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# INTERNATIONAL TRADE DEVELOPMENTS

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## U.S.–Japan Trade: Trends and Negotiations

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*The U.S. trade deficit with Japan increased from \$51.2 billion in 1996 to \$73.0 billion during 2002, or by 43 percent. This article analyzes trends during 1996-2002 of the leading U.S. exports to and imports from Japan. In addition, it reviews two major sets of bilateral negotiations aimed at addressing both sectoral and structural issues during this period.*

### Introduction

During the period from 1996 to 2002, the U.S. trade deficit with Japan increased by 43 percent to \$73.0 billion. The leading U.S. import category from Japan during 1996-2002 was motor vehicles and parts and the leading export item was parts of aircraft and spacecraft. This article analyzes the trends during 1996-2002 of the leading U.S. exports to and imports from Japan. There have been two major sets of bilateral negotiations aimed at addressing both sectoral and structural issues during the period under consideration. These negotiations are discussed, including the major provisions of the talks.

### Economic Profile

Japan ranks second behind the United States in terms of the size of its economy with a GDP of \$4.5 trillion in 2000. It also ranks second in scientific and technical competitiveness, non-governmental assets, foreign exchange reserves and trade surplus. However, Japan's economy has been in decline through the 1990s. The primary reasons cited for the deterioration in Japan's economy are the effects of the bursting of the economic bubble during which the value of land and other assets collapsed; Japan's fiscal policies,

which have emphasized budgetary restraint and increased taxes; and rigid government regulations.<sup>2</sup> Problems of debt overhang and high unemployment remain.<sup>3</sup> Japan's economy grew approximately 1 percent annually in the 1990s compared to about 4 percent per year in the 1980s. GDP fell from 2.2 percent growth in 2000 to a -0.6 percent contraction in 2001.<sup>4</sup> The process of reforming the economy has been uneven, although reforms accelerated in response to financial sector difficulties and a deep recession in 1998.

### U.S.-Japan Trade

The U.S. trade deficit with Japan increased from \$51.2 billion in 1996 to \$73.0 billion during 2002, or by 43 percent. The trade deficit reached a high level of \$84.9 billion in 2000 before declining to \$72.6 billion in 2001 and then reaching \$73.0 billion during 2002. The U.S. trade deficit with Japan totaled \$27.9 billion during the first 6 months of 2003 compared to \$28.9 during 2002, a decrease of 3 percent. The slowdown in the U.S. economy and the weaker dollar led to a decline in the U.S. deficit with Japan. Figure 1 shows the U.S.-Japan trade deficit during 1996-June 2003.

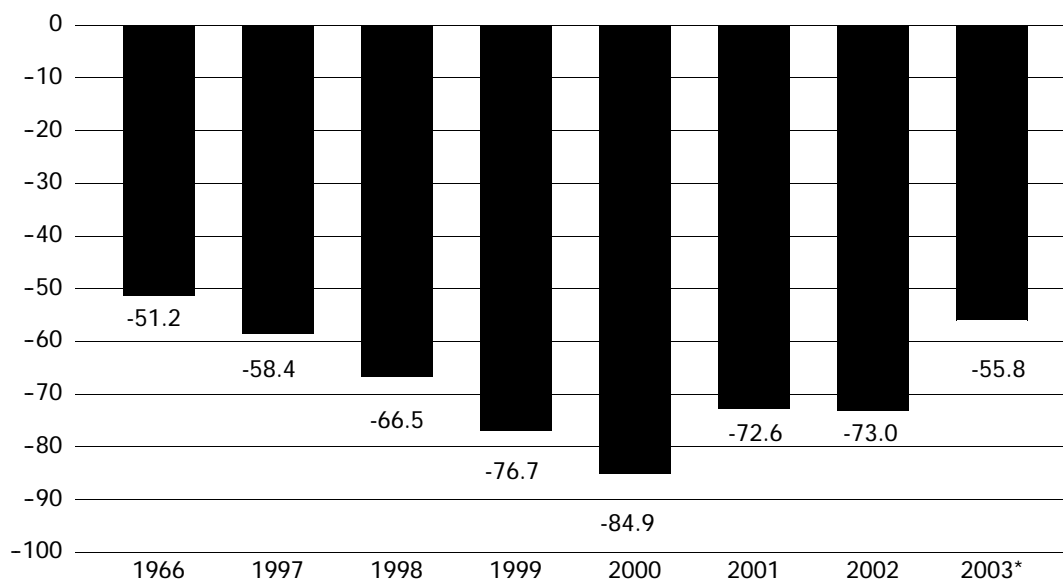
<sup>2</sup> William H. Cooper, *U.S.-Japan Economic Ties: Status and Outlook*, Congressional Research Service, July 31, 2003.

<sup>3</sup> Toshihiko Fukui, "Prospects for the Future of Japan's Economy," July 25, 2003, found at [http://www.org.jp/en/press/03/k0\\_0307/a.htm](http://www.org.jp/en/press/03/k0_0307/a.htm), retrieved Aug. 5, 2003.

<sup>4</sup> The World Bank Group, "Japan at a glance," found at Internet address [http://www.worldbank.org/data/countrydata/aag/jpn\\_aag.pdf](http://www.worldbank.org/data/countrydata/aag/jpn_aag.pdf), retrieved Sept. 11, 2002.

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Figure 1  
U.S.-Japan Trade Deficit  
Billion dollars



\*January-June 2003 at annualized rate.

Source: Official data of the U.S. Department of Commerce.

The persistent imbalance in U.S.-Japan trade has been explained by domestic savings-investment imbalances in the two countries. Other factors such as sudden changes in exchange rates can cause short-term shifts in trade balances as well.<sup>5</sup> Excessive Japanese government regulations have been the subject of bilateral negotiations between the United States and Japan for years. Nonetheless, Japan has made limited progress in deregulation. Sectors that have been the subject of recent reform measures include telecommunications, energy and transportation.<sup>6</sup> The exclusive purchasing behavior of corporate groupings or keiretsu, which control up to 40 percent of Japan's equities, also contribute to the trade deficit.

### U.S. Imports from Japan

U.S. imports from Japan rose steadily from \$114.8 billion in 1996 to \$121.3 billion in 2002, or by 6 percent (figure 2). Imports reached their highest level in 2000 at \$145.7 billion. In January-June 2003, U.S.

imports from Japan totaled \$58.2 billion, compared to \$58.3 billion during the same period in 2002. Leading U.S. imports from Japan were motor vehicles; parts and accessories for tractors, public transport passenger vehicles, and motor cars; automatic data processing machines; transmission apparatus for radiotelephony; and parts and accessories for typewriters and other office machines.

U.S. imports of autos and parts increased from \$26.4 billion in 1996 to \$36.3 billion during 2002. Japanese-based passenger vehicle makers increased their manufacturing capacity in the United States during the period 1996-2002. Although imports from Japan grew significantly during that period, they might have increased even more without increased localized production.<sup>7</sup> Imports of autos and parts increased during 2000 because of continuing popularity of Japanese models and the depreciation of the yen.<sup>8</sup>

<sup>5</sup> William H. Cooper, *U.S.-Japan Economic Ties: Status and Outlook*, Congressional Research Service, July 31, 2003.

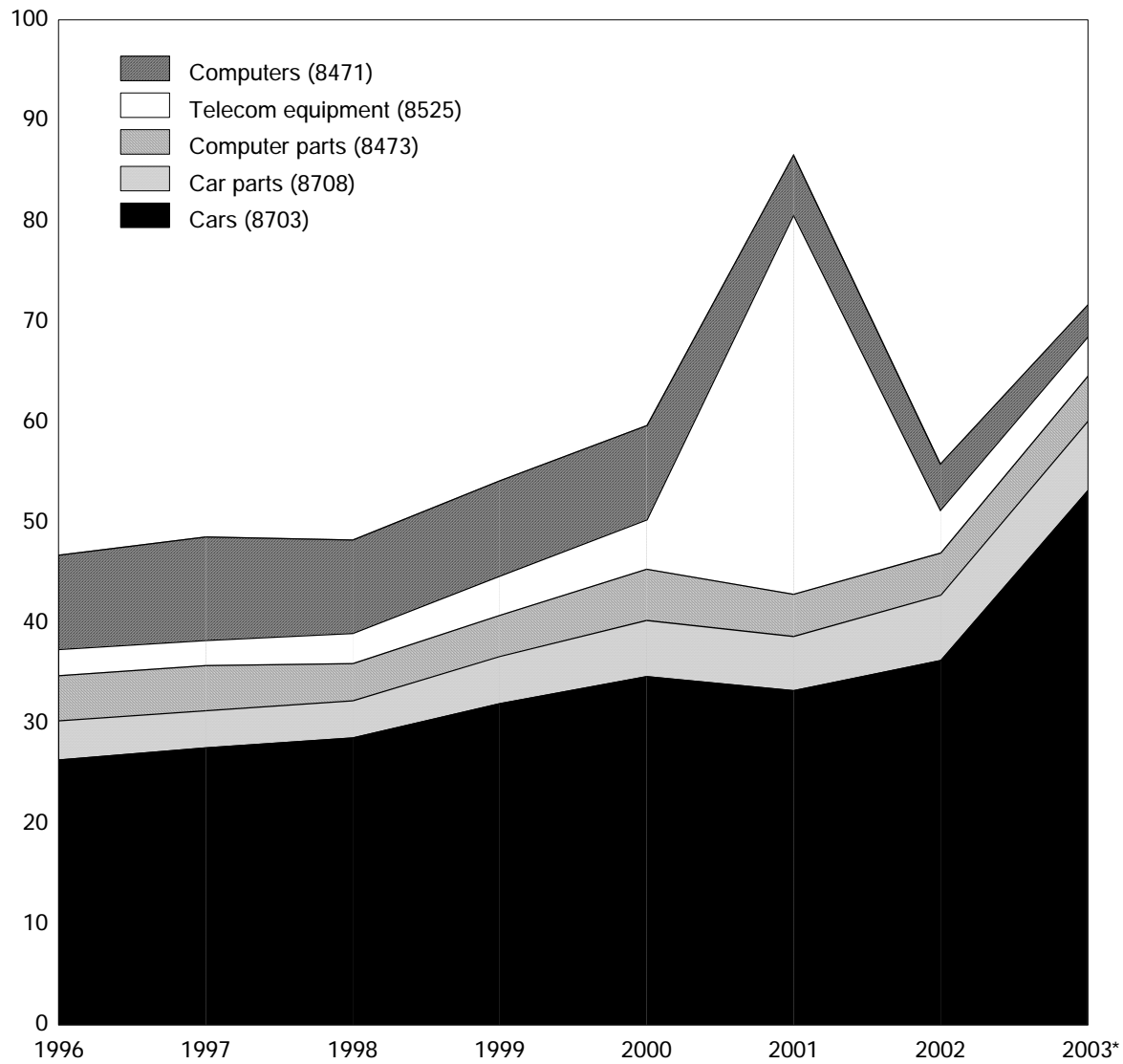
<sup>6</sup> William H. Cooper, "Japan's Economic Miracle: What Happened," *CRS Report for Congress*, Congressional Research Service, Oct. 1, 2001.

<sup>7</sup> "Motor vehicles" as defined in USITC, *Shifts in U.S. Merchandise Trade 2002*, July 2003, USITC Publication 3611.

<sup>8</sup> USITC, *Shifts in U.S. Merchandise Trade 2002*, p. 11-1.

**Figure 2**  
**Top U.S. Imports from Japan, by HTS chapter**

*Trillion dollars*



\*January-June 2003 at annualized rate.

Note.-See article for full HTS chapter descriptions

Source: Compiled from the U.S. Department of Commerce, U.S. International Trade Commission, and U.S. Treasury.

U.S. imports of automatic data processing machines and units thereof (computers) increased slightly during 1996-1997 and remained steady during 1998-2000. This trend was primarily due to advances in new technology and increased purchases due to the millennial change to the year 2000, commonly known as "Y2K." There was a decline of 38 percent during 2000-2002 to \$6.0 billion primarily because of lower corporate information technology budgets and the economic downturn in the United States.<sup>9</sup>

The increase from 1999 to 2000 in imports from Japan of transmission apparatus for radiotelephony; and television cameras, still-image video cameras and recorders resulted primarily from demand for still-image digital cameras. Imports of these cameras declined in 2001 following the terrorist attacks in the United States on September 11, 2001, the subsequent decrease in tourism, as well as a general economic downturn in the United States. However, imports of these items bounced back above their 2000 level as prices dropped, features were added, and more first-time buyers came to the market.

Imports of camcorders and cellphones fell from 2000 to 2001 as a result of decreased demand resulting from the September 11 attacks and, again, the general economic downturn. While much of the demand for digital cameras was likely from first-time buyers, cellphones and camcorders have been around for so long that most purchases are replacements and upgrades, rather than first-time purchases. Such upgrade purchases can be postponed more easily. While cellphone and camcorder imports increased in 2002, they did not return to 2000 levels.

Imports of satellite television receivers from Japan dropped off significantly as a result of the economic decline in the United States and did not appear to return to earlier levels.<sup>10</sup>

## U.S. Exports to Japan

U.S. exports to Japan decreased from \$63.6 billion in 1996 to \$ 48.3 billion in 2002, or by 24 percent, except in 2000 when exports rose to \$60.8 billion (figure 3). During the first six months of 2003, U.S. exports to Japan totaled \$24.4 billion compared to \$23.7 billion during the same period in 2002. The leading U.S. export categories were parts of aircraft and spacecraft; electronic integrated circuits; airplanes and spacecraft; automatic data processing machines and units thereof, and corn. Analysis of trends for each of these categories follows.

<sup>9</sup> Analysis provided by USITC, Office of Industries.

<sup>10</sup> Analysis provided by USITC, Office of Industries.

Japan is the largest foreign market for U.S. aircraft and aerospace products. In 2002, the United States accounted for 80 percent of Japan's aerospace imports. The Japan Defense Agency (JDA) accounted for 50 percent of domestic production of aircraft and parts.<sup>11</sup> U.S. exports of aircraft increased from \$1.5 billion in 1996 to \$1.7 billion in 2002. The trend in aircraft and aerospace products over the period reflected fleet replacement for civil aircraft and a downturn in demand as a result of the Asian financial (currency) crisis in the late 1990s.

The second largest category of U.S. exports to Japan during 1996-2002 was electronic integrated circuits and microassemblies (semiconductors) and parts thereof. U.S. exports of these products increased from \$2.1 billion in 1996 to \$3.0 billion in 2000, primarily because of the long-term growth in the telecommunications market and increased demand for computers which incorporate semiconductors. This was also a period of liberalization in global telecommunications markets which increased demand for semiconductors by major competitors. From 2000 to 2002, there was a decline in U.S. exports of semiconductors to Japan from \$3.0 billion to \$1.8 billion. The decrease in exports to Japan reflected the worldwide decline in the semiconductor market.<sup>12</sup>

U.S. exports of automatic data processing machines and units thereof declined steadily from \$3.0 billion in 1996 to \$1.6 billion in 2002, except for an increase during 1999 to 2000. This trend in exports reflects worldwide consumption patterns in this sector, including an increase in purchases in preparation for Y2K.<sup>13</sup>

U.S. corn exports to Japan decreased from \$2.5 billion in 1996 to \$1.9 billion in 1997, or by 3 percent. The value of exports continued to decline over the period to \$1.5 billion in 2002 primarily because of a fall in the worldwide price of corn from approximately \$150 per metric ton to \$100 per metric ton. In terms of quantity, U.S. exports remained steady. Japan's market for corn is relatively stable at 16 million metric tons.

## U.S.-Japan Trade Negotiations

### U.S.-Japan Framework for a New Economic Partnership

There have been two major sets of negotiations between the United States and Japan during the 1990s.

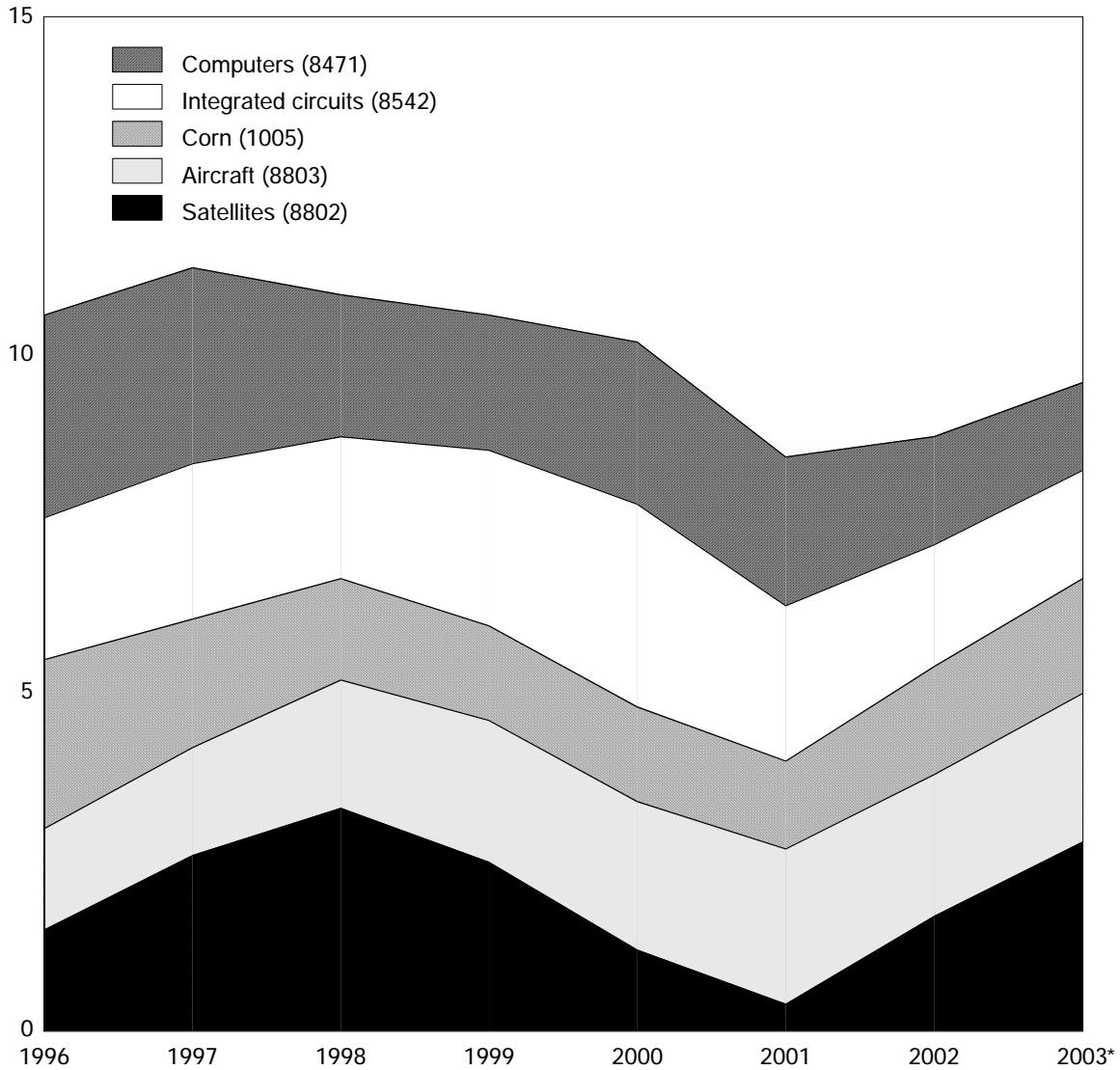
<sup>11</sup> United States Trade Representative (USTR), *2003 National Trade Estimate Report on Foreign Trade Barriers*, March 2003, p. 224.

<sup>12</sup> Analysis provided by USITC, Office of Industries.

<sup>13</sup> Analysis provided by USITC, Office of Industries.

**Figure 3**  
**Top U.S. Exports to Japan, by HTS chapter**

Trillion dollars



\*January-June 2003 at annualized rate.

Note.-See article for full HTS chapter descriptions

Source: Compiled from the U.S. Department of Commerce, U.S. International Trade Commission, and U.S. Treasury.

On July 10, 1993, the United States and Japan signed the U.S.-Japan Framework for a New Economic Partnership or the "Framework Agreement." The agreement provided a mechanism for conducting negotiations on both structural and sectoral issues. The initial "basket" areas for negotiation were (1) government procurement (telecommunications and medical technology), (2) regulatory reform and competitiveness, (3) other major sectors (autos and parts), (4) economic harmonization, and (5) implementation of existing arrangements and measures. Flat glass was added to the negotiating agenda the following year. The two governments were to assess the implementation of measures and policies taken in each sectoral and structural area within each basket; the assessment was to be based upon sets of criteria, either qualitative or quantitative, as appropriate. An update on progress toward reducing current account balances and other macroeconomic issues was to be included in biannual Heads of Governments' statements.

During bilateral negotiations under the Framework Agreement, the United States raised several issues with Japan regarding telecommunications: interconnection and pricing, rights-of-way, unbundling, and leased lines. In 2002, Japan finished a long-term review of its telecommunications framework in preparation for revisions to the Basic Telecommunications Law in FY 2003.

There are two bilateral insurance agreements in effect, a 1994 and a 1996 pact. Under these agreements foreign firms have increased their presence in both life and non-life insurance sectors. Nonetheless there are some remaining issues which the United States continues to raise. One issue of concern is the disparity between private industry and the public sector provider of postal life insurance products (known as Kampo) and uncertainty regarding future funding of the life and non-life insurance safety net systems, or Policyholder Protection Corporations.<sup>14</sup>

With regard to access to Japan's flat glass market, Japan's three domestic flat glass producers continue to maintain constant market shares through informal coordination and tight control over distribution channels, thereby restricting access for U.S. manufacturers. To improve access, the United States continues to urge Japan to strengthen the JFTC and enforce its rules against anticompetitive behavior.

<sup>14</sup> USTR, *2003 National Trade Estimate Report on Foreign Trade Barriers*, pp. 195-196, and 218-219.

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

The U.S.-Japan Economic Partnership for Growth was initiated on June 30, 2001. The Partnership established a new bilateral forum for discussing a wide range of global, regional, and bilateral economic and trade issues.<sup>15</sup> The Partnership was aimed at "promoting sustainable economic growth by focusing on sound macroeconomic policies, structural and regulatory reform, financial and corporate restructuring, foreign direct investment, and open markets."<sup>16</sup> Four working groups were set up under the Partnership for negotiations: telecommunications, information technology, energy, and medical devices/pharmaceuticals. Several new initiatives were started under the Partnership: the Regulatory Reform and Competition Policy Initiative, Investment Initiative, Financial Dialogue, and the Trade Forum.

Under the Regulatory Reform and Competition Policy Initiative, the United States and Japan issued a report to the leaders of each country. Achievements were made in various sectors including telecommunications, information technologies, energy, medical devices, pharmaceuticals and financial services. Progress was also made in areas such as competition policy, transparency, other government practices, legal system reform, revision of Japan's Commercial Code, and distribution.<sup>17</sup>

Legal and other barriers remain that affect growth in Japan's information technology sector. The United States is working with Japan under the Partnership to establish a regulatory framework that ensures competition, promotes innovation, allows private sector-led regulation where appropriate, and protects intellectual property rights.

Japan has undertaken measures to reform its energy sector, including electricity and natural gas. Nonetheless there remains a need for increased liberalization. Japan abolished its antimonopoly exemption for natural monopolies—including electricity and gas—although this has resulted in little progress toward lowering energy costs and improving efficiency. In 2003, Japan is expected to submit legisla-

<sup>15</sup> USITC, *Operation of the Trade Agreements Program*, 53<sup>rd</sup> Report, 2001, USITC Publication 3510, May 2002, pp. 4-25 and 4-26.

<sup>16</sup> The Governments of Japan and the United States, "U.S.-Japan Economic Partnership for Growth," June 30, 2001.

<sup>17</sup> USTR, *2003 Trade Policy Agency and 2002 Annual Report*, March 2003, p. 187.

tion to the Diet (Japan's parliament) to reform its gas sector.<sup>18</sup>

The United States and Japan continue to discuss market-access concerns in the medical device and pharmaceutical sectors regarding regulation and reimbursement. The United States has urged Japan to consider how different cost structures in various parts of the healthcare system influence each other and how faster access to innovative products can result in cost savings. In addition, the United States continues to emphasize the importance of a transparent and predictable pricing process to reward innovative medical devices and pharmaceuticals. The United States has indicated that it views Japan's foreign reference price as inappropriate. Another major goal of the United States is to gain expedited review and new product approval procedures.<sup>19</sup>

In conclusion, during the period 1996-June 2003, the U.S. trade deficit with Japan increased through 2000—reflecting higher levels of imports—and then

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<sup>18</sup> USTR, *2003 National Trade Estimate Report on Foreign Trade Barriers*, March 2003, pp. 198-199.

<sup>19</sup> USTR, *2003 National Trade Estimate Report on Foreign Trade Barriers*, March 2003, pp. 199-200.

declined—primarily because of the slowdown in the U.S. economy and the weaker dollar. U.S. imports rose steadily during this period primarily because of the strength of the U.S. economy relative to the Japanese economy and worldwide shipment trends. U.S. exports to Japan of aircraft and aerospace products—the largest category—increased due to cyclical trends in the industry.

As was noted, U.S. trade negotiations during the 1990s were conducted under the Framework Agreement and the U.S.-Japan Economic Partnership for Growth. Both sets of negotiations covered a number of structural and sectoral issues. Aside from autos and parts, the largest U.S. import category, most negotiations focused on items of smaller import or export values. Achievements were made in sectors such as telecommunications, information technology, energy, medical devices, pharmaceuticals and financial services. In addition, progress was made in structural areas such as competition policy, transparency, other government practices, legal system reform, and distribution. Further bilateral discussions are expected in these areas during 2004.