

**“EUROPEAN UNION AND JAPAN RELATION
SINCE 1990: A SURVEY”**

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By

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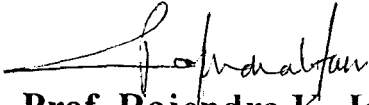
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Certified that the Dissertation entitled “**EUROPEAN UNION AND JAPAN RELATION SINCE 1990: A SURVEY**” submitted by **Dollina Kharwanlang** in partial fulfillment of requirement for the award of **Master of Philosophy** of this university.

This Dissertation has not been submitted for any other degree of this university, or any other university.

We recommend that this dissertation be placed before the examiner for evaluation.


Prof. Rajendra K. Jain

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PREFACE

The EU-Japan relationship, can be traced as early as 1543 when Europe discovered Japan, for there was no direct political relations between Japan and European Union for a considerable period. Which also saw the decline of Europe's role in the world and Asia in particular. Europe became more inward looking and Japan quietly assumed a greater role in the world stage with an economic expression.

Europe and Japan found it particular hard to communicate with each other for neither was sure where it or the other stood. Both tended to develop close links with the United States of America.

To persuade the Japanese and the Europeans to take greater interest in each other has not been an easy task. The Cold War witnessed considerable economic and trade friction between Japan and Europe. The crisis worsened because there was no broad interchange and understanding.

The relationship between Japan and Europe underwent a drastic change at the end of the Cold War, as the international community stood at crossroads. Japan and Europe recognized each others importance and felt it necessary to join hands and shape new world order.

This study is divided into five chapters. Chapter One provides the introduction about both European Union and Japan and their perceptions and images of each other.

Chapter Two, traces the evolution and growth of the relationship between EU and Japan till the end of the 1980's.

Chapter Three, examines EU – Japanese political relationship in the 1990, and asses the progress in enhancing political dialogue between the two.

Chapter Four, discusses the economic relation between EU and Japan in the 1990. It describes Japanese response to the Single Market, growth of Japanese Foreign Direct Investment and their responses to the Asian Financial Crisis in 1997, it also looks at how the two have responded to the various issues within the World Trade Organization.

Chapter Five, provides some concluding observations and looks at future prospects.

CHAPTER I

INTRODUCTION

The twentieth century was not a period of which humankind can be proud. Violence reigned throughout the first half and the second half was a mixture of progress and stagnation. As the world moves on to another century will Japan and Europe be able to contribute to the formation of a new international order?

The pace at which globalization is moving has made interdependence between states stronger than ever before, by promoting international co-operation for common interest¹. There is a power to create an international community that would go beyond the borders, and may eventually shape world order.

The European Union-Japan relationship has had harsh as well as light moments.² The scene is set by the weakening of direct political relationship in the twentieth century, brought about by the decline of Europe's role in the world and its withdrawals from Asia. Europe grew more inward- looking, concentrating on its trade and investments in markets closer home. Japan, on the other hand has quietly assumed a greater role on the world stage, its main expression being economics³

Therefore, a look into how the Europeans and the Japanese perceive each other and the development of this relationship will be interesting of study considering that the European Union and Japan are the two strong pillars⁴ of the

¹ Taka Kazu Kuriyama, "Challenges for Japan's foreign policy future", *Japan Review of International Affairs*, Fall, 2000, p.206.

² Endymion Wilkinson, *Japan Versus Europe*, [Penguin books , London, 1980] , p. 16.

³ *ibid.*, p.16.

⁴ " EU/Japan relations", *www.europa.eu.int*.

world economy, and therefore understanding their relationship becomes important.

There has always been a climate of relative indifference as far as the relations between the EU and Japan have been conducted, and those who seem to have a professional stake too have not been able to enhance this relationship. It is difficult to persuade the Japanese and the Europeans to take greater interest in each other, as there are no natural political ties to bind the two "reluctant partners"⁵. Since the Second World War Japan's main partner in the western world has been the United States and not Europe. Therefore it seems customary to bind Japan with the former than the latter, that Japanese play baseball and not cricket can be cited as an example of their commonness. Japanese interest in the European culture is the interest any one may have in a museum.

The Europeans too on their part have made very little effort to get to know the Japanese. They have preconceived ideas of Japan which has not helped in bridging the two. It is only recently that Japanese as a language, has been offered in European schools and interestingly European holiday packages make Thailand more important and attractive rather than Japan.

It is not surprising then that European policy towards Japan has been unbalanced and distorted.⁶

As far as Japan is concerned, the development of total⁷ relationship with Europe taken as an entity is becoming increasingly difficult.

⁵ Simon Nuttal, "Japan and the European Union; Reluctant Partners", *Survival*, Vol. 38; No. 2, Summer 1996, p.108.

⁶ *ibid*, p.105.

During the Cold War period Japan's interest by and large converged with those of the U.S. However, towards the end of the Cold War, Japan increasingly articulated its own position.

Japan modeled itself on Germany in many respects during the process of modernization in the Meiji era. From Germany Japan learned the legal and educational systems. Europe was felt at such close presence that it was taken for granted that members of the elite would be masters of the German language and also well versed in the works of Kant and Goethe⁸. All this ended with Japan's defeat in the Second World War. After the war, the interest in Europe declined rapidly.

Japan then came under the overwhelming influence of the American civilization, and the Cold War left Japan with no option but to place itself under America's wings especially with regards to the security aspect.⁹

The relationship is one of mutual distrust. In fact, Japanese-European relations have been characterized by a cultural infatuation with Europe on Japan's part and a lack of interest on the European side. For most Europeans, including politicians and business people, Japan has been of little concern.

In the context of the Cold War Europe and Japan saw in relations with the United States the key to preserving peace and prosperity and regarded European-Japanese relations as having no decisive role to play in international politics.

⁷ Brian Bridges, "Japan and Europe", *Asian Survey*, Vol. XXXII, No. 3, March 1999, p. 230

⁸ Noda Nobuo, "Japan in a world of Rival Empires", *Japan Echo*, vol.26,1999, p.8.

⁹ *ibid*, p.8.

The Europeans only began to become increasingly aware of Japan in the 1960's¹⁰ when it was a period of rapid economic growth which enabled Japan to export large volumes of industrial goods.

In fact the very first encounter of Japanese and Europeans which dates back to early 1543 gives the Japanese a view of Europeans as 'traders' and having an understanding of superior and inferior. On the other hand, the Europeans considered the Japanese as barbarians. Such stereotypes have stood the test of time, so much so that even now after more than four centuries, no major changes have altered the way Japan and Europe perceive each other.¹¹

The Japanese challenge is a development of global historical significance. Japan has had even greater success than Europe or even the United States in building an advanced society. At least from an institutional point of view, Japan has outdone European the guaranteeing of liberties.

The Japanese would always say that theirs is the most westernized country in Asia. It is true that Japan has had an extensive history of contact with the West. Even times when the country was officially closed to the outside world, the impact of Dutch learning or Rangaku¹² was considerable. The European Union's relationship with Japan was weak in substance and initially Japan had to deal with twelve European powers that have had long histories and traditions that are building up for an integration.

¹⁰ Ishi Rawa Kaoru, "Relations with Europe: Handle with care", *Japan Echo*, vol.18, 1-3, 1991, p.71.

¹¹ Arfin Bey, "Japan and Europe :A cultural view from South East Asia", *Japan Echo*, vol.11, 1992, p.45.

¹² *ibid*, p.48.

The bone of contention between EU and Japan has always been trade, Japan's trade surplus is huge, and the Europeans feel that Japan is virtually inaccessible for foreign investment.

This has become a source of complaints and accusations about the inequality of opportunities, unfair competition and the need to level the playing field.¹³

In this relationship another undercurrent is the threat of bilateralism, where benefits could be negotiated with the member states of the Union.

In the post- Cold War era, the international political scene is changing rapidly and continuously, creating an important and an ever increasing need and for closer political discussion and co-operation between global partners.

In the new geo-political climate, the economic and trading power of the EU and Japan means that consultation and a common approach to shared global responsibilities is both logical and desirable.

Political relations between EU and Japan are evolving in response to the new global challenges. There is a growing commitment from both sides

The EU and Japan are leading economic powers and important trading partners. Japan is the world's second largest national economy, accounting for one seventh of the world's GDP and around ten percent of the world's exports and imports. It also has the largest foreign currency reserves in the world at the end of

¹³ Dries Van Agt, "United States, Japan, Europe: The Unholy Trinity," *European Affairs* Vol. 4: 1990, p.61.

April 2000.¹⁴ It has a 5% share of the E.U. exports and it is the third largest export market. There are enormous potential opportunities for European business in Japan.

Europe too is equally important as a market for Japan, accounting for around 20%¹⁵ of total world exports and imports and 30%¹⁶ of a total world, stocks of foreign direct investment. The EU is the world's largest trading economy. Japan is also a major investor in EU.¹⁷

The EU and Japan have pursued close cooperation on trade issues for some time, in a world of increasing interdependence. neither partner can pursue its own interest effectively without cooperation.

Cooperation has developed on multilateral trade issues, notably in the context of the World Trade Organization where both share a common interest in strengthening free trade and to respond to new issues from time to time. Japan is Europe's most important partner in the Asian region, while for Japan, EU is the centre of stability and growth. The introduction of the Euro and its economic and political impact on Japan has been seen to strengthen the importance of a dialogue between the two, thus building a stronger relationship.

Coming together has never been so important in the post-Cold War era, especially with the political instability and economic crisis in Asia. Both have played their parts in meeting the demands created by these problems. Therefore one can expect this relationship to grow stronger.

¹⁴ "EU –Japan in 2000", www.infojapan.org/region/europe/eu/overview/econo-trade.html.

¹⁵ "EU-Japan economic relations", www.europa.eu.int.

¹⁶ "EU/Japan economic Relations", www.Europa.eu.int/intro/eco-trade.html

¹⁷ "Overview of EU-Japan relations", www.jpn.cec.eu.int/english/eu-relations.

The Europe of today is a new Europe, regional co-operation has emerged, but accompanied by regional conflicts. The difference is that all co-operation and all conflicts will take place within the framework of one Europe.¹⁸

The Economic and Monetary Union has equipped the EU with an international currency to match its economic weight. Further the EU's process of enlargement is on and this will make the EU an important partner in years to come.

Japan has been quick to react to these changes and at the same time Japan is also raising its global profile and forging a wider international role both in political and economic terms. For Japan this means that more attention will have to be paid to Europe than it used to. It is interesting to note that Europe needs the abundance of resources available in Japan and Japan needs access to a tremendous market.

On the surface, not much has changed, people like always still talk of a relationship of cooperation. Limited co-operation was already underway especially in the field of science and technology. The only difference is that there has been a significant shift¹⁹ in the attitude of member states in the EU. Traditional analyses of trade-policy position in the EC portray the Mediterranean countries as protectionist and the Northern countries as free traders and therefore pro-Japanese²⁰. The British had been the most anti-Japanese and so too were the Germans.²¹ But then the British changed tack recognizing the greater benefit to the UK. Trade issues continue to dominate day-to-day affairs although a conscious

¹⁸ www.cec.eu.int/english/press-info.html.

¹⁹ Simon Nuttal, "Japan and the European Union: Reluctant Partners," *Survival*, vol.38, no.2, Summer, 1996, p.108.

²⁰ *ibid.*, p.108.

²¹ *ibid.*, p.108.

effort was put into finding subjects like science and technology, environment and aid policy on which to begin a dialogue.

The 1992²² process, brought about the Trade Assessment Mechanism known as TAM which gave a new impetus to the overall EU Japan relationship.

Japan is changing, the Japanese society has been hit by a series of seismic shocks in recent years. Revelations of widespread corruption in politics have alienated the public. This may be a typically Japanese phenomenon, whether there is evidence of corruption or not.

Japanese diplomacy closely resembles Euro- American diplomacy in sensitive areas such as environment or human rights. Tokyo has been outspoken about France's decision to resume nuclear testing, for they have reason, as they are the only people to have experienced the horror of a nuclear explosion.

To talk about the 'Japanese' makes sense because they are organized in a way that makes their unity apparent. But it is difficult to talk of 'Europeans' in this sense, not because European Unity is not meaningful, but because, the concept of boundaries, defining unity, otherwise, keeps changing and shifting.²³

The Japanese are confused by this. Therefore this relationship presents opportunities as well as difficulties. For Japan, as for most Europeans, the uncertainty about the future size of Europe and the nature of its competence causes difficulties in policy planning. In general, Japanese policy-makers , whether politicians, officials or a corporate strategist need to think more clearly about

²² Ibid, p. 110.

²³ Ibid ,p .114.

Europe. There is an overall educative need to “think about Europe.”²⁴ Japan is changing radically in response to new economic conditions. The EU too is changing to adopt itself to the altered strategic situation following the collapse of the communist system in Europe and the drive towards enlargement.

Japan has apparently never been part of a regional organization. Thus finds it difficult to deal with bodies so multi-cultural as the EU where there is a pooling of national sovereignty in the common European interest.

Although the European Commission has been working hard to create a coherent strategy towards Japan, these measures are quite inconsistent.

The Japan- Europe relationship also depends on the interactions with United States. The EU has nothing to gain from escalating friction with US as is the case of Japan.

Protectionism in the US could lead to diversion of Japanese exports to EU in the long run.

The end of the Cold War has brought about a change in the way the Japanese perceive the world. They have stopped seeing the world as East and West, but see it as one. There is an emergence of a desire on the Japanese to create what might be called a new order²⁵ in relation with Europe.

In the absence of an East-West Confrontation, Japan will no longer be forced to rely so lopsidedly on its ties with the United States, and would be able to pursue a more balanced, multilateral foreign policy.

²⁴ Brain Bridges, “Japan and Europe; Rebalancing a relationship”, *Asian Survey*, Vol. XXXIII, March 1992, p. 241.

²⁵ Editorial, “Japan and Europe”, *Japan Echo*, vol.xvii,1991, p. 69.

The settlement of trade issues depends on the ability to communicate at the national level. In Europe particularly in France the long tradition of emphasizing public interest has led to a prominent public sector. With the Euro this can be seen as a trend even a to supra national level.

Discussions concerning creation of a larger European economic system through assistance to Eastern Europe is gaining attention.

Japan's commitment to Eastern Europe has little to do with economic advantage, rather it is a political gesture of solidarity with Europe and US. The Japanese might resent the expectation to pay for the bills without seeing or getting the benefits .Which is why the European must allow them a proper voice in the consultations over assistance to the East.

Legal solutions²⁶ are important for Europeans who value explicitness, and which in no way imply lack of trust. Working together to increase areas of agreement is a way to guarantee the future and to affirm the manner in which common interest are developed.

There is also an understanding of investment imbalance between the two, and one way in which flows take place has been foreign direct investment or FDI.

The Japanese FDI into the E.U. has increased over the years, However ,there is an imbalance as Japanese FDI in Europe is more than twice EU investments in Japan.

²⁶ Takenchi Swako , "Prime Ministers Cresson's Anti Japanese Rhetoric" , *Japan Echo*, Vol. XVII, No. 4, 1991, p. 8.

The automobile industry is one such example of FDI conflicts, as the Japanese sought to expand their direct investment into local manufacturing.

There has been change since 1995,²⁷ Japanese- owned firms were manufacturing more overseas than they exported from the home islands, which have resulted in loss of its security for many employees. This could be considered as an erosion of one of Japan's economic structures, where as on the other hand there has been an increased penetration of foreign firms in Japanese market.

The Asian financial crisis in 1997 , had brought many pressures on Japan to change from its long standing inefficient practices. In the midst of a struggle to move beyond the arrangements made more than thirty years the battle is being played. How Japan will come out of it at remains unclear.

The EU fully endorses Japan's commitment to reform its economy. It is clear that macro- economic developments in Japan and Europe constitute the primary explanation for changes in trade and services over the last couple of years.

In the past ,the Euro-Japanese relationship has appeared imbalanced in two respects, it predominantly has been based on economic interactions with little political or cultural interchange. Trade friction acted as a catalyst²⁸ in bringing the two together. In the post -Cold War era , political contacts have been developing and the relationship is marked broader than in the 1980's.

The Euro's introduction at the start of 1999, as a common currency of the European Union has brought a change. It was some what perfectly timed for the Japanese, many of the Asian countries are struggling with currency and economic

²⁷ Pempel , "Japan's search for a new path ", *Current History* ,Dec. 1998 , p . 436.

²⁸ Brian Bridges , *Europe and the challenge of the Asia Pacific*. [Edward Elgar Publishing Limited, UK. 1999]. p. 47.

crisis, Japan too has been stuck in a long recession. The United States is pushing Japan to adopt global standards and is becoming increasingly vocal in its demands concerning Japan's economic and financial policies. The feeling is that Japan is being bullied around by the United States. The Euro's appearance²⁹ on the scene therefore presents a possibility that it may develop into a key currency rivaling the dollar.

In the development of inter-regional relations with the EU, the penetration of Japanese economics into Europe, first in trade and later in investment has brought to the forefront of European concern the question of how to respond to the Japanese. In the post Cold War era, this is moving beyond economics to embrace more fully, political, security and cultural dimensions.

European political forces seem to have coalesced around the "benefits"³⁰ and is seen as EU's new East Asia strategy.

EU – Japan cooperation have come a long way. The process seems slow no doubt, but it a start, Japan and Europe need to trust each other more and learn from each other too, It is not easy to kick a habit of four decades of always turning to the US, but Europe ought to be part of the cure, whereby Japan and Europe could shape the world order.

The next chapter examines this relationship in a changing world environment. One needs to trace the historical background of the European Union and Japan.

²⁹ Noda Nobu, "Japan in a World of Rival Empires", *Japan Echo*, June 1999, Vol. 26, No. 3, p.8

³⁰ Hasegawa Harlikiyo , "Globalization, Japanization and Convergence?" *Japan Review*, 2000, p.36

CHAPTER II

HISTORICAL BACKGROUND OF JAPAN- EU RELATIONS

EARLY CONTACTS

It was not until 1542 and 1543¹ that the Europeans first set foot on Japanese soil, and until that time it was said that guns had never been seen too.

The Portuguese were expelled from Japan, but later we find Christian missionaries in Japan, and in the middle of the eighteenth century we find that there was more information in Japan about Europe than vice versa; an imbalance that still seem to have been carried on in some way or the other.

There was a European continuous contact through the Dutch trading station in Nagasaki. However, the Dutch were more interested in book keeping than writing accounts of Japan.

In general the knowledge of Japan in the Nineteenth century Europe was practically nil and only a cluster of images, of two elements, the image of Japan as a land of exquisite artistic refinement and the land of the charming geisha girls.

The first encounter with the Europeans sparked curiosity, mixed with anxiety, and it eventually led to a firm and complete rejection of foreigners and an effort to purify and strengthen Japanese tradition itself, during a long period of introspection conducted behind closed doors.

¹ Richard Storry " Europe's Impact on Japan: A historical overview" in Loukas Tsoukalis and Maureen White,[ed] *Japan and Western Europe* [Frances Pinter, London,1982]Pg.1

From the seventeenth to nineteenth centuries when Japan was closed, not all contacts with the west was lost. As part of the policy of closing the country (Sakoku)², not only were all foreigners forbidden to enter Japan, but Japanese were forbidden to go abroad or teach the language to any one outside. There was also enforced censorship on imports of western books.

WESTERNIZATION

The Meiji Era brought about European influence on Japan to its height. In these years the wearing of western clothes and the sporting of western hair styles was taken as a sign of cultural openness. The army uniform was westernized the court and the government sartorial impact bureaucracy adopted western clothes.

Another was to wipe out the shame of unequal treaties by which the foreigners in the Treaty Ports³ enjoyed extra territoriality, and the Japanese government had no tariff autonomy to show the world that Japan should be treated equally.

Knowledge too was no doubt influenced and the years 1866-1878 all the nine best sellers were translated books of western works: They were, Fukugawa Yurichi's "Conditions in the West", Samuel Smile's "Self Help", Fukugawa Yukichi's "The Encouragement of Learning" and J.S. Mill's on "Liberty".⁴

² Endymion Wilkinson, *Japan Versus Europe*. [Penguin Books, England, 1980] p. 99.

³ *ibid.* p. 108.

⁴ *ibid.* p. 108.

DISILLUSIONS

At the same time there was an increasing movement of nationalism, sparked off by the breakdown of efforts to negotiate the revocation of unequal treaties.

There were other factors of disillusionment with Europe. As people traveled, there was growing awareness of the gap between Europe and Japan and the racist treatment which many Japanese encountered overseas.

Further disillusionment with Europe came after the First World War, when the idea hitherto seen Europe as the home of liberty and enlightenment was shattered. The defeat of Germany also meant the collapse of one of Japan's most respected models.

In the 1930's there was a growing dissatisfaction with Europe, triggered off by the negative images evoked by the trade friction during the Depression period.

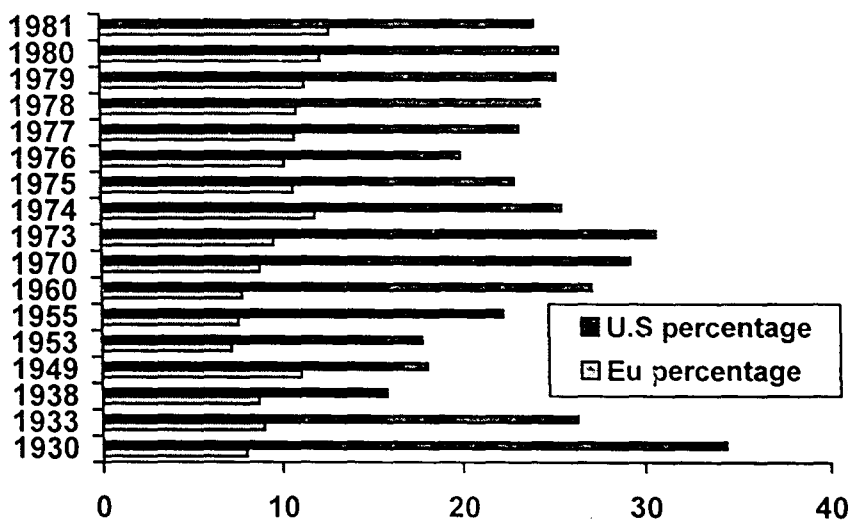
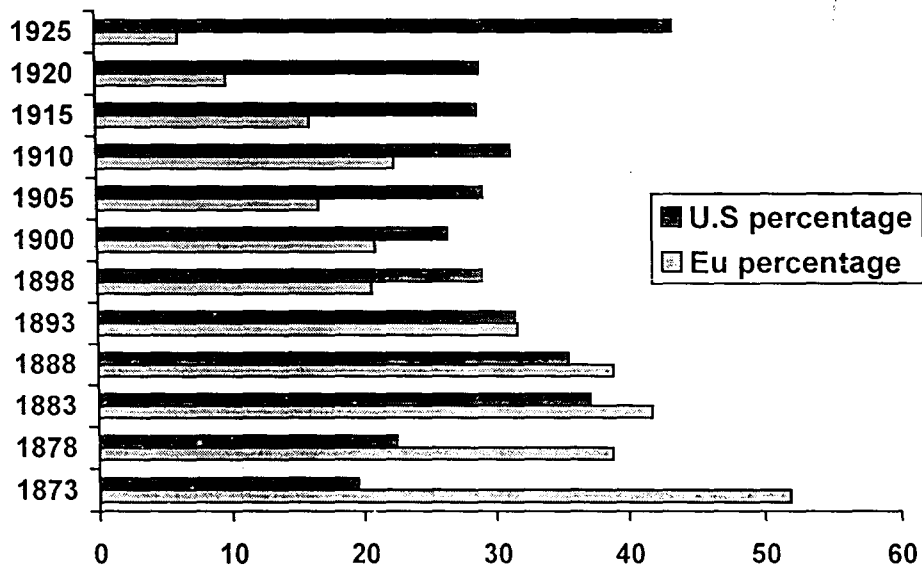
Trade also had been unequal in a sense that Europe has been a much more important source of supplies and market for Japan than Japan for Europe. Great Britain was Japan's main supplier of modern goods, viz., munitions, machines and cotton goods.

It was only until 1915 that the United States of America exported more to Japan than to the European countries. Europe was Japan's major export market for raw silk, tea and rice until the United States took Europe's place.

Trade relations were of those between a developed region and an underdeveloped country, not only in the nature of goods exchanged, but also the degree of importance attached to trade by each partner. While to Japan it was vital, to Europe it was marginal.

The figure below shows statistics of the trade relations between the two and also United States.

JAPAN'S EXPORT⁵



Source: Calculated from Ishibashi Tanzan, *The Foreign Trade of Japan*, Tokyo, 1935 for 1883 to 1981, Ministry of Finance, Tokyo.

⁵ Endymion Wilkinson, *Japan Versus Europe*, [Penguin Books, England, 1980]p.162.

JAPAN CATCHES UP

The government of Japan did pursue mercantilist policies of import substitution to which European businessmen complained bitterly, and echoes of which can still be heard today. As a result of the First World War, Europe was unable to maintain its exports to Japan and thus the United States became Japan's main supplier. Japan was far from the active in the theatres of war and her industries were able to take advantage of markets which Europe could not due to the war.

Bit by bit Japan built up her light industries and began to expand her exports to world markets. Denunciation of Japan's supposedly unfair trading practices reached a peak in the Depression period turning Europe against Japan. A delegation was sent to Japan in 1934, which on its return, did not achieve much. The report drew attention to the high productivity of the Japanese industry despite the economic depression in Europe and the outcry against Japan. It led to discriminatory quotas and high tariff which gradually led to the closing of European markets to Japanese goods, and made Japan turn Eastwards.

In 1955, when Japan entered the General Agreement on Tariffs and Trade several of the European countries refused to extend 'most favoured nation' treatment⁶ to her.

Japan's trade policy was therefore directed towards concluding individual trade agreement. The problem was that the old fears of Japan flooding European markets with cheap goods were still very much alive. It was much later that article

⁶ They involved article XXXV of GATT.

xxxv of GATT was revoked against Japan. However, several countries still had safeguard clauses included in their trade agreements in order to take unilateral measures to stop Japanese imports in case of emergency.

Such overt discriminatory restrictions have been reduced, although they continue to exist in some form or the other causing hitches in the E.U. - Japan relations.

The shape of the European community's policy towards Japan was determined by an act of conscious choice. The community's question on trade matters was set out in the Treaty of Rome and was to develop in to a common commercial policy. As per the Treaty of Rome the nation states could negotiate separately, however this came to an end in 1970.⁷ From this time on trade agreements were conducted by the European Commission on behalf of the Community.

The Commission delegation was set up in Tokyo in 1974, to facilitate contacts. However, the heads of Delegation had a hard time establishing their new position. There were also difficulties from the member states diplomatic offices who were bewildered by the precise functioning of the heads of delegation. This caused tension and serious difficulties arose in the pursuit of a European policy towards Japan. There were earlier efforts for an agreement with Japan, but these were not fruitful due to the Nixon shock of 1971 and the Oil crisis of 1973.

⁷. Simon Nuttall, "Japan and the European Union: Reluctant partners", *Survival*, vol. 38, Summer 1996 ,p.106.

The Japanese reacted very seriously to these changes in the economy and they redoubled their exports. This fueled Europe's resentment and causing it to press for greater market access in Japan a move unappreciated by the latter.

Four years later, the European Commission attempted to bring about Voluntary Export Restraints (VERS), which also failed.

The repeated efforts by Europe to gain market access finally led the European Community to challenge the validity of the Japanese economic system in international trade. It launched its complaint under Article XXIII⁸ of the General Agreement of Tariffs and Trades. (GATT). The Japanese then agreed to give some concessions by moderating the export of ten items, including from Video-tape, colour television sets, fork lift trucks and machine tools.

The replacement of Europe in the Industrial sector by the US and then Japan everything during the 1970's, which consisted of things that moved on wheels, example cars, trucks, tractors, motorcycles, bicycles as well as radios, stereos, televisions all made in Japan. These consumer durables were the most striking signs of the massive flow of Japanese exports and investment in Europe. European goods consisted mainly of luxury items like Mercedes Benz or BMW cars, resulting in the low volume of European exports to Japan⁹.

In line with these changes, the number of European business centres in other parts of Asia also declined and their place is taken over by the Japanese.

⁸. Ibid, p.106.

⁹. Endymon Wilkinson; *Japan Versus Europe*. [Penguin Books, .England, 1980] p .150.

The diminishing economic role of Europe and the increasing importance of Japan, are crucial to the understanding of trade friction in the 1970's and the emerging pattern of regional alignments in the 80's.

These instances of friction have usually occurred when a decline in the domestic demand in Japan and the resultant strong pressures to export coincide with a down turn of the business cycle in Europe, mostly in labour – intensive industries.

During this time the old fears of Japan flooding European markets with cheap goods were still very much alive and it made the Community to have a safeguard clause in any agreement it made Japan. At the same time it also sought assurances that the Japanese market would be opened to its number countries exports.

Between 1970 and 1980, in current dollar term, Japan's exports to the community increased ten times.¹⁰ For most of this period, the Europeans were thrown on the defensive and could only request the Japanese to co-operate by restricting their exports.

The best the Europeans could do was to seek a breathing space to enable their industries to restructure in order to meet the competition from Japan. The trouble was that this led to a decline of industries and therefore efforts to put protectionist pressure on access of Japanese markets, thus leading to lowering of tariffs.

¹⁰ *ibid.*, p.173.

In order to remove barriers, the EC Commission held talks with the Japan (on Non-Tariff Barriers) and a list of the topics covered were automobiles, agricultural processed food, chemical testing standards, tanking, trademark and sanitary fitting standards.

One of the main Non Tariff Barriers dealt with before the outbreak of the EC- Japan trade friction in October 1976, was the question of testing for automobile type approvals which were felt to be more cumbersome in Japan than in the EC, and the introduction of new emission standards which were stringent.

The Japanese car industry was gaining its lead in the 1970's while the European Industry was on the decline. European car exports to the world declined by 30% 1970 and 1980 largely because they could not compete with Japanese exports. In 1970, European car makers had a 68% share of the foreign car market while the Japanese had only 28%. By 1980, tables turned, and the Japanese took 76 % while the European share was 21%.¹¹

This issue became a Community one in 1975, and led to EC- Japan specialist consultations in Tokyo in May 1976. Eventually the Japanese authorities did recognize that there was a problem of reciprocity of market access and agreed that type-approval test for European cars for export to Japan could be carried out in Europe.

Over the years considerable progress was made in some sectors like chemical and pharmaceutical testing to bring them more in line with international

¹¹. Endymion Wilkinson, "*Japan Versus Europe*", [Penguin Books, England, 1980] p. 177

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practice, thereby giving the European exporters similar conditions of market entry as enjoyed by Japanese exporters in Europe.

There was a wide trade deficit of the EC with Japan and when a mission of industrial leaders to Europe led by Mr. Diko Teshio, President of the Federation of Economic Organization. The Delegation was confronted with bitter criticisms wherever they went. These were centered on Japan's export in five¹² problem sectors, steel, ships, home electronics, bearings and cars. On Their return to Tokyo. the Japanese delegation tried solving the problem by curbing the exports in the five sectors in an effort to head off protections pressures, the EC, Commission emphasized the necessity of increasing access to the Japanese market for European exporters.

Since then the EC and Japan went through bouts of trade friction and this was further complicated by the United demanding concessions for Washington as well, unable to see the EC walk away with the concessions form Japan. The friction so intense that each time Japanese negotiator visited Washington he was under tremendous pressure to visit Brussels.

In the 1980's Japan was found to have risen to the peak of the business cycle. The Japanese GNP grew three times faster than that of the European. Inflation was also lower. At the same time Europeans' bilateral deficit with Japan

¹² ibid. p.189

was rising. At this point of time there were new sectors that became sensitive¹³ like machines tools and computers.

There was considerable discussion of a trade war and calls for protection against Japanese imports intensified that was also heard in Germany, a staunch supporter of free trade in the European Community.

In the summer of 1980, the EC brought out a new proposal to the Council of Ministers to negotiate on EC-Japan trade agreement. The proposal fell on deaf ears as the EC members were reluctant to give up their restrictions against Japanese imports. Later, the Commission again set up a tougher set of proposals for a common Community approach towards Japan which was accepted by the Council of Ministers. Japan was warned that steps towards a further forward looking dialogue, will include, liberalization of each other's markets and Industrial Co-operation. In addition the government was to let the yen revalue and to have greater facilities for European investment and banking. The Japanese government reacted stiffly to these proposals and issued statements that were to make the Europeans work harder to export to Japan.

Meanwhile, the US began putting pressure on Japan, with its trade legislation for reciprocity, where by the latter would be required to imports cars. The Japanese set up a special Committee for International Economic measures. This new Committee announced two set of measures to increase the access to the markets. The first was tariff cuts and the removal of sixty seven out of ninety nine

¹³. Geoffery shepherd; "Japanese exports and Europe's problem industries", in Toukas Tsoulalis and Maurean White.[ed.]*Japan and Western Europe*. P.138.

non-tariff barriers and secondly, the establishment of a new office of Trade Ombudsman to handle specific complaints of foreign businessmen.

The European Community gave priority to opening up of the Japanese markets and for extensive removal of formal tariff barriers. During this time, the EC took Japan to the GATT, under Article 23¹⁴ over the keiretsu system.

At the Tokyo round of negotiations of GATT, the EC took a much sterner stance against Japan on a range of issues and without prior consultations with the Japanese government. The EC imposed anti-dumping duty on Japanese import on ball bearings. A number of other followed, such as acrylic fibres, and stereo cassette, colour televisions, cathode ray tubes, quartz watches, and electronic type writer.¹⁵

The EC investigated a total of twenty two antidumping cases against Japanese imports.

Increasingly higher the profile of the Commission in the EU – Japan relationship coincided with a more cordial environment as the decade progressed. It would be attributed to the end of the world's recession and a historic agreement signed for dialogue policy in the G7 meeting in 1985.

Japan agreed to re-value the yen, while the EC then adopted concessions on qualitative restrictions on Japanese imports.

¹⁴ Brian Bridges, "Japan and Europe," *Asian Survey*, Vol. XXXII, No. 3, March 1992, p.232.

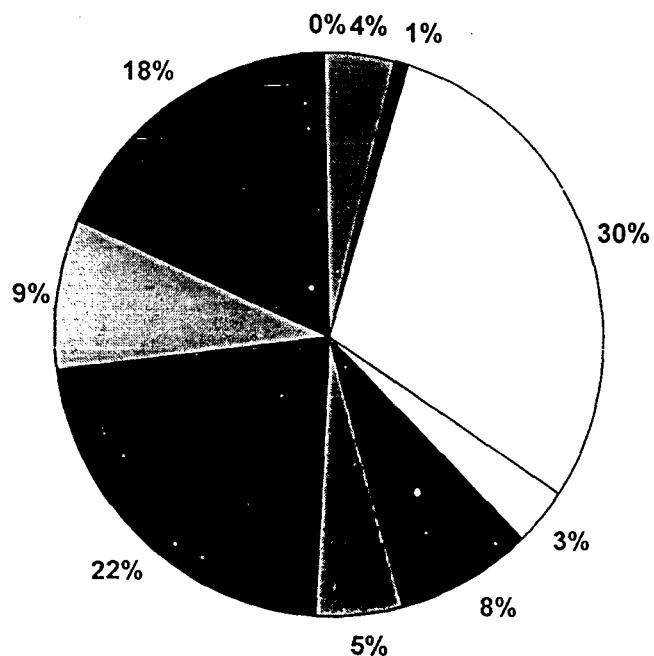
¹⁵ Christopher M. Dent, *The European union and East Asia*, [Routledge Publishers, London, New York, 1999], p.91

Japan's current account surplus was \$793 billion in 1985¹⁶. EC-Japan relations were further enhanced by the initially favourable view Japan took towards the Single European Act of 1986. however there was simultaneous concerns about the single European market that a "fortress Europe" was emerging.

Further Japan acknowledge that SEM would increase the community's weight on the international economic system.

¹⁶ EC documents, COM 86, 6th March 1986.

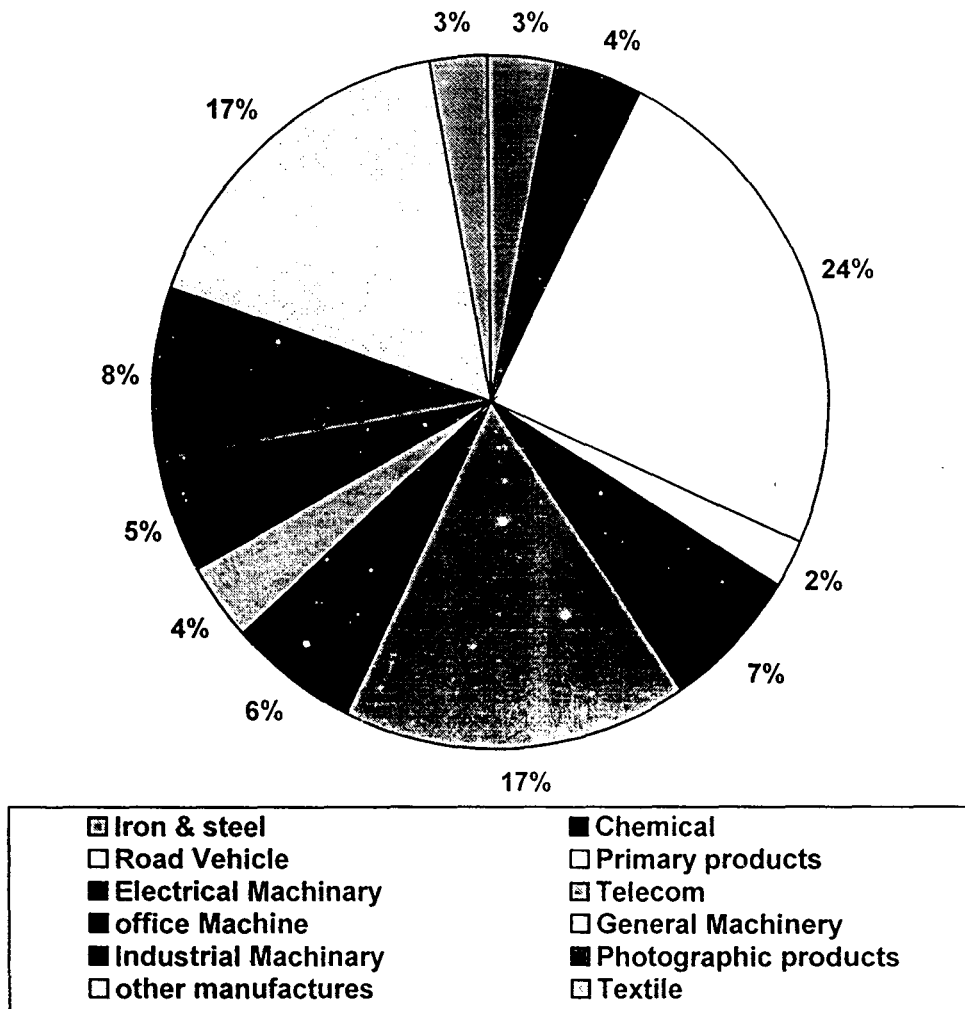
JAPAN EXPORT TO THE EU BY SECTOR 1980¹⁷.



■ Electrical machinery	■ Telecom & Audio
□ Chemicals	□ office machine
■ Road vehicles	■ General industrial machinery
■ other manufactures	□ specialize machinery
■ primary products	■ Misc.
□ Textile And Clothing	

Source: Eurostat.

JAPAN'S IMPORTS FROM THE EU IN 1980¹⁸



Source: Eurostat.

Japan-EC relations improved since 1988, albeit not to the point of being able to influence global politics. On the European side in 1988, the EC Council adopted a set of conclusions which altered the way the Community approached. Traditional analyses of trade –policy positions in the EC portray the

¹⁸ Christopher. M Dent, The European Union and East Asia, [Routledge Puplicher, London, 1999] p.104.

Mediterranean's countries as protectionist, and therefore anti-Japanese, and the northern Countries as free traders, therefore pro-Japanese. The British were in fact the most anti-Japanese and in 1988,¹⁹ the British changed tack. They realized that the Japanese were of greater benefit to the UK and it was during this time the EC won the liquor tax panel in Geneva. The British changed sides and the Community followed it. Trade issues continued to dominate the day to day exchanges, but more effort was put bring subjects like science, technology, environment and development aid policy on which to the dialogue table.

TRADE DISPUTES:

TEXTILES:

Textiles has gone further as a Japanese export and became a sensitive item. In the Inter-war period, Japanese cotton textile exports were making large inroads into Europe, particularly the U.K., which remained in the 1960's as well as making Japan the largest exporter of textiles on the other hand the Europeans limited the Japanese imports by means of quotas.

However in the 1960's Japan diversified into synthetic textiles, causing the U.S. to adopt protective legislation resulting in the imposition of VER's on Japan this made Japan to divert it's cheap exports to Europe. With this in mind, the Europeans and Japan agreed to a discussion at GATT, and the multi fibre Arrangement was signed in 1974.²⁰

¹⁹ Simon Nuttal, "Japan and the European Union: Reluctant Partners", *Survival* Vol. 38, No. 2, Summer 1996, p. 108.

²⁰ Geoffrey Sheperd, "Japanese Exports and Europe's Problem Industries", in Loukas Tsoukalis and Maureen White (ed.) *Japan and Western Europe*, (Frances Printer, London, 1982), p. 138.

Steel has many parallels with textiles. Japan's steel exports began to develop in the 1960's. Its share in the world production peaked in the 70's to 20%.²¹ 'The success of the Japanese Industry was largely due to large scale production which was linked with modern technology to car and ship building Industries.

The US issued VER's with the Japanese and the Europeans fearing diversion again, followed similar arrangement. The EC introduced a price minima or guidance on major products and Japan agreed to it.

The major difference in international trade barriers in textiles and steel is that the former involve many exporting countries and relate almost entirely to quantitative limitations while the latter concerns few exporters and emphasise price support as much as quantitative limitations.

CARS:

Japan's car industry only started serious production in the 1950's and achieved a significant growth, where by in the 70's it over took the Europeans export, which so far had dominated world market.

Japanese export strength has been based on concentration of small, fuel efficient cars, a limited number of alternative car specifications, high product reliability, increasingly automated process, high volumes of production and low part inventories.

The first major Japanese impact in Europe was in small non-producing Countries like Switzerland, Finland, Norway, Portugal and Australia.

²¹ . Ibid. p. 139.

U.K. had a Voluntary Export Restraint with Japan limiting steel import at to 11% not allowing it to exceed 3%²² in France. This also spread to Germany and other European Countries. This rapid spread of protection forced Japanese producers to envisage production abroad. This prospect was increasingly accepted by major countries as a way to solve trade conflicts.

The first step towards co-operation came in 1981, when UK decided to have Nissan bring a production sector to Britain to serve the European Community.

COLOUR TELEVISIONS:

Since 1950's Japan has gradually climbed to one of the Countries occupying a commanding position in world exports.

UK had privately negotiated a VER with Japan, France, Italy too obtained EC agreement to stop the import of Japanese T.V. sets.

Thus while trade conflicts with Japan eventually settle down, in one product area, they are inevitably rising in new product areas.

METAL WORKING MACHINE TOOLS

Japanese metal working machine tool production expanded in response to the rapid growth in demand from the domestic engineering industry, particularly cars.

However, Japanese exports to Germany, France, Britain and Netherlands doubled in value terms within a short span. While the Japanese government organised an export cartel of it's raise the prices to the exports to the EC.

²² Ibid. p. 142.

FOREIGN DIRECT INVESTMENT

It was in the 1960's that Japan embarked upon a rapid effort to expand direct investment. A number of factors both within Japan and the global economy, encouraged such expansion of capital flow outside Japan's borders.

The Japanese economy was reaching its peak of growing phase, which resulted in a higher domestic wage. The yen was strengthened as a consequence of the export competitiveness. At the same time there was a sharp rise of prices of rawmaterials and scarcity of energy .this led Japan to look overseas.

Europe lacked the initial attraction, due to the absence of natural resources, US offered a number of advantages over Europe. Japanese were more familiar with American markets, there investment in Europe was by no means large.

In 1960 it was 1.1 per cent by 1968 it reached 56 million which is 6%. In the 1970's it expanded to 15.8% and in 1980 it was 12.2% Japanese investment in Europe was connected with the exporting effort, as manufactures set up wide network for distribution.

In the early 70's, market forces tended to favour investment in the production of manufactures. In some sectors Japanese technology was already considered superior.

Out of the total Japanese investment in Europe in 1981, services and finance occupied more then 23% and 15%²³ respectively, and investment in

²³ Suelo sekiguchi, "Japan Direct Investment in Europe", in Loukas Tsoukalis and Maureen White (ed.) Japan and Western Europe, (Fracnes Pinter, London, 1982), p. 169.

commerce accounted to 17%. So a substantial investment was for services than production.

The relative strengthening of the yen was accompanied by the rise in the wage rates in Japan. The Japanese wage rate exceeded those of the Europeans, in comparison led This and the rising cost of infrastructure made overseas production favourable.

There was also a rising location cost for new Industrial sites in Japan, so in many cases it seems more favourable to produce certain products out side Japan.

Investment incentives offered by European government too, the use of FDI had become increasingly a common tool to promote capital flow into depressed regions. The incentives offered range from subsidized loans, export credits, favourable tax rates and many more.

JAPANESE DIRECT INVESTMENT IN EUROPE ²⁴

Country	Year		
	1970	1975	1980
U.K.	254	01505	1823
Germany	12	137	387
France	13	135	300
Netherlands	N.R.	91	257
Belgium	5	77	225
Switzerland	N.R.	64	163
Ireland	N.R.	N.R.	135
Spain	N.R.	N.R.	151
Others	19	175	160

Japanese direct investment in Europe by country in US million dollars.

Source: Data of Ministry of Finance and MITI.

Looking at country by Country breakdown of Japan investment, the largest portion has consistently been the UK, and an important factor could be the use of English as a language for communication.

Anticipation of greater restrictive trade policies in the future from the European Countries added the element of urgency to invest out more.

In fact by 1981, most of the European Countries succeeded in getting some sort of limit on car exports to their markets while to Belgium 7% of ²⁵,to West Germany 11%.²⁶

Apart from the above that are essentially defensive, Japanese manufactures too were gaining confidence in their ability to produce abroad.

²⁴ Suco Sekiguchi, "Japanese direct investment in Europe", in Loukas Tsoukalis and Maureen White (ed.) (France Pinter Ltd., London, 1992), p. 173.

²⁵. Ibid p. 173.

²⁶. Ibid. p. 173.

It was rather feasible to duplicate some of the advantages of Japanese production techniques.

Another area of European criticism of Japan is dumping of exports on world markets or unfair competition in pricing and marketing.

The Japanese experience with Europeans since the sixteenth century has been of dealing with individual nation states. This has changed since then. This can be attributed to the Europeans coming together as a Community, and its adoption of institutions.

In some sectors like Cars, TV's the EC does not act as single unified market, as there are special import restrictions from individual member states.

CHAPTER III

EU- JAPAN DIALOGUE: A SURVEY

In the Post Cold War era, the international political scene is changing rapidly and continuously creating an increasing need for closer political discussion and co-operation between countries. In this new geo-political climate, the economic and trading power of the EU and Japan and their long established relationship in these fields, means that consultations and a common approach to each other is both logical and desirable.

This was reflected in the 1991 Joint Declaration on relations between the European Community and its member states and Japan which established objectives and framework for political dialogue between the two at all levels.

The EC-Japan Joint Declaration 1991

The EC-Japan Joint declaration issued at Hague in July 1991,¹ introduced a political dimension into the relationship. The Declaration set out joint political objectives based on a number of shared principles including the need to promote freedom, democracy, the rule of law and human rights and the common attachment to the principles of a market economy.

The E.U.- Japan dialogue aimed to improved co-operation on promoting negotiated solutions to international or regional tensions. The main structures for pursuing these aims consisted the following:

An annual summit between the President of the European

¹ *European Commission Documents*, "A Consistent Global Approach", Brussels, 0/92/136. p. 1.

Council, the President of the European Commission and the Prime Minister of Japan.

EU-Japan Troika Ministerial Meeting: – biannual meetings between the EU Troika at the Foreign Ministers level and the Japanese Foreign Affairs Minister.

EU-Japan Troika Political Directors Meeting: – biannual meetings between the EU Troika and Japan at the level of Political Directors.

The EC –Japan Joint Declaration confirmed cooperation on international and trade questions and on access to each other's markets, on principle of equitable access based on comparable opportunities.²

- The intensification of dialogue in this new frame work allowed identification of new fields of cooperation between EC and Japan.
- To strengthened the EC-Japan center for industrial cooperation and also open to the EC and Japanese firms to conclude strategic alliances on the development and production of new products.
- The Joint Declaration explicitly identified environment as an area of cooperation. A clear impetus was given by the first high level consultation on environment held between the two countries.

² *European commission document*, "New European Guidelines for Relations with Japan", June, 1992, p.2

- The declaration also relaunched a coordinated effort approach by all donors to make sure that there is effective policy reforms adopted by developing countries.
- There was also a joint programme ,started to promote exchange of experts ,from government and industries to jointly study unemployment problems, train industrial relations and labour affairs.³

HAPPENINGS IN 1992

The Second EU-Japan Summit was held in London in 1992, and the third took place in Tokyo but nothing came out of it. There was always difficulties in organizing the diaries of busy Prime Ministers.

In 1992, the significant aspect of this relationship was reached, whereby two elements were important, the Trade Assessment Mechanism (TAM)⁴ and the new policy of industrial co-operation came about TAM enabled both sides to compare their respective trade performance on the basis of objective trade statistics.

This mechanism was useful for problem solving. The second purpose of TAM is to put trade discussion on an explicitly objective and reciprocal basis.

The third purpose is to provide a permanent meeting forum for the Japanese and the Europeans. There have been more meetings held under TAM.

³ *ibid.*, p.4

⁴ Simon Nuttal, "Japan and the European Union: Reluctant Partners", *Survival*, Vol. 38, 1996. p. 110.

The second element in 1992 was industrial co-operation⁵. EU and Japanese firms were to conclude strategic alliances on the development of production of new products. Both will share the cost and risk of new investment to engage in research.

The negotiations were not easy as both sides suspected the other of having a hidden agenda. Some Europeans felt that Japan by stressing for the need of political cooperation was trying to divert attention from core economic issues. The Japanese on the other hand felt that some Europeans were trying to impose managed trade as the price for engaging in political dialogue.

It is important to note that from the year 1986 to 1990, the EC-Japanese ministerial meetings were suspended and this was broken by the EC President Jacques Delors when he visited Tokyo in 1991.

Trade statistics show that, Japan's trade surplus declined in 1990 to 1993, in 1992 it was \$31.2 billion, and came down to \$ 26.3 billion in 1993. Trade imbalance is equal to the imbalance between saving rates and investment and to be addressed by both countries.

The sixth EU-Japan Ministerial meeting was held in Tokyo on 19th November, the main topics discussed were trade and economic relations, which included market access problems and EU-Japan co-operation and exchange of views on international relations.

⁵ *Europe Document* ,N. 1779/80, p. 6.

The areas⁶ of progress were: Market access – progress was made in public procurement, administrative procedures, competition law enforcement, foreign legal services and new measures were announced by the Japanese authorities, on the introduction of “use by date”⁷ on food product labels and also acceptance of the European Union certification for textiles, medical devices and electrical appliances.

Agreements system – a system of EU-Japan monitoring to ensure MNF treatment of EU products was established. Japan indicated that equality would be a priority and not political considerations.

MRA’s – The Mutual Recognition Agreement was launched during this time.

IMPROVED RELATIONS: 1994

In 1994, the community succeeded in inaugurating a continuing dialogue with Japan with regards to the deregulation question. The commission sent a request list to assist in the five year programme, announced in March 1995. In 1994, there was a “Gate-way-to-Japan”⁸, campaign, as Europe and Japan were showing signs of climbing out of long recessions. The campaign consisted of seminars on medical devices, and mechanical handling equipment. There were fairs for companies from the EU and outside.

⁶ *Europe Magazine*, No./Dec. 1994,p. 10.

⁷ *Ibid.*, p. 10.

⁸ *Focus Japan*,vol.21, July/August, 1994,p .8

In the same year the Japan Federation of Economic Organization issued a statement where by the following measures⁹ would be taken to improve relations.

- expand domestic demand and promote EU systems and business practices.
- Improve access to Japanese markets and to eliminate trade barriers.
- Promote increased technology transfer from Japan to EU.
- To assist European firms in designing stronger Japan market entry strategies.
- Promote a Japanese business climate more favourable to foreign investment.

A PROCESS ON: 1996

In 1996, the Japan-EU Troika Ministerial Meeting took place where issues such as EU-Japan relations, EU unification, problems in Myanmar, the situation in Bosnia and Middle East ect. were discussed.

In the same year the third Japan-EU Mutual Recognition Agreement Negotiation¹⁰ took place in Tokyo, Mutual Recognition applied to industrial products which are required to conform as a matter of law to relevant standards in order to be distributed in designated markets. It was agreed that the two parties must accept the test data issued by the other party's testing institution and also permit distribution of the products manufactured in other party's country in its own market if certified.

The objectives of these Negotiations were

- to establish a collaborative framework between Japan and the EU.

⁹ "Thoughts on the Future Economic Relations between Japan and Europe", www.ictsd.org/weekly/sto.y/4.30-01-01.htm.

¹⁰ "The 3rd Japan-EU Mutual Recognition Agreement Negotiation ,press release", www.europa.eu.in/comm/external-relations/japan.

- to provide consumers with increased direct benefits by simplifying and expediting the procedures, and
- to facilitate market access and wider trade between the two countries.

In September 1996, the Fifth EU-Japan summit¹¹ took place in Tokyo,

- which reviewed the events of the meeting in 1995 and expressed satisfaction with the developments in this relationship.
- confirmed their commitment to the terms of the joint declaration issued in 1991. The EU welcomed the involvement of Japan in the efforts to build a stable peace in former Yugoslavia and its contributions to the reconstruction assistance in Bosnia and Herzegovina. Japan too welcomed the contribution of EU to the Korean Peninsula Energy Development Organization (KEDO).
- stressed on the importance of Japan's contribution in supporting political and economic reforms in Central and Eastern European countries.
- Both sides welcomed the adoption and opening for signature of the Comprehensive Nuclear Test Ban Treaty (CTBT).
- They also agreed to work actively for the achievement of an effective international agreement to ban landmines.
- Food security was recognized as an area where EU-Japan co-operation would be beneficial.

The first European Union-Japan Round Table on higher education was held in 1996, the main objective of the round table was to start an exchange of

¹¹ *European Commission Documents*, "Fifth EU/Japan Summit- joint press statement" IP/96/867 Brussels, 1996, p1.

information on respective systems and programmes. It was also a confidence - building exercise which laid the basis for a number of initiatives like using the credit transfer system, language learning for both, exchange of university staff and intensive summer courses.

Japan gave \$800 million for the reconstruction of Bosnia and Herzegovina and \$ 200 million to Kosovo¹². Both the EU and Japan are closely co-operating in the reconstruction of former Yugoslavia where Japan is the third largest contributor after the EU and US. EU has also contributed to build a light water nuclear reactor in North Korea, in project known as KEDO, which is likely to alleviate serious concerns about non-proliferation in the peninsula and to ensure that North Korea adheres to the non-proliferation regime.

There is a persistently high Japanese current account surplus, and the EU sees this as a reflection of market access difficulties in Japan for foreign firms. There is evidence to show that policies and co-operation between the two are working, surplus fell to 2.2% of GDP in 1995 from 3.2% in 1992, to 1.3% in the first half of 1996.¹³

In the same year, the expert dialogue meeting was held, which discussed a number of regional issues, such as Asia, CIS, Middle East, and also evaluated the national elections in Bosnia and Herzegovina.

A Year of Improvement:

In 1997, some of Europe's biggest musical names enjoyed better copy right protection in Japan for the hits they produced during the fifty's and sixties. After a

¹² "EU-Japan Relations", www.jpn.cec.eu.int/English/eu-relations/index.html.

¹³ *European Commission Documents*, Memo 96/92/Brussels, September 1996, p. 3.

year of negotiations, the Japanese Parliament has agreed to back date the intellectual property protection. The EU and Japan also agreed to resolve the liquor tax dispute. Intensive discussions led to an agreement on tax on imports. This was a dispute that was taken to GATT ten years ago.

Both these issues will be discussed in the next chapter under the GATT and WTO section.

1997 was also a “Year of Japan in France”.¹⁴ In April the list included fifty seven events but in May the number rose to seventy one. The number of events increased every month more than half occurred in Paris, indicating that the capital plays a major role in defining the Japanese culture outside Japan.

An analysis of EU Japan sectoral patterns, reveals a shift in the technological balance of trade towards Japan in 1997.

The figure above shows that a relatively high proportion of EU exports to Japan in 1997 consist of primary products at 11%, compared to only 0.7% of Japanese exports to the EU. Also a high proportion of EU exports to Japan is concentrated in lower technology sectors like textile and clothing, while the share of Japan is high in high-techno exports. Thus the Japanese competitive challenge to the EU remains significant.

The year 1997, proved to be a critical year for Europe as well as Japan, in Europe, major progress was made towards creating a new order in the areas of politics, economics and security. The Amsterdam Treaty was signed which stipulated basic guidelines on EU expansion, structural reforms in line with

¹⁴ Sylvie Guichard Rovt. Auguis, “Japan through French eyes”, in *Globalizing Japan*. (ed) Harumi Bafu and Sylvie. G.A., [London, Routledge Publishers. 2001], p. 210.

deepening of EU and enlargement was carried out. The central and Eastern European countries were seeking admission to the EU, and this year negotiations for accession of five central and European states to EU came about.

In the economic sphere, progress was made regarding the economic convergence criteria necessary for the Economic and Monetary Union. Therefore Europe set a trend which will have an impact not only in the stability of Europe itself but also on the whole Asia Pacific region, therefore it is vital for Japan and Europe to work together.

Japan's course was to maintain and develop close consultation and dialogue with Europe.

A number of concrete co-operative frameworks were created, between Japan and the different member states of the EU. The Prime Minister met with leaders from United Kingdom, France and Germany and various key figures visited Japan.

Action Agenda¹⁵ for Japan-Germany Partnership was revised during this time, where bilateral co-ordination took place in the dispatch of special envoys to Cambodia.

1998

In 1998, the Seventh Summit, took place, between the two, they expressed their confidence in Asia's long term economic prospects, but stress the need of reforms through appropriate macro economic management, financial supervision and other structural measures.¹⁶

¹⁵ *Diplomatic Blue book*, 1998, Published by the Minister of Foreign Affairs of Japan, p. 139.

¹⁶ 7th EU-Japan Summit press release", www.infojapan.org/region/Europe/eu/summit.

Both sides committed to forge closer links between Russia and the international community, they also stressed on the implementation of the Dayton Peace Agreement for Bosnia and Herzegovina, agreed that UN reforms must be balanced and to work together for sorting out UN's financial difficulties.

The other areas of cooperation broadened, to landmines, where they agreed, to an effective ban on anti-personnel mines, social protection employment, and environmental cooperation.

In 1999 a remarkably extraordinary achievement in Europe was marked by the introduction of the Euro, as a single currency. There is no doubt that this has brought changes, firms were being forced to change with technological innovation.

The Euro has brought about changes in economic infrastructure, including transportation, electric power, telecommunication and finance.

The Euro has affected Japan, it can be seen in direct investment, from EU to Japan, which soared to more than ten folds a year, from about 100 billion yen in 1998 to over one trillion yen in 1999.¹⁷

Japan would deal with one currency, one interest rate and one standard of entry, also it would witness mergers at the euro's arrival.

The Ninth EU – Japan Summit was held in 2000,¹⁸ in Tokyo. and the following subjects were discussed, strengthening of Japan-EU partnership both in

¹⁷ "9th EU-Japan Summit, News and Views from Japan", www.boj.org.jp/en/press/koen

¹⁸ "The Euro", www.info.japan.org/region/europe/ev/summit/joint007.3.html.

economic and political matters, Japan EU cooperation in international fora like the G-8 summit, the United Nations and ASEM.

The ten years starting in 2001 were declared the “Decade of Japan-Europe Cooperation” and it was agreed to start preparation for the next summit. They agreed on four key objectives for the new dialogue.

1. Promoting peace and security

Japan and EU will promote peace and securing they will enhance political dialogue where concerted actions maybe included when necessary.

2. Economic and Trade Partnership

Japan and EU will jointly seek to utilize the dynamism of globalization. Areas of co-operation will include WTO, international Monetary and financial system, regulatory reform, improving market access, improving the environment and electronic commerce and telecommunication.

3. Coping with global and social challenges

Contemporary societies are facing such global challenges as environment, health and energy issues. Japan and Europe are also undergoing problems common to mature societies which includes ageing population and employment to meet these challenges, they will cooperate in environment, health issues, food safety, energy issues, bioethics, science and technology, gender equality and satellite navigation.

4. Bringing together people and cultures:

Japan and EU will encourage all forms of dialogue and exchange between people in particular. This will include cultural exchange, student, exchange, cultural events and exchange between citizens.

In 2000, Japan imposed a ban beef imports from the EU so to shut of mad cow disease. The Ministry of Agriculture, Forestry and Fisheries, decided to ban processed beef food stuffs ect. to prevent to disease from spreading to Japanese farms. The ban was to remain in force till safety was verified, it is interesting to note that Japan imported only 463¹⁹ tons of beef and beef products in 1999.

Japan and EU have underlined the importance of promotion on information technology for creating an appropriate electronic commerce environment. They have also brought about the Euro Japan Technology Month in 2000, bringing IT professionals together.

The tenth EU –Japan summit was held in Brussels. In this summit, a number of important international political issues, especially Afghanistan were discussed, Both sides underlined their support for reconciliation and reconstruction. Just after the summit EU – Japan agreed to bring peace to a war torn country, an Action Plan²⁰ to host the Donor conference for Afghanistan in Tokyo was agreed and preparations for this was done in Brussels.

During the summit, there was a Joint declaration.²¹ on Terrorism, they strongly condemned the Terrorist attack on the United States on September 11.

The both agreed that fight against international terrorism will not be effective unless it is based on sustained efforts, pursued in accordance with international law.

¹⁹ Japan News Letter, Published by the International Department Kyoto News, Tokyo, Dec. 29, 200. p.1.

²⁰ Japan News Letter, Published by the International Department Kyoto News, Tokyo, Dec. 14, 2001, p. 4.

²¹ Action Plan, www.jp.n.cec.eu.int/english/eu_relations/index.htm.

They expressed their support for military action taken by the United States and other countries. In order to give substance to fight terrorism, they resolved to cooperate, and an Action Plan for EU-Japan cooperation was highlighted. They also urged early signature and ratification of relevant counter terrorism conventions and protocols. To stop financing of terrorism, by freezing funds and other assets of terrorists, to strengthen non-proliferation regimes of weapons of mass destruction and technologies connected with terrorism, co-operation between the Europol and the Japanese police authorities.

The leaders discussed the international economic situation ,the synchronous down turn in the major economies and the sharp slow down in world trade. Both countries reached consensus to continue their efforts in the liberalization of trade. The European leaders expressed their conviction that structured reforms in Japan is essential for it's economic recovery as well as the world's economy.

Europe and Japan, have come close to environmental issues According to World Wild Life Fund, Less than 2%²² of Europe's forest is natural, and it also has a dismal record of protecting to woodlands. Areas such as global warming, world fishing capacity, e-commerce, electronic money and the list goes on, Europe and Japan are well placed to lead with new approaches.²³

The political dimension of this relationship, seems incomplete, even as we see improvement in this sphere, economics certainly dominate politics, so the next chapter will give the economic dimensions of this relationship.

²² *International Herald Tribune*, 24th Jan. 2001.

²³ *International Herald Tribune*, 29th Jan. 2001.

CHAPTER IV

EU-JAPAN ECONOMIC RELATIONSHIP IN THE 1990'S

The EU and Japan have pursued close co-operation on trade issues for some time. In a world of increasing interdependence, neither partner can pursue its interest effectively without cooperating with the other. While much has already been achieved, the continuing reinforcement of trade issues between the two is in the interest of both parties.

The EU's economic relationship with Japan has been affected significantly in the last decade by the less favourable evolution of the Japanese economy and the slow down of economic growth.

At the beginning of the 1990's the international community stood at an important geopolitical and geo-economic crossroad. The Cold War was thawing, Europe was on the verge of creating its single market and Japan had become the world's most important creditor nation. While the USA seemed to have won the ideological contest with communism, it simultaneously faced a more direct challenge to its economic hegemony. Further, globalization was blurring the demarcations of territorial based loyalties, requiring therefore a much wider range of co-operation in a wider range of issues.

The end of the Cold War has brought a change in the way the Japanese perceive the world. Though they may not be strongly conscious of it, most people

in Japan have stopped thinking of the world as being divided into east and west and have started to see it as one.

The Japanese have realized that they might have to pay some attention to the Community largely due to the launching propaganda of the Single Market. The European Union-Japan relations were given a further boost, indirectly by the end of the Cold War. This sets the general context of EU Japan Economic relations during the 1990's in this chapter. Specific sectors, ranging from Single Market to WTO would be discussed.

SINGLE EUROPEAN MARKET

The Single European Market brought about fears in Japan, with regard to trade with a third country. The fear was that a third country would deal with a 'Single Market' not with twelve national markets and this would increase imports. In principle, goods from a third country that are freely sold in one member country can be moved to the entire community and by the same token Brussels demanded concessions for new market access.

The Single Market attracted a lot of attention, because of a forecast of a bright future. It was estimated that there would be economic growth and creation of jobs, and this would be beneficial to Japan as well as the world economy.

These issues met with mixed reaction from the Japanese, for example, the Bank of Japan came out with a report which expected revitalization of the European economy through the 1992 process, which would also contribute to the stable expansion of the world economy as a whole.

On the other hand, it was observed, that since already European markets were already difficult to penetrate, a new unified market will be more difficult for foreign companies as the European community would be more selective about the type of business.

According to a survey carried out by the Japan External Trade Organization (JETRO) the number of Japanese manufacturing enterprises operating in Europe jumped dramatically from 157 in 1983 to 411 in 1988.¹ This rush indicates the response of Japanese business to the SEM.

The Japanese lacked a consistent strategy for the Single Market. Europe's vacillation between liberalism and protectionism² makes it difficult for Japan to respond. However despite all odds, the Japanese have come to terms with it. Japan insisted on multilateral negotiating sessions which keep in mind the GATT guidelines, where trade restrictions for Japanese products should be abolished.

Japan has been vehemently arguing that the EC countries should remove all import restrictions on Japanese automobiles and discriminatory quantitative restrictions. European market integration would remove such restrictions in areas like the automobile industry.

Specific measures related to market integration such as margin for unfair discrimination against extra-regional countries cannot be totally discarded, in areas such as finance, government procurement, mergers and acquisitions. Japan had

¹ Toshiro Tanaka, "The European Community and Japan", *Japan Review International Affairs*, Fall/Winter, 1989, p. 219.

². Karl-Rudolf Korte, "Japan and the single European Market" , *Aussen Politik* Vol.40, 1989, p.402.

requested the EC to ensure an appropriate management so the integrated market is truly open to the outside.

Considering that the EU constructs a new international order, Japan views that building the economic relationship of co-existence and co-prosperity is indispensable in the long term.³

The entire Community demanded concessions for new market access. The expansion of Japanese FDI in Europe peaked a record in 1989 when it rose to \$67.5⁴ billion. In the mid 1990's the Japanese underwent an economic boom, the period termed as a 'bubbling economy'⁵. During this period there was a large amount of accumulated money and this led to overseas activities.

It is important to understand the reasons for investing abroad; the traditional approach has usually been, when enough savings have been accumulated for the needs of investment and growth domestically. The next, is that when there are profitable investment opportunities abroad, provided that at the domestic market, there is lesser chance of profitability. Another factor is superior managerial skills supported by advanced production and trade networks compared with those found in the domestic market and Japan occupies an important position as an outward investor.

³ *Diplomatic Blue Book* 1991, Published by the Ministry of Foreign Affairs, Japan, p. 283.

⁴ K. Sheridan, "Japan's Direct investment", *Journal of Contemporary Asia* vol.125, 1995, p. 478.

⁵ www.aei.org/ct/ctglass2.htm.

Under the trend towards further liberalization of trade and investment since the establishment of the world trade organization (WTO) in 1995,⁶ there seems to be a shift in the economic fundamentals.

FOREIGN DIRECT INVESTMENT

Japan is promoting and accelerating its FDI activities considerably. Large parts of the country's national efforts are directed towards "multi-nationalization" and international expansion"⁷ of enterprises.

The first phase of Japanese foreign direct investment was in the service sector, nearly ninety⁸ percent of the Japanese FDI in Britain was in the non-manufacturing sector.

The picture began to change and Japan began to put more emphasis on the manufacturing sector, especially with the approach of the single market. Although in the early post war decades Euro-Japanese relation was dominated by trade issues, over the past few decades, investment has become an increasingly important facet of this relationship.

⁶ . Kazunori Ishiguro, "The WTO New Round and Japan's Role", *Japan Review of International Affairs*, winter 1999, p.230.

⁷ K. Sheridan, "Japan's Direct Investment, its development Pattern and Future Direction" . *Journal of Contemporary Asia*, Vol. 25, 1995, p. 474.

⁸ Brian Bridges. *Europe and the challenge of the Asia Pacific*, [Edward Elgar Publishing limited,U.K.,1999] P. 31.

FOREIGN DIRECT INVESTMENT IN JAPAN

FDI IN JAPAN IN Y BILLION⁹

Source	1992	1993	1994	1995	1996	1997	1998	1999
France	22	9	7	11	11	9	17	746
Nether land	27	33	54	54	80	146	128	471
USA	172	109	164	177	239	152	808	249
U.K.	34	8	13	11	41	45	37	90
Germany	16	12	54	17	48	55	34	47

Source: Facts and Figures of Japan 2001, Foreign Press Center, p. 78.

The table above shows that foreign investment in Japan from the EU increased by 505.8¹⁰ of investment from France rose to \$ 6.7¹¹ billion and replacing USA as the largest investor.

THE INVESTMENT GAP:

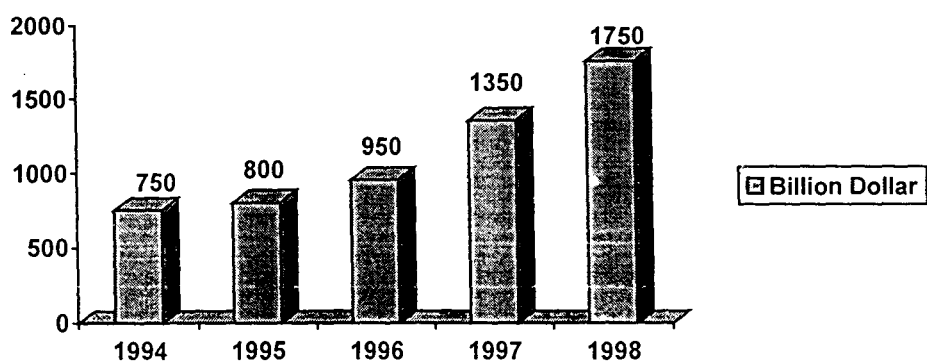
European FDI into Japan continues to lag behind the flows out of Japan into Europe. Britain still remains the largest recipient, contrary to expectations that a unified Germany could prove to be more attractive.

⁹ *Facts and Figures of Japan 2001*, [Published by Foreign Press Centre, Japan, 2001], p. 78.

¹⁰ *ibid.*, p.78

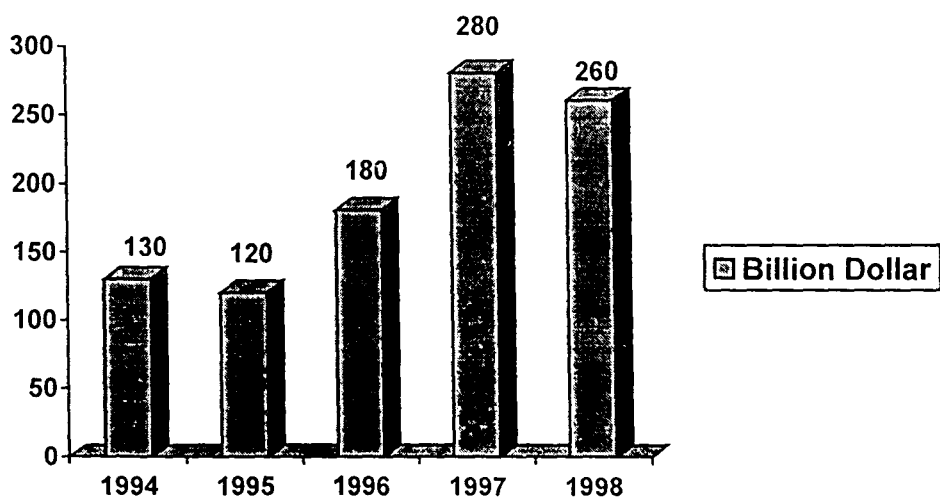
¹¹ *ibid.*, p.78

JAPANESE DIRECT INVESTMENT IN EU¹²



Source: Ministry of Finance, Japan

THE EU'S DIRECT INVESTMENT IN JAPAN¹³



Source: Ministry of Finance, Japan

¹² www.infojapan.org/region/europe/eu/overview/econo_invest.html.

¹³ www.infojapan.org/region/Europe/eu/overview/econo-invest.html.

The European Commission, no doubt would prefer that Japanese FDI is more evenly distributed but there is little it can do to influence Japanese investors from or towards any particular country. The European commission is also concerned about the poor record of EU FDI going into Japan, discouraging government regulations, and a business culture which abhors hostile takeover undoubtedly contributed to such situations.

In Japan the issue of car imports has taken as the litmus test of the EC's free trading resolve.

THE AUTOMOBILE INDUSTRY

In 1991, the European Commission and the Japanese Ministry of International Trade and Industry (MITI) announced the completion of an extraordinary agreement to limit the penetration of Japanese motor vehicles to the European Community, called the "Elements of Consensus"¹⁴ which placed numerical limits on Japanese motor vehicle exports to the Community as a whole and to specified member countries until the year 2000. Earlier, six firms accounted for the great majority of western European car production, viz Volkswagen, Peugeot, Fiat, General Motors.¹⁵ Ford and Renault¹⁶.

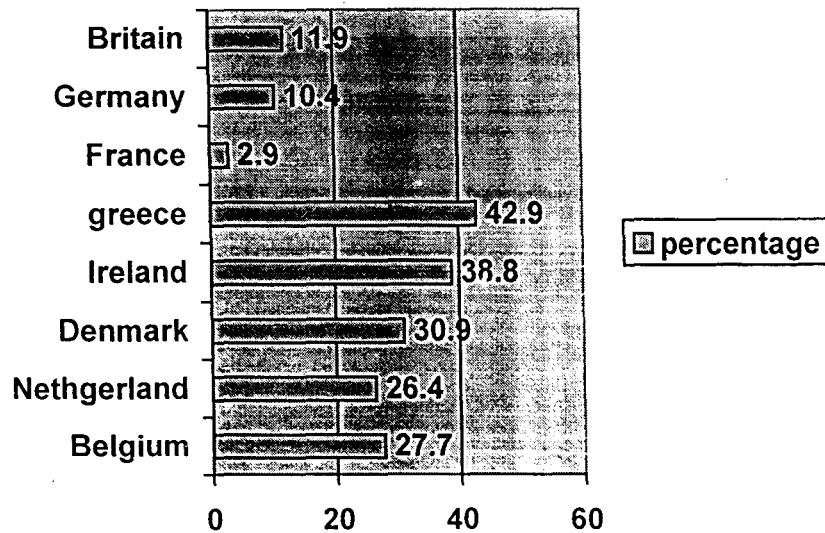
Growing concerns over Japanese competitiveness encouraged many European car makers to lobby for protection. By 1980's one could see that the Japanese auto firms had attained enormous shares in the EC markets.

¹⁴ . Mark Mason, "Elements of Consensus: Europe's response to the Japanese Automotive challenge", *Journal of Common Market Studies*, vol 32, Dec. 1994, p. 433.

¹⁵ . General Motors firm manufactured Opel and Saab.

¹⁶ Mason.n.14, p.434

JAPANESE SHARES IN THE EC AUTO MARKET



Source: Mark Mason, "Elements of Concensus: Europe's response to the Japanese Automotive Challenge", *Journal of Common Market Studies*, vol. 32, Dec., 1994, p.436.

Despite restrictions imposed, in 1989, Japan held roughly one-tenth of the overall EC market. The Japanese automobile challenge to Europe led to a long and complex negotiations where the officials were involved. In addition to it the major car manufactures too consulted with the government.

The accord took three years to complete and passed through various phases. The first phase is the involvement of the representatives of the European Commission with the officials of the EC member states. It brought out the determination to limit Japanese auto exports during a finite period and to seek Community assistance for domestic car makers. However, they were less clear about policy for Japan's local transplants.

The process entered a second phase in 1990, where officials of the European Commission and the MITI began to consider the modification and implementation of general principles. Article 115¹⁷ of the Rome Treaty, enabled member states to take national protective measures limiting indirect export from other states. In July 1991, these two countries reached a consensus on the conditions of import of Japanese motor vehicles from 1993 onwards.

This was to facilitate the industry to adjust towards international levels of competitiveness and Article 115 was not applied to vehicles imported from Japan. The two sides agreed that Japan would monitor its exports to the EC. Specific export levels were provisionally set for the year 1999.

JAPANESE AUTOMOBILES EXPORTS TO SELECTED EU COUNTRIES

IN 1999¹⁸

Country	Anticipated total EU market demand	Anticipated japanese market share through imports	Anticipated japanese market share through imports, %
France	2,850,000	150,000	5.3
Italy	2,600,000	138,000	5.3
Portugal	275,000	23,000	8.4
Spain	1,475,000	79,000	5.3
United kingdom	2,700,000	199,000	7.0

Source: Elements of Consensus

¹⁷ . Aaditya Mattoo and Petros C. Mavroidis, " EC- Japan consensus on cars", *World Economy* 1995. p. 348.

¹⁸ Ibid,p.445.

The pre-cast level of Japanese exports to the EC as a whole was set at 1.23 million¹⁹ vehicles.

TRANSPLANTS:

The issue of Japanese transplants in the Community were also discussed. The Commission isolated that the agreement covers only the shipment of automobiles from Japan to the EEC and not to the existing Japanese investment in the EEC. This is Europe's response to Japanese inflow of FDI, and marks a strong control over Japanese direct investment and trade.

Japan declared Voluntary Export Restraint on its car exports to the EU. VER's have become a prominent feature of the Japanese trade policy. VER's do not come under GATT²⁰ rules, and they are also not permanent, and also could be applied in a discriminatory way.

In 1999,²¹ we find that foreign companies are taking more interest in equity shares of Japanese company. Trade analysts have been insisting loudly that all multilateral and bilateral trade negotiations after the establishment of the WTO should aim at the contestability²² of national markets in global competition and that it is necessary to establish full defacto national treatment regardless of sector.

The Multilateral Agreement on Investment talks fell by under the weight of the European Union, specially the French Government, because it was focused mainly on maximizing protection of foreign investors which would enable

¹⁹ . Mark Mason, "Europe and the Japanese automotive challenge", *Journal of Common Market Studies*, Dec 1994 p. 445.

²⁰ . Ali M.EL-Agraa, "VER's and Japanese Trade Policy", *World Economy* 1995 p. 220.

²¹ . Roger schreffler, "Foreign Fit, Domestic Finish in Auto Industry partnership", *Japan Quarterly*, April 1- June 2001 p. 42.

²² . Ibid p.230.

multinational Corporations to suppress sovereign states. MAI's²³ central concern was to guarantee that even in situations like the Asian crisis. Foreign investors could withdraw funds when ever they liked, in other words, target countries around not be permitted to block this. This contradicted the trend of developed countries in the wake of a crisis to strengthen surveillance of short –term investment.

The Europeans resisted MAI because it was perceived as subordinating states which between obligation to protect its citizen's lively hood and culture and to pursue development to multi relations in the name of market economy and robbing nations economic policies of their Independence.

The Japanese government had strongly backed MAI negotiations, until the meeting of trade ministers in 1999. The government especially MITI would not admit to the breakdown of MAI talks. Fundamental to the Japanese government's stand was the strong desire to globalize the wave of administrative reform and deregulation that was sweeping Japan since the economy was in dire straits.

The WTO initiatives are based on article 6²⁴ of the General Agreement on Trade in Services. Regulations that hinder competition, and unfairly impede trade should be eliminated. WTO agreements have already been coloured by a notion of market access that goes beyond traditional national treatment.

The WTO and the Japanese government appears to be prepared for further liberalization across sectors, modeled on the understanding of commitments in financial services and reference paper used for the basic telecom negotiations. A

²³. Is a short form for multilateral Agreement on investment.

²⁴ www.Keinren.org.jp/english/policy/pol019.html.

safety net to deal with the harmful economic and social effects of liberalization.

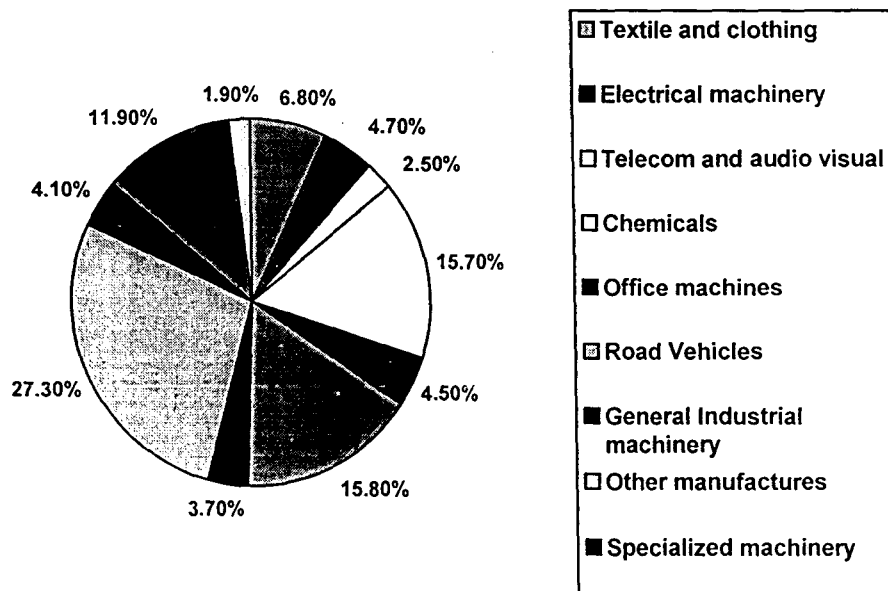
The Japanese government is keen to show leadership at the WTO.

The basic rules of free trade are indiscriminate treatment and the removal of export and import restrictions. In principle tariffs are recognized. However lowering tariffs internationally helps to expand trade and makes the distribution of resources efficient.

Trade statistics show that, Japan's trade surplus declined in 1990 to 1993, in 1992 it was \$31.2 billion. and came down to \$ 26.3 billion in 1993. Trade imbalance is equal to the imbalance between saving rates and investment and to be address by both countries. An analysis of EU Japan sectoral patterns, reveals a shift in the technological balance of trade towards Japan in 1997.

JAPAN IMPORTS FROM THE EU AND EXPORT TO THE EU IN 1997²⁵

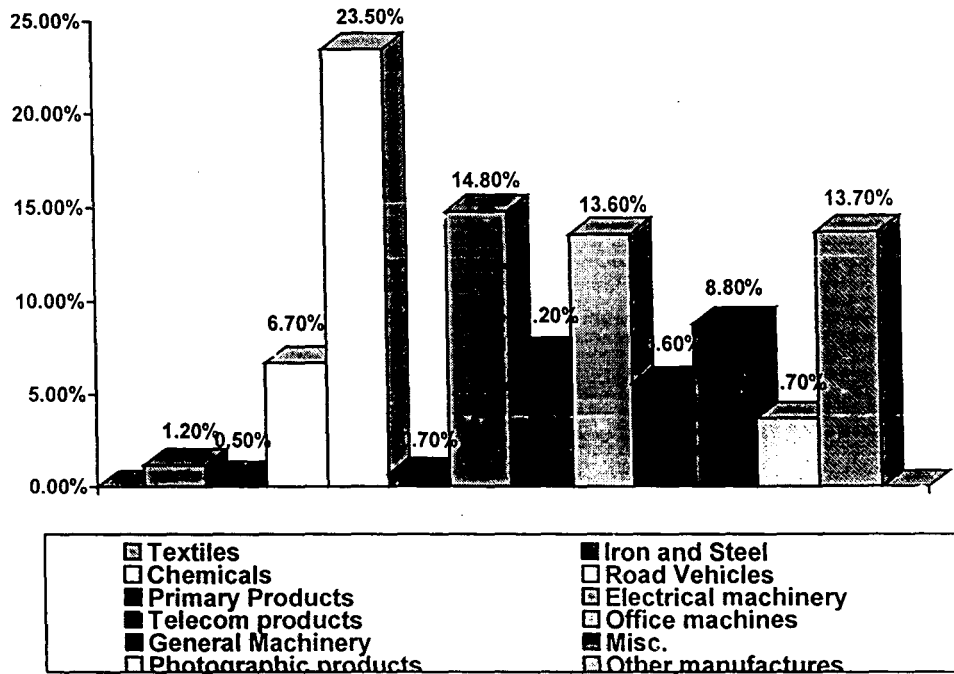
JAPAN IMPORTS FROM THE EU IN 1997



Source: Christopher M. Dent , *European Union and East Asia* [London, Routledge Publishers, 1999], p.105

²⁵ Christopher M. Dent , *European Union and East Asia* [London, Routledge Publishers, 1999], p.105

JAPAN EXPORTS TO THE EU IN 1997



Source: Christopher M. Dent , *European Union and East Asia* [London, Routledge Publishers, 1999], p.105

The figure above shows that a relatively high proportion of EU exports to Japan in 1997 consist of primary products at 11%, compared to only 0.7% of Japanese exports to the EU. Also a high proportion of EU exports to Japan is concentrated in lower technology sectors like textile and clothing, while the share of Japan is high in high-techno exports. Thus the Japanese competitive challenge to the EU remains significant.

WTO

The World Trade Organization was founded in 1995, and was seen as the embodiment of free trade. The round which led to the establishment of WTO, known as the Uruguay Round ended with remarkable achievements.

Bilateral trade and investment agreements have been there for some time, and one must note that Japan, however is a party to only six such agreements, and the core rule in protection and not liberalization.

It was agreed that a new round of negotiations will be conducted from 2000. For Japan the new round is significant for three reasons, first; liberalization will make further progress in keeping with globalization and second; the establishment of rules will progress through the WTO, and disputes over trade and investment can be handed neutrally and non-politically. Thirdly the new round will help to stem the rise of protectionism.

JAPAN'S WAY OF THINKING

Japan believes that there is a need to improve the competitive environment as it is one of the important pillars of economic structural reform, as anti-dumping measures are being used to restrict competition.

Japan also sees a need to lower tariffs on mining and industrial products and not only on agriculture and services. It also laid stress on drafting of investment rules is an urgent task, as overseas investment is growing. Japanese investors need to improve investment system of developing nations in terms of stability and transparency.

Japan also favours subjects like the abuse of anti-dumping measures, rule making on competition policy, increasing the transparency of government procurement operations, tightening intellectual property rights agreement and securing the environment for free electronic commerce.²⁶

Voluntary Export Restraint (VER's) agreements were concluded because of rapid increase of exports, and therefore many of the Japanese goods came under VERs. As managed trade came to spread to more and more industries, the system of free trade, was build up in the post Cold War era, VER was used to solve trade frictions that arose during this time.

JAPAN, THE EUROPEAN UNION AND THE WTO

This brings us to the discussion of the WTO being used as a dispute settlement mechanism when disputes arose between EU and Japan over various issues. One such issue is music copyright dispute.²⁷ The EU took a complaint to WTO with regards to the Japanese copy right laws not being in conformity with the WTO based agreements on Trade Related Aspects of Intellectual Property Rights (TRIPS) This agreement requires all WTO members to give at least fifty years protection to performers and producers of sound recording released since 1946. For example, a recording released in 1947 should enjoy cover up to 1997 and 1998 releases should be covered up to 2048.²⁸ Japan rules apply and extended to intellectual property cover back to 1971. This means that they missed out on some of Europe's most successful music export, which included the Beatles, the

²⁶ "Towards New WTO Round Negotiations-Japan's Position", Report by the International Economic Affairs Department, International Trade Policy Bureau, MITI, and *Journal of Japanese Trade Industry*, May/June, 1999, p.11

²⁷ European Commission Documents IP/97/16, Brussels, January 1997, P. 1.

²⁸ European commission Documents IP/96/165 Brussels, Febuar,t 22, 1996, p. 1.

Rolling, Stones, Jacques Brel, and also classical performers such as Herbert Von Karajan, Sir Georg Solti and Karl Bohm²⁹. The lack of such protection has led to a loss of up to one hundred million ecu a year through piracy, due to the absence of laws ensuring royalties for songs in compilation albums.

In 1997, the Japanese Parliament (Diet), has passed a bill which amended the copyright law, and has agreed to back date of fifty years ago, there by giving into World Trade rules.

Another longstanding dispute that was settled with the WTO is the liquor tax dispute where European producers of whisky, brandy, gin, vodka and other spirits enjoy lower tax when selling to Japan. This dispute was waged by the European Commission over ten years ago, a GATT panel ruled that Japan was violating GATT rules by taxing them at different rates. The Commission argued that foreign drinks exported to Japan were in direct competition with Japanese products. The panel report states that Japan has breached Article 111.2³⁰ of the GATT by taxing them in a way which protects domestic markets.

Intensive discussion between the two have led to an agreement under which tax imports into Japan will be reduced and brought closer to tax levels of local spirits. For brown spirits such as whisky and cognac the tax will be narrowed to 3%³¹. For white spirits like vodka and gin tax discrimination will disappear. The exception is for the Japanese spirit called Soochu B, where tax changes will be implemented over a longer period, till October 2001.

²⁹ Ibid,p.2

³⁰ European Commission documents, IP/96/635, Brussels, July 11, 1996, p. 2.

³¹ European Commission documents,ip/97/84,Brussels,4 feb,1997,p.2

The Commission will closely monitor the implementation of the settlement. The table below gives the main element of the agreement for the change in the Japanese tax structure.

MAIN ELEMENTS OF THE AGREEMENT FOR THE CHANGE IN JAPANESE TAX STRUCTURE³²

(Rates in yen per kilo litre per degree alcohol).

Drink	Current Situation	As of 1 Oct 1997	As of 1 Oct. 1998	As of 1 Oct. 2001
Brown spirits (Whisky Brandy)	24,558	13,775	10,225	10,225
White spirits Vodka, gin	9,927	9,224	9,924	9,924
Liqueurs	8,217	9,924	9,924	9,924
Shochu A	6,228	8,076	9,924	9,924
Shochu B	4,084	6,028	7,976	9,924

Source: European Commission Document, "EU-Japan agree on outcome on liquor tax", Feb, 1997.

In May 1998, the second ministerial conference has advanced the preparations for the launch of the new round of WTO negotiations, and Japan has made active contributions to the process. And Japan and EU have pushed for a comprehensive round which includes not only market access, but also strengthening of WTO rules.³³

³² *Diplomatic Blue Book, 2002*, Published by the Ministry of Foreign Affairs, Japan, p.89 .

³³ *Diplomatic Blue Book 2002*, Published by the Ministry of Foreign Affairs, Japan , p.89

At the E.U. Japan Ministerial Meeting held in Brussels on 11 January 2000³⁴ both sides reaffirmed the importance of the multilateral rule-based trading system embodied in the WTO. They committed themselves to further strengthen the WTO system in cooperation with other WTO Members.

For the multilateral trading system to function efficiently in the 21st century and to respond appropriately to new issues, the early launch of the new round of negotiations should remain the priority of the WTO. To this end, they agreed to continue their close co-operation to get the process back on track as soon as possible.

Both sides reaffirmed that the agenda for the new round should be sufficiently comprehensive to include not only the built in agenda (agriculture and services) and market access but also the improvement and reinforcement of existing rules and disciplines such as anti-dumping, as well as the establishment of additional rules for investment, competition and trade facilitation. Both sides also intend to continue cooperation so that the new round will pay due regard to non-trade concerns as well as factors such as the sustainable use of exhaustible natural resources and environmental aspects.

Both sides continue to support the establishment of a dialogue on trade, globalization and labour issues with a view to promote a better understanding of the issues between all interested parties

They concurred that it is important for the WTO to be open, transparent, and efficient so that it can effectively, address the concerns of all Members. Both

³⁴ www.ipn.ccu.eu.int/English/press-info/4-1-1-8.5

sides will study with other WTO Members how to assure appropriate balance between efficiency and transparency in decision-making at the WTO, in particular through better consultation procedures, so as to incorporate more effectively the views of all Members, irrespective of their level of development.

Both sides believe that the WTO should secure active participation by the developing countries and respond appropriately to their concerns. This will strengthen the multilateral trading system. They also emphasized in this context the importance of the issues relating to the implementation of the existing TWO Agreements, improvement in market access and technical assistance for capacity building. They agreed to take forward, with other developed country Members, a preferential market access initiative for least developed WTO members to extend and implement tariff-free and quota-free treatment for essentially all products originating in least developed countries.

They also stressed the major responsibility for WTO Members to respond to legitimate concerns of relevant parties outside the WTO, including business, consumers and other non-governmental organizations, in a balanced and transparent manner. At multilateral level, also, access to information should be facilitated.

Both sides also welcomed the newly acceding Members to the WTO and support the early accession of present applicants. Both sides acknowledged the negotiations on agriculture and services will start forthwith in the WTO under the built-in agenda. They agreed to pursue in the agricultural negotiations which will be based on Art 20 of the Agreement on Agriculture, their shared interests with

regard to the multifunctional role of agriculture. They also agreed in the services negotiations, which will be based on Art XIX of the GATS, to achieve progressively higher levels of liberalization.

Japan and the EU invite other WTO Members to join in their constructive efforts for the early launch of the new round and support the efforts by Mike Moore, Director General, to develop an acceptable and sufficiently comprehensive agenda for the negotiations.

EU JAPAN AND THE ASIAN FINANCIAL CRISIS

The discussion of EU – Japan relations against the financial crisis, will go underway, with a brief discussion of the crisis originated in Thailand with the plunge in the value of baht,³⁵ This surfaced the country's slow economic growth, behind the currency chaos Japan Review of International was the fact that Thailand depended on securities investment and other unstable funds for redressing trade and current account balances.

This currency turmoil spread to the neighbouring countries, the markets lost confidence and all the currencies were being devalued. Domestic demand in the countries contracted and imports fell. The East Asian Economies had developed close ties with Japan through trade and direct investment, with their currencies pegged to the Yen-dollar, they were destined to be affected directly by fluctuations in the dollar exchange rate. There was an inflow of Japanese FDI into East Asia, and they were different that the European counterparts in motive and effects. Japanese FDI is more oriented to promote trade and manifests itself in the

³⁵ Toshio Watnabe, "Facts of the Asian Economic Crisis". *Japan Review of International Affairs*, Vol. 14. Spring, 2000 p.85..

forms of joint ventures, product sharing, non equity arrangements and technology un-package transfer. Japanese FDI is macro-focused³⁶ and aims to develop the host countries, while the west is micro focused and aims to make profits for individuals.

Therefore when the yen fell against the dollar Japan's economy dampened, and the major financial institutions failed. The first to go was Hokaido Bank and Yamachi securities followed. In 1998, a frame work for stabilizing the financial system was approved, with new financial reconstruction laws. And the process is still going on.

The Impact of the Asia Crisis, can be examined, to begin with trade, exports from these two countries, these is likely to be an increase in exports from East Asia to EU. There is also a shift in their focus of markets to areas which are less affected by the crisis.

Since the crisis, EU has renewed its pressure in Japan to reconstruct its economy to reduce trade barriers in the Japanese market. These surprisingly too are backed by Japanese business traders.

The European leaders, example of Britain are doing what they can, by keeping the pound high and importing expensive four wheel drives by shipload. The Europeans have offered advice on how to reform the Japanese financial system and institutions. EU is ready to offer support and encouragement whenever they are needed. The EU has recommended very serious reforms in the Asian countries. The effort by the IMF and others cannot be ignored, it is true that Europe's effort is not so visible, one must peep in mind that Europe and Asia

³⁶ Dajin Peng, "The Changing nature of East Asia as an economic region", *Pacific Affairs*, Vol. 73, No. 2, Summer 2000. p.172

account for almost 60%³⁷ the total support provided in connection with the three IMF packages.

The EU has stressed for implementation of reforms in a transparent and open policy frame work is needed to restore growth. Japan on the other hand has acknowledge the importance of stimulating its domestic economy and understand that a reinvigorated Japanese economy will be vital to the recovery of the affected countries in Asia.

EU and Japan were very much aware of the importance of an open market, and since the crisis, these could by shifts in trade flows, which could lead to protectionist pressures in Europe. Therefore both EU and Japan must co-operate to resist such protectionist pressures and effective implementation of reforms will make it easier for both countries.

The European Union has established a Technical Assistance Trust Fund at the World Bank, to help in assessing and preparing actions to be taken in the financial and social sectors. A trust fund was established, to support the countries of the financial crisis. The EU is the largest single donor and has pledged about 15 million³⁸ (ECU) contribution.

One must also remember that Japan and EU, have a role to play, 40% of Japanese exports and 80%³⁹ of Japanese direct investment are in East Asia, and 9% investment come from the EU. There fore they both can help in the recovery of the East Asia economies.

³⁷ European commission Document, Brussels 6th April 1998, p. 1

³⁸ www.worldbank.org/html/extdr/extme/1872.htm.

³⁹ Nakagawa Katsuhiro, "The impact of the Asian Economic Crisis on trade"; *Journal of Japanese Trade and Industry*, , Jan./Feb. 1999, p. 35.

CHAPTER V

CONCLUSION

The early pre-war years reveal that Japan-Europe ties date back to the sixteenth century. There was a growing number of foreign traders, like the Portuguese, Spanish and the Dutch, who came to explore the commercial opportunities offered by Japan. However an isolationist regime closed the doors to Europeans, and it was only with the Meiji era that Japan became modernized and more outward-looking.

Japanese expansionist aspirations brought eventual conflicts with Europe's colonial powers in Asia. The Japanese were eager to learn from Europe's industrial and technological successes. The Europeans regarded Japan as an exotic playground, an ultimate in tourism, while the Japanese regarded Europe as disciplined, group-oriented society possessing the secrets of industrial production. In fact, it is exactly the opposite. The Japanese flock to Europe for exotic tourism and the Europeans who are regarding Japan as disciplined with amazingly efficient industries..

COMING TO TERMS

The European nations were wary of re-establishing trade links with Japan, on account of it being a former Axis power and also of its neo-mercantilist policies.

The United States tried to re-assimilate Japan into the international community, which was strongly resisted by the Europeans, when countries like UK, France and Belgium refused the Most Favoured Nation status to Japan.

Japan began to liberalize its tariffs and tried to form a foreign policy to promote cooperation between Japan and the European Community, and slowly Japan succeeded in gaining the MFN status.

Meanwhile, the European countries came to terms with Japan's growing international stature, because the member states could not come together as a United Front against Japan. During this time the trade figures show a steady rise from two percent in 1964 to 5.9 per cent in 1968.

JAPAN AND ONE EUROPE

The early 1970's we saw, EC-Japan economic diplomacy being conducted at a more corporate level as Europe became more aware of concentrated market penetration that Japanese producers were making in areas, such as, electronics, cars, motorcycles, ships and steel. As trade surplus began to grow there were streams of Voluntary Export Restraints imposed.

There were anti-dumping duty imposed on many Japanese exports which included ball bearings, colour televisions, watches ect. There were about twenty-two¹ anti-dumping cases against Japanese imports. The entire period witnessed a lot of trade friction.

¹ Christopher. M. Dent, " *European Union and East Asia*". [Routledge Publishers, London, New York, 1999], p. 91.

With the coming of the 1980's, things changed. In fact it is interesting to note that Japan and Europe have kept the political dimension of this relationship to a secondary place where as commercial issues have assumed priority. There are occasional signs of the European Community and Japan having common perceptions which differed from the Americans. At the EC level there were regular foreign ministerial meetings and these meetings did pave the way for greater cooperation between the two.

Initially, political dialogue between Japan and the European Community was quintessentially economic dialogue. The main issues continued to be trade and the opening of Japanese markets. At the same time, however, bilateral negotiations continued between Japan and the member states of the Community.

Subsequently ,the political dialogue was institutionalized between these two, whereby an institutional framework for political dialogue was established.

The 1991 Declaration, opened a political relationship in the post Cold War era, signifying, the need to intensify their dialogue for strengthening co-operation. The strategy of both sides , to mutually reinforce each other's aspiration for carrying out global and regional political roles was confirmed at the summit in 1995.

The attempts to give shape to this relationship was seen in a number of areas, such as, a joint proposal for the establishment of the UN Register of

Conventional Arms .The EU also has endorsed Japan's bid for a permanent seat in the UN Security Council.²

EU-Japan political cooperation has also moved forward in the area of environment, the two have been engaged in research in areas like global warming, acid rain and many others.

The relationship's maturity was seen in various aspects, where from disputes, both started solving them at various levels, we also see co-operation at global levels.

Thus we see that the sphere of cooperation increased, political dialogue intensified and both partners saw it necessary to take this relationship to new grounds.

In the economic sphere, we find Japan moving from an initial mixed reaction with reference to the Single European Market, but then we find that the Japan has understood the need to move closer to Europe. This led to an increase in investments during that time and trade between Japan and the European Union has increased

Japanese FDI appears to have had favourable influence on the bilateral trade balance between Japan and EU. It acts as an import substitution as well as export promoting.

Both the European and the Japanese seem to have come to a consensus regarding the benefits of Japanese FDI. They have recognized that the presence of

² Glenn. D. Hook , "Globalization, East Asian Regionalization and Japan's Role in Euro-Asian", *Japan Review*, 2000 ,p. 29.

other corporations can enable EU companies to become more competitive, create employment and introduce cutting edge- technology.

We have also seen that the policy of “bash the Japanese to boost the Japanese”³ is taking place. Japanese investment has been concentrated in Britain. Explanations include english in the medium of communication, which can be easily understood, where as in the other European Countries the language is a main barrier. Another could be low taxes on corporations, then even the government too is putting and introducing new policies to attract investment.

The fact is that there is more Japanese investment in the EU than vice versa. The resistance of the Japanese system inward investment, especially through mergers and acquisitions prevent sEU companies from having access to Japanese markets.

Therefore the introduction of transparent, and liberal multilateral rules will enable progress.

There have been so many developments and trends in Europe that have affected Euro-Japanese relationship, example the introduction of the Euro. There are about 300 million people integrated into one economy accounting for some twenty percent of the world GDP. There has been a widening and deepening of relations, because a whole range of new subjects and areas of cooperation have been included, deepened because they have worked together in a long-term systematic way as for the preparation of the WTO rounds.

³ Ibid ,p .26.

The Euro has brought talks about an economic integration in Asia. The scope being with the East Asian Nations such as China, Japan and South Korea all of them are large, both in terms of markets and their level of technological development, in this context, a view that is gaining ground is the introduction of the Yen as an international currency and Japan's role in it is must, as Germany took up leadership in the introduction of the Euro, so must Japan, and only time will tell, of Asia will see a currency. In fact Asia is seeking and receiving extensive European advice for its own coordination efforts.⁴

As we go further, the relations between the two with regards to WTO we see that the EU has used the WTO as a means of protecting European business, the EU and Japan had launched a bilateral consultation on the WTO ministerial meeting held in Nov. 2001 and have encouraged active participation of developing countries by paying specific attention to their needs and preoccupations.

Japan and the EU seem to have found a common ground for co-operation and support of globalization in the WTO and the Euro-Japanese stance is clear.

They both agree on the need to go by WTO rules and both have shown tremendous trust in each other by adhering to judgments passed by the WTO on various disputes . Both have taken leadership in the new initiative and in some ways have bypassed the United States. So we see that both can influence the international agenda when both take a common stance.

Most of Japan's foreign direct investment goes to East Asia. Both EU and Japan played an important role in helping these economies to recover from the

⁴ C. Fred Bergsten, " America's Two-front Economic Conflict", *Foreign Affairs*, March-April 2001,p. 21.

Asian Financial crisis. One must also keep in mind that Japan's economy to is in recession, the EU has helped Japan in its structural reforms and co-operated at all levels to help boost the economy.

We need to keep in mind that new forms of cooperation between Japan and EU have emerged as a balance to the predominance of the United States as partly as a response to global order. It is necessary for Japan and European Union, to come together so as to check America's leadership role⁵ and be able to have a say in global issue.

EU-Japan relations have to confront many important challenges encompassing economic, environment, political or security issues. As the world apparently moves towards a multi polar world both the EU and Japan will need to get used to dealing with a large number of key players. Keeping them in balance would be a complicated difficult and an extremely challenging task.

⁵ Kazuo Ogura, "Creating a New Asia", *Japan Echo*, Vol. 26, No. 3, June, 1999 , P. 12.

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