

# CRS Report for Congress

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## Japan-U.S. Relations: Issues and Outlook—Findings of a CRS Seminar

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### Summary

A CRS seminar on current issues in U.S.-Japan relations focused on salient economic and security difficulties affecting the generally cooperative U.S.-Japan alliance relationship.<sup>1</sup> On economic questions, participants concluded that the combination of Japan's slow growth, a depreciating yen relative to the U.S. dollar, curbed export opportunities in Asia, and halting steps toward Japanese economic deregulation presages a growing Japanese trade surplus that is certain to try U.S. patience. Regarding security issues, participants acknowledged that recently announced U.S.-Japan defense guidelines were mutually beneficial, but raised questions about the Japanese government's ability to implement them expeditiously and effectively. Some also noted that the guidelines do little to alter basic asymmetries in the U.S.-Japanese security relations that could be difficult to manage, especially during a regional crisis involving both countries' interests.

### U.S.-Japan Cooperation and Differences<sup>2</sup>

The United States and Japan have long shared goals of mutual economic well being and regional stability. In economic terms, the two countries have become increasingly interdependent: the United States is by far Japan's most important foreign market and Japan's market is the most valuable single country market for the United States, after

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<sup>1</sup> This report draws in part on information presented at a CRS-hosted seminar held on October 29, 1997. This seminar was made possible in part by a grant from the Henry M. Jackson Foundation. It heard presentations on U.S.-Japan economic issues by Tetsuo Kondo, former Minister in the Japanese Economic Planning Agency, Osamu Nariai, Reitaku University, William Cooper, CRS, and Dick Nanto, CRS. It heard presentations on U.S.-Japan Security issues by Admiral Michael McDevitt, Center for Analysis, Yoshihisa Komori, Editor-at-Large, *Sankei Shimbun*, Richard Cronin, CRS, and Larry Nicksch, CRS.

<sup>2</sup> For background, see among others CRS Issue Brief 97004, *Japan-U.S. Relations: Issues for Congress in the 1990s*.

Canada's. The trade flow runs heavily in Japan's favor. At the end of 1996, the U.S. trade deficit with Japan stood at \$47.6 billion. Japan is one of the largest sources of foreign investment in the United States (including portfolio, direct, and other investment).

The U.S.-Japan alliance establishes a U.S. guarantee for Japan's security (but does not obligate Japan to help defend the United States); gives Japan maneuvering room in dealing with its militarily more powerful neighbors; and supports an American strategic role in the Pacific. As two of the world's leading industrial democracies, the United States and Japan work closely together in dealing with international economic issues and other global and regional issues, ranging from nuclear nonproliferation to official responses to North Korea's nuclear program, peace efforts in Cambodia, and Chinese military assertiveness.

### **Strains in Relations**

Strains in bilateral relations, especially economic relations, grew markedly for over 20 years, subsided in the mid-1990s, and may be rising again. In the mid-1960s, U.S. manufacturers of textiles and light electronic goods complained about Japanese imports. Later, American manufacturers of automobiles, steel, and sophisticated electronic goods saw Japanese products take an increasing share of markets formerly held by the United States. By the late 1980s, Japanese manufacturers markedly increased their share of the international and U.S. markets, and some U.S. companies struggled to compete at home and abroad. There was strong U.S. criticism of prevailing conditions that appeared to allow Japanese firms to benefit from limited foreign access to Japan's home market and other unfair trade practices. Meanwhile, the end of the Cold War and collapse of the Soviet Union called into question some of the strategic underpinnings of the alliance.

The strains moderated somewhat in the mid-1990s. Japan's slow growth for several years contrasted with the U.S. economy's steady expansion and rising international competitiveness. For a time, the widely watched U.S. trade deficit with Japan began to decline substantially. After a period of strategic uncertainty in both countries over how to respond to the post-Cold War situation in East Asia, U.S. and Japanese leaders saw their interests as best served by strengthening the U.S.-Japan alliance to support their respective strategic interests in the region. By 1997, bilateral trade issues were rising again in line with Japan's newly rising trade surplus with the United States.

### **Economic Problems.**

Seminar participants were generally pessimistic about the near-term outlook for U.S.-Japan trade and economic issues. In recent years, the Clinton Administration has eased its previous hard line on U.S.-Japan trade issues, but conditions in Japan portend renewed antagonism. The closely watched U.S. trade deficit with Japan has grown in 1997, and could reach \$58 billion, a 20% increase over 1996.

Seminar participants broadly agreed on the reasons for this turn of events. The Japanese domestic market and overall economy remain in a seven-year slump, while large export-oriented companies in Japan remain highly competitive. Their edge has improved as the Japanese yen has lost over 20% of its value relative to the U.S. dollar during the past year. This gives Japanese manufactured goods a price advantage over comparable American products in the U.S. and other markets. A heavy portion of Japanese

manufactured exports used to go to burgeoning consumer markets in Asia. The deepening Asian financial crisis over the past several months appears to have prompted Japanese exporters to target even more the U.S. market. In sum, highly competitive Japanese manufacturers have little prospect for boosting sales in Japan or in other Asian markets, while the strong U.S. economy and a weak yen make the U.S. market a magnet for Japanese products.

U.S. opportunities to sell in Japan are limited by the same slow Japanese domestic growth and yen-dollar ratio. Some in the West and Japan have speculated that U.S. opportunities would grow as Japan carries out a broad economic deregulation plan under Prime Minister Hashimoto's leadership. Although seminar participants acknowledged that some U.S. companies are doing better in Japan as a result of past economic deregulation measures much more needs to be done to open inefficient Japanese sectors including distribution, telecommunications, finance, construction, and agriculture. They were pessimistic that the Japanese government would be able to carry out substantial changes in the near future.

The problem has centered on the ruling Liberal Democratic Party's (LDP) reluctance to upset economic and related bureaucratic interests that would be affected negatively by the changes. These "losers" in the economic change would be cast into a lackluster economy that the LDP seems unable to revive. In particular, the LDP's usual pump-priming methods of government deficit spending on construction and other government-funded projects cannot be used, according to the seminar speakers. This is because Japan's budget deficit has grown markedly as previous governments have tried in vain to engineer growth through such methods.

Thus, the ruling party faces very difficult choices. It hopes that planned economic deregulation will lead to future efficiency and growth that will be welcomed by Japanese voters. But the short term effect of the economic deregulation is to alienate constituencies tied to the economic status quo. Under the circumstances, seminar participants expected change to move slowly.

U.S. unhappiness with this situation almost certainly will grow, according to speakers at the seminar. U.S. officials encourage vigorous Japanese economic deregulation as a stimulus to Japanese economic growth that will absorb more U.S. exports and exports from Asia and elsewhere, and thereby promote balanced growth in the Asian-Pacific region. Such Japanese domestic growth would also boost sales of Japanese products in the home market and reduce incentive for increasing exports to the U.S. or other markets..

For over a decade, U.S. government negotiators have been working with Japanese counterparts to seek deregulation of Japanese industries and commercial areas in order to allow greater U.S. access to the Japanese markets. Recent focal points have been efforts to allow greater access to the Japanese market for U.S. suppliers of photographic film, autos and auto parts, flat glass, construction services, legal and financial services, telecommunications and medical supplies. If the trade deficit grows and the pace of Japanese economic change slows, U.S. Government negotiators are expected to exert greater political pressure on their Japanese counterparts.

## Security Issues.

In dealing with security issues, seminar participants focused on the implications of the U.S.-Japanese defense cooperation guidelines reached on September 23, 1997.<sup>3</sup> Those guidelines replaced more limited arrangements in force since 1978. In particular, they provide U.S. forces with more certainty about what Japan can do in support of U.S. forces both in peacetime and in the face of military contingencies or regional crises. Such activities include rear-area support, greater interoperability of forces, cooperation in evacuation of civilians and peacekeeping operations, surveillance, and mine sweeping in international waters near Japan.

Perceived problems with the guidelines focused on uncertainty that the Japanese government would implement them fully in the face of persisting pacifist feelings in Japan and continued strong criticisms from China. According to seminar speakers, Chinese opposition affects Japan in two ways. On one hand, it makes Japanese politicians wary of taking steps in implementing the guidelines that would antagonize Beijing. On the other hand, it strengthens the private resolve of at least some Japanese leaders to solidify security ties with the United States in order to be in a better strategic position to deal with China's rising influence in Asian and world affairs.

Japanese pacifism or other opposition to expanding the role of the Japanese military could complicate LDP efforts to obtain legislation needed to give the government authority to restrict civil airspace and make Japanese facilities available to U.S. forces during a military emergency. The ruling party has a bare majority in the lower house of the Diet, and depends on the Socialists, who oppose the revised guidelines, to have a majority in the upper house.

A broader concern voiced at the seminar was that the revised guidelines, even if implemented successfully, fail to resolve fundamental asymmetries and other problems in U.S.-Japan defense relations. During the Cold War, these difficulties were held in check by the strong common need to deal with the Soviet threat. As the Cold War has ended, new issues have emerged that will not be easily resolved. They include:

Host Nation Support. Part of the U.S. reasoning for undertaking the new defense guidelines was to show U.S. taxpayers that Japan was prepared to do more to reciprocate for the U.S. stationing of 47,000 troops in Japan. Without greater Japanese support, it is argued, U.S. political support for the U.S. military presence in Japan could decline, especially if the situation on the Korean peninsula were to become more stable.

Okinawa Bases. In the wake of an incident involving the rape of a Japanese school girl by three U.S. servicemen in Okinawa in 1995, Okinawans have pressed vigorously for a reduction in the 29,000 U.S. forces based on the island. The U.S. and Japanese governments concluded an agreement on December 2, 1996, under which the U.S. military will relinquish some bases and land on Okinawa (21% of the total bases land) over seven years, but U.S. troop strength will remain the same. Alternative sites are to

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<sup>3</sup> For background, see CRS Report 97-979, *Japan-U.S. Security Cooperation: Implications of the New Defense Cooperation Guidelines*, by Richard Cronin.

be found for training and the stationing of U.S. forces. Japan is to pay the costs of these changes.

Defense Technology Sharing. For many years, the United States has been pressing Japan to share technology of use in weapons systems and other ventures of benefit to both countries' security. Japan has sometimes been reluctant to share such technology for economic, security or other reasons. The Clinton Administration has been pressing Japan to develop jointly a theater missile defense system for the defense of Japan against missile attacks. The Japanese government is studying the issue and may make a decision in late 1997. Some in Japan are reluctant to commit substantial resources to this expensive and technologically uncertain project that is likely to antagonize China and possibly other Japanese neighbors.

Mutual Expectations. At bottom, some seminar participants noted, the most serious continuing problems in U.S.-Japan security relations center on each side's expectations of the other and the uncertainty that those expectations will be fulfilled. Thus, Japan expects the United States to protect Japan while Tokyo agrees to pay for U.S. forces, accept U.S. bases, and agree to some increase in support for U.S. forces in the event of military contingency. For its part, the United States expects Japan to contribute more to support U.S. forces, to accept large U.S. bases, and to do more in support of U.S. forces in the event of a military contingency. Some seminar participants warned that the U.S. could be disappointed on all three counts, especially if Japanese budget constraints, popular opposition to the large U.S. military presence in Okinawa, or Japanese government timidity during a military crisis in Korea or elsewhere involving American and Japan curb overall Japanese support for the U.S. military. Such a turn of events could prompt a fundamental reevaluation of the U.S.-Japan military alliance, according to some seminar speakers.