

# The Heritage Foundation **Backgrounder**

214 Massachusetts Avenue, N.E. Washington, D.C. 20002-4999 (202) 546-4400

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## RESCUING THE ASIA PACIFIC TRADE SUMMIT

(Updating Asian Studies Center *Backgrounder* No. 134, "Expanding Free Trade in Asia: The APEC Summit and Beyond," November 10, 1994.)

If the budget battles with Congress do not keep him in Washington, President Bill Clinton will travel to Osaka, Japan, this weekend to meet with leaders from Asia and the Americas to discuss trade and investment in the Asia Pacific region. They will meet under the auspices of the forum for Asia Pacific Economic Cooperation, or APEC, an organization of Asian and Pacific Rim economies dedicated to liberalizing trade and investment.<sup>1</sup> The members of APEC have pledged to create a free trade and investment area in Asia and the Pacific Rim by 2020.

However, this dream may be shattered if China, Japan, and some other APEC members get their way. Their unwillingness to open their agricultural markets may suffocate the once-bright promise, made by APEC in 1994, to achieve "free and open trade and investment in the Asia Pacific" region. This would represent a severe setback for regional trade liberalization. President Clinton and the other leaders at the APEC summit should agree that liberalization will be comprehensive, including the liberalization of agricultural trade, or the hope for free trade in Asia may wither.

APEC's backsliding is mainly the fault of the Japanese. Unlike President Suharto of Indonesia, who hosted the Leaders' Meeting in 1994, Japanese Prime Minister Tomiichi Murayama has been unwilling to develop a consensus plan for making good on the promise of free trade which APEC made at its last meeting in Bogor, Indonesia, in 1994. Instead, the Japanese government has proposed that APEC members be permitted to exempt so-called sensitive sectors of their economies from trade liberalization. According to the Japanese, the most sensitive sector of all is agriculture. China and some other Asian countries are siding with Japan against the U.S., while Australia and Canada, among others, support the American position.

APEC is critical to America's economic future. It serves an institutional link between the U.S. and the fast-growing Asian economies. It also is a hedge against the formation of an Asia-only trading bloc. APEC encompasses nearly 50 percent of the world's population, 60 percent of its gross domestic product, and 40 percent of its trade flows. U.S. two-way merchandise trade with APEC members was \$772 billion in 1994—65.6 percent of worldwide U.S. trade or 11.4 percent of U.S. gross domestic product. In 1994, American

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<sup>1</sup> Technically, APEC grants membership to economies, not countries. This legal fiction allows China, Hong Kong, and Taiwan all to join APEC. The other member economies are Australia, Brunei, Canada, Chile, Indonesia, Japan, Malaysia, Mexico, New Zealand, Papua New Guinea, Philippines, Singapore, South Korea, Thailand, and the United States. The heads of government in all member economies except Hong Kong and Taiwan attend APEC Leaders' Meetings.

investment in APEC economies was \$202 billion, and APEC foreign investment in the U.S. was \$163 billion. APEC's goal of free and open trade and investment is consistent with long-standing American policy supporting trade liberalization around the world.

Free trade and investment is too important to America's future to let APEC die because of irresponsible behavior in Japan and protectionism in other countries. Therefore, while in Osaka, President Clinton should:

- ✓ **Tell** Japanese Prime Minister Murayama that selective exemptions to APEC trade liberalization are unacceptable and threaten America's vital national interest in trade liberalization in Asia.
- ✓ **Work** closely with the leaders of Australia, Canada, Chile, Indonesia, and New Zealand to block Japan's protectionism. These leaders should urge Japan to accelerate implementing Uruguay Round trade liberalization commitments while seeking new agreements on antidumping, competition policy, product standards and testing, and investment protection.
- ✓ **Make clear** that blocking or delaying comprehensive APEC trade liberalization would undermine APEC's institutional credibility. Backsliding on free trade at Osaka could ring the death knell for APEC as an organization.
- ✓ **Support** Taiwan's accession to the World Trade Organization if the issue is raised bilaterally by the Taiwanese.

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## JAPAN'S ACTIONS SINCE BOGOR

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As host of this year's APEC Leaders' Meeting, Japan must chair all preparatory meetings and work with senior officials from all APEC members to develop a consensus on the summit's agenda. The main challenge is to decide how to implement the Bogor Declaration for free and open trade and investment in the Asia Pacific region for developed members by 2010 and for developing members by 2020.

The performance of Japanese Prime Minister Tomiichi Murayama in fulfilling this vital role has been unsatisfactory. Murayama's unpopular Socialist-Liberal Democrat coalition government has been unwilling to undertake any bold trade liberalization initiatives to move the APEC agenda forward. The Japanese government sought to deflect APEC away from trade liberalization in February 1995 by proposing a "Partners for Progress" scheme that would turn APEC into little more than a regional conduit for foreign aid. The proposal would have established a new secretariat that would coordinate foreign aid by advanced APEC members to less developed members such as China or Papua New Guinea. Senior officials from other APEC members condemned Japan's "Partners for Progress" scheme as an unnecessary duplication of existing aid programs and as a distraction from trade liberalization. As U.S. Ambassador to APEC Sandra Kristoff remarked in February 1995, "the proposal raised in our minds some questions about whether it was duplicating ODA<sup>2</sup> activities already happening elsewhere."<sup>3</sup>

Japan later withdrew its "Partners for Progress" proposals, but it has failed to offer concrete proposals for APEC trade liberalization. Instead of taking action this year, Japan has suggested merely that APEC members wait until 1996 to table their proposals for "concerted unilateral" and "collective" action at the Leaders' Meeting in the Philippines.<sup>4</sup>

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2 ODA stands for "official development assistance," or economic development aid by governments.

3 "APEC Members Negative Japan's Proposal for New Aid Forum [sic]," *Japan Digest*, Vol. VI, No. 28 (February 16, 1995).

4 Concerted unilateral actions are trade liberalization measures undertaken by each APEC member on its own accord. Collective actions are trade liberalization measures undertaken by all APEC members as a result of APEC negotiations.

More ominously, Japan has proposed that APEC members be permitted to exempt sensitive sectors of their economies, such as agriculture in Japan or clothing manufacturing in the U.S., from APEC trade liberalization. The Japanese proposal has become a flash point dividing APEC into two warring camps. One camp is led by Japan, which is unwillingly to open its agricultural markets beyond the concessions made in the Uruguay Round agreements. Supporting Japan is China, which not only seeks to maintain agricultural sector barriers, but also wants to protect broad sectors of manufactured goods. In the other camp are Australia, Canada, Chile, New Zealand, and the United States. These countries have vehemently rejected the Japanese proposal for exempting sectors from APEC trade liberalization. Most of the ASEAN countries, especially Indonesia and Singapore, also oppose Japan.

## THE EMINENT PERSONS GROUP

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During the last three years, the Eminent Persons Group (EPG) has provided APEC with a free trade vision and shaped its successful agenda. The EPG is an APEC-appointed advisory panel composed of one person from each APEC member and chaired by C. Fred Bergsten, a former U.S. Treasury official and executive director of the Washington-based Institute for International Economics.

In its first report, the EPG recommended “a bold, forward-looking and realistic vision for APEC: the progressive development of a community of Asia Pacific economies with free and open trade and investment.”<sup>5</sup> The Leaders’ Meeting near Seattle, Washington, in November 1993 accepted this challenge as APEC’s goal. In its second report, the EPG recommended that “APEC now adopt a comprehensive program to realize the vision of free and open trade in the region...and complete the liberalization process by 2020.”<sup>6</sup> Responding to this challenge, the leaders agreed at their meeting in Bogor, Indonesia, on November 15, 1994, that APEC should achieve free and open trade and investment in the region by 2020.

On August 25, 1995, the EPG delivered its third annual report, *Implementing the APEC Vision*, recommending a series of practical steps to begin implementing the Bogor Declaration.

**Step #1: Accelerating Uruguay Round Liberalization.** The EPG suggests that all APEC members agree to accelerate the implementation of their Uruguay Round commitments based on the following principles:

**Principle 1:** Unlike preferential trade agreements such as the European Union or North America Free Trade Agreement whose trade liberalization benefits accrue to their members, APEC should offer the benefits of an accelerated liberalization timetable to all members of the World Trade Organization (WTO), including those that are not members of APEC. In other words, APEC members would not discriminate against other countries in trade policy.

**Principle 2:** APEC members should adopt a “50 percent rule” under which they would cut in half the time for lowering tariffs, removing non-tariff barriers, or reforming domestic laws. For example, developed APEC members could speed the timetable for Uruguay Round tariff cuts from the current four years on most products to two years. Developing APEC members could slash the period for phasing out non-agricultural subsidies from eight to four years.<sup>7</sup>

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<sup>5</sup> *Achieving the APEC Vision: Free and Open Trade in the Asia Pacific*, Second Report of the Eminent Persons Group, Asia Pacific Economic Cooperation, August 1994, p. 1.

<sup>6</sup> *Ibid.*, pp. 3-4.

<sup>7</sup> In addition, the EPG recommends that developed APEC members should accelerate implementing Uruguay Round reductions in agricultural subsidies from six to three years. Developing APEC members should accelerate implementing international rules on intellectual property rights from four to two years for obligations concerning patents, trademarks, copyrights, and

**Step #2: Broadening and Deepening the Uruguay Round Agreements.** The EPG recommends that Uruguay Round agreements be broadened in the following four areas:

- ① **Antidumping.** The EPG finds that antidumping laws have been abused to protect domestic firms at the expense of consumers. Antidumping proceedings are biased because they consider only the interests of import-competing firms and their workers, but not the interests of consumers and domestic firms dependent on imported supplies for production. They also penalize foreign competitors for normal business practices. For example, the legal standard for proving a domestic firm guilty of predatory pricing is far more stringent in most countries than the legal standard for finding a foreign competitor guilty of dumping cheap goods on a domestic market. Thus, the same pricing policies that are legal for domestic firms may be held illegal for their foreign rivals under antidumping laws. This is pure protectionism. The EPG recommends that APEC leaders commit themselves to eliminating such abusive uses of antidumping policy.
- ② **Competition Policy.** Competition policy encompasses the regulation of monopolies, mergers, cartels, and government aid to business firms. Many of the trade disputes in Asia arise from differences over competition policy. For example, the recent automotive trade dispute with Japan centered on whether the *keiretsu* system of interlocking equity, debt financing, and personnel sharing among Japanese companies prevented American suppliers from selling their auto parts and cars to Japan. Because the WTO does not deal with competition policy, the EPG has called on APEC members to cooperate in applying competition policy laws to reduce their differences over time.
- ③ **Product Standards and Testing.** Product standards and testing can be used as protectionist devices. For example, Japan has refused to accept U.S. test data on medical equipment and requires American suppliers to conduct another round of tests in Japan before certifying their products. Multiple testing can be expensive and may deter manufacturers from offering some products in certain markets. The EPG recommends that APEC should negotiate agreements on standards and testing. It also suggests that all APEC members should accept the test data and product certification of any one member, so long as they are based on internationally recognized standards.
- ④ **Investment Protection.** Private-sector investment has produced rapid economic growth in the Asia Pacific region. Improving protections for foreign investors will help to sustain this growth. The EPG recommends that APEC members strengthen their protection of investment in the areas where they fall short of international norms. For example, APEC economies should adopt the rules followed by NAFTA countries that prohibit imposing restrictions on the transfer of funds related to foreign investment such as profits, dividends, royalties, loan payments, and liquidations in freely convertible currencies. Moreover, APEC should minimize the use of performance requirements such as local content or trade balancing rules.<sup>8</sup> Such rules are inconsistent with the new WTO Agreement on Trade Related Investment Measures, which bans local content or trade balancing requirements. The EPG urges each member to adopt these accommodations and affirm them in a binding agreement among all APEC members.

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administrative and procedural requirements and from nine to four and one-half years for patent protection for certain agricultural and pharmaceutical products.

<sup>8</sup> A local content rule requires a firm to use a certain percent of locally made parts and materials. A trade balancing rule requires a firm to offset its imports by a certain percent of exports.

**Step #3: Dispute Mediation Service.** The EPG also has recommended that APEC create an official mechanism to settle regional trade clashes, to be known as the APEC Dispute Mediation Service. The EPG recognizes that many of the recent trade disputes in the Asia Pacific region involve subjects not covered by current WTO rules. One such subject is competition policy. The WTO has no jurisdiction to settle disputes in competition policy and other subjects that its rules do not cover. Had an APEC Dispute Mediation Service already been established, it could have helped diffuse the Japan-U.S. automotive trade wrangle that occurred earlier this year. By resolving disputes that the WTO cannot handle, an APEC Dispute Mediation Service would supplement and strengthen the WTO.

## RESCUING THE OSAKA MEETING

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The Japanese proposal for exempting certain sectors of the economy like agriculture would undermine the comprehensive free trade and investment regime envisioned by the Bogor Declaration. Once one member is permitted to exclude a sensitive sector, other members will follow suit with their own protectionist demands. If Japan gets its way, APEC free trade would be more the exception than the rule.

President Clinton must not let any country undermine APEC's bright promise. Therefore, he should:

- ✓ **Tell Japanese Prime Minister Murayama that selective exemptions to APEC trade liberalization are unacceptable and threaten America's vital national interest in trade liberalization in Asia.** The U.S. cannot accept an APEC trade liberalization regime that excludes sectors such as agriculture where Americans excel. In an interview with the *Sydney Morning Herald* on November 6, U.S. Ambassador to APEC Sandra Kristoff said, "To provide for sector exclusions because of domestic sensitivities would be to turn Bogor on its head and to call into serious question the continued interest of many of us to participate."<sup>9</sup>
- ✓ **Work closely with the leaders of Australia, Canada, Chile, Indonesia, and New Zealand to block Japan's protectionism.** The U.S. is fortunate that most other APEC members disagree with the Japanese proposal. President Suharto, who views the Bogor Declaration as his legacy, once again may play a key role in bridging the division and building a consensus in Osaka. The U.S. should support his efforts if he does.
- ✓ **Make clear that blocking or delaying comprehensive APEC trade liberalization would undermine APEC's institutional credibility.** Asia's economies have benefited greatly from trade liberalization since World War II. Without credible international institutions promoting free trade, liberalization and the ensuing economic boom in Asia would not have occurred. Calling for special exemptions would rob APEC of needed credibility in pushing for free trade in the Asia Pacific region.
- ✓ **Support Taiwan's accession to the World Trade Organization if the issue is raised bilaterally by the Taiwanese.** The WTO accession issue likely will not be raised by Taiwan in the plenary session of the APEC Leaders' Meeting. It is possible, however, that Taiwan's representative will do so in informal bilateral meetings with the U.S. In that case, the U.S. should be supportive. Taiwan's membership in the WTO should not be held hostage to the People's Republic of China's membership in the WTO. Once Taipei meets the WTO's standards, it should be allowed to join. Taiwan's membership in the WTO would contribute to the overall goal of trade liberalization in the Asia Pacific region.

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9 "APEC May Not Get Trade Deal, Kristoff Says; Dole Doesn't Want One Anyway," *Japan Digest*, Vol. 6, No. 194 (November 6, 1995), p. 4.

## CONCLUSION

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APEC is at a crossroads. If Japan is successful in gaining selective exemptions to trade liberalization, APEC will lose credibility as an institution and will be unable to achieve its dream of "free trade and investment in the Asia Pacific" by 2020. President Clinton must fight the Japanese proposal for granting selective exemptions and insist upon comprehensive trade and investment liberalization in APEC. The U.S. has a number of allies in this dispute, especially President Suharto of Indonesia. If the U.S. can join with Australia, Canada, Chile, Indonesia, New Zealand, and Singapore to overcome the reluctance of Japan, China, and some other countries, APEC may lead the world toward a bright future of growing trade and economic prosperity.

Robert P. O'Quinn  
Policy Analyst