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## *Exporting the TPP Melting Pot: Americanizing Japan*

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by Peter Clark**

U.S. stakeholders' submissions to the USTR on Japan's application to join the Trans Pacific Partnership negotiations suggest that Japan would be better off by adopting U.S. regulatory systems and rules. It is a broadly based attempt to extend the U.S. melting pot to Japan. If the suggestions were directed at the Japanese people instead of the USTR, they would be insulting. Rather, directed as they are at USTR, the objective is to ensure that U.S. negotiators and legislators understand how important Japan is to the TPP and to the USA. And not in that order.

Japan is not the USA. The Japanese do things differently – not wrong or inefficiently, just differently. The most successful foreign investors in, and exporters to, Japan have learned to adapt to the system and live with it. Change does not come quickly to Japan. The Japanese are masters at the art of making haste carefully.

Is being different wrong? China too is different – so is Korea and other countries in Asia. APEC has been trying to achieve certain goals, but it is safe to say that differences based on national identities and preferences remain.

If Japan were to adapt its regulatory systems to North American business needs no doubt trade and investment flows would increase. A major goal of the TPP is regulatory coherence. It would be dangerous if Japan interpreted this as “the American way or the highway”.

That approach would be doomed from the start.

Let's review some of the items on the U.S. stakeholders shopping lists:

The demands of the American Automotive Policy Council (AAPC) could kill the deal. This would certainly please the Council's members.

AAPC is concerned about Japan's Weak Yen Policy and the Auto Regulatory Regime. The first is rather bizarre given the contrived weakness of the U.S. dollar. One might suggest that Japanese action in the exchange markets is defensive. The second challenges the Japanese practice of linking licensing fees to motor size.

AAPC argues that Japan should not be admitted to the TPP because:

- Japan joining the TPP now will delay the current negotiations and risks turning the talks into a WTO Doha Round-like process that will drag on for years with little hope of a fruitful conclusion.
- A free trade agreement with Japan will not open the Japanese economy, it will simply prolong and incentivize an export driven economic model that benefits Japan at the expense of American manufacturing and the jobs it supports. Moreover, it would encourage others to follow that same economic model.
- Japan would strongly resist the inclusion of disciplines on the key NTMs, so having Japan involved at this stage would likely hold up the completion of the agreement or lead to one that does not meet the overall objective of establishing a high-standard 21st Century agreement.
- A one-sided free trade agreement with Japan will drag down the United States' leading sector of exports, and will deeply undermine the business case for additional auto investments in the United States while undermining the competitive gains that are allowing new jobs to be created.

Accepting the AAPC position would mean that Japan could not participate in the negotiations and accession to the TPP would be on a "take it or leave it" basis with extra concessions demanded.

This will not happen.

The U.S.–Japan Business Council (USJBC), expressing the views of a range of U.S. industries, refers to the TPP with Japan as a "game changer" because including Japan in the TPP would make the Partnership a credible Preferential Trade Agreement, which could attract other participants. Having Japan in the deal is the only credible, persuasive reason for Canada joining the TPP. There are other participants but, with the exception of Vietnam, they are small. And if the U.S. wants to re-negotiate NAFTA, then let's begin from ground zero – not a deal that Washington has been able to impose on smaller countries – some already with FTAs and others really quite minor players in the global trading system.

The USJBC notes "it is important for U.S. stakeholders to evaluate Japan's readiness to participate in TPP (based on) an understanding of what Japan is like today". This ties in to the views of the Keidanren, the Japan Business Federation, which is anxious to change in order to survive and grow.

The USJBC positioning has support from Corporate Japan – but relatively little from the Japanese people – because their changes have not been disclosed to or discussed with the people. Its 18-page submission is a shopping list which urges that Japan avoid initial requests for exclusions in “sensitive” areas; this would undoubtedly dampen enthusiasm for Japan’s participation in the TPP.

The USJBC calls for Japan to make significant policy changes, innovations and improvements in the following areas:

- competition policy;
- financial services;
- foreign direct investment policy;
- government procurement and technology co-operation;
- intellectual property protection;
- labour rights/worker protection rules (seem as too restrictive and hindering labour mobility);
- medical technology approvals;
- regulatory transparency and regulatory coherence; and
- state-owned enterprises (including Japan Post).

The broad range of U.S. demands include:

- more English in official documents (will the U.S. put more Japanese and French in theirs?);
- make it easier for financial services to engage in short selling as well as other “americanizations” to financial services to make them more functional;
- remove exchange rate charges on non-residents transfers, especially U.S. Social Security payments; and
- Japanese investment incentives should be made more attractive so that Japan can give U.S. investors incentives to match those in other Asian countries.

The USJBC’s suggested phase-out periods of up to 10 years on Japan’s sensitive agricultural tariffs will not be enough. For some Japanese farm interests, never is soon enough. Increased volumes, cheaper imports from Australia and New Zealand and heavily subsidized imports are not the big attractions that the USJBC seems to believe.

Will the U.S. demands be acceptable to Japan – where more than 11 million people have already signed a petition opposing participation? Many of the high tariffs on agricultural products – including peas, wheat, barley, beef, pork and potatoes will also be interesting to Canada’s farmers and ranchers. Indeed, there is no way Japan can hope to maintain its across the board, prohibitive tariffs on 100 plus agricultural products. The view in Japan is that agriculture could be better protected in agreements with Asia – which could be expanded to include ASEAN.

Demands to phase out rice tariffs will be a major problem. The US Rice Federation wants increased access and to get around the import monopoly to sell direct to the consumer.

Japan imports about 8% of its rice but it does not find its way to Japanese rice bowls. I suspect that the Japanese consider the highly subsidized U.S. rice to be more suitable for flour and pig feed than for human consumption.

Ja Zenchu – the Central Union of Agricultural Cooperatives — has rejected the U.S. overtures on opening agricultural markets. They argue that:

- the devastation of the Japanese agricultural sector will undermine the long-term friendship between Japan and the United States;
- removing Japan's agricultural tariffs will affect security conditions of East Asia, which is not in the economic or geopolitical interest of the United States or Japan;
- elimination of Japan's agricultural tariffs will seriously increase the number of starving and undernourished people in the world;
- a “one-size-fits-all” approach under the TPP is not instrumental for sustainable development of agriculture in the Asia-Pacific region and that co-existence of agriculture has to be at the center of consideration in any agricultural trade negotiation that Japan joins;
- Japan must now focus on restoring its living and working conditions in the aftermath of the devastation caused by the Great East Japan Earthquake and clean up the damage caused by the nuclear power plant accident in Fukushima. In other words, it is not TPP negotiations that Japan should address right now.

A very substantial part of U.S.–Japan trade is already duty free under the WTO. A Doha solution or any other type of multilateral deal is, in my view, at least 10 years off, so the rest must be addressed, particularly the 25% U.S. duty on light trucks.

There are no U.S. tariffs on imports of steel. The value of the yen – at record highs because the U.S. keeps the dollar weak – and signals from the Fed suggests this will not change until 2014.

This, however, does not prevent U.S. claims that Japanese moves to temper the strength of the yen constitute currency manipulation. One should put these claims in context by reference to a Cato Institute release which trace U.S. currency manipulation campaigns back to the Great Depression and explain the unexpected consequences of these belligerent challenges.

Is extending the U.S. melting pot to trade with Japan a real option or even desirable?

In the Bretton-Woods period, trade policies and negotiations were based on foreign policy considerations as much as, if not more than, economic considerations. Have the traditional goals of trade policy changed so much?

Since the end of the GATT-based trading system and certainly since the WTO – which has been incapable of concluding broadly based agreements – mercantilism and economic conquest have become the norm for many countries and particularly for the U.S.

Why do I consider that applying this approach to Japan's inclusion in the TPP is doomed to crash and burn? My instincts and experience developed over more than 40 years in the business see no other option.

One of my earliest jobs in government was negotiating "voluntary" textile restraints with Japan and developing countries, mostly in Asia. This required great sensitivity to the nature and priorities of one's counterparts. Japan then was much like what China is today.

Canada had no moral or ethical authority to ask Japan, Korea, Hong Kong, Taiwan and others to limit their legitimate trading opportunities in textiles and apparel. Their only "crime" was excessive competitiveness, which could not be disciplined by anti-dumping and countervailing duties. The incentive for the targets was that an agreement which preserved reasonable or traditional trade was better than a trade ban.

We were trained to understand our counterparts, their culture and sensitivities, to be courteous, to understand how they make decisions or reach consensus, never lose temper or show anger – and most of all to be patient. Ultimatums were to be avoided as long as possible and delivered with regret, never with anger or frustration. And impasses were referred back for consideration at senior levels.

Many of our superiors had seen military service in World War II. My first director at the Department of Finance was a former Commando who was one of the first ashore in the liberation of Hong Kong.

We were taught about the importance of "face" to our Asian counterparts – and that we should not impose decisions or try to score clever debating points in negotiating sessions. This could cause the head of the other side to look bad or weak (thus losing face) with his team. This would have been incredibly unwise and unforgivable behavior, as personal relationships would become impossible.

Taking account of Japanese sensitivities and the extreme importance of "face" was crucial in negotiating with Japan. One had to have the confidence of Japanese counterparts to determine the real reason for an impasse. Building relationships were essential and these were built on non-business factors. Logic and explaining how good your deal was generally did not fly. Helping each other through problems and finding mutually beneficial solutions is key. One learned from the Japanese how oblique was far better than direct.

I learned, for example, that leather tanning was important to Japan because the people who did this work were outcasts for a variety of reasons. Many worked in "unclean" occupations such as undertaking, embalming, animal butchery and leather tanning – in short, anything that had to do with death. It was necessary to keep them working because they could not be integrated into society. This limited Japan's negotiating flexibility.

More than once a Japanese friend (because after a time, with much patience, mutual respect developed and opponents on issues did become friends) would suggest "perhaps

you should ask me this” and when you asked it, the road to agreement would become obvious.

You might think that this was a long time ago and it was. Has Japan changed that much? No it has not.

Japanese society is still heavily influenced by tradition. Important among these traditions is social status and authority, the way they treat each other, particularly in the presence of foreigners. Clearly, life and society in Japan is changing. The Japanese are having fewer children – which absent other changes will mean a shrinking population. There are lifestyle changes – but the saving rate is still nearly 30%.

Nothing changes in Japan without a lengthy consensus building process. The extensive changes which U.S. business wants to impose on Japan’s business and insistent regulatory system will also play well in Canada. Let the U.S. fight for them. If there is change, Japan will not be able to maintain one system for TPP or the USA and another for the rest of the world.

Some in Japan will consider that U.S. demands for negotiating the Trans Pacific Partnership are insensitive to the point of being culturally belligerent. This will not be a universal view. The Keidanren – essentially the Japanese version of the Business Roundtable – issued a White paper identifying the need for reform and modernization in many aspects of business and government regulation in Japan. The White paper identified many of the same needs for the same issues as have been listed in U.S. business submissions on the TPP.

But will this be enough? Will the government be able and willing to manage such mega changes – or will they look for other less intrusive free trade solutions in Asia?

Prime Minister Noda was pushed towards the TPP by Japanese business. The high yen, rising costs and declining competitiveness was one driver, the other was a desire to be present at the TPP negotiating deal to help to shape the deal.

Corporate Japan has signaled that it needs more duty free access to the U.S. and other markets or they will move production offshore. Indeed, with the negotiation of U.S.-Korea Free Trade (KORUS), both Toyota and Honda are shifting their exports to Korea – to their U.S. plants. When one considers the massive difference in distance between the Japanese and U.S. plants, this is very difficult to understand.

The USTR, on the other hand, driven by an unrealistic and unattainable target end date, wants to serve up to Japan, Mexico and Canada a fait accompli on a take it or leave it basis. One of Noda’s most persuasive arguments for joining the TPP will crash and burn.

Japan has never participated in a preferential trade agreement where it would be asked to commit to concessions in advance; indeed, it has never entertained any pre-conditions in

trade negotiations. This is a peculiar U.S. style of negotiation, based on the value of access to the U.S. market.

This “Chutzpah” Doctrine is based on the value of free access to the U.S. market. It ignores that the U.S. has already sold duty free access to many countries. This fish has been sold, re-sold, cleaned, gutted and digested numerous times. There is a risk that the U.S. will paint itself into a corner and overplay its hand.

President Obama actively courted participation in the TPP by Japan, Canada and Mexico. It will be necessary to include Japan to give the TPP critical mass and credibility – not only for trade reasons, but to re-enforce U.S. military presence and influence in Asia. And including Canada and Mexico ensures that the U.S. and North American stakeholders will be regulated by uniform rules and access conditions.

President Noda, Prime Minister Harper and President Calderón could reasonably expect that when POTUS invited them, there would not be a price tag – or an admission price — to what is supposed to be a negotiation. I can find no definition of negotiation which envisages major concessions to be conceded before it starts. Obama can’t risk making the leaders of the other countries look bad and, in the case of Prime Minister Noda — already under severe pressure at home — or lose face.

Prime Minister Noda will have a tough task in trying to defend TPP if the U.S. demands appear to be too one-sided and arbitrary and insensitive. Presenting a completed TPP with no Japanese input is a face-killing non-starter.

Should Washington be allowed to run roughshod over its large trading partners because this is an election year? Isn’t it always? The TPP will not deliver jobs for Obama until well after the election. And few actually believe that the deal will be done before the election.

There is far too much to do – and too many differences to resolve to hope for this. Former USTR Sue Schwab, who knows the trade negotiating game as well as anyone, says Obama simply does not have time to try to ensure TPP is done on the ambitious timeframe. Clearly, as the election looms larger and closer, priorities will shift to political survival and a quest for four more years.

Obama’s political survival agenda will come first. That his invitees have problems of their own just does not resonate in the White House or whatever they call the Committee to Re-Elect the President (CREEP in the Nixon era).

There is another option for Japan. China has been trying to negotiate a three-way FTA with Japan and Korea. Japan seems interested but is nervous about China’s expanding military presence and power in the region. Korea seems very keen on concluding negotiations before Japan because being there first will give Korea an important edge over Japan. And while Korea has an FTA with the USA, it is not in the anti-Chinese TPP compact. This may become the most attractive option for Japan.

If Washington adopts an insensitive and exclusionary approach they will likely see this golden goose flee the coop. Canada must keep its options open, including negotiating free trade bilaterally with Japan.