion of chain stores, including those owned by foreigners, and acquisitions of existing Japanese enterprises, as other countries do.

(b) Eliminating the protectionist policies of government-owned monopoly enterprises.

(c) Further elimination of unnecessary standards and product testing as barriers to trade.

(d) Avoiding the temptation to protect declining basic industries against increased import competition, primarily from developing countries.

(e) Discouraging the close relationship between Japanese businesses that tends to exclude import competition.

The above suggestions, to which others on this Committee could easily add a substantial number of additional ideas, are steps that I feel should be explored now and implemented as soon as possible. The current turn-around in the Japanese global balance of payments figures may provide a breathing space. But it should be used effectively. Fears of the oil-related Japanese deficit may too easily result in a shift in policy away from the trend toward openness and bring a return to a more defensive, protectionist posture. The danger is sufficiently real that every effort should be made to reinforce the progress that has been made, rather than waiting for the next resurgence of economic friction which may not be so readily managed the next time.

Senator BENTSEN. Mr. Wolff, I strongly share your deep concern about the growing complacency with regard to trade relations between the United States and Japan. I believe we got where we are in bringing about some improvement by some very tough negotiations. And you

and Ambassador Strauss did a very good job. The Japanese are very able negotiators.

I was one of those that chose to play the role of heavy in those negotiations. I know when I was in Geneva, I was again playing the role of the heavy. I brought up to the Brazilian negotiator that Bob Strauss had to go back and deal with those Senators who are so tough on trade. He said, "Well, Bob Strauss uses that argument very often. But I answer him by telling him that, 'When you have to go back and deal with Senators, that doesn't really impress me; I have to go back and deal with generals.'" [Laughter.]

But I for one will continue to do all I can to see that we work toward continued improvement in that relationship with Japan. It's very important to all of us.

Ms. Hadley, one of my staff, has come quickly to my defense on the numbers I've used insofar as to state productivity per man-hour. My staff cites numbers prepared by the Bureau of Labor Statistics for Japan and the United States. And they've been collecting these numbers, they tell me, for 15 years.

Now, to make you feel better, let me also say that they call it unpublished data. I don't know how they do that, when they've published it this way. [Laughter.]

I understand the semantics of it. But they must not be very confident of their numbers when they say unpublished.

Ms. HADLEY. That may be. I was talking with one of the persons in the compiling unit who had made this statement to me, because we likewise had sought them.<sup>1</sup>

Senator BENTSEN. Our next witness is Mr. H. William Tanaka, who is a partner in the law firm of Tanaka, Walders & Ritger, in Washington.

Mr. Tanaka, we are very pleased to have you. If you will proceed, sir.

#### **STATEMENT OF H. WILLIAM TANAKA, PARTNER, LAW FIRM OF TANAKA, WALDERS & RITGER, WASHINGTON, D.C.**

Mr. TANAKA. Thank you, Mr. Chairman. I am certainly pleased and honored to be invited by this committee to testify on a very important and timely subject.

My statement touches on various aspects of the four types of constraints which have prevented the U.S. export performance from achieving its full potential: Economic and business constraints, technology constraints, national policy and legal constraints, and sociological constraints.

This committee is familiar with the kinds of economic and business constraints I have in mind: The decline in our productivity growth and in the price competitiveness of American goods, the cost of complying with regulatory burdens, the quality control problems, the mixed export blessings of multinational corporations.

Technological constraints begin with the fact that our Government support for research and development has been channeled principally

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<sup>1</sup> Reference was to industry comparisons, not the economy as a whole. Iron and steel is the only industry for which BLS produces comparative statistics.

into space and defense industries, not those manufacturing commercial products having export potential.

Many private industries have been slow to develop or incorporate advanced technology. The preference and need for smaller cars have been visible for years, but Detroit, content with large profits on large cars, has only recently acknowledged them.

National policies and laws also hamper our exports. Concern over national security, with such matters as fixed exchange rates and anti-trust considerations, and more recently communism, foreign boycotts, bribery, immigration policy, human rights, terrorism, nuclear proliferation, environmental degradation, and racial policies, have all found expression in ways adversely affecting our exports. These policies have not been counterbalanced by either coherent national export policies or policies designed to keep this country in the forefront of technological progress.

Certainly my own experience with our import-related antidumping and countervailing duty laws convinces me that their mechanical application of a static injury criterion serves to keep alive low technology industries and distorts investment and resource allocation decisions to our disadvantage.

The sociological constraints on our exports, in many cases, represent orientations and types of behavior endemic to the free enterprise system in America. The adversarial relationship between labor and management in this country harms exports. The participative and consensual relationship in Japan favors them. Management indifference toward exporting further depresses exports. With our huge and diversified home market, Americans have often found neither rewards for exporting nor penalties for failing to do so. The short-term bottom-line orientation of our corporate managers make it difficult for them to subordinate near-term gains to the long-term planning and investment necessary for successful export performance.

These attitudes are particularly relevant to the problems faced by U.S. exporters seeking to enter the Japanese market. As with any foreign market, management must be prepared to make substantial investments of money and management time. This is especially true in a country as different from our own in language and culture as Japan.

Setting up a distribution system is difficult in a country where a large number of middlemen handle a small volume of business for a limited territory.

Products must be especially designed to meet Japanese tastes. Labels and pamphlets must be in Japanese. Adequate support must be committed. Most of all, we must have the patience and persistence which the Japanese have demonstrated in developing our own market for their products.

Mr. Chairman, you have asked my comments on four matters relating to Japanese Government policies and practices as they relate to imports into that country. I should note at the outset that my experience principally involves Japanese exports to the United States, rather than the other way around. Most of my practice has been concerned with U.S. laws and policies as they affect Japanese business.

As my prepared statement indicates, I have also had occasion to consider how laws and policies, as well as our attitudes and traditions, affect U.S. exports.

Although I can, therefore, claim no expertise in those matters which you have suggested for comment, all of which involve Japanese Government policies toward imports, I can offer a few relatively informed comments.

Your letter of October 3 poses the question: To what extent will the past pattern of Japanese protectionism create problems for the United States?

I would say that Japan has made substantial progress over the past decade in opening up its markets to foreign competition, including particularly products from the United States. In fact, during the recent MTN negotiations I think that our negotiators have stated that the Japanese have been much more forthcoming than the Europeans.

For a number of years Japan has also been instituting unilateral tariff reductions and other unilateral actions to eliminate certain of the administrative and other nontariff burdens imposed on imports.

As for the future, Japan is a dynamic market in which companies with new products, well-designed to Japanese tastes, can be successful. But American companies must be interested in trying to sell that market, to take advantage of the openings achieved in the recent MTN agreements. If U.S. companies persist in their past habits; namely, of lackadaisical export efforts and a tendency to invest abroad to serve the foreign market, we obviously will make little export progress.

Your second question asks: As opposed to tariffs or explicit quotas, how important are administrative rulings or indirect Government pressure in restricting access to the Japanese market?

Mr. Chairman, this is the kind of comparative analysis which my background has not equipped me to make with any real competence. But I wish to note that the resistive quality to imports is inherent in the type of an economy which a country has.

One would start with perhaps the Communist countries, which have the most highly planned economies of any countries in the world, which are most resistant to imports. Then you have countries like Japan, which are basically democratically oriented with a generally free enterprise system but nevertheless are relatively more highly planned than the American economy which still adheres, in large part, to the free enterprise system and the thought that government interference is essentially evil.

Senator BENTSEN. Mr. Tanaka, if you'd forgive me, I just have to leave. Senator Jepsen will be presiding, and I appreciate the candor of your statement.

I would like to submit some questions to each of you to be responded to in writing.

Senator JEPSEN [presiding]. Please continue.

Mr. TANAKA. Thank you.

I was saying that the Japanese economy, basically, is a relatively highly planned economy and, to the extent that it is, it tends inherently to be more resistant to import penetration.

Third, you have asked: How does Japan select and foster key industries, and what will these practices mean in terms of future trade problems?

I think that any government's policies, in determining which industries to foster, which industries to disinvest from, is determined largely



in terms of the institutional setting and the economic circumstances in which that country finds itself.

In the case of Japan, as we all know, the country is almost totally lacking in domestic energy sources and mineral resources, and is substantially dependent upon imported food. Accordingly, the Japanese Government selects as key industries those with growth potential which are resource efficient, energy efficient and nonpolluting, and which essentially do not require any substantial future indebtedness to imported energy and mineral resources. This contrasts with the United States, where raw materials and energy resources until recently were bountiful.

Finally, you have asked for my comments on continuing United States-Japan negotiations on allowing foreign firms to bid on NTT contracts.

First, to put this question in proper perspective, I would like to call the committee's attention to the Comptroller General's report of September 30, 1976, entitled "Governmental Buy-National Practices of the United States and Other Countries; An Assessment." The report indicates that in the case of the United States, based on a survey of procurement of six Federal Government agencies covering the year 1974, out of \$44.6 billion of sales, only \$1.3 billion was viewed as open to competition, both from domestic and foreign sources. I think that this indicates that our Government, as well as all other governments, tend, for various national policy objectives, to favor the domestic industry to imports.

Certainly there are a number of reasons why domestic industries should be favored over foreign industries; some of them are the fact of geographical proximity, the absence of a language barrier, the ability to closely coordinate supplies and manufacturing procedures. And these are some of the things which tend to cause all governments to favor their domestic sources.

As far as the NTT problem is concerned, I think this has to be viewed as merely a stage in the process of establishing acceptable limits to government procurement restrictions, that is, buy-national restrictions. I think that in the future these issues will probably be raised with respect to other countries. As far as the United States is concerned, we must examine our buy-national policies to determine the extent to which these restrictions and shelters can be eliminated on a reciprocal basis.

Thank you.

[The prepared statement of Mr. Tanaka follows:]

PREPARED STATEMENT OF H. WILLIAM TANAKA

Mr. Chairman, I am William Tanaka, a member of the Washington law firm of Tanaka, Walders & Ritger. Our firm has practiced principally in the area of international trade. This statement is submitted in response to the committee's invitation. The views expressed are my own and do not necessarily represent the opinion or positions of the firm or any of its clients.<sup>1</sup>

I am pleased to be able to present today my views on U.S. export performance and some of the domestic factors which influence that performance.

Our export record is, of course, impressive in an absolute sense. By a small margin, the United States is the world's largest exporter. Yet, we have also been

<sup>1</sup> I am registered with the Department of Justice as an agent of a number of foreign principals.

described as the world's most reluctant exporter. Relatively speaking—as a percentage of our GNP, for example—our export performance lags behind that of other developed countries. And in recent years our exports have not risen nearly fast enough to balance our surging import costs. As a result, we have accumulated massive trade deficits. These, in turn, have been major contributors to undermining the value of the dollar.

Much of the blame for the recent trade deficits must be charged to a growing volume of petroleum imports at ever rising prices. Last year alone imported oil cost us \$39.1 billion. But solving the energy problem and putting a cap on Petroleum imports is only part of what is needed to put the dollar on a sound basis. The other essential ingredient is a national export policy, supported by fundamental changes in the attitudes that have kept exports low on our list of national priorities.

The huge U.S. trade deficits have at least served to broaden official and private sector interest in expanding our export trade. This interest comes at a fortuitous time. With the conclusion of the Tokyo Round of the Multilateral Trade Negotiations, new opportunities to export have been opened up to Americans. If we are to take advantage of them, we shall have to overcome a number of factors which have constrained our exports in the past, and which to a large extent continue to do so.

The subject is not one that can be simplified to one or two basic issues. The roots of the problem can in some cases be traced to fundamental and pervasive aspects of our society—to value orientations and to perceptual, social, legal and organizational characteristics. That our country was built on the notion of an ever-expanding frontier and grew to be the world's largest single market are facts which are relevant not only economically but psychologically.

Moreover, forces which by themselves might not significantly inhibit exports have coalesced to form a sizable internal barrier to exports. These forces fall into four major categories that I will elaborate on: Economic and business constraints, technology constraints, national policy constraints and sociological constraints.

#### ECONOMIC AND BUSINESS CONSTRAINTS

Turning first to economic and business matters, it is noteworthy that, except for certain industrial goods and high technology products, an increasing number of American manufactured goods are not competitive in foreign markets. Until the mid-1950's, American goods in general were exported with great success. The subsequent erosion of American firms' ability to compete abroad was not entirely due to traditional business factors such as costs of labor and capital or productivity problems. To the ordinary costs of production were added the costs of complying with ever-increasing governmental regulation, a burden not likely soon to abate. The quality of American products relative to the competition declined. The overvaluation of the dollar made the price of American consumer goods less attractive. Multinational corporations (MNC's) based in the United States built production facilities abroad rather than increasing domestic production to meet the foreign market demand. I will touch on each of these factors in turn.

#### PRODUCTIVITY

Without doubt, growth in the productivity of U.S. labor has slowed. Neoclassical economic theory attributes this to four causes:

First, the ratio of capital to labor hours normally increases in a productive economy. This rate of increase has been slowing, due both to rapid growth in the labor force and only modest growth of savings and capital formation.

Second, the labor force is becoming demographically unfavorable. More young workers are entering, more old workers are retiring, and there is high turnover even among young workers. The average level of experience in the work force has therefore suffered a real decline.

Third, the movement of labor from agriculture into industry has fallen off. In the past this shift of workers out of low-skilled seasonal work has helped boost national productivity rates.

Fourth, the rate of development of new technology, has declined, affecting the efficiency with which capital combines with labor to produce output. One cause is the decline, in real terms, in spending on research and development.

Other economic theories suggest different causes for the productivity decline—our large, economically-wasteful military sector, alienation of U.S. workers,

inevitable "limits to growth", deviation from free-enterprise precepts. But whatever the cause, one might expect a decline in productivity to be accomplished by an increase in unit labor costs—that is, labor costs per unit of output. Unit labor costs are significant not only for their relatively direct impact on final product prices. Over the long term, if real unit labor costs are higher in the U.S. than abroad, U.S. capital will tend to flow to other countries and thereby impair the quality of U.S. capital stock, accelerate the decline in productivity growth, and reduce export competitiveness. In fact, however, during the 1970's unit labor costs have risen more slowly in the United States than in any of the other principal industrialized nations, which of course started from a lower base. Therefore, although U.S. unit labor costs have risen absolutely, they have not been a negative factor in our export performance.

#### PRICE COMPETITIVENESS

The deterioration of the U.S. trade position since the mid-1960's has reflected, to a considerable degree, an erosion of price competitiveness. The origin of the decline is attributable to the relatively high rates of inflation in the U.S. and, in the early years, an increasingly overvalued dollar in a fixed exchange rate environment. The dollar devaluations in 1971 and 1973 eased the latter problem somewhat. U.S. export price competitiveness was improved substantially, and in 1973 and 1974 U.S. exports made sharp gains. These were largely reversed in 1974 and 1975 as currency appreciation and higher inflation raised the prices of U.S. exports relative to those of its major trading partners. The U.S. balance of trade subsequently deteriorated, at least in part due to price considerations.

The depreciation of the dollar beginning in 1977, although worrisome in some aspects, helped to counteract the slide in price competitiveness and tended to ameliorate the trade deficit. The relatively favorable state of the dollar today makes this an opportune moment to undertake new efforts to expand our exports.

Next to exchange rate relationships, relative inflation rates are perhaps the most important determinants of price competitiveness. A significant element in domestic inflation is the incremental costs to business of complying with various forms of government regulation. These costs, estimated at between \$50 and \$150 billion annually, are of course reflected in increased prices to both domestic consumers and foreign buyers.

Price competitiveness, while important, is not the only determinant in the overall competitiveness of American goods. Non-price factors such as market familiarity, salesmanship, reliable delivery, product quality and suitability to local tastes, after-sales service and credit terms have a crucial effect on the U.S. exporter's ability to exploit a relative price advantage. Deficiencies in these areas probably account for much of the recent U.S. failure to surpass Japan in the growth rate of its exports to the European Community and Middle East export markets, despite price and exchange rate movements that substantially benefited the U.S. relative to Japan. United States exporters will have to improve their performance in these non-price areas if they are to maintain and increase their share of export markets.

#### QUALITY

A first order of business in this regard must be quality and quality control. In recent years, the U.S. has been losing export markets to competition from abroad, particularly from Japan. In many cases this has been due to the inferior quality of the U.S. product. Today Japan sets the standard for quality and reliability in many products and markets. However, in some of the markets hardest hit by Japanese imports, U.S. corporations have instituted quality management programs that are starting to show results.

The Japanese emphasis on quality has been an integral part of Japan's national strategy to build an export economy, not just a company-by-company decision. The strategy began with a massive training program at all levels, amounting to indoctrination in quality control. Ironically, many of the concepts in quality control came from the United States, where Japan turned for help.

Other countries have decided to emulate the Japanese. For example, Taiwan, Argentina and Brazil either have or are developing plans whereby plants are graded according to quality and assessed a tax if quality drops.

Catching up in the quality area is essential if we are to improve our export performance. Some U.S. corporate managers seem to think this is an impossible task. They have expressed the belief that U.S. workers are inherently different

from the Japanese, who are described as dedicated, industrious and loyal as a result of their culture and traditions. This belief has been debunked by the experience of Sony and other Japanese firms establishing manufacturing facilities in the U.S. In 1972 Sony built a TV plant near San Diego, California. That plant now holds Sonys' world-wide record for quality of 200 days of production without a major defect. In addition, studies of defects and their causes have shown that over 80 percent are correctible only by management—design changes, for example—and not by workers.

The difference between the American and Japanese management approach to quality has been aptly expressed by ITT Vice President for Quality Philip Crosby, who instituted at ITT a highly successful program with "zero defects" as a goal. He said: "Every Japanese manager is long-range, defect-prevention oriented. American management is short-range, defect-detection oriented." Crosby has also noted that ITT makes the same product in many parts of the world. "Without exception", he says, "we find that the best workmanship, the best worker attitudes are here in the U.S."

#### MULTI-NATIONAL CORPORATIONS

Mr. Crosby's comments highlight the critical role in exports of multi-national corporations such as ITT. Their presence cuts both ways. Though they account for about 85 percent of all U.S. exports, their enormous investment in overseas production limits the export markets they are willing to enter, and has preempted others. The basic aim of MNC's is anational, that is, to maximize world profits. They export from the U.S. only if that will better serve this goal, not from patriotic or idealistic motives. In short, they heed practical incentives, not exhortations.

At the same time, MNC's do have well-established export networks and are in the best position to exploit the new price competitiveness. Moreover, their overseas plants buy many U.S. goods. The greatest part of MNC exports consists of intracompany transfers of products.

The MNC's because of their large overseas production capacity, in many cases source foreign markets from abroad and use domestic production for the home market. General Motors exports only 4 percent of domestic production, meeting foreign demand from overseas plants. This is in contrast to Japanese automobile manufacturers, who until recently had virtually no production facilities outside Japan to service their worldwide sales.

Foreign governments have come to rely upon the plants of U.S. MNC's within their borders to provide, among other things, a healthy level of exports. Consequently these governments press for continued local production, increasingly requiring that this be accompanied by an influx of technology so that local production may ultimately replace imports entirely. These pressures have distorted the ability of the MNC's to make "pure" marketing decisions, sometimes causing them to refrain from sourcing from the U.S. even where it would be cheaper to do so.

#### TECHNOLOGY CONSTRAINTS

Technological constraints can also hamper exports. The technological pre-eminence of the United States in the areas of space and defense is renowned and virtually unchallenged. In the commercial and industrial applications of technology, however, we are losing our leadership in certain product areas important to our economy. Significant technological gains by other industrial countries have given rise to fears that the future viability of the American economy may be in jeopardy.

During the Cold War, most U.S. research and development was directed to space, which in recent years has suffered a drastic cutback in funding, and to defense. Meanwhile most other countries directed their R & D toward commercial products and adaptation of imported technology.

Until around 1970, the overall U.S. trade balance reflected a persistent surplus, led by aggressive export performance of high technology industries that were largely by-products of this country's DOD- and NASA-funded R & D push. Between 1963 and 1969, the aggregate trade surplus of technology-intensive industries rose from \$7.7 billion to \$11.1 billion. But problems were mounting in exports of other manufactured goods. A trade deficit in these goods of \$1.0 billion in 1963 increased sharply to \$7.5 billion in 1969. Early in this decade the U.S. trade balance began to suffer substantial deficits, despite continued excellent performance by high-technology exports.

These changes reflect in part the inevitable consequences of development abroad. But regardless of their cause, the changes highlight the need for our government to play a positive role in fostering non-inflationary economic growth through renewed funding and promotion of R & D efforts more directly focused on incremental commercial and industrial technology. If justification for government intervention be needed, it can be found in the fact that compliance with growing safety and environmental regulations, imposed by the government, has adversely affected productivity and increased costs, at the same time that federal R & D funding was being cut back.

Two characteristics distinguish the R. & D. effort and environment in the United States from that of most of the industrial countries. While the U.S. concentrates on space and defense, Japan, for example, focuses its national R. & D. spending on commercial applications of known technology. Second, in the United States there is no national policy fostering joint government-industry R. & D. In our country, as in the United Kingdom, the relationship between government, academia and industry is fundamentally adversarial, often characterized by hostility and competitive distrust. In contrast, Japanese industry and government have been more successful in working together in consensual collaboration and joint endeavors. These factors may be at least partly responsible for the competitive advantage of many Japanese goods.

#### AUTOMOTIVE INDUSTRY CASE

Thus, empirical evidence suggests a link between U.S. R. & D. practices, our productivity and our trade performance. The automotive industry provides a good example of this.

The American automotive industry, though the largest in the world, has not been in the forefront of technological innovation for at least the last 25 years. Typically, American auto executives have followed a marketing policy of creating "planned obsolescence" through annual model changes. Rather than innovation, U.S. auto makers have been concerned mainly with selling style, comfort and status. What improvements have taken place have largely been from the use of off-the-shelf, existing technology. The major impetus to fundamental change in U.S. automotive design and construction has been federal regulation. The need to down-size cars for better fuel efficiency and handling has been recognized for years, but Detroit has only recently begun to manufacture its own small cars.

Resistance to entering the small car market is attributable to one obvious fact—large cars are far more profitable to build than small cars. Fixed investments in plant and machinery, advertising expenses and labor costs do not vary substantially for a sub-compact and a standard-size car. Raw material costs do not vary more than about \$500. Yet the standard-size car sells for as much as several thousand dollars more than the sub-compact. The result for years was huge profits, well above the U.S. average for manufacturing companies. American industry has been reluctant, however, to reinvest an adequate proportion of these profits to improve its product or manufacturing technology.

Contrary to popular myth the U.S. automotive industry's failure to compete with imports has little to do with the high hourly wages paid American workers. According to one analyst foreign manufacturers sell cars more cheaply because of their high level of productivity, and because they accept smaller profits than American corporations. General Motors' profit on each vehicle it produces is about three times that of its foreign competitors.

In fact, the evidence shows that were it not for the federal mandate on average mileage of the domestically-produced fleet, U.S. producers might well have imported all or almost all of their requirements of compact and sub-compact cars. It is thus clear that until now the domestic producers have had no serious plans to export their domestically-made small cars. A lack of desire to export therefore seems to be a larger factor in the adverse net U.S. trade balance in cars than foreign import barriers.

#### NATIONAL POLICY AND LEGAL CONSTRAINTS

Our exports are further inhibited by policy and legal constraints. The United States has no national export policy. With our vast resources and huge home market, until recently we had no pressing need to export, either as individual companies or as a nation. Most other industrial countries, on the other hand, have had to export to live. The Japanese, in particular, have inadequate food supplies and virtually no energy or raw materials, and so must import virtually every-

thing an industrialized nation depends on. Early on they realized that to pay for this would require a national effort by both industry and government to fill their own needs for manufactured goods and at the same time to develop exports.

The United States is, it seems, at last coming to a similar realization, spurred by our need to import much of our oil, and by our choice to import many of our consumer goods.

Although lacking an export policy, the United States has had an international economic policy since World War II. Unfortunately, some of its aspects have served as disincentives to a thriving U.S. export trade. Under the fixed-exchange rate system instituted at Bretton Woods, under our leadership, the U.S. dollar became overvalued. U.S. firms invested in new plants overseas, rather than modernizing or expanding existing facilities at home, since foreign assets cost fewer dollars than comparable assets here.

When the U.S. finally ended dollar-to-gold convertibility, and other nations allowed their currency to float against the dollar, the value of the dollar began to seek more realistic levels. This should have stimulated exports, but the response was not as dramatic as might have been expected. One reason is that the major types of exports of the United States—capital goods, industrial supplies and agricultural products—are price inelastic. Sales levels are governed largely by non-price factors such as the state of the business cycle, quality of workmanship, availability of service, reliability of delivery, etc. Moreover, some of the major U.S. export markets are not responsive to the apparent price advantages which accompany a decline of the dollar against major foreign currencies such as the mark, the franc or the yen. Almost half of all U.S. exports go to Canada and the developing nations, whose currency values closely follow the dollar.

Formulation of a constructive and coherent international economic policy is hindered by a fragmentation of policy-making authority. The United States, alone among the major trading countries, has no single government agency responsible for advancing its foreign trade. Other countries rely on trade ministries to help their exporters probe markets abroad, develop new export products, coordinate export bidding, arrange subsidized financing, insurance, and shipping and bargain with foreign governments to insure market access. The plan for the reorganization of trade responsibilities proposed by the Administration falls considerably short of the export support structure available to our principal competitors.

Once again, the Japan experience and government organization provide an interesting contrast. The undervalued yen for years served both as a disincentive to Japanese investment in manufacturing facilities abroad and as an incentive to development of foreign markets by their exports. Moreover, the Japanese Ministry for International Trade and Investment has provided coordinated support to Japanese corporations in marketing their products abroad.

#### LEGAL CONSTRAINTS

Ironically, at a time when other governments provide positive incentives to exports, we find numerous instances in which our own government imposes restrictions on or disincentives to U.S. exports. Each of these self-imposed market foreclosures should be reexamined to determine whether the policy sought to be promoted still outweighs our compelling need for an aggressive export policy.

The Export-Import Bank is our principal government instrumentality for the promotion of exports. Although the present management of the Bank has adopted policies to provide aggressive financial support to our exporters, these policies must operate within the confining limits imposed by Congress. The Bank's statutory charter has become encumbered with restrictions relating to financing trade with Communist countries, Rhodesia and South Africa, and to such diverse considerations as human rights, international terrorism, nuclear proliferation and environmental degradation. The export credit agencies of our chief competitors do not suffer under such limitations.

The Jackson-Vanik Amendment to the Trade Act of 1974 is a singular example of how extraneous considerations are made to intrude in Eximbank's export financing, as well as in other trade matters. It is hard to make a rational connection between a foreign nation's emigration policy, on the one hand, and, on the other, Eximbank financial support for our exports to it, or most-favored-nation for that country's goods destined for the U.S. Yet, under Jackson-Vanik, we penalize our own exports if a foreign country's emigration policies are not to our liking.

The complete ban on exports to Cuba, to China, and to other countries which have been imposed in the past three decades under the Trading With the Enemy

Act have cost us heavily in exports lost to other. Before the trade embargo with Cuba, two-way trade was over \$1 billion annually. The cumulative loss of exports to Cuba during the 17-year ban has been at least \$5 billion. In the absence of the ban, the U.S. could easily sell \$300 million worth of goods to Cuba every year. Yet it is difficult to see what positive results have been achieved by these abdications of markets.

Similarly, while some form of national security export controls such as are provided by the Export Administration Act and the munitions control legislation are essential, there is room to question the effectiveness of the administration of those laws. Of particular concern is the cost in lost U.S. exports—especially in cases where similar technology is sold to the potential customer by one of our allies—compared to the extent to which we have in fact succeeded in restricting the delivery of western technology to the Soviet Union and its satellites.

There are also valid policy reasons and wide public support for the recently-enacted anti-boycott and anti-bribery laws. But I know of no foreign exporters who are subject to similar restraints on their ability to exploit export possibilities.

Much the same is true regarding exports of nuclear plants. While we in the United States may feel growing apprehensions about reliance on nuclear power, many other countries regard this as luxury they cannot afford. The restrictions we place on such exports are not always well adapted to a competitive world.

Even our cargo preference laws, designed in part to promote the export of shipping services, can cost us exports of goods and, with them, related services. For example, the Russians are currently required to ship at least one-quarter of their commercial grain purchases on U.S. flag vessels. This makes U.S. grain the most expensive in the world for the Russians, because U.S. flag rates range two to three times higher than comparable non-U.S. flat rates.

There is considerable debate today over whether our antitrust laws inhibit U.S. exports, and particularly whether antitrust rules prevent American businessmen from teaming up to bid on major foreign projects in competition with powerful, government-backed European and other foreign consortia.

I have already mentioned the direct impact on our exports of government regulation in various areas. The costs of compliance with environmental, safety, energy, food and drug, antitrust, and other forms of regulation add not only to the price of particular export products. They permeate our entire economy and fuel economy-wide inflation. The competitiveness of our exports is impaired, imports are sucked in, and our trade balance suffers.

Excessive regulation also inhibits investment in new technology and product innovation. It lowers productivity and diverts capital to non-productive ends.

Finally, I would note the indirect effect on U.S. export performance of our laws to protect U.S. industry from certain types of foreign competition. The recent amendments to our antidumping and countervailing duty laws perpetuate the concept that any domestic industry which can show injury from imports is worthy of protection. In practice, this involves application of a static criterion which serves to keep alive low-technology, labor-intensive industries and allows many high-cost, inefficient producers to survive. The process of disinvestment and reallocation of resources to the higher end of the technology scale is retarded. Our economy is weakened, and saddled with an inflationary bias. Once more, our exports suffer.

The contrast with Japan is again striking. The Japanese Government plans the nation's industrial policy years ahead in an effort to promote leading-edge technologies. Growth industries are selected for promotion. Moreover, when the United States seeks to restrict Japanese imports by orderly marketing agreements or other devices, in low or medium technology fields such as steel, or, today, even TV sets, the Japanese Government goes along relatively gracefully. Why? Because in its long-range planning it realizes that production in industries at the lower end of the technological spectrum will in any case have to be ceded to developing countries if Japan is to sustain a dynamic economy.

In short, our laws, being indiscriminating in the industries they protect, end up protecting those which are a drag on our economy. Meanwhile, the Japanese are consciously discriminating in favor of industries which will promote domestic economic growth and vitality.

#### SOCIOLOGICAL CONSTRAINTS

The policy and legal constraints I have been talking about largely represent conscious national choices, or a balancing of choices. If we have the will, the choices or the balance can be changed. I would like to turn now to some socio-

logical constraints on exports which are not only more difficult to analyze but will prove more resistant to change.

I am referring principally to certain orientations and patterns of behavior which are endemic to the free enterprise system in America. I will only mention in passing the debate over whether there have been changes in the American work ethics that have affected productivity. Certainly many workers are dissatisfied with their jobs, and some of this no doubt results from changing values regarding work. Sometimes this dissatisfaction is expressed through reduced productivity, degraded quality of work, and even pilferage and sabotage. Interesting programs to increase worker motivation are being tried by a number of companies, some of which show considerable promise.

To the extent that negative attitudes exist, I am persuaded that much of the blame can be traced to the nature and quality of the relationship between labor and management. In the United States, too often this relationship is a corrosively hostile adversarial one. This is in sharp contrast to the fundamentally consensual and synergistic perception of labor-management relations characteristic of Japan. I will cite just a few examples of the differences between the two systems:

In Japan, wages are negotiated by unions within a single company, rather than by industry-wide unions. Yet the union's power is not significantly less, because it has access to information on the results of negotiations in other firms.

The typical Japanese worker stays with one company during his entire working career. His job is secure, even during production cutbacks. This gives him a greater interest in the long-range vitality of his company, which is often expressed in a greater degree of worker participation in management decision-making.

Japanese labor willingly embraces new technology rather than resisting its introduction, and management retrains its existing work force as necessary. The resistance of American unions to new technology, based largely on the threat to job seniority and employment security, causes American management to delay implementation of technological improvements.

The factors just cited give Japanese companies a relatively high average level of worker experience and maximizes benefits of the learning curve.

Finally, while in America a strike often leads to a complete shutdown of the business, during the infrequent Japanese strike the union will usually keep some workers on the job so that the company can meet at least part of its production schedule.

These differences, which to a large extent spring from deeply-ingrained cultural distinctions, tend to affect adversely the relative productivity, product quality and export competitiveness of American industry.

#### AMERICAN BUSINESS ATTITUDES TOWARD EXPORTS

As I noted earlier, the specific attitude toward exporting of American business as a group has also been shaped by cultural factors—more specifically, by our geography and abundant natural resources. American industry enjoys the world's largest and most diversified home market. At least until very recently, there has been simply no need to export in order to have growing sales. Export markets have been widely perceived as marginal business, laden with risks, worth cultivating only when business turns down at home. Company personnel responsible for exports have been given low status within the organization.

Most of today's business leaders grew up and received their education in an era in which these attitudes were pervasive. Even today, the leading business schools are discovering they are neglecting the international side of business education. The advantages and methodology of exporting simply are not being taught to businessmen. And the American public in general is not absorbing the day-to-day effect a trade deficit can have on their lives—the fact that, according to Charles Schultze, for every 10 percent decline in the value of the dollar, the Consumer Price Index rises up to 1½ percent.

The ingrained "short-term, bottom-line" thinking of corporate America limits the willingness of management to make the substantial investments an all-out export effort often entails. The managers are accountable every quarter to the shareholders, who demand constantly rising numbers. Exacerbating the problem is the rise in stock ownership by institutions whose investment criteria demand short-term profits, successive bottom-line increases and high earnings ratios. Long-term planning by American corporate management, an essential ingredient of solid export performance, is made more difficult.



The question we must answer is whether, given these attitudinal problems, the pressures pushing individual companies to export will be strong enough, as they have been with our competition, to overcome the perceived obstacles to exporting. It is true that the up-front expense of entering any foreign market is considerable. Not only money but large blocks of management time are required. Setting up a distribution system is costly, particularly if Japan is the target market. Japan does not have the ultra-efficient distribution systems to which American businesses have become accustomed. A large number of middlemen handle a small volume of goods for a limited territory. This system increases the costs and planning necessary for market entry. Moreover, a potential U.S. seller may have to convince existing distributors to displace major Japanese firms, one of which might be the parent company of the distributor.

Another problem of tremendous importance is that American products are very seldom designed expressly for the foreign market. Often only minor product changes would be required, but U.S. companies seem reluctant to make them. This contrasts with the Japanese practice of designing both for the foreign and home markets. For example, much of the world outside the U.S. uses 220 volt, 50 cycle current for power. Japanese goods often have a switch on the product which allows it to work on either 120 volts or 220 volts. Such small changes make the difference between success and failure in foreign markets.

When American companies do attempt to enter foreign markets, they often neglect to promote their products properly and to provide the ongoing staff and management support essential to success. Japanese Diet Member Kabun Muto has summarized the differences between the Japanese approach to promoting exports and that of U.S. companies:

First, there is a difference in the number of trading offices and employees of each in the other's country. In 1977, American enterprises had 162 trading offices in Japan, with a total of 1,901 employees. In contrast, Japanese concerns had some 764 such offices in the U.S. employing 20,884 workers. \* \* \* Second, Japanese exporters have gone through research on the language, way of life, and other facets of the U.S. as part of their efforts to promote their exports. Again in contrast, study by American exporters of the language and way of life in Japan falls way short of the necessary level, and there are even some exporters who are ignorant of the FOB, CIF, and other trading prerequisites to setting export price. Third, Japanese exporters prepare pamphlets and other materials in English for use in the U.S., in this and other ways making continuous efforts to achieve exports. Here, too, there is a difference, as almost all American exporters use promotional materials in their own language and break off their export efforts after only a few attempts.

The impatience, or "drive", of the American businessman has much to commend it. But it is not the trait needed to overcome exporting difficulties. Instead, patient and painstaking perseverance is required to penetrate some of the more difficult but potentially lucrative overseas markets.

It is my belief that none of the problems I have discussed is unsurmountable. Radical changes in the American way of doing business are not necessary to success in the export field. But we will need some changes in our way of thinking. Most of all we will need risk-taking, patience and planning.

As a French trade expert recently said: "U.S. manufacturers have good products. The price is right; the markets are there. But they don't care to sell in Europe or don't know how to go about it." We must all start to care, and we must learn how to go about it.

Senator JEPSEN. Thank you, Mr. Tanaka.

In your prepared statement you note the Japanese Government plans the nation's industrial policy years ahead in an effort to promote leading edge technologies. Part of that promotion has been a series of policies that keep high technology imports out of Japan.

First, Mr. Tanaka, how should the United States respond when a highly industrialized trading partner restricts imports of the very goods in which we have a clear competitive advantage?

Second, should the United States adopt any similar mix of government subsidies and import barriers for our own high technology industries?

Mr. TANAKA. First of all, as a result of the MTN negotiations with respect to some of the high technology industry products such as computers and semiconductors, I believe that the average Japanese tariff levels are or will be substantially lower than the average tariff levels which the European countries imposed against imports of the same products. So that I think, as far as the tariff and quota barriers are concerned, this is a problem of the past.

As far as promoting leading edge technology firms or products with a growth potential, it is my view that the U.S. policy, particularly as it relates to R. & D. funding and procurement, should be oriented more toward the promotion of commercial and industrial products and not so heavily concentrated on an essentially NASA and DOD orientation.

Senator JEPSEN. Mr. Sevin, you mention in your prepared statement that Americans encounter a myriad of barriers in gaining access to specifications necessary to sell to a Japanese business. This complaint seems to be echoed by other industries besides the semiconductor industry.

Can you give us some other examples of these barriers?

Mr. SEVIN. Other barriers are classic ones, the administrative difficulties of actually importing into the country. Unless a company has a corporate presence in Japan every order requires a separate import license.

For example, there are instances that are documentable that each little semiconductor part, as it goes through customs, has to be inspected and counted which is the kind of problems that is non-existent here in the United States.

There is a great deal of difficulty in really getting NTT specifications, knowing what they are. There is a general claim that most of these Japanese specifications are not written down, which one finds hard to believe.

There are any number of these restrictions that impede imports into Japan.

The semiconductor industry and the computer industry, for that matter, have been among the most aggressive, in fact the most aggressive exporters of American products in world trade. We have had a very positive balance of trade. We still have a very positive balance of trade in Europe.

But our imports into Japan, which have been high in the past because they have been needed, have been going down dramatically over the last 7 years. And we have lost substantial market shares while maintaining that market share in other markets. So there has got to be a cause and effect relationship.

We are not a weak industry. We are not an industry with management which is not export oriented. We are extremely export oriented and we are having a great deal of difficulty penetrating the Japanese market.

Senator JEPSEN. Is this an accurate statement? It doesn't seem that our specification requirements elicit any similar complaints from our foreign suppliers, do they?

Mr. SEVIN. Our specifications are well documented. In fact, the products that are being traded throughout the world today, these high technology products that the Japanese are developing, are pro-

ducts we developed here under the specifications that we have made available to the world.

Each company has well documented, very thorough data sheets. We have meetings like the JEDC committee, Joint Electronic Devices Council, to which the Japanese companies are invited.

But there are no similar activities in Japan. We are not invited to the councils in Japan to discuss product specifications. But the product specifications for products marketed in Japan are the ones that were developed here. They have total, open, complete access to our markets, to our specifications, which we don't have in Japan.

Senator JEPSEN. I'd certainly like to acknowledge, and extend our appreciation and thanks to Comptroller General Staats, and the GAO, and thank him for his attendance. I was intrigued with the material that he presented on Japanese policy toward key industries.

As I read your report, the Japanese firm that is in a favored industry and that was reasonably export oriented, can deduct almost 50 percent of the cost of a new machine the first year. Do you see any advantages of the United States moving in that similar direction with regard to accelerated depreciation?

Mr. STAATS. Yes, sir. I might say, Mr. Chairman, in response generally to this whole problem, certainly there are matters involving trade restrictions in this picture, and these are very important. But it is also very important that we get our own house in order in relationship to the growth of productivity.

We have been doing a great deal of work in this area studying different sectors of the American economy, and it's inescapable that the conclusion is that we as a government and we as a nation are not focusing adequately on the need to improve our productivity. We have, as we have indicated in our statement, the lowest increase, the lowest growth in productivity of any industrialized nation.

We can talk all we like about the relative level of productivity of the United States with other industrialized countries, but that loses sight of the significant point of what is happening to the growth of our productivity.

We believe that this committee has taken some very good leadership in this area and we want to encourage you in any way we can to continue to focus on the whole problem of the ways in which we can improve our productivity in this country. We have many suggestions along this line, and we will continue to make reports to the Congress in this area.

But accelerated depreciation is one of the things which we would like to see given greater attention by our Government.

Mr. SEVIN. Can I make a comment on productivity?

Senator JEPSEN. Yes.

Mr. SEVIN. It will be very brief.

I think you'll find that the semiconductor and computer industry, for example, stands alone. We have a situation where our productivity has been increasing in recent years. We haven't been declining with the rest of the economy. Yet, we still have a serious problem in remaining competitive with the Japanese. I think if you do examine productivity, we have a first-rate record. In semiconductors, for example, productivity has been increasing quite a bit in the last few years. Productivity is not the problem.

Senator JEPSEN. I'd like to ask the rest of the panel in general: To what extent do you think the U.S. massive trade imbalance is due to our own inflation and lack of productivity?

Mr. Wolff.

Mr. WOLFF. I think that's only a part of the problem. I think the major inroads the Japanese have made in the market would not have been made by lowering the rate in the semiconductor area, automobiles. There are a variety of factors; we could go into some depth in many of these areas.

And in the end, there are many barriers to trade that price competitiveness will not surmount; the closeness of the interrelationships between trading companies which handle a great deal of Japanese imports. And resistance, really, by the Japanese mentality.

And that's difficult to tear away in trade negotiations. You can get at the visible barriers—tariffs, some of the nontariff barriers.

And I don't think this is just paranoia on the part of the U.S. businessman or the U.S. Government.

There are a number of close interrelationships and the feeling that purchasing domestically is in a way a loyal thing to do. And that's difficult to overcome and price won't do it alone.

Senator JEPSEN. Being from Iowa, not specifically, but I am especially interested in the agriculture exports. In your prepared statement, you mention that in fact although Japan is the best customer for agricultural exports the United States has, the resale price is particularly weak on sales from imported products from Japan. Is that kind of what you were referring to?

Mr. WOLFF. In many areas, the Japanese economy is entirely insulated from price effects, and the large trade agricultural items happen to be so insulated. Even soybeans, as the GAO study notes, have a substantial increase in price in the Japanese market, although this has not brought in substitutes.

Senator JEPSEN. Do you think the multilateral trade negotiators—how do you think they'll assist in this?

Mr. WOLFF. To the extent that the barriers were visible, in a number of areas, we asked the Japanese for, I think, \$1.4 or \$1.5 billion in concessions in agriculture, and they responded on 90 to 95 percent of what we asked, favorably. They gave us a commitment not to ever impose a tariff on soybeans, \$900 million worth, which I think is very important. A number of other specific products—namely, the specialty crops of the Pacific Northwest and California—received benefits.

On the main traded items, we did not make major inroads. We already have a very good customer there, and what we're dealing with is competition with rice, which is the most basic and most sensitive issue for the Japanese. There was no fundamental change there.

Senator JEPSEN. Following along this, you advocated the use of section 301 of the trade law. Now, ultimately, using 301 may require the use of unilateral retaliation by the United States. Are you prepared to face that possibility?

Mr. WOLFF. I think you have to be prepared to take the final step and withdraw concessions if others won't play the game by the rules they agreed to. But if we retaliate, we've lost. I mean, the exporter who wanted to get additional agricultural goods into Japan doesn't

get anything more, and instead the Japanese get less in here. That means everybody loses.

But you have to be prepared to act, or else the process won't work.

Senator JEPSEN. Mr. Tanaka, as a lawyer specializing in international trade, do you have any comments on that?

Mr. TANAKA. Well, especially, I think that now that the MTN has been negotiated and the protective devices against unfair trade practices are in place, we have entered a new stage where we should look toward positive measures, affirmative measures rather than negative measures.

I conceive of retaliatory measures and import-restrictive measures as negative measures because they have absolutely no impact of promoting productivity, for example, or increasing the quality level of products or increasing generally the competitiveness of the industries protected.

I really do think that we ought to shift our gears at this point. We've entered a new stage. We ought to look at our own selves and determine what we can do to make ourselves competitive instead of relying entirely on protective measures.

I think the comptroller general has suggested some affirmative steps in that direction, such as fast writeoffs to encourage private businessmen to renew their capital equipment so as to increase efficiency and become more cost-competitive in the world.

Senator JEPSEN. Mr. Staats, Japan has a budget deficit of about 40 percent of their budget. Yet, because of her very high savings rates, she seems to find enough money both to cover her Government deficit and to provide ample funds for a vigorous investment program.

Where did this very large savings rate come from in Japan, and does Japan treat savings or saving and debt differently in her tax structure than the United States does? It's kind of a three-part question. And is there a tax code more inclined to favor savings than ours?

Ms. HADLEY. This question as to how Japan has such high levels of savings has intrigued economists on both sides of the Pacific Ocean for some time. And, really, no one has come up with an altogether satisfactory answer. A variety of replies are given, but they don't really fully add up.

Professor Goldsmith of Yale, who was doing a comparative, financial study, noted a few years ago that this enormously high rate of personal saving was occurring in Japan at actually negative interest rates. There have been various hypotheses put forward—that Japan saves out of the bonus system of payments under which wage and salary earners, twice a year, get large lump-sum amounts; out of the underdevelopment of consumer credit; out of the absence of insurance, such as fire insurance on houses, which we carry. A variety of explanations are put forward. But it really is something that nobody has altogether very satisfactorily answered.

Mr. STAATS. As you know, Mr. Chairman, the savings rate in this country is just about half, currently, what it was back in the early 1960's. It's dropped from between 8 and 9 percent down to about 4½ percent. This is a matter of great concern, and should be a matter of concern.

How do you remedy it? You have a lot of difference of opinion as to how you might remedy it. But certainly some experts in the field

believe credit restraint and greater interest rates on savings could play a part in turning this trend around. A lot of inflation is due to anticipatory buying today, which has stretched out the consumer credit and reduced the savings rate. But without some increase and turnaround on the savings rate, it's going to be much more difficult to develop the money for the capital markets that we need to provide for modernization and improved productivity.

Senator JEPSEN. Now, Japan's finance ministry and her ministry of international trade and industry seem to coordinate their efforts to encourage the development of capital-intensive and technology-intensive industries. In other words, the Government of Japan pursues a program of research, development, investment, and capital formation; and they get behind and support the industry.

How much of an influence does this have on the ability of major growth industry to raise money and to start producing?

Mr. STAATS. I don't think I can answer that question.

Ms. HADLEY. Japan has financed, up until the last few years, if we take the postwar period, primarily through bank borrowing, and this has made a very efficient channel of taking personal savings into banks and then banks lending in accordance with Government wishes out of direction from their central bank which is not an independent central bank.

So, it has made a highly effective instrument for channeling funds to those industries which the Government is most eager to encourage.

Senator JEPSEN. Did I hear you correctly? Did you say banks would lend according to the government's wishes?

Ms. HADLEY. Right. This is because, for a great deal of the postwar period, the commercial banks lent beyond their resource base. They were accordingly obliged to borrow from the central bank, and it was out of coming to the central bank to borrow that the central bank was then able to impose conditions of how their portfolio would be.

Senator JEPSEN. Does this probusiness attitude in Japan extend into areas of Government regulation and redtape and this type of thing which we have a lot of in this country?

Ms. HADLEY. I am not completely sure whether I understand the question.

Senator JEPSEN. They have a Government; the Government is very supportive in promotion in this way. Now, in the areas of regulation and redtape, which our business and industry have a lot of comment about in this country, is the Government of Japan, their progrowth attitude, does that extend over into the regulatory areas in Japan?

Ms. HADLEY. Yes. I guess we use "redtape," of course, pejoratively. Their regulation is more jointly done. They also have a quite different attitude toward Government in the economy than we do. Probably, I guess, the difference between the attitude with which they begin and the fact that many of the regulations are jointly developed between the Government and business, affects their not speaking of them as "redtape."

They do have a number of regulations, though, fascinatingly enough, that they are reconsidering. They are beginning to review to deregulate a number of areas. They are impressed with what was achieved in the United States with airline deregulation. The OECD restrictive business practices committee has been recommending review, and

their Fair Trade Commission, which is a combination of our Anti-trust Division and Federal Trade, is at the present time starting a comprehensive review to deregulate.

Senator JEPSEN. I am just curious. What is their equivalent to the EPA? Do they have something equivalent to that?

Ms. HADLEY. Environmental planning?

Senator JEPSEN. The Environmental Protection Agency.

Ms. HADLEY. The Japanese counterpart is called the Environmental Agency and they have some extremely tough environmental rules; in a good many instances, tougher than our own. In the case of automobiles, they are operating under the Muskie Clean Air Act, which they adopted in toto from us.

Senator JEPSEN. Mr. Staats, in the automotive trade section, you know, Japanese car makers maintain exclusive dealerships in which it is impossible to piggyback the sale of foreign vehicles. Now, this seems to be an outrageous violation of American competitive practice.

How do the Japanese car makers answer the charge that they are liable to no such rules in the American car market?

Mr. STAATS. Perhaps Mr. Wolff could respond to your question better than I can.

But it's one of those trade practices which makes it almost impossible for the American automobile companies to market their product in Japan.

Senator JEPSEN. Do you want to comment on that?

Mr. WOLFF. The series of barriers that have plagued our car manufacturers in Japan are legion. The distribution system is certainly one of the most difficult problems. The cases of the problems with individual imports are really quite impressive, so that the sticker price of a car, the problems in the distribution system, a commodities tax, and a number of other barriers, as well as standards and testing problems, result in very high prices indeed. And I think the market is artificially limited.

I was over in Japan last December with the chief of staff of the Senate Finance Committee, who took a ride, and we drove for 2 days. We decided that we would look for the number of U.S. automobiles that we could identify, and it wasn't difficult keeping a tally. There was one in about 20 hours of driving.

The barriers are just extremely high and hard to get over.

Mr. STAATS. I am told that the Japan Fair Trade Commission, has this particular practice under investigation. But I have no idea what they're going to do about it.

Senator JEPSEN. Now, there are numerous proposals being made here in the United States to reorganize the trade sections of the various departments involved in trade matters in Commerce, State, the Office of the Special Representative for Trade Negotiations, and even the establishment of a Department of International Trade. Do you think this would improve things?

Mr. STAATS. We've been following this matter quite closely, and we have presented testimony before the Senate Governmental Affairs Committee. Our view is that the most recent proposal is a very distinct step forward and should result in a great deal of improvement. I guess if we had our particular preference, we might have gone a little bit further than the administration proposal, but we certainly agree that it's a great step forward.

Senator JEPSEN. Mr. Tanaka, you appear to be recommending a restructure of the U.S. export policy at the Government level to a more centralized and coordinated program. What sort of agency or policy should we be developing in this area?

Mr. TANAKA. I agree that the administration's reorganization plan is a major step forward. There has been an identification and recognition of a need to coordinate at a Government level the development of export competitiveness and commercial exports.

Of course, the policy mechanisms which might be used in any country to promote exports really are essentially determined by the socio-economic settings, and the institutions of those particular countries.

I think that, in view of the fact that generally Government interference tends to be disavowed by the private sector, there are inherent limitations on the types of policy mechanisms which might be utilized here in this country to promote our exports. I think that fundamentally the judicious use of the taxing power, certainly, to provide incentives and disincentives would work to promote the industries which we feel hold the greatest possibility for growth and export potential. This can be, I think, encouraged by greater use and effective use of the taxing power.

Mr. WOLFF. If I could just add one point on reorganization, I think that a major step has been taken in the right direction, partially as a result, if not completely as a result, of congressional initiatives. I don't think that it goes as far as most people would like, but it represents what's achievable at this time.

The one point that I would make in addition is that adequate staffing is needed. I doubt if there's a single person in the Department of Commerce, and I know there isn't at STR, which spends all of its time on the semiconductor problems or steel, or any of the other problems that affect our country. There is no longer anyone at the Special Trade Representative's office, or ever will be again, who deals with the problems of Japan, trade relations with Japan.

We have a Government that seems to have adequate resources when we are regulating American business, whether it is environmental protection or antitrust matters or other areas. When it comes to trade issues, in the past we have undermanned and understaffed.

That is principally the reason why the countervailing duty law and the antidumping statutes were not well administered: Not because of Treasury bias in one direction or another, but because of inadequate resources. So what I hope is that the President's plan, which I think is a major step forward, a good step forward, is given the resources and the support it needs to make it work well.

Senator JEPSEN. You think it's a much needed step in the right direction?

Mr. WOLFF. Yes.

Senator JEPSEN. To kind of wind this up, I'll ask before we finish, and you might be thinking about it, if there's anything you'd like to add, to submit for the record or state, we'll plan to wind this up in the next 5 minutes.

Mr. Staats, in your report, you conclude rather mildly:

Although Japan has adopted a new trade policy reflecting a substantial reduction of tariffs and a lowering of many nontariff barriers, attitudes on both sides of the Pacific have been slow to adjust to the new circumstances.



Can you tell me why your report doesn't say much or really explain how severely handicapped American industry has been in establishing necessary footholds in the Japanese market, which I think is borne out here by some of the testimony this morning? It seems to me the report doesn't really get to the heart of how much this pattern of past discrimination has really deeply affected the present behavior of our American businesses.

Mr. STAATS. I'm not sure I'm following the thrust of your question completely. What we are saying in our conclusion was that there are problems on both sides. There are things that this Government needs to do in a positive way to try to promote exports, to penetrate the market.

At the same time, we've got to continue to work to try to remove these barriers that have been created. And the automobile industry, I think, is a good illustration. But I think there are things that can be done on both sides.

Senator JEPSEN. I gather, I think, from the panel, from Mr. Tanaka and Mr. Wolff, that you're saying that it's not a matter of a defense-offense type of thing, but get on the offense and do some things for ourselves, if necessary 301, that you mentioned, getting our own house in order and moving along to strengthen—I think that's the historic American way of going about things.

It is frustrating to run into the historical difference in thinking, perhaps, the sense of fair play and gentlemanly ways of negotiating and worrying about setting up contracts. We're salesmen in this country; we're impatient. We would kind of like to close the deal, compromise a little bit. We find that in everything we do.

Mr. STAATS. Senator, Mr. Milgate would like to add a little to my response.

Mr. MILGATE. What we wanted to note was this, Senator, that past Japanese policies have an impact, certainly, on present attitudes of U.S. businesses. Once the Japanese industry was well established in that market, then American businessmen tended to apply their resources elsewhere. They didn't see the opportunity.

Mr. STAATS. When you're discouraged, you go somewhere else.

Senator JEPSEN. OK. Since that isn't necessarily a typical historical posture, I don't think, in American business, maybe that's the reason we're looking and digging into these things that we have here.

Mr. TANAKA. As far as the potential for export to Japan in the future is concerned, it seems to me that we can look to what happened in this country. As it moved from a manufacturing-oriented economy to a service-oriented economy, market forces exerted a pull on imports, and our imports drove up.

I think the same process is going on in the Japanese economy, where the manufacturing sector as a percentage of the GNP is declining in relation to the service sector. And to the extent that the service sector in Japan continues to grow, this will have the effect of inducing and sucking in imports.

So I think that this change in Japanese economic orientation will have a salutary effect with respect to increasing imports into Japan.

Senator JEPSEN. Well, looking at the differences between the trade policies of the United States and Japan, they've been borne out here

in the testimony, and so on. And we find several distinctive features in the Japanese situation.

I'm just kind of rebounding these off to get verification, only in the event you find that you disagree with what I say.

The Japanese situation presents a strong industrial policy; the extensive use of accelerated depreciation to keep industry internationally competitive; and a much more deliberate approach to foreign trade. We also discussed to a quite large extent the Japanese use of import restraints to shield old industries and to develop new ones.

So I find running throughout this whole thing a persistent pattern of Japanese protectionism. That pattern raises two questions.

First of all, how much will past protectionism continue to haunt the future? We've touched on that. And can we really expect American exporters to confidently approach a door that has been slammed shut so often in the past?

Second, despite their emergence as a major industrial power, the Japanese continue to use protectionist measures to foster their goal in technologically dynamic areas such as telecommunications, where serious domestic employment problems will result if we continue to tolerate those kinds of trade practices by the Western World's second largest economy.

Mr. Wolff.

MR. WOLFF. Well, I think that major progress has been made, and as Senator Bentsen indicated, in part, in large part due to the interest of the Congress in this issue.

There is Japanese protectionism in quite a number of areas, just as there is in this country. NTT, the telecommunications area, is a serious problem, and we don't have a solution to it yet. We have a framework for one that Ambassador Strauss and Ambassador Yoshida worked out June 2, but there's no agreement yet. That's going to be a very difficult issue, and it's solely protectionism.

There is a list of reasons why the Japanese say we ought not to be in their market in telecommunications. And it all boils down to protectionism. There is no valid reason why we ought not to be there.

Will U.S. businessmen keep trying? As long as there is a profit to be made, I would hope that they would. And all of the things that Mr. Tanaka cites as the difficulties on our end of pushing things out of this country and having the interest are, I think, substantially accurate. But I would look forward to a renewed effort.

One of the things we could use, for example, is MBA programs in this country, business degrees combined with area studies, so that we have people who are trained in the Japanese market, corporate executives who have an intimate knowledge of the Japanese language and culture.

There are a number of things we can do, a hundred different things that I think we ought to be working on. I worry a bit about a conscious industrial policy in this country. I think we ought to know more about our own economy and what is going on. I think we ought to have tax incentives for research and development, and accelerated depreciation of capital goods.

But I don't trust central planning. I don't think that would be a healthy step for the U.S. economy. And I would have to see us target industries for special aid in this country, because I'm not convinced

that the redtape that would follow—because there are always strings, as the World Bank has learned, in getting money from the United States. There are always strings.

I would be cautious in going in that direction, but there is a lot that we can do. And I think that the GAO report is really an extremely useful document; and I would hope that STR and Commerce and DOL would reinstitute their own interagency watch mechanism on trade problems with Japan and get out ahead of them. They are visible in aircraft, in computers, in semiconductors, and there are some solutions out there.

Senator JEPSEN. Very well said. Thank you.

Mr. Staats.

Mr. STAATS. I would like to associate myself generally with Mr. Wolff's statement.

I would like to, if I may, go back to a point of increasing our own productivity and increasing our programs for export promotion. These are the two areas, it seems to us, that we have not still come to full recognition of their importance and their relationship to our balance-of-payments problem that we face worldwide.

If it's agreeable with you, I would like to insert in the record at this point some of the recommendations we have made on both these points, both on export promotion and on increasing our productivity. We feel that this committee can play, for example, an important part. One of the 10 recommendations we made in the field of productivity would be for this committee to, for example, make an annual assessment or a biennial assessment of where we are, of where we've come, and what other problems really are providing barriers to improved productivity.

Senator JEPSEN. If you submit those, they will be included in the record.

[The information referred to follows:]

#### GAO RECOMMENDATIONS ON EXPORT PROMOTION AND RELATED TRADE ISSUES

Over the years, GAO has made numerous recommendations to the executive branch and to the Congress for improving the U.S. trade and payment performance. These recommendations concerned:

The need for coordination of long-range international economic policy issues.

The possible need for legislation to establish a centralized mechanism for developing and coordinating long-term economic policy planning.

Strategies for guiding U.S. commercial activities in foreign countries, Agriculture, Commerce, and State should develop trade objectives for market development.

Fragmentation of responsibilities. We asked Congress to consider establishing a joint executive-congressional group to consult on a variety of East-West trade matters.

Difficulties in the timely processing of export license applications. We suggested that Congress have export license application management responsibilities centralized in Commerce and have a multiagency group established to provide guidance to Commerce to make the system more responsive.

Imports. We made a series of recommendations to (1) improve administration of the Antidumping Act and (2) provide for a better information base to permit a more comprehensive analysis of the effects of antidumping actions on prices, U.S. trade, and other interests.

Productivity. We concluded that the United States needs to make manufacturing productivity a national priority in order to remain internationally competitive and to maintain strong industries.

U.S. technology transfer policies. We recommended a change in the method of accumulating statistics so that the implications of U.S. transfer policies can be better evaluated.

GAO believes that a Federal program to improve national productivity is needed and should include the following:

1. Periodic needs assessments must be developed to determine the nature and extent of public and private sector productivity problems.

2. The program should bring together various groups on neutral ground to discuss widespread industry productivity problems.

3. A productivity clearinghouse must be operated to provide national and international data and information on various aspects of productivity to all sectors of the economy. In particular, we need to provide private industry with more information on developments in foreign countries that may be applicable to the United States or which may affect our competitiveness on the world market.

A productivity clearinghouse now exists, but it appears to exist in name only. To be effective, the clearinghouse must actively seek and disseminate needed data.

4. A special analysis of the Federal budget should be developed to document where funds to enhance productivity are being spent. This analysis will help to identify gaps, duplication, and overlapping programs in the Federal productivity effort.

5. A periodic assessment of the productivity impact of fiscal, monetary, tax, and regulatory policies on the private sector should be made by the Joint Economic Committee of the Congress, the Council of Economic Advisers to the President, and the Federal Reserve Board.

6. The program must take the lead in developing improved and acceptable measures of productivity. Our current productivity statistics do not adequately reflect the role which capital investment, improved technological processes, and innovation can play in improving productivity. The Bureau of Labor Statistics and the National Academy of Sciences have done good work, but more needs to be done. In addition to better overall economic measures which help improve Government policies and programs, more attention is needed on the company level where the measures can be used to help improve productivity. After all, it is at that level that productivity improvement takes place.

7. Policies must be adopted which will stimulate private sector productivity—improving investments—both in capital and in research and development—through tax and other incentives. The Revenue Act of 1978 contained two important changes directed toward this end—a reduction in corporate tax rates and an improvement in the investment tax credit. While this is a step in the right direction, more change is needed in this area.

8. The program should foster the establishment of labor-management committees. The activities of these committees often are the key to agreement on the various types of cooperative efforts which can lead to improvements in both productivity and the quality of working life. Recently enacted legislation seeks to improve labor-management relations by authorizing funds to establish labor-management committees at the plant, area, and industry levels.

9. Better ways must be developed for measuring the costs and benefits of both existing and future regulations which can affect productivity. The entire regulatory process needs to be subjected to a rigorous discipline of costs and benefits analyses. This is particularly true for those regulations which have been designed to deal with health, safety, and the environment.

10. And, finally, the Federal Government should accelerate its efforts to measure and improve productivity within the Federal Government and take a strong leadership role in assisting State and local governments to reduce their costs through improved productivity. A recent study estimates that 20 to 30 percent of State and local government employment growth between 1967 and 1976 resulted from low productivity. Underscoring the importance of this point is the fact that State and local governments now employ 80 percent of all government employees in the Nation.

This ten-point program should be led by a statutory body consisting of representatives of selected Federal agencies that have productivity-related missions. The major task of this organization would be to develop a national productivity plan to guide Federal efforts for improving private sector productivity. There should also be an external advisory group reporting to this body made up of representatives from industry, labor, and the general public. This advisory group would suggest particular productivity issues for the Council to address.

Senator JEPSEN. Anything else? Do you have anything?

Ms. HADLEY. No, thank you.

Senator JEPSEN. Mr. Tanaka.

Mr. TANAKA. I would echo what Mr. Staats has said. I think over the long term the most important aspect of this whole subject is the improvement of productivity in America. And I think that this problem is very complicated because of the social value orientation which we have in this country. The mode of settling disputes, for example, between labor and management is entirely different from the mode of settling those disputes in Japan.

For example, going into strikes. Let me give you an example. In 1959 the U.S. Steelworkers Union had a nationwide strike. Ever since 1959, we've had an unfavorable balance of trade in steel products. Why? Because in a concentrated industry a strike by a major union knocks out the entire productive capacity of the United States. Therefore, the United States becomes an undependable supplier.

There are numerous other examples. For example, in 1958 when PPG and LOF controlled 65 percent of the total domestic capacity of sheet glass, there was a 112-day strike at PPG and a 12-day strike at LOF which overlapped. So during a 12-day period, virtually 65 percent of our sheet-glass capacity was knocked out by this nationwide strike. As a result, the two major user industries, namely, the construction industry and the automotive industry, went scurrying abroad to Belgium to source their sheet-glass requirements with Glauber-Bell, and with Asahi in Japan. So ever since that major strike, imports have maintained a certain percentage of this market.

Therefore, the mode of settling disputes, I think, has an adverse impact on export competitiveness. Certainly, the mode of settling disputes has an adverse effect on the attitudes of workers, for example. The workers feel that they are not part of the team.

A consensual method, a participatory method of settling disputes or coming to a consensual agreement, I think, promotes the participation of workers and worker identification of his interests with the interests of the company. It results in expanding the worker's perception of the existence of a commonality of interests.

All of these problems have to be looked into in considering what can be done with respect to increasing our productivity.

Mr. STAATS. Could I just add one word to that?

In our work in the productivity area, we have been interested in what other governments have done by way of centralizing the focus on productivity. Most of the industrialized countries have done something in relation to a productivity center. Japan has a very good one.

But I was much impressed, when I visited them 2 years ago, expecting to find the emphasis on technology. But I found that that was not the case at all. The heavy emphasis is on the very point that Mr. Tanaka has referred to, of how can labor and management and the Government work together to prevent work stoppages, create work incentives, and matters of this type, which have been very important in their case.

We believe that more can be done through the Federal Mediation and Conciliation Service by way of encouraging the establishment of labor-management committees in this country. Wherever they have been tried, they have been successful. And the president of Motorola just last week was telling me about the work that they were doing in

the participatory management area, and apparently it is working extremely well. So these are exactly the kinds of things that the Government can take more leadership on.

Senator JEPSEN. Mr. Sevin.

Mr. SEVIN. I have to take issue and disagree with much that has been said by Mr. Tanaka and Mr. Staats on productivity. The U.S. semiconductor industry does not have an adversary relationship between its management and its people. It has never had a strike. It has high and increasing productivity. Yet we're having trade problems with the Japanese.

Maybe productivity is a problem in other areas. It is not a problem here. We had better not ignore the disruptive trade practices of the Japanese in our market. Yes, we agree we need tax incentives. But we had better not turn our back on the import practices of the Japanese and their practices in protecting their own markets.

Senator JEPSEN. In summary, I think you're—everybody's right. How's that [laughter] for political astuteness and evaluation of the situation?

We will bring it to a close. But I was delighted and pleased to hear your remarks, in fact, all of them. Goods and services come from labor and capital. I don't know that there's any other place that they come from, and we'd better wake up and smell the coffee in this country, because labor and capital can no longer afford to be adversaries.

It's my turn to get on the soapbox. And I was pleased to hear your remarks. We all want clean air, clean water, safety, and health. I don't know of anybody, I have no knowledge of any Senator that doesn't want those things. If we can all just work together as advocated here and at the same time be realistic and recognize that there are some things we're going to have to deal with and negotiate with, but dealing with productivity and dealing from strength of productivity, then you can afford to make deals, be compassionate, and all the other types of things. That's true in our defense, as well as in our trade.

Thank you very much. It's been a very interesting hour. It is the most informative I have had since I have been in the Senate. The committee stands adjourned.

[Whereupon, at 12 noon, the committee adjourned, subject to the call of the Chair.]

[The following information was subsequently supplied for the record:]

RESPONSE OF HON. ELMER B. STAATS TO ADDITIONAL WRITTEN QUESTIONS  
POSED BY SENATOR BENTSEN

*Question 1.* With regard to trade reorganization, you said that you would have gone a bit further than the President. What should be the next step in reorganizing and strengthening our trade bureaucracy?

*Answer.* We believe the President has not provided sufficient staff for the greatly expanded duties assigned to STR. In his supplemental budget request, the President asks for an increase in positions from 59 to 116. This, for example, provides for one position for export policy. If anything stands out from our study of U.S.-Japan Trade it is that Japan "thinks" exports whereas the United States tends to focus on protecting the domestic market. We need much more attention to exports. While we are fully cognizant that STR's export policy person will be in a position to draw on resources within STR as well as elsewhere in the government, we believe the problem is far bigger than what can be handled by

one person. We use this example illustratively. We believe that the President's request should have been somewhat bigger.

*Question 2.* Ambassador Wolff expressed some concern that the recent improvement in our trade account could lead to complacency with regard to our trading relationship with Japan. Do you have any thoughts on how we can best proceed to monitor overseas compliance with the new multilateral trade codes? Because so much of the past pressure for trade has come from the Congress, should there be something of a joint Executive-Congressional effort to monitor the trade practices of our trading partners?

*Answer.* I believe there would be advantage in the Congress relying on its existing institutional mechanisms supplemented by ad hoc solutions here in the manner of the task force on Japan established by the Trade Subcommittee of Ways and Means and your request to GAO to do a trade study for your Joint Economic Committee. It is the responsibility of the Administration to monitor trade programs. If the Administration fails to discharge this responsibility, then I think it is desirable for Congress to step in but I do not see it doing so before a failure by the Administration.

In my judgment, Ambassador Wolff has an important point in our staying on the course. This leads me back to the previous point, of the importance of sufficient staffing for STR.

*Question 3.* Returning again to your discussion of the computer industry in Japan and your prescription that we would avoid the fate of the American radio and television manufacturing industries, how can we do that? What balance should be struck between industrial policy, tax incentives and trade policy to assure the future health of our technologically-advanced industries?

*Answer.* Let me take this question in steps. You ask how this country can avoid the fate of its radio and television industries? I would say we are doing this for one thing by the presence of our industry in the Japanese market. By our presence in Japan and the competitive challenge that this poses, IBM and the other American companies are in a position to temper the performance of Japanese companies. This puts us in a stronger position. In this industry, patents provide an important protection, and we are in a very strong patent position. Unlike the situation in radio and television where are companies focused on the domestic market, the U.S. computer industry operates in terms of the world. The difference in orientation gives me encouragement.

The next part of this question relates to the balance that should be struck between industrial policy, tax incentives and trade policy to assure the future health of our technologically-advanced industries. As we all know, the United States does not have industrial policy, which is to say, that the government regards all "well", civilian industries to be of the same importance. In this country, we regard it as appropriate for the government to provide special benefits for sick industries to supply special benefits for defense industries not special benefits otherwise. In such circumstances investment tax benefits are extended on an equal basis to all.

In contrast to our situation, Japan has operated with industrial policy throughout the postwar period. A good many of the European countries operate with industrial policy. In situations where foreign governments operate with industrial policy and the United States does not, we inescapably are somewhat disadvantaged.

Industrial policy is very importantly implemented through tax incentives. In countries which have industrial policy, tax incentives are structured to give greatest advantage to those industries which are to be encouraged. Since in the United States, outside of defense, we do not have industrial policy, we extend tax credits without "favoritism" among industries.

Your question is "trade" policy but I presume the focus is export policy. Currently, the United States operates its export policy as it operates its tax incentive—without distinction as to industry. Our study of Japan's export policy makes it clear there are gains from operating with special benefits to particular industries rather than for example, treating shoes and computers as equals in export potential.

At the present time American opinion does not favor the United States operating an industrial policy so that the Executive and Legislative Branches are alike handicapped in developing measures for our technologically-advanced industries comparable to those used in foreign countries. However, a certain amount of industrial policy—though not so identified—operates in consequence of our defense establishment. It is our technologically-advanced industries which are the

recipients of government R and D grants, of assured markets, of attractive returns on capital, of other preferences. Accordingly, it would seem likely that in this field the United States will remain in a strong competitive position.

*Question 4.* In summing up the study on color television receivers, the GAO finds that "... the U.S. industry was seriously impaired by tariff and nontariff barriers from entering the market." At the very same time, the Japanese were capturing the lion's share of the American market. I am not one to waste time closing the barn door even if a herd of horses have fled—but I would like your guidance about some of our horses that are still left in the corral. What if we find ourselves in a similar situation with semiconductors, microprocessors or some other product. Should we quietly accept a closed market on the part of one of our trading partners while that very partner steadily increases her exports to the American market? Do we have any choice but to use the weapon of our large, open, integrated market when we find markets closed to us in Japan or elsewhere?

*Answer.* In Section 301 of the Trade Act of 1974, the Congress has provided a mechanism with which to meet this contingency. It is available for use in whatever retaliatory way the Administration chooses.

*Question 5.* We have all heard a great deal about how qualitatively different Japanese business and government linkages are from those in the United States. According to a lot of what we read, informal arrangements between business and government are much more common in Japan, and a great deal more emphasis is put on obtaining consensus between business and government leaders. In your section on computers you note that after the repeal of quantitative restrictions on the importation of computer main units, MITI sent letters to the public sector, utilities and banks urging them to adopt a "Buy-Japan" policy. How can we best respond to that type of administrative pressure?

*Answer.* However the information came to the attention of the Government—through the Embassy, through private complaint brought to the attention of the Embassy, STR or some other part of the government—I would see an STR investigation of the matter and the initiation of STR discussion with Japanese officials. If these bilateral diplomatic efforts did not resolve the matter satisfactorily, I would see STR taking the matter to the GATT. Much effort in the recent multilateral trade negotiation was spent in strengthening GATT dispute settlement. If the GATT panel found in favor of the U.S. and Japan still had not taken corrective action, I would see STR initiating a Section 301 action. As Section 301 is written it provides the Administration with wide latitude in the actions it might take.

*Question 6.* In the report's section on color television sets, you note that "Japanese retail and servicing facilities are generally owned or controlled by the major manufacturers. Exclusive distributorship are heavily, if not totally financed and supported by CTR's manufacturers. As a result, these distributors normally do not carry foreign brands because they fear losing their franchises with their normal suppliers?" Now again, this brings up the question of informal mechanisms affecting business behavior. Are there actual laws prohibiting the selling of more than one brand name product in a distribution network? How are the threats of losing a franchise made? Are there cases that you could find where this happened? Did you find evidence that this goes on in many types of industry where a distribution system is important, not just in CTR's and automobiles?

*Answer.* Because of the limitation of time under which staff worked, there was not opportunity to investigate beyond the assertions by dealers that they were "afraid" of losing their dealerships if they carried other products. However, as observed in the report (p. 48) and as I mentioned in my testimony, Japan's Fair Trade Commission is currently looking into the anticompetitive effects of exclusive dealerships in automobiles, and I believe it is reasonable to expect that the Commission is likely to extend that investigation to exclusive dealerships in other product lines. Exclusive dealerships go far beyond CTR's and automobiles.

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RESPONSE OF L. J. SEVIN TO ADDITIONAL WRITTEN QUESTIONS POSED BY SENATOR BENTSEN

*Question 1.* "In the course of your prepared testimony, you expressed some concern that Japanese industry has had relatively little trouble in acquiring U.S.



technology either through licensing or through the partial acquisition of U.S. firms. Do you favor restricting foreign access to U.S. technology? And if so, what specific measures would you propose?"

Answer. At present, we do not suggest restricting foreign access to U.S. technology either by limiting licensing or by prohibiting further foreign acquisitions of U.S.-owned firms. We are concerned, however, with restrictions on technology transfers and acquisitions presently imposed by the Japanese government. For example, the massive Japanese government VLSI semiconductor research program (described at page 29 of the GAO Report) resulted in many developments which the Japanese government deems to be "property" of the government. While these developments are not shared with foreign semiconductor firms, we suspect that the Japanese-owned firms have full access to the technology. Further, the Japanese government allegedly sponsors research laboratories to which the Japanese-owned firms have exclusive access. See the GAO Report at page 66. At the same time, foreign enterprises continue to invest in and acquire U.S. semiconductor companies and to hire away our salesmen and our engineers. State-of-the-art U.S. semiconductor production equipment is available to foreign competitors. They have access to all of our technology, our people, our "brains."

There must be an end to the Japanese government policies which foreclose reciprocal treatment. The Japanese government permits (and possibly requires) the Japanese-owned companies to play by different, discriminatory rules. Our government should insist that the Japanese adopt our non-discriminatory policies and permit equal access to Japanese technology, productive assets, personnel, capital and markets. Fair play dictates that everyone operate under the same rules. We ask nothing more than fundamental fairness.

*Question 2.* "What are the prospects for the European semiconductor industry? Can we expect similar government involvement in the development of the European semiconductor industry? What will be the implications for U.S. investments in Europe and for the American market?"

Answer. The European-owned semiconductor industry is developing rapidly, principally because of the financial assistance received from European governments. Europe is not, however, developing as rapidly as the Japanese-owned industry.

European development has been encouraged by such protectionist steps as the 17 percent EEC tariff on semiconductors, which was not even opened for negotiation by the EEC during the Tokyo Round. However, unlike Japan, the European development effort does not discriminate on the basis of the nationality of stockholders of semiconductor companies, and both direct investments and joint ventures by U.S.-owned firms have generally been welcomed by EEC governments on equal terms with European-based firms. My company, for example, is building a semiconductor plant in Ireland to service semiconductor customers in the EEC.

The perspectives and prospects of the Europeans, as well as development efforts by European governments, are documented in the MacIntosh Report which I cite in my written statement of October 10.

*Question 3.* "You mentioned that Japanese firms have had a great deal of success in collaborative research—the sort of program that would be prohibited by American antitrust laws. Do we need to re-think our antitrust laws when it comes to high technology research?"

Answer. Given the high cost of research which may impede new entrants into the semiconductor industry and retard growth of small semiconductor companies, a limited exemption from the U.S. antitrust laws could facilitate cooperative research in generic support technologies identified as important by industry participants. The results of such research would be available to all participants. However, to place the benefits of antitrust exemptions in proper context, no exemption from the U.S. antitrust laws, however broad, will be a panacea for the U.S. industry. Such an exemption will not eliminate the threat of imports from Japan.

*Question 4.* On page 24 of your prepared statement you urge the Joint Economic Committee to study whether "... U.S. investments by the Japanese undermine the earning power of U.S.-owned firms, making them less competitive both in the United States and in world markets."

Could you give us some specific details contrasting the earning levels of U.S. and Japanese semiconductor firms?

Answer. Set forth in Table 1, below, are comparative earnings as a percentage of sales of Japanese and U.S.-owned semiconductor firms.

TABLE 1.—Comparison of Japanese and United States-owned semiconductor firms—Return on sales

	<i>Net income after taxes as percentage of sales</i>
Japanese-owned firms (fiscal year March 3, 1979) :	
NEC -----	1.2
Hitachi -----	2.5
Fujitsu -----	2.4
Toshiba -----	1.6
Average -----	<u>1.9</u>
U.S.-owned firms (fiscal year December 12, 1978) :	
Texas Instruments -----	5.5
Motorola -----	5.6
Advanced Micro Devices -----	6.4
Intel -----	11.0
National Semiconductor -----	4.6
Average -----	<u>6.6</u>

The average return as a percent of sales for the U.S. firms was thus approximately three and one-half times as high as the Japanese return. As I indicated in my October 10 statement to the Committee, the U.S.-owned firms will be seriously hindered in efforts to attract needed capital if they are forced to match Japanese prices and hence to accept the earnings levels of the Japanese-owned firms. U.S. firms are prohibited by law from affiliation with commercial banks, and they receive no capital grants from the U.S. government. Instead, they must prove their credit worthiness on a regular basis by reporting respectable earnings levels. The Japanese have guaranteed sources of capital which are available independent of free market criteria such as net worth and current earnings. As they are not restrained by free market considerations, the Japanese can price their products with the goal of long-term market dominance.

*Question 5.* On page 27 of your prepared statement, you suggested that the Congress should consider legislation which would "tax U.S. operations of foreign-owned firms . . . to offset the advantages which they derive from foreign governments." Could you be more specific about this particular proposal?

Answer. My response divides into two parts: First, a more detailed explanation of the subsidy and "internal dumping" advantages which the Japanese bring to this country when they build plants here and, second, further discussion of possible methods of addressing this very real threat to U.S.-owned industries.

(1) "The Japanese Advantages in Locating Plants in the U.S." The GAO Report indicates that a key part of the Japanese economic planning is the "growing" of selected target industries. As described in my response to question 4, above, the Japanese government channels consumer savings through the banking system as loans to Japanese-owned companies in the "target" industries, thus eliminating any concern by these industries regarding capital formation. As they are not concerned about short-term profitability to enhance borrowing capacity or to support sales of securities in free capital markets, the Japanese-owned semiconductor firms can price their products substantially below free market levels. If forced to match the Japanese prices, free market firms would be hindered in raising capital. As U.S. law prohibits industry/bank affiliations such as those which are permitted in Japan, and as our government does not subsidize commercial enterprises, U.S. firms must depend on retained earnings and capital markets to finance expansion.

The levels of the loans to preferred Japanese semiconductor firms far exceed amounts which could be borrowed by a U.S. firm in free capital markets:

TABLE 2.—DEBT/EQUITY RATIOS OF LEADING JAPANESE-OWNED SEMICONDUCTOR FIRMS

	Mar. 30, 1979		
	Long-term debt <sup>1</sup>	Total equity <sup>1</sup>	Debt/equity ratio <sup>2</sup> (percent)
Japanese semiconductor company:			
Nippon Electric (NEC).....	\$1, 116	\$694	161
Hitachi.....	1, 470	2, 342	62
Fujitsu.....	558	742	75
Toshiba.....	1, 410	1, 580	89

<sup>1</sup> Millions of dollars.

<sup>2</sup> Long-term debt divided by total equity.

TABLE 3.—Debt/equity ratios of U.S. semiconductor firms

	Debt/equity Dec. 31, 1978 (percent)
Motorola.....	22. 4
Intel.....	0
National Semiconductor.....	1. 1
Texas Instruments.....	2. 3

The Japanese debt/equity ratios are even higher if short-term debt is included. Stated short-term debt of NEC, for example, has averaged 2.6 times its stated long-term debt. Hitachi and Fujitsu have stated short-term debt which is, respectively, 5.2 and 2.6 times larger than their stated long-term debt. When short and long-term debt are included, the NEC debt/equity ratio exceeds 48 percent, and Hitachi exceeds 350 percent.

These long and short-term loan proceeds by the Japanese banks will unquestionably be used by the Japanese-owned semiconductor firms to finance plants in the United States and to subsidize prolonged price cutting of the products of these plants. Once inside our borders, shipments from the Japanese owned plants will be largely immune from the U.S. trade laws. We respectfully submit that one result of the Japanese plants in the United States will be to weaken the competitive posture of a U.S. industry, both in the U.S. and worldwide.

It is no answer to say that Japanese-owned plants in the United States will "save" U.S. jobs. If these plants are used to undermine the financial strength of U.S. firms, a greater share of the growing semiconductor market will be captured by the Japanese, and prospective U.S. jobs, particularly high paying research and design jobs, will be lost to Tokyo.

(ii) Possible Solutions for Subsidies and "Internal Dumping". Remedies are available under our trade laws when imports from government-supported Japanese industries disrupt the U.S. market with imports which are subsidized or which violate the antidumping laws. We suggest that similar sanctions be adopted immediately against U.S.-based plants owned by the Japanese which are wholly or partially financed and operated in accordance with the designs of the Japanese economic planners. A subsidy equalization tax would be designed to force all sellers in the U.S. market to pattern their marketing practices in accordance with the dictates of a market economy such as exists in the United States. The goal, of course, is to neutralize the structural advantages of foreign-owned firms whose parent companies are participants in "planned economies" and thus are supported in their worldwide business efforts by a foreign government.

In addition to the subsidy equalization tax, an equalization tax should be imposed on "internal dumping" in the United States by foreign-controlled U.S.-based plants. Traditional dumping involves shipments from foreign-based plants into the United States at prices below those charged in the foreign market. One purpose of dumping is to dispose of excess foreign production. Other goals might be to cripple a U.S. industry, prevent its growth and foreclose development of new products. These latter goals can also be achieved by "internal dumping," whereby the foreign firm establishes a plant in the United States and sells its output at very low prices.

RESPONSE OF ALAN WM. WOLFF TO ADDITIONAL WRITTEN QUESTIONS POSED BY  
SENATOR BENTSEN

*Question 1.* You referred to the need for a "more effective" American commercial presence in foreign capitals. After your recent trip to the Far East, do you have any additional thoughts on how to make our overseas commercial presence more effective?

Answer. With the effectiveness of President Carter's Reorganization Plan No. 3 of 1979, the commercial officers at various embassies abroad will be transferred from the Department of State to the Department of Commerce. This will provide a major opportunity to enhance our commercial representation abroad. Attention will be needed to developing a career "U.S. Commercial Service" that can attract dedicated individuals to the government to help be catalysts for U.S. export efforts. The Government can never substitute for private sector initiatives to sell U.S. products abroad, but it can provide support primarily in the form of information to American businessmen about foreign market opportunities and conditions and information to foreign purchasers about the availability of U.S. products. The Government can also provide official backing when this is needed to reduce or eliminate foreign barriers to trade.

In many of our embassies abroad, there is substantial expertise with respect to the host country's market. The commercial officers ought to be able to mobilize the energies of the embassy from the Ambassador on down to give attention to U.S. export opportunities as each of these officials perform their duties. The Embassy's Economic Minister and Counselor can give particular attention to the host government's policies that affect United States exports, and to an increasing degree can with the help of the Ambassador give direct support to the sale of American goods, particularly where it is the foreign government that is the purchaser.

As I have testified previously, I believe that the U.S. Commercial Service should make provision for senior internships by private sector corporate executives who could take a two or three year tour of duty with the government, thus providing a very healthy interchange between the private sector and the Commercial Service.

*Question 2.* The President's recent trade reorganization proposal was generally billed as a first step in the right direction. Do you have any thoughts about what the next step should be in terms of further reorganization of our trade bureaucracy?

Answer. Ultimately, I believe that the U.S. Government should move towards the adoption of a reorganization of trade functions along the lines of that proposed by Congressman Gillis Long. I believe that a single trade agency should eventually be established that would handle all trade issues.

As an intermediate step, that is within the terms of Reorganization Plan No. 3, I would suggest that policy with respect to all international commercial negotiations be coordinated by the interagency Trade Policy Committee. This would include policy for negotiations concerning aviation, maritime affairs, transfer of technology, information services, official export credits, procurement practices in connection with official development assistance, telecommunications, banking, anti-trust policy (including restrictive business practices), etc. There is a very long list of negotiations affecting U.S. commercial interests. A first step would be to conduct a survey of the negotiations that take place and determine how best to coordinate these negotiations. Currently, most of these matters are so compartmentalized that United States policy is not formulated as part of a coherent whole, and inconsistencies are likely to occur. Leverage is lost.

Increasingly, the attention of the Executive Branch will have to be turned to the problems of the service industries, where the international rules are few and government obstacles are growing over time. The Office of the Special Trade Representative has begun bringing international attention to this question and a major effort is warranted to follow through on this initial work.

*Question 3.* In Mr. Sevin's testimony, he mentioned the possibility that some products could be obsolete before the tariff reductions negotiated as part of the Tokyo Round would have any effect. How will tariffs on new products be handled after the latest round of trade negotiations?

Answer. Trade negotiators are far from omniscient, but I believe that our score in this regard will be better in this negotiation than it was in the 1967 Kennedy Round. This improvement will be large'y due to relying heavily on private sectors advice as to the objectives for these trade negotiations.

However, the rate of technological change has also increased markedly, and therefore new products will continually be emerging, that were not contemplated in the original negotiation. These products will be classified by the Customs Service and the courts under the existing nomenclature of the Tariff Schedules of the United States. This can give an unintended penalty or benefit (a higher or lower duty) than was intended in the reciprocal bargaining that took place during the round of negotiations. This can be remedied by renegotiating the tariff applicable to the new product to create a separate tariff item for it. In some instances, the development of new products was foreseen and basket categories were created to include the products as they are developed. This is particularly true in the case of chemicals.

*Question 4.* In your discussion of exchange rates, you noted that energy (or raw material) dependence can depreciate the value of the yen and thus strengthen the international competitiveness of Japanese industry. England suffers the opposite problem as the North Sea oil induced appreciation of the British pound weakens the competitive standing of British industry. Are you suggesting that the future economic wealth of nations will be substantially dependent on the high technology industrial sector and that U.S. trade and exchange rate policy should be directed to strengthening that particular sector?

*Answer.* Much of the future of the industrialized countries is bound to be dependent on production of high technology goods. The United States, of course, has a broad range of goods in which it has now, and is likely to maintain in the future, a substantial comparative advantage, both in high technology products and in agriculture. With respect to international competitiveness of our high technology goods, government policy should help to assure that sufficient capital is available for research and development and production of these items. This issue will be no doubt given attention in the course of consideration of the "Capital Recovery Act" proposals which will be before the Congress next spring.

Exchange rate policy is not a suitable tool for preserving the future international competitiveness in high technology goods, although, of course, it has a role in the overall competitiveness internationally of U.S. products. My purpose in pointing to the experience of recent years with the dollar-yen exchange rate is to indicate that exchange rate changes cannot be relied upon to bring about complete adjustment on a sectoral basis. Too many other factors have a major impact for the floating exchange rate system to be seen as the sole "policy tool" for this purpose.

*Question 5.* In Mr. Sevin's remarks, he contends that the ability of the American semiconductor industry to export to Japan has been limited by their inability to make direct investments in the Japanese economy. You make a similar comment on page 9 of your prepared remarks with regard to the distribution system. Should we consider restrictions on direct foreign investment that have a significant impact on trade flows as an unfair trade practice that would fall within the purview of Section 301 of the Trade Act of 1974?

*Answer.* I believe it would be premature to consider offsetting actions that might be taken with respect to foreign investment policies of other countries. First, one would have to construct a policy as to the foreign direct investment that the United States wished to favor, both with respect to outward foreign direct investment and inward foreign direct investment. The restrictions on direct investment in Japan, including those applicable to the distribution system and to retailing activities, however informal, do have an impact on the structure of Japanese trade, and contribute to the relative imperviousness of the Japanese market to imports. Manufacturing investment in Japan often has a pull-through effect on purchase of goods from the country from whose nationals made the investment. This point is addressed in the study of the American Chamber of Commerce in Japan on investment in Japan, which I recommend to the Committee.

*Question 6.* In your prepared remarks, you mentioned the "special surveillance product list" of Japan's Ministry of International Trade and Investment. If a firm ignored the MITI guidelines, what range of sanctions could MITI bring to bear to encourage the firm to follow government policy?

*Answer.* I would not hold myself out as an expert on corporate behavior in Japan and how it can be influenced by the government in Japan. Obviously there is a strong feeling in Japanese industry that cooperation with the government is preferred conduct. The closeness of the Japanese government to the private sector and the interrelationships among the Japanese government, manufacturing sector, trading companies, and banking system, have been remarked upon extensively by

those who have studied the Japanese economy. In a highly-leveraged system of corporate finance, the access to capital for increasing production contrary to government policy (and therefore arguably contrary to sound economic policy) might be difficult. This need not be considered a direct sanction. I suspect that, in the main, corporate policy is greatly influenced by a desire to be cooperative with the government wherever possible. The adversary relationship that so often characterizes relations between our private sector and U.S. government agencies is far less in evidence in Japan.

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RESPONSE OF H. WILLIAM TANAKA TO ADDITIONAL WRITTEN QUESTIONS POSED BY  
SENATOR BENTSEN

*Question 1.* In the course of your oral testimony, as well as in your prepared remarks, you pointed to America's low rate of productivity growth as a major explanation of our current trade problems. You also suggested that relative to Japan, labor strikes had been an additional cause of America's lagging economic performance. In Mr. Sevin's oral response, he pointed out that the semiconductor industry had never had a strike and benefits from a very rapid increase in productivity. Do you agree with Mr. Sevin's assessment of the semiconductor industry?

Answer. Although Mr. Sevin is probably correct in stating that the semiconductor industry has few labor problems and benefits from rapidly-increasing productivity, it is perhaps a unique case, the exception that proves the rule. Equally significant to the Committee's inquiry is the fact that the semiconductor industry illustrates the way in which American manufacturers avoid domestic labor and productivity problems by establishing manufacturing plants abroad.

Because of high labor rates and incidence of strikes in the United States, at least a dozen major semiconductor manufacturers have established overseas plants in less developed countries for the purpose of undertaking labor-intensive operations, such as assembly. Mostek, for example, has plants in Malaysia, the Philippines and Taiwan which we understand assemble components originating in the U.S. The unfinished or partly assembled products are generally shipped back to the United States under the provisions of TSUSA items 806.30 and 807.00, which provide that only the value added abroad will be dutiable. Shipments of this type count as foreign imports and in 1977, for example, accounted for over 80 percent of the total dollar volume of all U.S. imports of transistors and integrated circuits. An analysis of a recent annual report of one U.S. company shows that 76.6 percent of its employees, but only 49.9 percent of its capital investment and 30 percent of its sales, are offshore.

The result of this fragmentation of the manufacturing process is that the labor-intensive—i.e., strike-prone and low-productivity—aspects of manufacturing are located outside the United States, while the high-productivity, capital-intensive side of manufacturing is retained at home. Although this might be regarded as maximizing comparative economic advantages, such dis-integration of manufacturing has in fact postponed the full and integrated automation of semiconductor production in the United States which is now the norm in Japan.

U.S. semiconductor companies are vertically integrating their manufacturing facilities located abroad, allowing them to produce a complete line of semiconductor products. This has substantially increased sales of U.S. companies in foreign markets because these products made offshore are cost effective and priced competitively. However, every sale of a finished, assembled product manufactured in a foreign plant is one less sale from a domestic plant. Therefore, the semiconductor companies' practice of integrating their foreign operations tends to reduce exports of semiconductor products from the United States.

TSUSA items 806.30 and 807 have encouraged U.S. manufacturers in general, not just in the semiconductor industry, to establish overseas manufacturing plants to partially assemble products or components. As I have already indicated, this may adversely affect the quality of production technology in the United States and the quality of the ultimate product. To the extent that items 806.30 and 807 encourage U.S. companies to take advantage of cheaper foreign labor they correspondingly discourage these companies from implementing new, more efficient product technology in the United States. Failing to use the latest production technology will impact on the ultimate quality and competitiveness of the product.

Having noted that Mr. Sevin's assessment, while misleading, is technically correct, I must go on to say that the U.S. semiconductor industry has other chronic

problems which act as disincentives to U.S. exports. Foremost among these is a current lack of manufacturing capacity. According to Bruce Threewit, Product Marketing Manager for Fairchild Camera and Instrument Corporation's MOS Products Division, U.S. demand will exceed domestic supply by a factor of four in 1980 and by a factor of 2.5 in 1981, taking 1980 production capacity increases into account. As one might expect when demand exceeds supply to this degree, sales are booming. According to an article in the November 14, 1979 issue of the Wall Street Journal, worldwide shipments of the U.S. semiconductor industry in 1979 will reach 6.5 billion, a 36 percent increase over 1978.

I have surveyed the Securities and Exchange Commission's files of the latest Form 10 Q's of a dozen of the largest semiconductor firms and have discovered that not only are sales up in 1979, but net earnings have risen an average of 35 percent. The latest figures are not yet available from Mostek, but for the first calendar quarter of 1979 the company had sales of \$40 million, up from \$29 million for the same period last year. Moreover, Mostek had completely sold their 1979 production of 16K RAM's by June of this year. Needless to say, the U.S. semiconductor industry is not only healthy, it is thriving.

As I read Mr. Sevin's statement, the U.S. semiconductor firms admit this, but are concerned that they will not be able to raise sufficient capital to make the investments necessary to be competitive in the next generation of semiconductors and end products. They appear to argue that the Japanese either have engaged in predatory pricing or dumping in the U.S. market, thereby keeping U.S. producers from raising their prices. If this is their position, it is contrary not only to the facts but to logic. Any sensible analysis of current demand, and prospects for increased demand, would show that the Japanese have no reason to price their products unreasonably. Not only are they operating at current capacity, but the demand outstrips both present and future worldwide manufacturing capacity. In any event, a report in the November 8, 1978 issue of Electronics states that price increases by the U.S. firms are likely, indicating that Japanese pricing has not stopped market-justified price hikes.

*Question 2.* According to Mr. Sevin, the American semiconductor industry has had much more success in its dealings with Europe than it has with Japan. Mr. Sevin contends that the explanation is not American productivity or quality within the semiconductor industry, but Japanese barriers to trade and investment. Would you agree with Mr. Sevin's assessment of the situation?

Answer. No, I do not agree with Mr. Sevin's assessment. The disparity between the success of the American semiconductor industry in Europe and its success in Japan can be explained by examining the nature of the two markets.

America was and is the leader in semiconductor technology. The United States has been responsible for the invention of all but two of the major semiconductor devices since 1948. Because of this technological superiority, the American semiconductor industry has dominated the worldwide market and continues to do so. From 1963 to 1967, U.S. manufacturers had an average 85 percent share of the worldwide semiconductor market. From 1968 to 1973, their average share was 72 percent.

Companies based in the United States have managed to dominate completely the European market because they have virtually no competition. Of the 25 largest semiconductor firms ranked by sales, only two are based in Europe, Philips and Siemens. All the other European firms have less than one percent of the worldwide market.

One reason for this has been the European companies' relatively sparse outlays for research and development. For example, Germany is the world's third largest market for semiconductor products, yet their research and development expenditures have lagged far behind the U.S. and Japanese firms. For example, Japan's very large scale integrated circuit (VLSI) program has been under way since 1975, and the U.S. program was initiated before that, but Germany got its VLSI program off the ground just last year. Thus, the relatively high U.S. market share in Europe is due to the initial dominance of U.S. companies and the subsequent lackluster competition from European producers.

The history of the Japanese market is different. Initially United States manufacturers enjoyed the same market share in Japan as they did in the rest of the world. In the early 1960's the Japanese domestic semiconductor industry began to develop. The way it did so was most unusual, and was unique to Japan. In the late 1960's and early 1970's, all the current large Japanese producers, Toshiba, Hitachi, Mitsubishi Electric, Matsushita Electric, Fujitsu, and NEC, were manufacturers of end products incorporating semiconductors. They sought out and obtained licenses and other forms of production technology from U.S. manu-

facturers, then vertically integrated manufacturing back to the production of the basic electronic device, the semiconductor. Of course, the market share of U.S. produced semiconductors in Japan fell off because, to the extent that these Japanese manufacturers could produce semiconductors in-house, they curtailed purchases from abroad.

Thus the principal reason the U.S. market share fell was that the former purchasers of semiconductors, the endproduct manufacturers, began producing their own semiconductors. As the in-house capacity of the Japanese grew, it eventually exceeded their in-house requirements and the manufacturers began to sell their excess production, first within Japan and ultimately to the rest of the world.

During this transition period, the Japanese government perceived that electronic products would be a market of vast export potential in the coming decades. The government encouraged the semiconductor companies with tax incentives and guidance—in the form of the Electronic Industry Development Provisional Act of 1957, which allowed the government to formulate industry policy objectives—but with little direct assistance, such as loans, subsidies, or R&D grants.

The failure of the United States semiconductor manufacturers to regain the market share they had originally held was due not only to the growing Japanese domestic industry, but to quality and service deficiencies relative to the available Japanese products. Japanese semiconductor users purchasing from American firms complained that the American products had a much higher rejection rate than comparable Japanese products and often were cosmetically unacceptable. In addition, the advantage of having local suppliers, who could perform custom manufacturing and design components especially suited to the end product, caused Japanese semiconductor purchasers to favor local semiconductor manufacturers.

Thus, the barriers to trade that Mr. Sevin complains of, where they exist, are mostly of a practical nature and probably not due to protectionist policies.

The relationships between the various geographic markets can perhaps best be put in perspective by the following table relating to one significant semiconductor product, the metal oxide semiconductor (MOS) memory unit:

	Percent of worldwide—		
	Production, by nationality of plant ownership	Production by location of plant	Consumption, by country
United States.....	80	65	56
Japan.....	17	20	23
Western Europe.....	2	14	17
Other.....	1	1	4

These figures show that the United States continues to be the only net exporting country or region. They also show the extent to which U.S. companies have pre-empted the European market, which consumes 17 percent and produces 14 percent of world MOS output, but whose domestic-owned companies account for only two percent of world output.

Most interestingly, the figures show that Japanese-owned companies account for only 17 percent of world production. An additional three percent of world output is produced in plants located in Japan but owned by foreigners (i.e., U.S. companies). Japanese consumption, however, is 23 percent of the world total. One can infer that Japanese-owned plants produce 74 percent of Japanese consumption; 26 percent of Japanese consumption is supplied by U.S. companies, half from U.S.-owned plants in Japan and half imported. In fact, these percentages of Japanese market share attributable to U.S. companies are probably low, since part of the production of Japanese-owned companies is exported from Japan.

*Question 3.* I was very interested in your discussion of Japanese industrial policy and the intricate manner in which government and business cooperate in Japan. I wonder if you could elaborate on a point or two:

First, to what extent is the Japanese government involved in promoting Japanese exports to the United States?

Second, how does the Japanese export promotion effort compare to that of the United States—here I am thinking of budgetary expenditures including everything from advertising to trade association activities?



Third, to what extent are the actual export policies of individual Japanese companies directed by the Japanese government?

Answer. First, as to the extent of Japanese government involvement in promoting exports to the United States, I think it is accurate to say that for the past several decades Japan has followed an ambivalent export policy, particularly regarding exports to the United States. On the one hand, as a general matter the government has of necessity encouraged exports as being essential to national economic survival; on the other, it has regulated and imposed limits on exports in certain industries in order to avoid disrupting markets in other countries, to discourage pricing at dumping levels, and otherwise to avoid confrontations with Japan's trading partners.

As I noted in my testimony, Japan has virtually no raw materials and is energy poor. Early on, leaders in both industry and government realized that Japan must export if it is to earn the foreign exchange necessary to pay for essential imports. They understood that Japan would have to emphasize industries which utilize skills Japan had or could develop and which make products competitive in the world marketplace. Moreover, both industry and government realized that, until very recent years, the size of the Japanese domestic market was too small to support the rapid growth and economies of scale which maximize investment return over the long term. Only exports could provide the market size necessary to success.

These mutually shared perceptions mean that the Japanese government does not in fact have to involve itself in massive export promotion or subsidy to achieve national goals. It is noteworthy that the American consumer electronics products (CEP) industry, for one, has for years sought to document charges of Japanese subsidies so as to justify the imposition of countervailing duties. In 1972, segments of that industry filed complaints resulting in massive investigations into whether the Japanese government supported CEP exports with "bounties or grants. After an exhaustive inquiry, the Treasury Department dismissed the complaints on grounds that any subsidies were at best de minimis.

Included in the record of that case is an airmag from our Embassy in Tokyo to the State Department on "Japan's Export Promotion Program." Although written in 1972, I believe it still reflects the situation today. The summary portion of the airmag, a copy of which is enclosed with this letter, concludes as follows:

"It is the Embassy's conclusion that all of the Japanese Government's promotion activities separately and in sum are not major factors in accounting for Japan's excellent performance in export markets. Most of Japan's direct trade promotional work is carried out by trading firms and the Government's role, other than in assisting small and medium firms, is minimal. The Japanese Government's financial assistance of exports, other than to developing countries, is also believed to be of limited significance. The basic factors accounting for Japan's success as an exporting nation involve the domestic willingness to keep prices at competitive levels, to innovate and to make substantial efforts to service even relatively small markets, and overall Government-business attention to foreign trade which far surpasses that of most other countries."

Despite official U.S. government determinations of nonsubsidization such as that in the CEP countervailing duty case, many American businessmen persist in the false assumption that the Japanese government targets industries having export potential and then subsidizes them with direct grants for research and development and with loans, allowing a high debt-to-equity ratio. The truth is that the Japanese government provides only 30 percent of the funds spent on research and development in Japan, while industry supplies 70 percent. Half of the government funds are allocated to universities and research institutes, which tend to distrust government and be unconcerned with practical applications of R&D.

In the U.S., the ratio of public to private R&D expenditures has historically been the reverse of that in Japan—70 percent government, 30 percent private. Moreover, Japan devotes relatively fewer funds to R&D than does the U.S. In 1974 the United States expended 2.29 percent of its GNP on research and development, whereas Japan expended 1.99 percent.

As for loans, it is true that the Japanese government has evidenced its support of the VLSI program by making a loan of \$100 million to finance the \$250 million project. The balance is being supplied by the Japanese industry. The entire loan will be repaid by the companies benefiting from the products developed. And while it is true that many Japanese companies are far more leveraged than are U.S. corporations, some of the most competitive Japanese concerns, such as Mitsubishi Electric and Sony, are capitalized in equal portions by equity and debt.

The nature of the support accorded to Japanese and American exporting companies by their respective governments is of course determined by the differing circumstances of the two nations. The United States finds itself as the principal military defender of the West and Japan, while Japan maintains only modest defense forces. Consequently, the U.S. military provides a vast market for high-technology products, many of them produced by small but growing concerns which are fostered in a variety of other ways as an aspect of national security policy. Conversely, the Japanese government has resources available, since they are not needed for defense purposes, which can be devoted to other forms of support for its high-technology companies, including encouragement of commercial, rather than military, applications of R&D.

A second assumption of American businessmen is that government and industry in Japan cooperate so closely that they act as one organism, "Japan, Inc." This attitude is partly attributable to the fact that American business is essentially hostile towards the government, with which it has an adversarial relationship. Consequently, it is difficult for American businessmen to acknowledge that cooperation between business and government can be both part of capitalism and an acceptable method of competition.

In Japan, however, government has historically played a paternalistic role with respect to business, and businessmen look to government for guidance. For example, the Economic Planning Agency presents long-term plans that are merely advisory, intended to indicate the most efficient directions for the economy to move in and the areas where government support should be focused. While this is not sufficient to establish a consensus on priorities, it does give Japanese businessmen a sense of purposefulness and narrows the dimensions of their differences. The Japanese system is not tightly centralized and is pragmatically flexible, as shown by their response to the recent trade imbalance. The Ministry of International Trade and Industry and the Ministry of Finance both are emphasizing imports, struggling to overcome current problems in the balance of trade.

American misunderstanding of the Japanese are reflected in a comment, in a somewhat different context, of Robert W. Barnett, a former Deputy Assistant Secretary of State for East Asian and Pacific Affairs in Foreign Policy (Spring 1974, at page 153) :

"Japan's deficiencies are not lack of purpose or ineffective performance; Japan merely lacks the talent to elucidate, at home and abroad, its virtually irreversible national commitments. History may reveal that these commitments proceed from principles others must embrace for the balance of this century, or perish."

I mentioned earlier that in some instances Japan regulates and limits exports in order to assure orderly, non-disruptive competition with foreign concerns in their home markets. Once again, the consumer electronic products industry serves as an example. A variety of devices have been used by the Japanese government to moderate exports to the U.S., from the "check-price" system of minimum export prices, designed to guard against dumping and predatory price wars, to the present orderly marketing agreements which limit exports of color television sets from Japan to the United States.<sup>1</sup>

The second part of this question asks for a comparison of the Japanese export promotion effort with that of the United States in terms of budgetary expenditures. Although this is a subject well outside my expertise, perhaps a few comments from my perspective are in order.

It is difficult to draw a meaningful comparison along the lines you suggest because of the significant export role of the private Japanese trading companies (JETRO), a semi-autonomous, "mixed" entity. The United States has no comparable organizations. The Department of Commerce is the official agency which operates the principal export promotion program, which was funded in 1979 with \$19.6 million.

The trading companies are of considerable assistance to Japanese exporting companies particularly smaller manufacturers, in tailoring their export efforts to the needs of target markets. They provide market, product, managerial and industry information, based on in-depth studies of foreign markets, principally to the less-sophisticated companies. The trading companies also act as intermediaries between other firms, expediting a variety of transactions rapidly and efficiently. They help manufacturers to relocate outside Japan and to diversify to accommodate changing economic conditions. The trading companies have been

<sup>1</sup> An informative discussion of the impact of Japanese industrial policies on individual companies is found in Rapp, William V., "Japan: Its Industrial Policies and Corporate Behavior," "The Columbia Journal of World Business," Vol. XII, No. 1, Spring 1977, p. 38.

remarkably successful in bridging language and cultural gaps between Japan and its trading partners.

JETRO is, as noted, a semi-autonomous government agency whose trade promotion efforts encompass both imports and exports. Forty-eight percent of its fiscal year 1974 budget of \$63.3 million was provided by MITI, which retains discretionary control over it, and the remainder was provided by private businesses and promotional activities. According to the Japanese Embassy, MITI's support to JETRO in fiscal year 1978 was 9.8 billion yen, which is about \$39 million at an exchange rate of 250 yen to the dollar.<sup>2</sup> JETRO is a multi-function organization which supplements rather than competing with the trading companies. It assists primarily in the earlier stages of export marketing, organizing product exhibitions for Japanese companies at trade fairs and paying about 25 percent of the costs of exhibiting. JETRO performs or underwrites market surveys and publishes the results. It maintains extensive information services, including a computerized retrieval system. It also arranges trips to Japan by high-level foreign businessmen and officials and provides them market research data in order to encourage imports.

JETRO is not the only government-related trade promotion entity. MITI supervises the export financing and insurance programs mentioned below, supports research organizations and training in various types of overseas technical co-operation, finances non-JETRO market research, operates a floating trade fair, and subsidizes the Japan Overseas Development Corporation, which financed about \$5.2 million in joint ventures in developing countries in the first six years of its existence. All told, the Japanese government, through MITI and the Ministry of Finance, spent an estimated \$60.7 million on export promotion programs and services in 1976.

As for tax incentives to exports, the United States offers postponement of taxes through the Domestic International Sales Corporation (DISC). The 1977 Annual Report of the Treasury on the DISC (April 4, 1979) estimates that the DISC was responsible for \$3.9 billion in exports over what would have been exported without DISC, although acknowledging that this figure may be somewhat overstated. The estimated cost of the program, in terms of lost tax revenues, was \$780 million, down somewhat from the 1976 figure of over \$1 billion because of certain tax reductions. Plainly, this single cost, which could be characterized as an export subsidy, greatly exceeds what the Japanese government directly expends on export promotion. In order to be exact, however, there are other factors that should be included in the Japanese expenditures, principally tax incentives to exports, for which no estimates of costs were easily available, as well as export financing and insurance.

The specific tax incentives to exports provided by Japan include:

- (1) Deduction of a percentage of export profits from taxable income during a period of overseas market development;
- (2) Deduction for foreign exchange losses on net long-term receivables;
- (3) Special deductions for a portion of the proceeds of certain overseas transactions, such as technology transfers and the rendition of technical services abroad; and
- (4) Between 1961 and 1972, accelerated depreciation for export sales in general; currently accelerated depreciation only for electronics industry products, expiring in 1979.

I am afraid that in the area of export financing and insurance I can offer no useful figures on comparative budgetary impacts. The Export-Import Bank of the United States engages in all forms of export financing, including direct loans to foreign borrowers and a variety of insurance and guaranty programs. While it carries on all its operations without using any appropriated funds, Eximbank's "net lending" is reflected in the budget. In Japan, the Export-Import Bank of Japan is responsible for direct lending but MITI handles insurance and guarantees. I do not have available the impact of their respective operations on the Japanese budget.

All told, however, the direct support of the Japanese government to exports does not appear to be very large. As the Congressional Research Service has said:

"What is clear is that the extent of government-assisted and/or funded export

<sup>2</sup> All of the other data on Japanese export promotion was taken from "Export Stimulation Programs in the Major Industrial Countries: The United States and Eight Major Competitors," Library of Congress 1978, a document prepared by the Congressional Research Service for the House Committee on International Relations.

promotion programs is extremely small when compared with the efforts made by Japanese firms and associations on their own."<sup>3</sup>

The third question asks to what extent the actual export policies of individual Japanese companies are directed by the Japanese government. In my experience, such direction has been limited to the regulatory sphere and has not extended to affirmative, or promotional, direction. As indicated earlier, regulation may involve minimum export prices, quantitative restrictions, or both. They may also include minimum design and a quality standards. Such export regulations may take the form of mandatory controls or administrative guidance.

Over 90 Japanese industries have been subject to a variety of restraints on their exports. For example, as a result of pressures on steel producers to limit their exports voluntarily, particularly to the United States, producers implemented voluntary quotas and established minimum prices designed to prevent market disruption in the countries to which they sold their products.

*Question 4.* With so much reliance on government direction and a particular form of planning, how does the government plan for foreign-based multinational firms with operations in Japan? What array of sanctions does the government have to encourage cooperation of reluctant firms, and are there any special provisions that apply to the foreign firm?

Answer. At the outset I would take issue with the opening premise of this question, namely, that the Japanese economy is based on "reliance on government direction and a particular form of planning." As my earlier comments suggest, government direction is of limited scope and planning is largely along broad, macroeconomic lines which point to goals without imposing detailed means for achieving them.

I would also note the ambiguities inherent in this question, since foreign-based multinational firms may operate in Japan through one of a number of legal entities: A wholly-owned corporation organized under the laws of Japan, a branch office located in Japan, or a joint-venture Japanese corporation partially owned by a Japanese company.

Given these qualifications, I believe the answer to the first part of your question is that companies located in Japan, regardless of the nationality of their ownership, are treated as part of Japanese industry and the economy for purposes of government planning and direction, and are therefore generally subject to the same restrictions and incentives as are companies which are entirely "Japanese."

As for the sanctions available to the government to encourage the cooperation of reluctant firms, I can speak only to the question of sanctions for refusal to abide by export restrictions. The various Japanese laws relating to foreign trade give the Ministry of International Trade and Industry (MITI) broad powers to regulate export trade. Violators of these laws, as implemented by MITI, may be punished by fines, imprisonment, or the suspension of restriction of their exports. No special provisions are made for "foreign" firms.

*Question 5.* Finally, you detailed a number of areas where the United States had erected legal impediments to our own exports. In looking specifically at our antitrust laws, do you feel that the Webb-Pomerene Act provides a sufficient antitrust exemption to stimulate exports? What recommendations would you make for change in the Webb-Pomerene Act?

Answer. I believe that, especially with respect to high technology products, the subject of antitrust law as it impacts on exports does bear close examination. I do not think, however, that the Webb-Pomerene exemption, even if expanded, will significantly contribute to export expansion.

#### A. EFFECT ON WEBB-POMERENE ACT ON EXPORT PERFORMANCE

Proponents of amending the Webb-Pomerene Act and proponents of abolishing it entirely have agreed that, to date, it has failed as a vehicle for substantial export promotion.<sup>4</sup> Critics of the Act, including the Department of Justice, have argued that no antitrust exemption is necessary for effective export activity.<sup>5</sup>

<sup>3</sup> "Export Stimulation Programs . . .", *supra* (see footnote 2) at 203.

<sup>4</sup> See, e.g., Statement of Luther H. Hodges, Jr., Under Secretary of Commerce, before the International Finance Subcommittee of the Senate Committee on Banking, Housing, and Urban Affairs, September 17, 1979; Statement of Daniel C. Schwartz, Deputy Director, Bureau of Competition, Federal Trade Commission, September 18, 1979.

<sup>5</sup> See Statements of Ky P. Eving, Jr., Deputy Assistant Attorney General, Antitrust Division, Department of Justice, before International Finance Subcommittee, September 18, 1979 and before Senate Committee on Governmental Affairs, October 31, 1979.

They argue that if uncertainty over the scope of any exemption has restricted the growth of export associations, the best solution is to scrap the exemption and rely on the "Rule of Reason." The National Commission for Review of Antitrust Laws and Procedures and the F.T.C. each has called for careful consideration of this option.<sup>6</sup>

Proponents of expanding the Act have argued that, if uncertainty surrounding the antitrust exemption were removed, more, and more active, associations would exist. In my opinion, certainty sufficient to increase association activity significantly can be achieved only through undesirable curtailment of antitrust enforcement.

The lack of clear precedent caused the Justice Department in 1977, after years of dialogue with the President's Export Council and other business groups, to publish the "Antitrust Guide for International Operations." Yet, the two decades prior to 1977 saw a huge amount of international licensing and joint venture activity. The fact is that American businessmen were willing to and did proceed notwithstanding the uncertainty.

I believe, then, that the benefits of curtailing antitrust jurisdiction sufficiently to encourage substantial export association activity are illusory. In my opinion, a significant increase in association activity would occur only if members were seeking an antitrust haven not necessary, or even ancillary, to export expansion. If the risky activity spurring new association membership were, indeed, necessary or ancillary to export expansion, businessmen would already have tried it. For years the Department of Justice has called for examples of such activity that has been foregone because of antitrust fears, and I am not aware of any such examples being cited.

With respect to high technology products on which this Committee has been focusing, I think it is even less likely that expanding the Webb-Pomerene exemption would be useful. I also think that the same can be said for legislative proposals to establish American trading companies on the Japanese model. Experts inside and outside of government have observed that Webb-Pomerene associations, and even successful Japanese trading companies, are least suited for promoting highly differentiated, high technology products, which require close co-ordination between marketing and production functions. Recently Assistant Secretary of the Treasury Bergsten testified:

"Webb-Pomerene associations have not worked to promote exports by small producers of differentiated products. Because those producers' marketing success depends so heavily on distinguishing their products in small ways from the products of their competitors, cooperative behavior is generally not attractive to them. Their exemption from antitrust laws does not remove the underlying sense of competition that exists between them and thus is of limited significance in promoting joint export efforts."

Similarly, Frederick W. Huszagh, Executive Director of the Dean Rusk Center, University of Georgia, told the same Senate Subcommittee:

"As the opportunities diminish for [capital, information and scale] cost reductions . . . the vitality of Japanese exports and of the trading companies must rest increasingly on manufacturers' capacity to provide improved service on their products in foreign locations and develop new technology as opposed to adapting European and U.S. technologies to Japanese production techniques. Some feel that trading companies are not well suited for success in these areas as opposed to extension of the manufacturers' capabilities, and thus will play a declining role in export expansion. The only exception would be in the commodities area where research and development and servicing are relatively unimportant attributes of sales success."<sup>8</sup>

#### B. ACTIVE GOVERNMENT SUPPORT OF EXPORT-RELATED ACTIVITIES

I am optimistic that the government, in addition to approving deserving ventures passively, might take an active role in encouraging and financing them. In my full statement on October 10 I noted that technological investment is an area in which we appropriately can emulate the Japanese experience. The Japanese government consciously fosters key industries, and disinvests in others,

<sup>6</sup> See Statement of Daniel C. Schwartz, *op. cit.*

<sup>7</sup> Statement of the Honorable C. Fred Bergsten, Assistant Secretary of the Treasury for International Affairs (Sept. 17, 1979).

<sup>8</sup> Statement of Frederick W. Huszagh (Sept. 17, 1979). See also Statement of Fred C. Bergsten, *id.*

depending on the country's institutional and economic circumstances. The United States, accustomed to bountiful raw materials and energy resources, has been more inclined to participate in the nation's industry by stressing space and defense, and by bolstering low-technology, labor-intensive industries. The result is that high technology items of the sort that should be attractive to overseas consumers receive little or no support.

I think the prospect of guiding technological investment in non-space or defense areas raises two basic questions for government policy makers: (1) is government investment in such areas compatible with our institutions and our commitment to a free market economy; and (2) if so, how do we choose proper targets?

I think the first question can be answered positively. In times of crisis the government has invested temporarily in areas previously limited to private investment, and with good results. During the Second World War it built aluminum plants, which were later disposed of in a manner calculated to deconcentrate the industry. Government decisions launched the space program and its technological "spin-offs". Today the energy crisis, in the administration's judgment, is serious enough that government investment in synthetic fuels is warranted.

The government, as I have mentioned, also actively resists disinvestment in industries where it would otherwise seem appropriate. Given the record of positive and negative investment in times of political or economic crisis, I don't see why investment in a time of crisis in technology and international trade should be inappropriate.

As to specific criteria for such investment, I think they should reflect established antitrust policy concerns. The U.S. government should not be in the business of discouraging effective competition and competing investments in new technology just because federal funds are being made available. Where, however, it appears that a joint technology effort among potential competitors would seem to have more long-term competitive promise than separate development, the government would appear to have several options. First, separate government investment with each potential competitor might obviate the need for cooperation and/or temporary competitive restrictions. In such instances, the judgment might be that separate development of competing approaches is more promising competitively, if adequately funded, than joint efforts on a single approach. Thus, in supplying venture capital, the government would be preserving potential competition.

If, on the other hand, the situation is one in which joint development appears to be a better investment under all circumstances, government participation can increase potential competition in two ways: (1) To the extent that joint corporate investment can be considered necessary or ancillary to some competitive restraint, government investment reduces the justification for such restraint pro tanto; and (2) government participation assures an active negotiating role for the government in insisting on the greatest possible sales competition. In short, government investment, by lowering the private investment threshold, lowers the extra-competitive return on successful investment that a firm might feel compelled to expect before risking a go-ahead decision.

There are, of course, many consequences, details, and ramifications to a program of government supported investment in export-related technology. I cannot explore all of them here; I can merely suggest that the idea is worth pursuing.

Enclosure.

[Airgram]

JAPAN'S EXPORT PROMOTION PROGRAM

FEBRUARY 18, 1972.

DEPARTMENT OF STATE.

This airgram brings up to date the Embassy's last full report on Japan's export promotion programs (Tokyo's A-2130, November 6, 1968). It includes detailed descriptions of measures currently in force, and assessments of their significance. For purposes of description, the Japanese governmental programs can be broken down into the three categories outlined below. In addition, export trade promotion is carried on by a quasi governmental organization, JETRO, which is fully described in Tokyo's A-33 of January 20, 1971, and A-235 of April 1, 1971.

## SUMMARY

*Export related tax incentives*

Perhaps in part because the Embassy had never previously provided an assessment, the belief has grown up that export related tax incentives play a significant role in Japanese export performance. In actual fact, even in their heyday, such measures played a relatively insignificant role in accounting for Japanese overall export performance and measures have been severely curtailed over the years. In 1968, a U.S. tax expert estimated the amount involved for an actual large Japanese corporation to be less than 1.0 percent of the firm's export sales. In JFY 1971, export-related tax benefits to all Japanese firms were equivalent to less than 0.01 percent of the value of total exports. This ratio will be even lower in JFY 1972, largely as the result of a recent GOJ decision to abolish the special depreciation allowance.

*Tariff rebate system*

The Japanese tariff rebate system takes the form of the usual drawback and bonded area provisions common to most other countries. In addition, there are a limited number of fixed rate rebates on industrial components.

*Export finance and export insurance programs*

Until August of 1971, the Japanese Government provided a short-term export financing system involving preferential interest rates. At present, no preferential rates are provided and the only assistance that the Bank of Japan can be said to provide in the export field is the willingness to refinance eligible export bills without limit. As a practical matter in the Japanese present financial situation, this offers no particular advantage, since abundant financing is available. With respect to medium and long-term financing, the Japan Export-Import Bank provides services similar to its equivalent in other developed countries though its terms may be slightly softer. In addition, the developing countries the Overseas Economic Cooperation Fund can provide financing for exports on considerably softer terms than the Ex-Im bank. A unique aspect of these two institutions appears to be the willingness to blend the two types of financing in some overseas projects. Blending with Japanese banks also occurs. This results in an effective decrease in the cost of export financing and contributes to Japan's competitive position in developing countries.

Government-sponsored export insurance covers a broad range of political as well as commercial risks under a program for which there is no counterpart in the United States. However, premiums are charged according to the degree of risk involved and although the system is government-operated it has been entirely self-sustaining.

It is the Embassy's conclusion that all of the Japanese Government's promotion activities separately and in sum are not major factors in accounting for Japan's excellent performance in export markets. Most of Japan's direct trade promotion work is carried out by trading firms and the Government's role, other than in assisting small and medium firms, is minimal. The Japanese Government's financial assistance of exports, other than to developing countries, is also believed to be of limited significance. The basic factors accounting for Japan's success as an exporting nation involve the domestic willingness to keep prices at competitive levels, to innovate and to make substantial efforts to service even relatively small markets, and overall Government-business attention to foreign trade which far surpasses that of most other countries.

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COMMITTEE TO PRESERVE AMERICAN COLOR TELEVISION (COMPACT),  
Washington, D.C., November 21, 1979.

HON. LLOYD M. BENTSEN,  
Russell Senate Office Building,  
Washington, D.C.

DEAR SENATOR BENTSEN: On October 8, your office released a report prepared by the General Accounting Office which analyzes a variety of issues concerning U.S.-Japanese trade. The report, "United States-Japanese Trade: Issues and Problems," is essentially a series of case studies which examines the U.S.-Japanese trading relationship across a wide range of products, including color televisions. COMPACT is pleased that you have taken an active interest in these issues, and applauds the GAO's efforts in preparing the study. The section

on color television, however, contains certain misconceptions and gaps which we would like to bring to your attention, and which might also have implications for the report's overall conclusions.

In September 1976, COMPACT filed a petition with the U.S. International Trade Commission seeking temporary import restrictions on color television receivers under the terms and conditions of Section 201 of the Trade Act of 1974. In March 1977, the International Trade Commission unanimously determined that increased imports of color television receivers are causing or threatening serious injury to domestic manufacturers. It was this determination that ultimately led to the President's negotiation of an Orderly Marketing Agreement (OMA) with Japan, and later with Taiwan and South Korea, restraining imports of complete and incomplete color televisions entering the United States for a three-year period. In the case of Japan, the import relief period commenced on July 1, 1977. Imports from Japan accounted for the vast majority of all U.S. imports of color television receivers prior to the Commission's decision.

The Commission's Report to the President in this case includes substantial documentation indicating that Japanese claims of the U.S. product's technological and qualitative inferiority in comparison with Japanese color televisions are groundless. In this regard, the Commission's Report reads:

"During the past several years, U.S. producers of television receivers have made, and are continuing to make, intensive efforts to compete with foreign producers of television receivers in at least four general areas. They have taken advantage of low-cost foreign labor and the duty-savings provisions of TSUS item 807.00 by establishing foreign assembly plants; they have incorporated many product-design improvements and technological advances in their television receivers; they have made use of new cost-saving production techniques; and they have improved their quality-control procedures."<sup>1</sup>

Moreover, in their written opinion, Commissioners Parker and Bedell determined:

"The reason imports of color television receivers have been able to achieve such a significant penetration of the U.S. market lies primarily in the price advantage they enjoy. Generally speaking, the imported sets possess no qualitative advantage over domestically produced sets. Domestic producers also offer color television receivers in a competitive range of sizes through a variety of marketing outlets."<sup>2</sup>

Unfortunately, however, these critical findings of the International Trade Commission were apparently overlooked in GAO's preparation of its report.

A similar difficulty arises in the GAO's treatment of Japanese direct investment in U.S. color television assembly facilities. While these facilities employ U.S. workers, they tend to import more components and thus be much less labor-intensive than the U.S. production facilities which were adversely affected or displaced entirely by earlier increases in imports of color televisions from Japan. Indeed, the latest data available from the International Trade Commission indicate that while U.S. production of color television receivers has increased since the negotiation of the OMA with Japan, total employment in the industry has actually declined.

It is also important to emphasize that the GAO report grossly understates the degree to which the Japanese market has been closed to foreign competition in the production and sale of color televisions throughout the post-war period, not simply as a matter of Japanese Government policy, but also as a result of the restrictive activities of the Japanese manufacturers, themselves. This is plainly evident in the quotations taken from the Nichimen letter which appear on page 87 of the GAO report, indicating that "Nichimen's sales program [for Zenith products] was halted by pressures within Japan such as:

Japanese Electronic Industry Association (EIA) pressure on the Japanese Government;

EIA's pressure on leading chain and department stores; and

Attempts to persuade Nichimen not to indulge too aggressively in the distribution of (Zenith) products.

It is clear, therefore, that even in cases where a U.S. manufacturer sufficiently "understands" the Japanese market, overcomes the official tariff and non-tariff barriers, and is in a position to commence sales to Japan, events are ultimately

<sup>1</sup> USITC Publication 808, p. A-81.

<sup>2</sup> *Ibid.*, p. 42.



controlled by his Japanese competitors, apparently with the Japanese Government turning a blind eye.

Indeed, the permissive nature of Japanese laws and practices regulating competitive behavior is not mentioned at all in the GAO report. Due to this permissive climate, Japanese manufacturers are free to engage in joint research activities, export cartels and "rationalization" cartels, all of which would never be tolerated by the Justice Department if carried out by U.S. manufacturers. Clearly, to the extent that such activities spill over and affect competition in the U.S. market for color television, their consequences for U.S.-based competitors can be quite profound. Yet the GAO report does not explore any of these areas.

It is COMPACT's view that this point has profound significance for the report's overall conclusions. If the ultimate regulators of foreign competition in the Japanese markets are the private Japanese competitors, themselves, then no amount of government-to-government negotiation and no amount of official Japanese Government "liberalization" of its trade policy will have the effect of truly integrating Japan into the Western liberal trading system. As long as our U.S. trade negotiators fail to realize this phenomenon, the United States will continue to grant meaningful trade concessions to the Japanese Government in return for assurances that will ultimately prove to be of very limited significance. It is for this reason that COMPACT has adopted the position that only vigorous enforcement of existing U.S. trade laws, including the "escape clause" procedure, against Japanese manufacturers and exporters can stem the dramatic negative consequences that have been brought about by Japanese methods of competition for many U.S. industries, and in particular the color television industry.

Equally important is that the GAO report fails to draw the most obvious conclusion from the overwhelming body of evidence indicating that Japanese penetration of and direct investments in the U.S. color television market occurred directly as a result of unfair trade practices.

As early as 1968, a committee of the U.S. Electronic Industries Association filed an anti-dumping petition against Japanese manufacturers of television receivers. Following continued delays, the Treasury Department in 1971 finally determined that the Japanese manufacturers in fact were engaging in less-than-fair-value pricing in the sale of televisions to the United States. On March 4, 1971, the U.S. Tariff Commission (presently the International Trade Commission) issued the following determination with respect to these LTFV sales:

"In the Commission's judgment, an industry in the United States is being injured by reason of the importation of [color and monochrome] television receivers from Japan, which are being sold at less than fair value (LTFV) within the meaning of the Anti-Dumping Act, 1921, as amended.

"In reaching this determination, three reasons have been persuasive: (1) imports of television receivers from Japan, determined by the Treasury to have been sold at less than fair value, have increased and now supply a substantial share of the U.S. market; (2) the sellers of the LTFV Japanese receivers have for the most part undersold U.S. manufacturers of television sets in the domestic market; and (3) sales of the LTFV television sets have contributed substantially to declining prices of domestically produced television receivers."<sup>3</sup>

The importance of this statement is readily apparent. During the period 1966-1970, Japanese color television receivers imported into the United States were continually being sold at unreasonably low prices despite the prevalence of higher selling prices in Japan. This led to a finding of "dumping." As a result of this dumping, the U.S. television industry was being injured.

Interestingly, however, until 1979 few dumping duties were collected by the U.S. authorities. Hence the dumping continued and the magnitude of the resulting injury increased dramatically. U.S. officials have recently estimated the total value of dumping duties that remain to be collected for the period 1973 and 1978 to be in excess of \$400 million. To date, only a fraction of this amount has actually been paid. Moreover, representatives of the Administration have suggested to the Japanese on several occasions that some "settlement" should be reached which would require only partial payment of the outstanding duties, despite the magnitude of the injury and despite the fact that grand juries in several U.S. cities are now considering evidence that the Japanese engaged in customs fraud in an attempt to conceal the true extent of the color television

<sup>3</sup> "Television Receiving Sets from Japan," Investigation No. AA 1921-66, T. C. Publication 367, March 1971, p. 3.

dumping margins. In fact, these "settlement" offers were made secretly, and were not authorized by the Anti-Dumping Act.

COMPACT considers that the history of the television dumping case represents what is at the heart of the U.S.-Japanese trade problem. As long as those responsible for the conduct of U.S. trade policy with respect to Japan fail to recognize that the Japanese use of unfair trade practices is not a symptom of the problem, but rather is the essence of the problem, and so long as those individuals also fail to appreciate that the only effective solution is a vigorous, timely and effective enforcement of our trade laws against the Japanese manufacturers and exporters, the long succession of U.S. industries that have fallen victim to these Japanese practices will continue to lengthen.

In closing, we would like to emphasize once again that we appreciate the interest that you and others in the Congress have demonstrated in U.S.-Japanese trade problems, and respectfully request that this letter be inserted in the record of the recent hearings that were held in conjunction with release of the GAO report.

Sincerely yours,

JACOB CLAYMAN,  
ALLEN W. DAWSON,  
*Cochairmen.*

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