

# NONTARIFF BARRIERS TO JAPAN'S TRADE\*

By KIYOSHI KOJIMA\*\*

## INTRODUCTION

International trade has achieved remarkable growth at a rate of more than 8 per cent annually since the end of World War II, thanks to the efforts towards liberalization of trade and foreign exchange in which the GATT and IMF have played a central role. The recovery and growth of the Japanese economy and foreign trade owe much to this growth of world trade. This very liberalization and sustained high growth of international trade, a phenomenon totally different from its prewar performance, is one of the most important elements underlying the rapid growth of the Japanese economy. The efforts toward tariff reduction centering around the GATT have attained substantial results, climaxing with the "Kennedy Round" which was the sixth round of negotiations in global tariff reductions and which reached an agreement in June 1967. After the tariff reductions agreed upon are completed in 1972, the tariffs on dutiable non-agricultural goods will average only 9.9 per cent in the United States, 8.6 per cent in the European Community, 10.8 per cent in the United Kingdom and 10.7 per cent in Japan. However, the liberalization of world trade with the Kennedy Round as its peak will soon come to a standstill. Rather, the trend toward liberalization may be reversed with the advent of protectionist sentiment in the United States and the appearance of an enlarged European integration which may become more inward-looking. A way will have to be found to break out of this nascent protectionism by applying drastic measures to this impasse to promote further liberalization and expansion of world trade. A new order of the world trade is being sought, for instance, by promoting a second Kennedy Round under the leadership of Japan or proceeding toward the establishment of a multilateral free trade arrangement. When the water level of an ocean is lowered, mountains on the ocean floor that had hitherto been submerged become navigation hazards. Similarly, when tariffs have been lowered, nontariff measures have appeared as increasingly harmful barriers to trade.

Gradually it is being felt that nontariff barriers are as cumbersome; even more cumbersome trade deterrent factors to deal with, than the remaining tariff barriers. Thus the reduction and elimination of nontariff barriers have begun to be advocated by the Nixon Administra-

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\*\* Professor (*Kyōju*) of International Economics.

tion of the United States as a way to follow the Kennedy Round toward the liberalization of world trade. This is certainly a major target to be attacked. For in the present world when a trend backward to protectionism is discernible, it should be quickly reversed. The elimination of NTB may become a major breakthrough in expanding not only trade among advanced countries but also their imports from the less developed nations.

A thorough analysis of nontariff barriers will have major implications today, particularly for Japan. Misunderstandings and attacks against Japan's import restrictions and export incentives as manifested, for instance, in the Japan-United States textile negotiations, the dumping problem, the strong request for liberalization of agricultural product imports pervade the economic world. Between Japan and the United States the problem has gone so far as to cause a strain in relations. Japan's nontariff barriers are not well enough understood and are rather over-estimated by foreign countries. We Japanese, too, have not examined and recognized this problem sufficiently. Especially, we should analyse the matter thoroughly, show our cards and appraise them objectively, and thereby dissipate international misunderstandings. A thorough examination will show that, as a whole, Japan's nontariff barriers are of surprisingly small number though there are some which are readily apparent, for example the residual import restrictions. Anyway, it is essential to remove the foggy and vague misunderstandings that Japan is a nation of strict protectionism and mercantilism surrounded by numerous nontariff barriers. At the same time, a request should be made of the Japanese government that by a thorough liberalization of trade, Japanese trade transactions should be simplified and rationalized so as to lead the growth of multilateral free trade.

This article is attempting to make a systematic overall appraisal of Japan's nontariff barriers. We shall also examine whether there is room for improving or removing them, and further, explore ways for the solution of the world-wide problem of nontariff barriers.

For such a systematic arrangement and examination of the nontariff barrier problem in Japan, we must first establish a criteria to determine what a nontariff barrier is. An appropriate definition and classification of NTB are presented in Section I. In Sections II, III, and IV, the major NTB in Japan is briefly examined by category. Following those fact-findings, in Section V, the characteristics of NTB in Japan are summarized and the direction and measures to be taken for the improvement are discussed. Finally, in Section VI, measures for a global advance toward the reduction and removal of NTB are suggested.

## *I. DEFINITION AND CLASSIFICATION OF NONTARIFF BARRIERS*

Tremendous variety, substantial complexity and great tenacity are characteristics of nontariff barriers. To give a clear definition of what is a nontariff barrier is most important and this is the first step to approaching and solving this nontariff barrier problem. It is almost impossible to measure the trade restrictive effect of nontariff barriers. However, if one is not clear of even what the nontariff barriers are, or what one country calls a nontariff barrier and another country does not, it will be difficult for these countries to even

begin negotiations. Some pioneering studies<sup>1</sup> on nontariff barriers have previously been published abroad. All of them, however, substitute only the citation of major forms of nontariff barriers for their definition.<sup>2</sup> Considering the importance of this problem, we present here a definition of nontariff barriers and criteria for judgement capable of dealing with the nontariff barrier problem in Japan, taking into consideration the suggestions made by Professor Komiya<sup>3</sup> who participated in our study.

#### A) *Definition of Nontariff Barriers*

We arbitrarily define:

Nontariff barriers are measures other than tariffs that restrain or disturb free international trade, and are selective regulations which directly or indirectly discriminate between indigenous and foreign goods (or domestic and overseas markets).

This might need some paraphrasing.

(1) "Regulations that restraint or disturb free international trade" might be changed, in terms of economic theory to "regulations that distort optimal resource allocation in the world and which reduce potential real income." However, this definition in terms of economics is not necessarily easy to understand. Therefore, the words "free international trade" should be interpreted as satisfying all the conditions necessary to assure "optimal allocation of world resources and the maximization of real world income as far as the trade of goods and services is concerned apart from international movements of capital and emigration."

Probably another way of defining the same would be "governmental interventions which bring about deviation between private and social costs of trade in each country and prevent the maximization of total social production." Trade barriers, both tariff and nontariff, come into existence as a result of pressure from various vested interest groups for favorable discriminatory regulations and government's acquiescence. Government intervenes in trade in the name of the more sophisticated objective of national economic policy such as the improvement of balance of payments, the attainment of full employment or the fostering of key and dynamic industries. If each country strives for the maximization of total social product by eliminating deviations of private and social costs, then the optimal allocation of world resources and the maximization of real world income will be achieved. To define the same thing in another way, the expression "of each country" rather than "of the world" will appeal more directly to the interest of each country. It will also help those peoples reflect upon their mistaken attitude that they could not unilaterally reduce trade barriers unless they could get equitable concessions from their trading partners.

(2) Concerning the expression "the selective regulations which directly or indirectly discriminate between indigenous and foreign goods (or domestic and overseas markets)," we have to consider

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<sup>1</sup> See the bibliography at the end of the report.

<sup>2</sup> Gerard and Victoria Curzon (Curzon [2], p. 1-10) undertook the definition and classification of nontariff barriers. They referred to the classification made by Ingo Walter ([11] p. 20). It is considered that their definition and classification do not differ in substance from ours.

<sup>3</sup> See Ryutaro Komiya, "Japan's Non-Tariff Barriers on Manufactures," a paper presented to the Fourth Pacific Trade and Development Conference, October 7 to 10, 1971, Carleton University, Ottawa.

(a) who regulates trade. The regulators are central and local governments, and non-governmental organizations (trade associations, export and import cartels and labor unions). However, in the case of Japan, almost all intervention and regulation is made by the central government in accordance with national law. So we will simply refer to "the government."

(b) Whether the government exerts selective regulations or not makes an important point. Overall adjustment measures which are aimed at adjusting the international balance of payments, for instance, changes in foreign exchange rates, fiscal and monetary policies, et cetera, do not constitute nontariff barriers.

(c) Whether they selectively discriminate between indigenous, and foreign products, or between home and foreign markets, or discriminate against certain foreign suppliers is an important criterion in judging whether the practices are nontariff barriers.

(3) Direct interventions in trade designed to inhibit imports and promote exports can easily be identified as *direct* nontariff barriers. In addition there are what we call *induced* nontariff barriers which are regulations introduced with policy objectives other than trade restriction which have a trade deterrent effect as a by-product. Even such obviously direct NTB as import quotas are justified by policy-making authorities in saying that it is originally introduced not to intervene in trade but to achieve other policy objectives such as improving the balance of payments position, fostering infant industries, or improving the income distribution in favor of subsistence income earners or low income areas (protection of agriculture and medium-and small-sized enterprises). If they are interpreted in this way there would exist no direct nontariff barriers and all would be induced nontariff barriers. Certainly we can not agree with such an interpretation. Economic analysis of restrictions, direct or indirect, might become a criterion for judging whether such measures constitute nontariff barriers or not. However the judgement of whether certain policy objectives are rational or irrational would be difficult. It might be more realistic to admit that there was one reason or another for the introduction of such measures. Therefore, those measures which were based on rational policy objectives at the time of introduction but which have already become unnecessary as a result of subsequent changes in economic conditions, or those which are too discriminatory in their restriction of trade in the light of their policy objectives should be recognized as nontariff barriers.

For instance, the "infant industries argument" is generally regarded as a case for protection which can even be agreed to from the standpoint of economics. But in a strict sense there are almost no justifiable cases for protection judging from Mill-Bastable's and furthermore Kemp's tests.<sup>4</sup> As a matter of fact, we face a difficult problem in deciding which specific industries are worth protect, what is the optimal degree of protection, or when protection should be discontinued. Therefore, we tentatively admit that the protection of infant industries is a correct policy objective, but that the degree of protection and whether it has already become unnecessary should be objectively examined.

When judged from the criterion of free trade, the protection of mature and declining industries which have fallen into comparatively disadvantageous positions cannot be permitted.

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<sup>4</sup> See Murray C. Kemp, "The Mill-Bastable Infant Industry Dogma," *Journal of Political Economy*, Feb. 1960, p. 65-67.

We will not argue the appropriateness of the introduction of protective measures. We would, however, like to examine individual cases as to whether the protection is still necessary in the light of changing conditions, whether if we continue the protection we can shift to measures other than quantitative import restrictions for instance, tariffs, or whether we should provide adjustment assistance to the affected enterprises to promote a shift to other industries.

To take another example, if the system of disease inspection of animals and plants, though rational in principle, is so uniform and severe as to prohibit importing those which are not contaminated, then this inspection is excessive and might constitute a nontariff barrier which must be moderated.

(4) There exists a means for attaining, by an alternative and more rational measure, the same policy objective which has led to a certain trade restricting measure. In case a shift could be made to an alternative measure but where nothing is done, the trade restricting measure should be thought of as a nontariff barrier. On the other hand, in case there is no room for rectifying it, it should be regarded as a mere "inconvenience." It is similar to the case where we cannot blame the geographical distance between countries or natural protection for its trade-restricting effect.

Among measures alternative to nontariff barriers, (a) there is overall adjustment measures which do not affect individual industries selectively and discriminatively but do affect the entire national economy without discrimination. These are represented by those measures such as changes in foreign exchange rates, fiscal and monetary policies, the so-called incomes policy, et cetera, which are taken with the object of adjusting the balance-of-payments position. If a system of overall adjustment measures has been built up for prompt functioning, might it not be possible to dismantle the greater part of the existing nontariff barriers? This is one of the important problems which should be looked into.

(b) Uniform tariffs or surcharges on all imports and uniform subsidies on all exports have an effect equivalent to devaluation. Therefore this might be regarded as a kind of overall adjustment measure.

(c) Actual tariffs differ in rates according to import item. Consequently, they are selective, distort the comparative advantage structure, disrupt trade, and are not desirable. However, tariffs are publicized and known to all interested parties, domestic and abroad, and are levied as prices on all foreign suppliers indiscriminatorily and objectively (with the exception of preferential tariffs and other special levies). In this sense, tariffs (including tariff quota systems, fixed uniform surcharges and other similar measures) are trade barriers which are simple, clearly identifiable and in line with the price mechanism. Being thus simple and clearly identifiable, international negotiations for their reduction or removal are easy to carry on. In contrast, nontariff barriers, nicknamed "hidden barriers," are trade barriers which are hard to identify clearly or grasp quantitatively and they are non-objective, or hidden and not discernible. But they can be managed directly by the hand of a national government and can attain the expected effect speedily and spontaneously. This is different from tariffs which bring about effects indirectly through the response of markets. From this point the former is preferred by government authorities to the latter. Their qualitative trade deterrent effect is as important. They might have a far stronger effect of distorting the trade pattern than tariffs, even though their effect of reducing trade quantitatively might be smaller. Needless to say, since they are not so simple, clearly identifiable and objective as

tariffs are, international negotiations for their reduction is more difficult. For these reasons, tariffs are considered preferable to nontariff barriers though they are equally trade barriers. It is deemed desirable therefore that efforts should be directed toward the use of tariffs including tariff quota systems and fixed surcharges and not toward the recourse to nontariff barriers in case the same policy objectives can be attained by the former or in case changes in the economic conditions permit the shift from the latter to the former.

In addition there is the difference that in the case of tariffs, customs revenues go to the government and are used for the nation's welfare, while premiums from import quota systems go to the private firms to whom quotas are granted. It might be said that tariffs are more desirable from this viewpoint. However, it is difficult to immediately determine which will have more of a trade deterrent effect from the national economy or global viewpoint.

(d) Though both belong to the same category of import quota systems, global quotas are regarded as preferable to more detailed quota systems which discriminate between countries and firms, voluntary export restraints imply discrimination between supplier countries from the outset. But among them category-wise controls are regarded as "worsen" than overall restrictions. In short, they are nontariff barriers since they involve a discriminatory and selective nature, but that when such nontariff measures have to be resorted to, a choice should be made of those measures which are the least discriminatory.

The search for alternative measures and the study of their order of preferability is an important task for the improvement and solution of the nontariff barrier problem.

(5) On one hand there is the opinion that the maintenance of trade restriction systems is a problem, while on the other there is a counter-argument based on the "real effect" that, though the systems are maintained, they ought not to be considered NTB since they are administered so as not to have a trade deterrent effect. This is a problem which has been a subject of discussion in the committee meetings of the GATT. In our view, if these measures come under the category of "direct nontariff barriers" in the classification we are making below, the very existence of the system constitutes a trade barrier even if they may not have a real trade effect. It can be argued therefore that the system should be abolished. On the other hand we need not to be so rigid as to regard induced nontariff barriers as nontariff barriers if they are so administered as not to have an important real trade restrictive effect.

## B) *The Classification of Nontariff Barriers*

As it has already become clear from the above examination of criteria for determining nontariff barriers in this study, we are inclined to classify nontariff barriers as follows.

(1) Direct nontariff barriers:

(i) Direct nontariff barriers to imports—Regulations (other than tariffs) which a government has introduced to restrict imports by discriminating between imported and domestic products. Typical examples are import quotas, licensing, import deposit systems, state trading and the like.

(ii) Direct nontariff barriers to exports—Measures which provide extra incentives for exports as compared with production and sales for domestic consumption, and include export subsidies (long-term deferred payment for exports of plant and equipment, among

others), production subsidization (interest subsidization to shipbuilders for example), export credit incentives, export tax incentives and the like.

(2) Induced nontariff barriers:

(iii) Indirect nontariff barriers—Measures originally not designed to discriminate against imports substantially in favor of domestic products and introduced with policy objective other than trade but involving elements which work against imports as an induced effect.

(iv) Illusionary nontariff barriers—Measures which are introduced for the same reasons as indirect nontariff barriers, but which have no trade deterrent effect and therefore might be regarded as mere inconveniences.

It is not easy to distinguish indirect nontariff barriers from illusionary nontariff barriers among induced nontariff barriers. We must judge on a case by case basis.

We have examined in this study the following two in addition:

(v) Voluntary export restraints, and

(vi) Discriminatory treatment against Japan.

Voluntary export restraints are nontariff barriers imposed by trading partners. However they are not necessarily defined as such, because they have an aspect that Japan is “voluntarily” controlling exports for her own reasons. As it were, they are of an intermediate nature for which it is not necessarily clear who is to blame, Japan or her trading partner. It is even questionable whether they should be judged as nontariff barriers or should be estimated as measures which have a positive role to prevent market disruption. In contrast the discriminatory treatment against Japan is clearly a nontariff barrier imposed by her trading partners. These two restrictions are being examined from the viewpoint of whether they can become a bargaining item for Japan in reducing nontariff barriers against her or whether there is room for improvement by replacing these discriminatory restrictions with other alternative measures. Japan's export nontariff barriers and the nontariff barriers imposed by other countries against Japan's exports will be taken up again in Section IV with reference to the criteria for judging them.

In the following sections, we would like to examine by category those cases which are suspected to be the major nontariff barriers in Japan in accordance with the above classification. In this process we will analyze whether these cases really constitute nontariff barriers and at the same time explore possibilities whether there is room for altering them to measures which are not nontariff barriers or to more desirable NTBs.

## II. *DIRECT NONTARIFF BARRIERS TO IMPORTS*

In Japan, trade barriers which are identified clearly as nontariff barriers are more abundantly found in the field of its imports. They are distinctively discernible in the case of the residual import restrictions, other import quota systems and import credits. There are also many cases which are evidently nontariff barriers as import control systems but so operated not to have a trade deterrent effect in their administration. This leaves room for a divided opinion.

### A) *Residual Import Restrictions*

The most notable among Japan's nontariff barriers is her residual import restriction with a great number of items still remaining on the restriction list. Thanks to the stepped-up liberalization during the past year, the number of items on the list has been reduced to forty including 28 agricultural products (according to 4-digit BTN), 3 mineral products (petroleum, sulphur and coal) and 9 industrial goods.<sup>5</sup> The number is expected to decrease further to around 30 by the end of 1971 or late March 1972. Agricultural products and non-agricultural goods<sup>6</sup> on the residual import restriction list are given in Tables 1 and 2 respectively.

Of these items, the residual import restriction on mineral products poses no problem because, of the three remaining items, petroleum and sulphur will be liberalized in the not distant future with coal alone remaining. The problem of the residual import restriction on industrial goods might be said to have nearly come to an end with only nine items remaining unliberalized. These nine items can be classified into two groups. One group comprises four items including raw hide and leather (bovine cattle leather, equine leather, sheep, and lamb skin leather, and goat and kid skin leather) and leather footwear. It is said that there is hardly any hope of liberalizing these items because of the protection that will have to be accorded to subsistence producers in the so-called "dowa" districts. The justification is being sought in the protection of declining industries or in the social problem of assuring employment and income. Their liberalization should be considered when assistance measure for promoting the adjustment of industrial structure has been worked out.

The second group comprises five items including digital-type electronic computers (2 items), their machinery and parts, and integrated circuits. However some of these goods have already been liberalized. In short the only remaining restriction is on the items related to large-sized electronic computers. Japan has protected and fostered the large-computer industry, one of the most promising growth industries, as an "infant industry." The residual import restrictions on the industry is also justified since early liberalization may simply lead to IBM's dominance and monopoly of the market.<sup>7</sup> Certainly, it will take some time before the complete import liberalization of peripheral goods of large sized electronic computers is realized. What conditions will have to be met for the authorities to determine that the computer industry has grown out of the stage of infant industry and liberalize it? When will it be? They should give a time table.

The liberalization of agricultural imports presents a difficult problem for Japan. As can be seen from the 28 items, classified into 9 sub-groups, agricultural products under the residual import restrictions are of wide range and variety. The most important items of interest are meat, meat products and fruits. Overall consideration will have to be given to the problem, taking into account the state-traded goods such as rice, wheat and barley and milk products though the number of items is limited. There is a strong view that it is

<sup>5</sup> We examine in this report nontariff barriers to Japan's trade through the end of September 1971. Further developments since then should be considered as forecasts or estimates.

<sup>6</sup> According to the conventional classification, agricultural products cover BTN 0-24, while non-agricultural goods BTN 25-99.

<sup>7</sup> Ryutaro Komiya, "Japan's Non-Tariff Barriers on Manufactures," *op. cit.*, p. 11.



TABLE 1. AGRICULTURAL PRODUCTS UNDER THE RESIDUAL IMPORT RESTRICTIONS  
(as of Sept. 30, 1971)

	No. of items	
Dairy products	3	Milk and cream (04.01), non-sugared condensed milk (04.02), and processed cheese (04.04)
Meat and meat products	3	Meat (02.01), ham and bacon (02.06), and other products of meat and pork
Rice, wheat products	3	Rice and wheat flours (11.01), rice and wheat meal (11.02) and malt (11.07)
Fruits, vegetable and their products	7	Fresh oranges and tangerines (08.02), stored oranges and tangerines (08.11), pineapple products (08.01), baked groundnuts (12.01), fruit juices (20.07), tomato juice (20.07), fruit pureé (20.05), fruit paste (20.05) and tomato pureé, paste (20.02)
Sugar-starch products	3	Refined sugar, rock candy, cube sugar and the like (17.01), grape sugar, malt sugar, sugar syrup and the like (17.02) and starches (11.08)
Other regional agricultural products	2	Pulses, groundnuts (excluding those for oil expression; 12.01), tubers of konnyaku (14.05) and the like
Fishery products	4	Nishin, tara, buri and the like, hard roes of tara and nishin (fresh and refrigerated; 03.01); same (salted or dried; 03.02); cuttle fish and scallop (03.03), genus porphyra and sea tangle (12.08)
Others	2	Other processed food and sweetened forage (23.07)
Total	28	

Note: Figures in parenthesis are BTN code numbers.

TABLE 2. NON-AGRICULTURAL GOODS UNDER THE RESIDUAL IMPORT RESTRICTIONS: 12 ITEMS  
(as of Sept. 30, 1971)

Sulpher	(25.03)
Coal	(27.01)
Petroleum	(27.10)
Bovine cattle leather and equine leather	(41.02)
Sheep and lamb skin leather	(41.03)
Goat and kid skin leather	(41.04)
Footwear with outer soles of leather	(64.02)
Digital-type electronic computers	(84.52,* 84.53*)
The terminal machines for digital-type electronic computers	(84.54*)
Parts of the digital-type electronic computers	(84.55)
Integrated circuits	(85.21*)

\* Partial liberalization of a BTN 4-digit item.

not justifiable that Japan alone is blamed for protecting agriculture and imposing trade barriers on agricultural imports for that purpose when all other advanced countries are doing the same things. It is also argued that the United States having been granted a waiver

by the GATT restricts agricultural imports, and that the EC and the United Kingdom obstruct imports by other means—the former by variable surcharges and the latter by deficiency payments to provide protection to their agriculture. Whereas Japan depends as means of protection solely on residual import restrictions and state trading which attract notice, the United States, the EC and the United Kingdom apply restrictive measures which have actually a larger trade deterrent effect than the Japanese measures.

However, with the exception of rice which is a state-traded item for the present, there is little justification for positively maintaining the quantitative import restrictions on other items. It is opined that imports of ham, bacon, canned beef and pork should be liberalized from direct control. It is thought that efforts should be made in this direction, even if the total abolition is difficult, gradual removal of import quota systems on agricultural products other than rice and the shifting towards more objective measures such as tariffs, tariff quota systems or fixed surcharges.

#### B) *State-trading*

The items set aside for state trading are the following eleven items:

Rice and wheat, barley and rye, major dairy products excluding natural cheese, butter, tobacco, salt, alcohol, poppy, cannabis and raw opium.

These items are subject to import quotas under the import quota system which will be dealt with later. So they comprise part of the IQ systems. They differ from other ordinary import quota items in that their transactions are monopolized by particular government agencies (such as the Food Agency of the Public Monopoly Corporation).

State-trading conforms to the Article XVII of GATT and therefore is legitimate under that agreement. Judging from the present conditions of the Japanese economy, however, as touched upon previously, though rice could not be liberalized yet, the justification is becoming weak for maintaining the quantitative import restrictions on wheat and barley. (Especially, in the case of wheat since domestic production has decreased to only 15 per cent of total consumption. Its production will no longer be expanded or maintained.) Import quotas are continued on dairy products with a view to aiding the dairy industry. But a shift to tariff quota or tariff system instead of state trading restriction might well be considered.

#### C) *Exempted Items*

These are commodity items on which member countries are allowed to impose import restrictions by GATT rules. Let us deal with all of them under the name of “exempted items.”

They comprise 36 items including:

Exemptions under Article XX (b) “to protect human, animal or plant life or health,” and Exemptions under Article XX (c) “relating to the importation or exportation of gold or silver”——Narcotics, gold, silver, et cetera (11 items).

Exemptions under Article XXI (b) “the prevention of security interests”——Uranium, atomic furnaces, airplanes, tanks, et cetera (26 items).

Similar to state-trading, the trade in these exempted items is conducted monopolistically by specified agencies under import quota systems. Though legitimate under GATT, they can be criticized, for instance, civilian airplanes, light planes and gliders are included en

bloc in the exemption list as related to airplanes and consequently treated as if they were "arms" connected with national security. However, their liberalization is now being considered. Including as many items as permissible on the ground that they are legitimate is not a rational attitude. There seems to be ample room for liberalizing a considerable number of such items, if this attitude is to be rectified.

#### D) *Import Quota Systems and Import Approval Systems*

The residual import restrictions, state trading and the exceptions mentioned above are administered under the import quota system. This import quota system requires traders to acquire quotas from the Minister of International Trade and Industry (MITI) for each import transaction. Therefore, this system unmistakably constitutes a nontariff barrier. Their implementation also involves some elements of NTB (this will be touched upon later). In addition, the automatic import quota (AIQ) and the automatic approval (AA) systems are in force.

The AA is an import permit system or in other words, "mere licensing system." Even though the importer of goods subject to this system has to obtain approval at a foreign exchange bank, an import license is issued immediately after the application has been filed.

In contrast, in order to import goods under the AIQ an importer must first get the issue of an automatic import quota certificate from MITI (as a rule a certificate is automatically issued on application). Then attaching this certificate he files an import application at a foreign exchange bank and receives an import license. Therefore, the AIQ system is an intermediate type having the characteristics of both import quota and simple licensing system. This may be interpreted in two ways. One interpretation might regard it as a lenient type import quota system and the other, a strict type licensing system. Which interpretation is right depends much on the actual way of administering the system. Anyway, the AIQ system is one of the sophisticated ways the government intervenes in import trade. It is unique to Japan.

The AA system is not a nontariff barrier so far as it is only a simple licensing system and it has no trade deterrent effect. It cannot be denied that some labor and expense is required in obtaining import permits such as preparation of necessary documents, and going to exchange banks. However they are negligible and should rather be regarded as part of marketing expenses to be borne as a matter of course, and are not considered to have a trade restrictive effect when the far larger price differentials between domestic and foreign goods is taken into account.

There remains the fear that it might be used as an import restrictive measure in an emergency. However it was not for that purpose that the AA system was created. The AA system is simply retained as a counterpart to the IQ and AIQ systems in order to check whether or not the application belongs to an IQ or AIQ category. Therefore, attention should first be directed toward the removal of the AIQ system and the reduction of the number of items under the IQ system. These systems are related so that unless the AIQ and IQ systems are dispensed with, there can be no abolition of the AA system. If the AIQ system is completely abolished and if the IQ commodities are reduced to a very few items, for instance only rice, then there may be no problems even if the AA system is abolished. Anyway, an independent abolition of the AA system is impossible. In this sense too, the

AA system is a mere inconvenience which is unavoidably maintained and therefore should not be judged as a nontariff barrier.

Next, an explanation is made by the authorities concerned that the AIQ system has no framework of quantitative quotas, and that the import approvals by MITI are a formality and automatically granted three days after application, and that it does not affect trade. Thus, the authorities hope that the measure will not be regarded as a nontariff barrier. It is argued against this view that, if such is the case, the AIQ system might well be abolished and that all goods subject to this system be shifted to the AA system. To this criticism the authorities cite the following reasons for maintaining the AIQ: (1) when goods are removed from the list of IQ goods (that is, liberalized from import restrictions) there is the necessity of watching the import trends of that commodity. They cannot be included among AA items until the situation does not bring about abrupt increases in imports; (2) such a cautious attitude provides a psychological sense of safety to domestic business circles which feel uncertain in the face of import liberalization and thereby contribute to the promotion of liberalization. In other words they argue that the AIQ is a transitory measure and a cushion for the progress toward import liberalization. As will be dealt with later, such scrupulous care in the promotion of import liberalization is discernible in other regulations too.

However, so far as the AIQ involves regulation in the form of approval by MITI, it is unquestionably a nontariff barrier. No matter how prudently it may be administered in order to avoid a trade restrictive effect, the system is open to the charge of being a nontariff barrier. Therefore, it should be abolished promptly. It would be well that such a complex and misleading system unique to Japan be abolished. The belief that import liberalization could not be promoted without the help of such a cushion is gone. In fact, it is expected that the majority of the AIQ system will be abolished at an early opportunity (probably by the end of 1971).

Finally, the IQ system is definitely a nontariff barrier since quantitative import controls are the basis. In addition the system is the worst nontariff barrier among import quota systems.

Since all the Japanese IQ systems are global quotas, they might be estimated as less discriminatory than other formulas which impose more detailed quotas. Though the system is global quotas, however, it is not immune from discriminating against particular trading partners or particular firms depending upon its operation. Quota systems inevitably involve such evils no matter how good the system may be.

As regards the operation of IQ system the following two points are criticized by foreign countries: (1) Import limits are not publicized; and (2) Emphasis is placed on quotas based on the past performance of importers.

The authorities concerned cite the following reasons for the non-publicity of import limits. In the past, import limits for each item was published. This invited demands by related domestic industries or legislators for a reduction in the quantity of import quotas, resulting in the retardation of progress toward substantive trade liberalization in the form of an enlargement of quantitative limits. There were cases that the publicity encouraged excessive competition among importers, making orderly imports difficult to maintain. It also provided the exporting countries opportunities to raise their prices, placing Japan in a disadvantageous position in import transactions. Thus, the authorities explain that these evil effects led them to discontinue the publication of quantity limit for imports.

In our opinion, however, these reasons are not persuasive justification for the non-publicity. In particular, it is to be noted that (b) represents one of the cases that in Japan nontariff barriers are firmly tied with the prevention of excessive competition. Perhaps the truth is the reverse. It cannot convincingly be argued that the import limits be left unpublished because their publication causes excessive competition. The truth is that the very existence of import quota system which imposes quantity limits on imports gives rise to "excessive competition" and disturbs the orderly import trade. Presumably, if import quota systems are maintained the importer who has succeeded in getting a quota can earn premiums by selling imported goods at a domestic price higher than the import price. Therefore they compete each other to obtain import quotas. The so-called "excessive competition" of this kind does not end unless the quota system has been dismantled. Moreover, if the import limit has been published importers can anticipate both import and domestic prices and consequently the profit margin which will materialize when that quantity of goods has been imported. As a consequence, would not the excessive competition for obtaining quotas be weakened? This is particularly the case when the import limit is large. As regards (c), it is because of the existence of quota systems and not necessary because of the publication of import limits that exporting countries can raise their prices.

With respect to the performance-based quota principle, though the authorities emphasize that it helps maintain the order of fair trade, this is not convincing.

Though such criticism as stated above is raised against the way Japan administers the import quota system, it is minor as a trade barrier and might be regarded as a mere inconvenience in transactions. So long as it is a quota system, it unavoidably involves more or less discrimination or unfairness. Therefore, efforts should be exerted toward the reduction of the number of quota items and further toward the elimination of the system itself rather than improvement in its administration.

In this connection, a quota system to be administered by import associations had once been introduced on Taiwanese bananas. However the system has already been dismantled or will soon be abolished.

#### E) *Non-standard Method of Settling Import Account*

For the settlement of import and export accounts, both standard and non-standard methods are in force. We will examine here what part of such settling methods constitutes nontariff barriers with respect to imports. When an importer wants to settle his accounts by a special method of payment, for instance, payment deferred more than four months after the imported goods are cleared through customs, he has to apply MITI for permission. This is called the "non-standard method of settlement." Ordinary methods of settlement which do not come under this regulation are called "standard method of settlement." The standard method can automatically be settled through authorized foreign exchange banks. Settlements by the standard method are checked by foreign exchange banks, together with the import permit procedures under the AA system, as to whether they conform with the conditions of the standard settlement.

The non-standard settlement method is quite similar to the IQ and AIQ systems on one hand, and the standard settlement method to the AA system on the other. The system for settling import accounts is similar to licensing import exchange. Among them the

standard settlement method as similarly to the AA system is a simple licensing and cannot be said to have a trade deterrent effect. On the other hand, the non-standard settlement method is a strict exchange licensing system corresponding to quantitative import quotas under the IQ or AIQ systems and undeniably a nontariff barrier. Only those items which are under the AA system and in conformity with the conditions of standard settlement method are eligible for the simple licensing scheme which requires no other procedures than an automatic approval at foreign exchange banks. In case a commodity does not conform with the conditions of standard settlement even if it is under the AA system, it becomes subject to either exchange control or import quotas. In case a commodity under the IQ or AIQ regulations is imported for settlement by non-standard methods, it is subject to a dual regulation. It is proved here that imports into Japan are placed under a water-tight supervision regulated dually from both sides of trade and foreign exchange controls. In such a closely woven net of systems might be found one of the reasons why the nontariff barriers imposed by Japan are mistaken to have a more protectionist element than their actual trade restrictive effects.

Criticisms are raised by foreign sources against the import settlement system regarding the time limit of less than four months in case of standard settlement method and also, though a minor case, against the advance payments for imports with regard to the limit of less than 1.8 million yen or equivalents. It is pointed out by domestic traders, too, that this practice disrupts transactions not conforming to the conditions. However this might mean that the *non-standard* methods which have a limit of four months do constitute a nontariff barrier and not that the standard method is defective. If this time limit of non-standard settlement method is relaxed, for instance, to six months as it is case with exports, then what they call a defect in the standard method will cease to exist. The standard settlement method is a necessary evil and is nothing but a mere inconvenience in trade which exists as the counterpart or shadow of the non-standard method. The former cannot be abolished unless the latter ceases to exist. Their relation is exactly same as that which exists between the AA system and IQ and AIQ systems. Therefore the relaxation of conditions of non-standard settlement or its abolition should be aimed at.

It is noted that the need of this system is explained by the authorities in the following way. To prevent the deferment of payments for speculative purposes, the checking through the non-standard method is necessary. The limitation of advance payment is necessary to prevent importers from settling their accounts by advance payment in excessive competition. Here again the consideration has full play for the prevention of excessive competition. The non-standard settlement method is a system which is capable of restraining imports like the IQ and AIQ systems, though the authorities explain that it is administered so that it has no trade deterrent effect. Therefore, it is a nontariff barrier as far as the system is concerned, and efforts should be exerted for its abolition. Furthermore, as it is not necessary to check imports dually on both sides, trade and foreign exchange, it could be considered to first dismantle either the IQ and AIQ systems or the non-standard settlement system.

#### F) *Import Deposit System*

This is a system under which those who want to import goods are requested to deposit import deposit money which represents a fixed percentage of import value, in principle,

at the time of application for import permit in the authorized foreign exchange banks where they file the application. The deposited money will be returned to them immediately when goods worth 80 per cent of the value written in the import certificate have been cleared through customs. The importers have their funds in hand reduced by the amount which they are requested to deposit as deposit money or incur interest costs if they seek to finance the money by borrowing. This will force them to restrict imports much. In short the system has clearly an import restrictive effect. In addition it entails discrimination against foreign goods in favor of domestically produced goods. Therefore the system unmistakably acts as a nontariff barrier. However, effective on May 18, 1970, the import deposit money has been reduced to zero and ceased to be charged. Therefore the system no longer has an import deterrent effect in practice. But the system *per se* is still retained. The problem is that the system remains unabolished. We interpret this that the system is maintained so that it can be reactivated at any time when such emergencies arise like a sharp increase in imports or deterioration of international balance of payments position.

The ratios of deposit were as high as 10 per cent for raw materials and 36 per cent for consumer goods in September 1961. As far as consumer goods are concerned, the ratio was later lowered to 5 per cent in December 1962, then raised again to 35 per cent in March 1964, reduced to 5 per cent in April 1965, to 1 per cent in October 1969 and 0 per cent in May 1970. As will be clear from these changes, a possibility exists that the ratio may be raised at any time.

According to the authorities concerned, the system is aimed at preventing speculative imports rather than restricting imports by making traders more cautious in applying for import permits (because an extra cost will be incurred). The system is also expected to have an effect that importers will carry out with certainty the imports permitted because they have deposited import deposit money. This is aimed at preventing the practice, for example, of obtaining the right of importing a certain quantity of goods and then reselling that right to others. It is notable here also that a strong intention is to prevent excessive competition. It is clear, however, that it is impossible to justify this system by the "excessive competition" argument.

### III. NONTARIFF BARRIERS IN EXPORT FIELDS

#### A) *Criteria for Identification*

Various measures have so far been taken to favor, encourage or promote export activities. We will first discuss them en bloc under the name of "export incentives." In the field of exports nontariff barriers which foreign countries impose on Japanese exports, discriminatory treatment against Japan, pose a problem. There is another problem of voluntary export restraints which are on the borderline between nontariff barriers imposed by Japan and those imposed by foreign countries. They are of a great concern to Japan. We will also examine them in this section.

We have considered the definition of nontariff barriers and the criteria for their determination in Section I already. They were exactly applicable to nontariff barriers in the field of imports. However, as the problem of what constitutes nontariff barriers in

the field of exports differs more or less from those in the import field, we would like to re-examine them here.

Export incentives are schemes designed to provide incentives for promoting exports by making export activities more profitable than sales to domestic markets and thereby enabling exporters to sell abroad without loss at somewhat cheaper prices than in home markets. This entails discrimination in favor of export-oriented production against that for domestic markets. Resource allocation will be distorted from the optimum. This will lead to the deviation between private and social costs—that is to say, export activities will bring big profits to private enterprises and will expand substantially but this will not result in increasing gross social product to the maximum. If we are to search for the most proper criteria for identifying nontariff barriers in the field of exports, it will be found in such distortion of resources allocation and deviation between private and social costs in the exporting country itself. Let us call this the “exporting countries’ criteria for nontariff distortion.”

In reality, however, exporting countries do not feel that export incentives they provide do constitute nontariff barriers. Rather, they make it imperative to improve their international balance of payments position by increased export earnings. They feel that exports are indispensable to expand effective demand, and to accomplish and maintain full employment. It is also thought that for particular industries the exploration of overseas markets and the increase of exports are indispensable factors for realizing economies of scale. However, export incentive measures can be justified in case they are motivated by temporary balance-of-payments difficulties. But there can be no justification after an export surplus trend has been restored.

However, is there any reason why export incentives adopted by country “A” be blamed as nontariff barrier by another country “B”? The question has to be examined in two separate cases. One is a charge that the export incentives in country A have an effect to increase unduly imports into country B, thus oppressing competing industries in the latter country.

If they are based on the right interpretation that the advantage of international trade can be found in getting imported goods at cheaper prices and in greater quantities, there will not arise such criticism and the bargain sale resulting from the export incentives by country A should be welcomed. The reason why country B blames the measure instead of welcoming it is that the country takes a position of protecting domestic industries similar to cases where it adopts import restrictive measures. In other words country B accused its trading partner, country A, of taking export incentive measures as the reverse of its own restrictive trade policy and on the basis of the same way of thinking. It may rather have a tinge of accusing the trading partner A of their export incentives in order to defend its own import restriction. If such is the case, it is extremely doubtful whether this accusation will contribute to expanding world trade.

Country B does not explicitly say that its accusation has been motivated by the protection of its own domestic industries or the attempt to justify its own import restriction. Instead they insist that country A’s export incentives are harmful because they lead to excessively large imports into country B and disruption of its markets and therefore constitute nontariff barriers. For this “market disruption reason,” many import deterrent measures including the long-term textile agreement, a variety of discriminatory treatments against Japan, anti-dumping measures and the like are justified. Voluntary export restraints too are designed



to regulate and prevent market disruption which country B may suffer from the influx of imports from country A not by import restrictions by country B itself but at the responsibility of exporting country A. And on the part of exporting country A also the voluntary export restraints are accepted, recognizing that orderly marketing is necessary.

It may be gathered from these views that there has been introduced a new definition that measures which have a market disruptive effect are nontariff barriers in the field of exports, apart from the definition of nontariff barriers to imports which defined nontariff barriers as measures obstructing the expansion of world trade. As touched on earlier, however, it might be also interpreted in such a way that, fundamentally, the problem originates in the protection by the importing country B of its domestic industries and that this country B is accusing the exporting country A of its export incentives being nontariff barriers or having country A to take the responsibility of preventing market disruption in order to justify its own import restrictions or to refrain from taking import restrictive measures itself.

If such is the case, the identification of export-related nontariff barriers for the market disruption reason will become quite difficult. This is because of the difficulty in determining the extent of market disruptions.

The importing country B will try to interpret market disruptions as broadly as possible from the standpoint of protecting its domestic industries, while the exporting country A will attempt to define the words as narrowly as possible so that there exist no cause for market disruption or, if any, to reduce their illegitimacy to the minimum. An internationally unified view on the definition of market disruption and the illegitimacy of its causes might be wanted. Even if one has been produced, however, again the question will recur about its interpretation. The matter will end in a fruitless debate with a result that a country in a stronger bargaining position will force its partner country to yield to its views.

Therefore, the market disruption reason is an important factor which will have to be taken into account, but cannot become a conclusive one when identifying nontariff barriers in the field of exports. Hence, it follows that the exporting countries' criteria for nontariff distortions are the very criteria that can identify exactly whether certain measures constitute nontariff barriers. It also might be said that after all there is no other way to improve nontariff disruptions in the field of exports than their voluntary abolition by the exporting countries on the basis of its own interest.

Another criticism which might be raised by foreign countries against export incentive measures of country A is that, when country B is competing with country A in a third country C's markets, country B will be placed in a disadvantageous position by country A's export incentive measures. The assumption is that when countries A and B compete with each other in their export markets in country C, the competition is not fair unless all conditions for such competition except production costs of exports are the same. The argument is being waged as to whether they constitute nontariff distortions from this viewpoint. Let us call this the "fair trade reason." The financing of exports by deferred payment method is a representative example in issue.

There may arise two questions. First, when not only one country but other countries also are adopting similar export incentive measures, should it be ruled that fair trade is in practice (a) if any differences that may exist between them have been ironed out, or (b) should it be so ruled that all countries have to abolish their incentive measures? Perhaps the common concept of fair trade is the former (a). In the light of the exporting countries'

criteria for nontariff distortions which we would like to adopt, all countries concerned have to dismantle their export incentive schemes. However, this may be an ideal which will never be accomplished.

If such is the case, it is absolutely impossible for the country which places itself in an advantageous position in international competition by the adoption of export incentive measures to dismantle such measures unilaterally. Therefore the legitimacy of such nontariff barriers should be judged by the fair trade criterion. In other words the most desirable is the across-the-board abolition by all the countries of their export incentives. If this is impossible, however, first of all there should be established an internationally unified criteria for allowable export incentives, and only excessive incentives should be identified as nontariff barriers.

The second problem is what are the competitive conditions that will have to be made internationally uniform and to what degree. The conditions of financing exports by deferred payment is an example easy to understand. But others are hard to interpret. One example is a scheme adopted by Japan under which a lower rate of interest is charged on export credits. It is not entirely a groundless argument to say that, since interest rates are higher in Japan than in foreign countries, subsidized low interest rates are accorded to exports alone in order to help Japanese exporters wage fair competition with foreign exporters in third country markets on an equal footing as far as interest rates are concerned.

If such is the case, this scheme is a nontariff distortion which will naturally be eliminated in the light of the exporting countries' criteria, but admissible when judged from the "fair trade reason." Here the only problem will be whether the degree of favoritism is more pronounced in Japan than in foreign countries. However, the argument that unless wage differentials between countries are ironed out there will be no fair trade is nonsense. So it is not logical to argue that all countries must have equal interest rates when they compete in export markets. On the contrary, an interpretation might be given that interest on short-term export credits is not a production cost of export goods but is part of marketing cost. In fact, disputes on the fair trade reason are often focussed on the international unevenness of marketing conditions. However, if trade practices are to be considered from marketing reasons, it is undeniable that criticism might be raised that the existence of powerful trade firms peculiar to Japan obstruct fair trade. It is desired, after all, that the extension of the fair trade reason for interest rates be avoided. It should be interpreted that the difference of international competitiveness due to the differentials in interest rates between countries are reflected in their respective foreign exchange rates. Therefore Japan should abolish its export incentive interest rate scheme and in case balance-of-payments difficulties arise, they should adjust foreign exchange rates.

As it is known from the interest rate problem, the abuse of the fair trade reason will give rise to many troubles. We said earlier that it was undeniable that an argument might be made that it is not fair trade unless the same wage levels are maintained in all countries. But it is also impossible to deny the possibility that such broad interpretation might be made as follows:

Japanese enterprises do not bear anti-pollution expenses fully; they still continue the practice of long working hours; or even that the Japanese language itself impairs the conditions of fair trade.

It is clear that these are not nontariff barriers because they are not due to governmental

intervention nor do they discriminate between internal and overseas markets by selective measures. Therefore it is necessary to strictly limit the use of the fair trade reason.

First, we would like to adopt the exporting countries' criteria for nontariff distortions. Second, in limited cases identification should be made in the light of fair trade reason. Third, the remaining problems of market disruption and orderly marketing would not be dealt with from the viewpoint of whether they are nontariff distortions or not. Their solution will be considered later from another standpoint.

#### B) *Export Incentive Measures*

Export tax and interest rate incentives, long-term export credit on deferred payment basis, and subsidies for export and export-oriented production can be cited as major export incentive schemes in Japan, about which it is questioned whether they constitute nontariff barriers. It is perceived that while the incentive measures in import fields involved such direct control as quota and licensing schemes, those in export fields are indirect measures such as tax and interest rate incentives and subsidies which are designed to encourage export by influencing the profitability of enterprises engaged in export activity. In this sense they are much more objective and leave less room for the government to intervene by administrative guidance than those in import field.

##### (1) *Export Tax Incentives*

The old "export income exemption" was abolished in 1964 as it went against Article XVI of GATT which prohibits export subsidization. In substitution, however, there have been introduced and are still in effect two sets of schemes which have other names but fulfil almost the same function—overseas market development reserve fund and export incentive depreciation allowance.

*Reserve fund for development of overseas markets*—For the development of new overseas markets enterprises are allowed to set aside as reserves a sum not exceeding a fixed percentage (in case of trading firms 1.7 per cent for those capitalized less than 100 million yen, 1.0 per cent for less than 1 billion yen and 0.5 per cent for more than 1 billion yen and in case of manufacturing enterprises 2.3 per cent for less than 100 million yen and 1.5 per cent for more than 0.5 billion yen) of their export value in the previous year and to calculate it into loss accounts. This reserve will be broken down equally over a period of 5 years beginning from the following year and put into profit accounts which are subject to taxation. In other words this is a scheme that allows export-related enterprises to defer payments of corporate tax that long.

*Export depreciation allowance*—Enterprises engaged in exports are allowed to depreciate their properties up to an amount which will be obtained by multiplying by 80 per cent the ratio of export income to total income in addition to the ordinary depreciation limit. This is also a scheme that allows great reduction of taxable income.

Though skillfully named, no positive policy objectives are perceived, except for favorable treatment of export activities. Since it unduly increases resource allocation to export activities, it is unmistakably a nontariff barrier in the light of the exporting countries' criteria for nontariff distortion. There is no longer a necessity for this system now that the favorable trend of trade balance has been firmly established. It will be abolished sooner or later, but there seem to be many complications before such a decision will be reached.

## (2) Export Interest Subsidization

As with imports, the system of standard and non-standard settlement methods is in force in the export field too. Where as in the import field there was a possibility that the system had a restrictive effect to imports, functioning as foreign exchange licensing, in the export field the system is mainly aimed at the prevention of capital flight by pooling foreign exchange earnings. No criticism is raised against the system that it has an export promoting or conversely a deterrent effect.

However, it is worth noting that it is pointed out that the enforcement of strict regulations regarding non-standard settlement of export accounts is motivated by the consideration to prevent excessive export competition. However, the system is devised in such a way that incentive interest rates will be accorded to foreign exchange bills which conform to the rule of standard settlement. Such trade bills will become eligible to be rediscounted by, or qualified as collateral acceptable to, the Bank of Japan, and enjoy the benefit of discount or borrowing at interest rates lower than those prevalent in the country. Export interest subsidization becomes a nontariff barrier which will have to be abolished when judged by the exporting countries' criteria for nontariff distortion. However similar systems are adopted by other countries. Such being the case, an argument may be made that only the excessive margin of Japan's export interest incentives be regarded as a nontariff distortion from the fair trade reason. But, as mentioned previously, we do not maintain this position.

Worth noting is the criticism raised by both domestic and foreign sources against the existence of large unbalance in Japan regarding export and import credits. It is argued that the fact that no measures were taken in the past in favor of the financing of import funds resulted in the disruption of imports as compared to exports. In reality, however, traders could get loans for imports from foreign banks at interest rates lower than domestic rates in Japan and sometimes lower than export subsidized rates. Therefore this criticism is not justified. However, with a rise of interest rates in foreign countries and a decline within the country as a background, an import fund loan system was introduced effective as of June 1, 1970, under which loans are made on imports at subsidized interest rates (official rates).

The introduction of import interest subsidization has added a new discriminatory character which will make domestic production less profitable and imports more advantageous. This might be desirable from the standpoint of foreign exporters but not from the viewpoint of optimal resource allocation in Japan and thus constitutes a nontariff distortion. It is not justifiable that, in order to balance against a nontariff distortion called "export interest subsidization," another nontariff distortion named "import interest subsidization" is introduced.

It is a *fait accompli* that there was unbalance between exports and imports regarding financing. But it is not a correct solution to add nontariff distortions in order to keep balance between the two. Since it is the export interest subsidization that is blamed originally, the right solution might be its abolition. Not recognizing interest subsidization on either exports or imports will assure equality in treatment. In fact the Bank of Japan raised interest rates on export related loans to the level of interest rates on domestic-related loans effective August 10, 1971, thus eliminating export incentives with regard to interest rates. However, the system itself which gives special treatment to export credits has been retained.

Even if differentials in interest rates between Japan and foreign countries affect, favorably or unfavorably, their competition in third country markets, they should be considered differences in costs and should be offset by the adjustment of foreign exchange rates, if necessary. The time will come in a not so distant future when the gaps in interest rates on trade credits disappear, if the short-term international capital flows are set free by a relaxation of foreign exchange controls.

### (3) Long-term Credits to Exports on a Deferred Payment Basis

This is a system under which the government grants permits of exports on the non-standard settlement method of long-term deferred payment basis to those who export large-sized machinery and equipment such as plants, vessels, vehicles to developing countries in particular and provide incentive low-interest loans through the Japan Export-Import Bank or Overseas Economic Cooperation Fund. This is one form of export subsidization. Since no preferential loans are extended to the sale in domestic markets of similar large sized machinery and equipment, the system can be regarded as nontariff distortions if judged by the exporting countries' criteria. However, preferential finance of this kind is now an international practice. Therefore when judged from the "fair trade reason" criterion only the excessive part, if any, of such treatment could be blamed as nontariff distortion. In fact, the excessive export competition through the softening of the terms for deferred payment is posing a problem internationally. Sooner or later an internationally uniformed criterion will be worked out.

Official development assistance to less developed countries promotes exports from aid giving countries with some advantage than from other countries, particularly in case it is tied aid. It might be one question whether or not such aid should be blamed as a nontariff distortion from the "fair trade reason" criterion. We had better evaluate the case from other viewpoint of the "aid to LDC's." Rather, further softening of terms of aid are now sought internationally. It is desirable for LDC's too that fair trade be assured and efficiency of aid be raised by untying aid. Japan's aid is gradually proceeding towards untying ever since August 1971.

### (4) Interest Subsidization to Shipbuilding

The interest subsidization to the shipbuilding industry which is criticised by foreign sources as a nontariff barrier will now be analyzed. Under this the government subsidizes part of the interest which shipowners have to pay on loans to finance the domestic building of ships. The Japan Development Bank provides 70 per cent of the fund, and the city banks 30 per cent. The government subsidizes 1 per cent of the 6.5 per cent interest which the JDB usually charges on its loans, and 2 per cent of the 8.2 per cent which the city banks charge. Thus the rates of interest the shipowners pay are 5.5 per cent and 6.2 per cent respectively and 5.65 per cent on average. This scheme makes it more advantageous for shipowners to build ships within the country than to import them. Therefore, it is one form of industrial subsidization and has an import deterrent effect and is a nontariff barrier. In this sense this was a problem to be discussed in the Section on "direct import nontariff barrier." From the point of prevention of import, there is no justification for subsidizing Japanese shipbuilding since it is the most competitive in the world.

Rather, this system is a scheme which is deemed necessary to balance against the long-term, low-interest rate deferred payment loans granted on ship exports mentioned earlier. In other words if no such scheme operates, all ocean-going vessels would be built for export-

purpose and none built for domestic use because of profit disadvantages (This has something common with the previously mentioned case that, in order to balance the existing low-interest export credits, the short-term low-interest loans had to be provided for financing of imports). In such sense, the interest subsidization to shipbuilding can be said to be a nontariff barrier which is a necessary evil to assure equal treatment with exports. Therefore its abolition will be very difficult. If the deferred payment export credit system is discontinued, then the interest subsidization to shipbuilding might be dismantled. However this could not materialize until all countries abolish their deferred payment export credit systems.

### C) *Discriminatory Treatment against Japan*

Needless to say, the nontariff barriers imposed by foreign countries which have an import-inhibiting effect work against Japanese exports. However, since they will be examined in detail in the respective national study of this joint research project, they will not be taken up here. Of particular interest to us is the discriminatory restrictions which foreign countries are imposing on imports from Japan alone. Of importance among such discriminatory treatment against Japan are: a) the invocation of Article XXXV of GATT, and b) the discriminatory import restrictions against Japanese export applied by Western countries.

When Japan was granted admission to the GATT in 1955, 14 countries including the United Kingdom, France and Australia invoked Article XXXV withholding their application of the Agreement based on most favored nation treatment to Japan. In addition in the early 1960s when the British and French colonies got independence and were admitted into the GATT, they followed the United Kingdom and France and withheld their application of the Agreement to Japan, bringing the number of countries which have invoked the article to nearly thirty. However major Western and British Commonwealth countries withdrew their invocation later. At present 22 countries (most of the LDCs) are still deviating from GATT rules in their trade with Japan.

Though great in number, those still invoking Article XXXV (22 countries of the 79 GATT members) have had no real trade deterrent effect. As there will be no significant consequence whether or not they withdraw their invocation of the article, they apparently do not dare to proceed with withdrawal, or they may be reserving their right as a possible bargaining item for some reciprocal action by Japan. For Japan this is a matter of international prestige rather than of economic interest. Therefore, it is more than ever desired that they would withdraw the invocation voluntarily. But it might not be worth while for Japan to force their withdrawal even in exchange for some reciprocal concessions. It might be better to leave the matter as it is. Also it might be better to refrain from taking such countering discriminatory measures as not providing the benefit of the "general LDC preference." General preference should be granted independently of the problem of invocation of the article. Our hope should be placed on their voluntary withdrawal of the invocation.

This problem is important, however, in the sense that the invocation played a role in inviting discriminatory treatment by Western countries against Japan. Namely, though the leading Western European countries had withdrawn their invocation of Article XXXV, they retained instead discriminatory treatment against Japan in the form of quantitative restrictions or licensing. In addition, such countries as Germany, Italy and Sweden which

had not invoked Article XXXV in their trade with Japan came to adopt various forms of discriminatory treatment against Japan.

Excepting the "voluntary export restraints" which are dealt with separately, a) we can first cite the quantitative restrictions as an example of discriminatory treatment by Western countries against Japan. It is rather difficult to give an exact number of items affected. But according to the 4-digit classification of Brussels Tariff Nomenclature Demark applies discriminatory quantitative restrictions against Japan on 78 items: Germany 14, Benelux 22, Norway 25, France 38, Italy 45 and Sweden 52. This averages about 30 items per country. The total number of items, avoiding double counting, subject to discriminatory quantitative restrictions against Japan in these seven countries comes to 118.

Besides quantitative restrictions, there may be cited b) Sweden's discriminatory licensing system against imports from Japan; and c) Switzerland's import price supervisory scheme (a price supervising system which does not permit imports from Japan below the floor prices).

It is not thought that these discriminatory measures against Japan have so far had a serious trade deterrent effect. Rather noteworthy is the fact that the following two facts have constituted major economic reasons for the invocation of Article XXXV of GATT and the alternative introduction of discriminatory treatment against Japan: a) the possibility that a flood of cheap Japanese imports might disrupt domestic markets or give rise to unfair competition; and b) the access to Japanese markets is barred by the residual import restrictions on a wide range of commodities. (a) requires separate examination and will be dealt with later, as to if the "market disruption" is or the orderly marketing is an effective and necessary solution. Regarding (b) it might be assumed that there is an indication that Western countries are retaining their discriminatory measures against Japan to bargain for the liberalization of Japan's import restrictions. Japan, on its part, is suspected to have retained import restrictions on many items which no longer need restrictions. Such being the case, there is enough possibility that either bilateral agreement or Japan's unilateral action to reduce the number of items subjected to the residual import restriction, might result in a substantial relaxation of discriminatory treatment against Japan.

#### D) *Voluntary Export Restraint*

There are a large variety of voluntary export restraints. It is not easy to exactly identify the countries concerned and ascertain the number of commodities affected. It is said that the number of items which are under voluntary export control imposed at the request of importing countries and reported to the GATT by the Japanese government as nontariff barriers reaches 264 by the BTN 4-digit classification, of which 51 are at the request of the United States, including cases dublicately requested by different countries. One criterion for determining nontariff barriers is governmental intervention in export control under the Export-Import Transaction Act or the Export Trade Control Ordinance. The number of items subject to the Export-Import Transaction Act is 184, of which 94 items involve quantitative restrictions. The total number of items, export of which require permits under the Export Trade Control Ordinance, comes to 210, of which 21 items are motivated by maintenance of an orderly export trade (of these, 15 items involve quantitative restrictions). A total of about 205 items comprising these 21 items and 184 items under the Export-Import Transaction Act are under voluntary export control. Of these, 109 items involve quantitative

restrictions. Of the 43 major items which require export permits, 29 items entail quantitative restrictions. And then examination of the motivations for the restraints shows that 16 items have been motivated by import restricting campaigns in the importing countries and 27 items by the prevention of excessive competition on the part of Japan. It has to be noted here that more have been motivated by the "excessive competition" reason on the part of Japan. There are also such cases as voluntary restraints of steel exports to the United States which involves no governmental intervention.

The causes and responsibility for imposing trade restrictive measures of such intermediate character as voluntary export restraints which are not clear as to whether imposed by the importing countries or by Japan lie in both parties. First, when a country's imports from Japan are increasing or threatening to increase sharply, it accuses Japan of causing market disruption, or sometimes threatens to raise tariffs or impose import quotas on such imports though their real intention is to furnish protection to competing domestic industries (in most cases declining industries) in the country. Secondly, Japan on its part accepts the request to impose voluntary export control on the judgment that voluntary restraints are less damaging and more palatable than import restrictions by the importing country. The reason why Japan judges voluntary control "more palatable" is that voluntary actions leave Japan with wider room for discretion. For instance, as has been seen in the course of the Japan-United States textile negotiations, if the United States puts a product-by-product quantitative import restriction into legislation Japan could do nothing but obey it, with the fixing and changes of quantitative ceilings on the respective item being left to the United States, even though Japan could petition to the GATT on the charge that the practice undeniably constitutes a nontariff barrier. On the other hand voluntary restraints allow Japan to use the discretion that, for instance, even though the rate of total export growth were restricted to a certain percentage the export of items in rapidly growing demand could be increased and the growth of items not in such demand be held down or reduced. If subjected to product-by-product regulations, it is often true that in the aggregate even the permitted growth rates cannot be attained.<sup>8,9</sup>

However, there is one more problem on the part of Japan. It is a fact that there were cases of excessive competition, that Japanese exporters were engaged in cut-throat selling competition with each other thus inviting a fall in prices. Voluntary export restraints are applied in order to avoid such excessive competition and to realize orderly marketing. Furthermore, as suggested by the statistics given earlier, there are many cases where voluntary export controls have been introduced on the pretext of avoiding excessive competition even if there is no threat of import restrictions being imposed by the importing countries. This is an abuse of export restraints.

Anyway there are too many items under voluntary export control. The reduction of the number of such items should be considered. Since the greater part of them have been introduced for the excessive competition reason, voluntary export controls on these items should be removed by devising some other measures appropriate to avoid excessive competi-

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<sup>8</sup> It is also noted that as compared with tariffs imposed by importing country, some premium margin, if any, between the importing country's price and exporter's cost may be retained as profits of exporters who are practising voluntary restraints.

<sup>9</sup> Since 1 October 1971, wool and synthetic textiles are subject to the governmental agreement between Japan and the USA (also Canada), i.e., product-by-product regulations.



tion. Major voluntary export controls involve quantitative allocation to exporting firms. This allocation is based on their past performance and therefore tends to function in favor of large against small firms. As a consequence, voluntary controls are applied under pressure from large business which wants to get monopolistic profits on the pretext of avoiding excessive competition and realizing orderly marketing. To some extent, undercompetition, not excessive competition, is the cause.

In order to avoid excessive competition and to realize orderly marketing, might not a system be preferred to the quantitative restriction (and consequently quantitative allocation to exporters) that floor export prices be established on particular goods which require such prices for observance by exporters and that those exporters who export cheaper than these prices be hit with export taxes? This is because foreign criticism is often directed to the disorderly marketing of Japanese firms in the form of price-cutting. Export quantities will fix themselves depending on the import demand in importing countries and will not get excessively large if the floor prices are appropriate. Regulations through floor prices will avoid extra intervention such as allocation of export quantities to domestic firms individually, and the conditions for competition will be maintained. However, for a substantial number of commodities voluntary controls can be completely abolished. Disorderly exporting that the authorities are concerned about may no longer occur.

As regards voluntary controls which are introduced to cope with the threat of import restrictions by foreign countries, though orderly marketing might be an unavoidable solution to such situation, we must re-examine whether orderly marketing is really necessary. The 15 to 20 per cent annual growth of Japanese exports, twice as fast as the growth of world exports, is one of the causes of threat to, and criticism by, foreign countries. However if Japanese exports grow in balance with its imports, there will be no ground to blame us, since the increase of Japan's imports will contribute to the growth of foreign economies. If the favorable balance of Japan's international payments is sustained, it deserves criticism by foreign countries. In such case an overall adjustment measure, such as revaluation of the exchange rates instead of export restraints on individual commodities, should be taken.

The problem is sharp increases in exports to particular markets of particular goods. This is the result of Japanese style excessive competition. Once the export to a particular market of a particular commodity is alleged to be promising, all firms flood that market following each other blindly, and waging a cut-throat price-cutting competition. As a measure to cope with such practice control through use of floor export prices might be most useful. Other causes of excessive competition in exports are attributed to export credit incentives. In domestic sales it takes a considerable time to collect bills. In the case of exports exporters can get payment immediately after shipment of goods by discounting bills at subsidized interest rates. Therefore, the abolition of export interest subsidization will help prevent excessive export competition.

Sharp increases in exports to particular markets of particular commodities do not give importing countries sufficient time to reduce or convert their competing industries and thus cause problems in the importing country. This is an irritating problem. Considering the possibility that Japan will face a sharp increase in imports from LDCs in a not so distant future, we should be concerned about this. Therefore Japan's export growth will have to be held to the level which conforms to the total of net increase in demand and decline

in supply due to a reasonable structural adjustment in the importing country. It might be said that orderly marketing is necessitated by consideration for the industrial conversion of competing producers in the importing country (and a third country which competes in exports. However in most cases these industries are mature and declining ones with comparative disadvantage which should shift to other promising industrial fields as early as possible. However, they often blame the inflow of Japanese goods as market disrupting and demand protection through import restrictions et ceteras.

In order to help such industries shift smoothly to other promising lines, measures to assist structural adjustment should be promoted as being internationally responsible.

#### IV. *INDUCED NONTARIFF BARRIERS*

There are cases where regulations, which have been introduced with other major policy objectives, have trade inhibiting effects, even though they are not directly designed to have such effects. These are called "induced nontariff barriers." Since they do not make trade regulations their prime objective, they are not nontariff barriers institutionally. However in case their real trade deterrent effect is considerable, we have to identify them as nontariff barriers. In such cases we call them indirect nontariff barriers. When no real trade deterrent effect is evidenced in them they are classified as illusionary nontariff barriers. We will briefly examine below cases of induced nontariff barriers which pose problems in regard to Japan. They are all minor cases and mostly mere inconveniences which might better be identified as illusionary nontariff barriers.

##### A) *Internal Excise Taxes*

Two cases, automobiles and whisky, pose problems. Commodity taxes and automobile taxes (which are local taxes) on passenger cars are levied at much higher rates on large-sized cars than on ordinary sized cars [for instance, 40% (or ¥90,000 per car) as against 15% (or ¥21,000 per car)]. This has an inhibiting effect on the import of large-sized cars. Similarly, in case of whisky, higher alcoholic taxes on high-quality whisky as compared with taxes on domestic products deter the import of foreign whisky. These taxes, however, are really progressive taxation on luxury goods than discriminatory measures against imported in favor of domestic goods. They were necessary in the past when the income level was low. It has become less necessary, however, to regard large-sized cars or high quality whisky as luxury goods. In fact excise taxes on large cars are expected to be lowered.

##### B) *Government Procurement*

Since the practices do not discriminate against purchases from abroad there is no problem legislatively. In administration, however, government contracts are hardly given on a competitive basis and governments invite only certain contractors to submit their bids, or give contracts to suppliers on a noncompetitive basis. This practice might result in the exclusion of foreign suppliers. However, as far as the practices do not involve procurement of goods worth large values, they should be regarded as mere inconveniences.

C) *Customs Valuation*

There is no problem since the valuation is based on c.i.f. prices. A report was made to the GATT that a raise in the customs valuation of Swiss-made watches might constitute a non-tariff barrier. However, this was an ordinary adjustment measure in conformity with the GATT rules. They were adjusted upwards to ordinary prices in order to assure equal opportunity between those who can import cheaper because of their special relations with suppliers abroad and others who have no such relations. It is also charged that the customs classification are too detailed. But they are unavoidable inconveniences seen in almost all countries. There exist no non-tariff barriers worth the name.

D) *Industrial Standards and Safety Regulations*

Complaints are heard about the fact that a long time is required for the test of electrical and fire-extinguishing machinery and potentially explosive equipment. There certainly remains room for improvement in the regulations. But since they don't discriminate against imported in favor of domestic products, they are inconveniences and cannot be regarded as non-tariff barriers. Differences in industrial and safety standards which still exist among countries are the cause of these complaints. Until an international uniform standard is established and at the present stage that we cannot say definitely which country's standards are best, nothing can be done but to negotiate and compromise as cases arise.

E) *Domestic Animal Infectious Disease Control Act and Plant Sanitation Act*

There were problems regarding the shortage of space at quarantine stations, an import ban to prevent foot-and-mouth disease and swine fever, and imports of Taiwanese shad-docks and Nicaraguan bananas. But all of them have been settled as a result of consultation or investigation. They do not constitute non-tariff barriers.

F) *Food Sanitation Act*

There are complaints that the regulations of food-additives and the obligations for indication of food content are too strict. The solution will be found in international standardization. This might belong to the category of illusionary non-tariff barriers.

G) *Measuring System*

Since the use of units of measurement other than the metric system is prohibited in Japan, the erasure of measurement indications on imported goods other than in the metric system is ordered. This is somewhat unreasonably restrictive. However this practice too belongs to the category of inconvenience and cannot be said to be a non-tariff barrier.

H) *Administrative Guidance*

An administrative guidance was once given regarding the installment of larger thermo electric generators that the first generator be imported but the second be domestically manufactured. The government has also been suggesting that domestic oil-refiners purchase from

the Arabian Oil Company (100% Japanese owned) a certain percentage of their crude oil imports. Criticisms are raised against both cases. However, it is doubtful whether the protectionism of this degree should be judged as nontariff barriers, since the businesses would have done things of this proportion had they not been given such guidance. If this measure be condemned as a nontariff barrier, the regulations stipulating the domestic content ratios of import substitution industries which many countries are applying might have to be taken up as a problem of more importance.

I) *Restrictions on the Activities of Branches of Foreign Enterprises*

Problems concerning the liberalization of foreign direct investment in Japan should be dealt with separately. It might be better not to mix them with the nontariff trade barrier problem.

J) *Antidumping Restrictions and Countervailing Duties*

We have so far dealt with problems of induced nontariff barriers which might have mostly an import-restricting effect. There are antidumping restrictions and countervailing duties as a method to prevent market disruption which might be caused by exports of foreign countries. It is because they have, if abused, an import deterrent effect that these measures are subject to criticisms as nontariff barriers. Japan applies an international dumping code (agreed upon on July 30, 1967 at a GATT meeting) and has never imposed antidumping or countervailing duties. Therefore there is no problem in this area. This is because Japan has so far not been in a position to be subjected to dumping. It is feared, however, that we cannot deny entirely the possibility that trouble might arise in future when the imports of manufactured and semi-manufactured goods from developing countries increase sharply.

K) *Others*

We cannot deny that complaints might be raised that Japanese customs are different, such as right hand drive in automobiles, and constitute trade barriers. In the extreme case the Japanese language is the most important of this kind. There is no need to say that these are mere inconveniences and not nontariff barriers. It has to be understood that the expenses incurred in overcoming these inconveniences are part of marketing costs which exporters to Japan naturally have to pay.

## V. *THE CHARACTERISTICS AND OUTLOOK FOR JAPAN'S NTB PROBLEMS*

Though they have already been mentioned, we will survey again the whole problem of nontariff barriers in Japan and pick out their characteristic problem points in the expectation that a guiding principle might be drawn about the direction and measures to be taken for the improvement of the nontariff barrier problem in Japan.

A) *A Water-tight Control System*

Major nontariff barriers in Japan are surprisingly limited. To put it strongly, we can

say that the residual import restrictions applied on 40 items (28 agricultural and forestry and 12 non-agricultural items as of the end of September 1971) are only nontariff barriers that are inconsistent with the GATT rules. Nevertheless, Japan is blamed as a notorious protectionist country. Where does the cause lie? There seems to be something foggy, producing an atmosphere which makes business transactions and government-to-government negotiations hard to conduct.

Though explicit nontariff barriers are confined to the residual import restrictions, a net of trade control and governmental interventions in trade is closely woven. Water-tight control has been enforced. Commodities are classified into residual import restrictions, state trading, exceptions and liberalized items. The regulations are administered classifying them into three categories of import quota (IQ), automatic import approval (AA) and automatic import quota (AIQ) which is the intermediate form of the above two systems. In the aspect of settling trade accounts, a system is devised so that every transaction is screened again into two categories: standard and non-standard methods of settlement. It is surprising that such a complicated and full-fledged control of trade and foreign exchange has been carried out smoothly with cooperation between government and private business. This is why the criticism expressed in the "Japan, Inc." argument has been raised. It also provides the reason why charges that administrative guidance, the differences in customs, and even the Japanese language deter international trade are made. Presumably, for foreign people or enterprises these things create thick walls impossible to break. However, it is not possible to call them nontariff barriers.

Another characteristic is the asymmetric governmental intervention in exports on one hand and imports on the other. There is a sharp contrast between the measures favoring, encouraging and promoting exports and those restricting imports. A number of incentive measures are applied to exports such as tax and credit incentives (short-term, low-interest rate loans and credits to deferred-payment exports) which are designed to make export business more profitable. On the import side, there had not only been no tax or credit incentives until recently, but instead schemes such as residual import restrictions and non-standard settlement systems and so forth which check and restrict imports. Though introduced publicly for balance-of-payments reasons, these measures explicitly expose a protectionist sentiment based on a mistaken concept of "national interest" that exports are gains and imports loss. Though such mistaken concepts are not confined to Japan but are common among countries, we cannot help but say that Japanese trade policy was more deeply based upon it, as compared with other countries. The unfavorable trade (or current) balance which continued from the end of World War II to around 1965 was the most important factor which restrained Japan's economic growth. Therefore, an improvement of the balance of international payments was an imperative and justified to some extent the export-drive and import restrictions. However, Japan became an Article XI status country of GATT in 1963 and Article VIII status country of IMF in 1964 and, objectively speaking, has lost the right to continue trade restrictions for balance of payments reason. Furthermore Japan may have been too slow and cautious in the subsequent liberalization of trade too. (This will be dealt with later.) However, since 1965 the favorable trend of trade balance has established itself and with this as a turning point, since 1969, the need to change the trade policy has at last come to be recognized with a resultant rapid liberalization of trade. From here the outlook is optimistic for a solution to Japan's nontariff barrier problems. However,

the announcement of a package of dollar saving measures (including the imposition of import surcharges and the suspension of dollar-gold convertibility) by the Nixon Administration on 15 August 1971 has created an uncertain atmosphere. It was thought that Japanese trade liberalization might have to be delayed to cope with the imposition of U.S. import surcharges and the Yen revaluation.

However, in order to bring about a substantial abolition of nontariff barriers and a furtherance of tariff reductions, it is necessary to change the mistaken concept of "national interest" that exports are gains and imports losses. The current concept of gains from trade is that the real gain is to import cheaply and in a great quantity while exports, which are not a gain *per se*, should be accommodated to the level where they can finance imports efficiently. Japan will have to shift its objectives toward the realization of this true gain from trade. Needless to say, such a conversion of philosophy is required not only of Japan but of all other countries. Dismantlement of nontariff barriers and tariff reduction will not be realized after all, unless all countries act voluntarily on the basis of such true concepts of gains from trade, irrespective of what the partner countries will do.

It is not only in regard to trade that the change of philosophy is requested. Too many resources have been poured into export activities. Furthermore the import restrictions have acted to protect less-efficient industries in the country. In this way the Japanese economy attained and maintained full employment and has continued to grow at a rapid pace. As compared with the possible state of the nation where the optimal allocation of resources would have been attained, the industrial efficiency and the welfare of people have been distorted. Abandoning the pursuit of mere high growth of aggregate national product irrespective of its quality and content, Japan ought to change its philosophy towards the attainment of economic growth by utilizing its resources more efficiently (Let us call this the "welfare economy" tentatively).

It will still take a long time before such a conversion can occur. Without such a conversion, however, the vague misunderstandings now entertained by foreign countries can not be eliminated.

### B) *Too Cautious and Elaborately Worked*

The fact that Japanese trade restrictions are administered under such a "water-tight" system as to double and triple controls, implies that a network of nontariff barriers has been elaborately established. In administration, these controls are applied very cautiously and extensively. The governmental guidance given about their administration involves an element which is often subject to misunderstanding by foreign countries. In reality, however, since the system *per se* has been constructed in such legal detail, the system is being administered uniformly, strictly, in fairness, and in conformity to the law. Trivial, insignificant guidance for administration, is of minor importance. Rather the whole legislative system for regulating trade, *per se*, does constitute administrative guidance. Here lies a problem, towards which criticism should be directed.

The cautiousness of the authorities concerned is best manifested in their way of reducing and eliminating trade restrictions. It is too cautious and elaborate.

a) A typical example of this cautiousness occurs when a commodity is liberalized. It is not shifted from the strict IQ to the lenient AA directly but to the intermediate AIQ system.

b) Always when a commodity is liberalized from import restrictions, a safeguard measure of one form or another is introduced. Here lies one reason for the existence of the AIQ system. When a certain commodity is liberalized, higher tariff, tariff quotas, emergency tariffs, or seasonal taxes are introduced in exchange. For future liberalization, an introduction of surcharges, deficiency payments system or differential tariffs are being considered as far as imports of agricultural products are concerned. The government tries to justify the introduction of these measures by arguing that the measures will help persuade domestic industries, give them a sense of safety and thus contribute to the promotion of trade liberalization. Though these measures might certainly be needed by the authorities concerned in order to evade political pressure, there might be no obstacles which would prevent them from proceeding directly to real liberalization. It is also feared that in order to liberalize imports other more restrictive trade barriers might be introduced. Anyway we must say that the authorities concerned are too cautious in their implementation of trade policy.

c) There are some measures which have already become unnecessary in practice, but are still retained as systems. For example, the import deposit system has ceased to have an effect with the ratio of deposit reduced to zero, but is retained institutionally for possible reactivation in emergency. Similar is the case with the export interest subsidization. This might be deemed as a typical example of the cautiousness of the authorities concerned. This is the case also with the AIQ system. The AA and import and export standard settlement methods have already become mere licensing systems and are unnecessary. However, the circumstance is that they cannot be abolished because the IQ, AIQ and non-standard settlement methods which are their counterparts are still maintained.

d) In the export field there are many instances that when excessive export incentive measures are abolished substitute measures are introduced under the pressure from domestic industries or in a compromise with them. This is another manifestation of the cautiousness of the authorities concerned on one hand and an aspect which admits doubt of possible *rapprochement* between the authorities and industries on the other. For instance, when the export income exemption system was abolished, similar export incentive measures such as reserve fund for development of overseas markets and export depreciation allowance were initiated in exchange. The steel industrialists are petitioning the authorities for introduction of such measures as depreciation allowance for constitutional improvement investments of enterprises, import (not export) market development reserve and, imported steel material price stabilization reserve and expanded tax incentives for antipollution investments in exchange for a possible abolition of the existing tax incentives for exporting activities in the future.

Other examples are the provision of a large sum of compensation to the textile industry in exchange with their enforcement of voluntary export restraints or the subsidization of small- and medium-sized industries in order to balance against the grant of general tariff preference to developing countries.

Another example is the interest subsidization for shipbuilding of domestically used vessels which is aimed at balancing against credit incentives granted for exports of vessels on a deferred payment basis.

If the protection by tariffs, though not nontariff barriers, is also taken into account, there are a considerable number of industries, which have already grown enough to dispense with protection and yet are still being protected. An example is the automobile industry.

Thus, as a result of the cautiousness of the authorities, and the connection between industries and the government, direct and selective restrictions remain in force. The authorities believe that direct restrictions of the nontariff barrier type have a more accurate and prompt effect than indirect adjustment of exports and imports by means of overall adjustment and tariffs. They feel uneasy unless these measures are retained at least residually. On the part of industries they welcome direct and selective restrictions or incentive measures which provide them with a chance to get discriminatory favoring treatment. We recognize that tariffs or nontariff barriers are irrational things, being the product of compromise made with the pressure from individual vested interest groups. However it should not be allowed that one restriction brings about another and that the abolition of one restriction gives rise to the introduction of another. Here again a change of philosophy is needed. This change of philosophy should follow: a) that export promotion and import restriction (when required) may be better conducted by overall adjustment of foreign exchange rates or fiscal and monetary policy instead of direct and selective control or incentive measures; and b) when nontariff barriers are lowered or abolished no other direct and selective control measures should be introduced in order to cushion its impact. Rather resort should be made of tariff measures (including such measures as tariff quotas and import surcharges which are along the line of price mechanism) and they are sufficient.

### C) *Excessive Competition*

As one of reasons to justify almost all trade restrictions the "prevention of excessive competition" or the "maintenance of orderly trade" is cited. This "excessive competition" reason is quite peculiar to Japan and probably no example will be found in other countries. (One more, the luxury restriction reason which is the motive for excise taxes on automobiles and whisky might be Japanese, but they are also common in low-income countries.)

a) Voluntary export restraints are its representative case. There is a tendency that these voluntary restraints have been accepted by Japan in order to prevent excessive competition and to ensure orderly marketing taking into consideration the possibility that price cutting competition among Japanese exporters or flooding of Japanese goods into foreign markets might induce restriction on imports from Japan. Besides, there are a considerable number of cases that export controls are applied solely from the Japanese standpoint of preventing excessive competition under the name of voluntary export restraints notwithstanding that there is no pressure from importing countries. It is noted in this connection that Western countries cite Japan's excessive export competition as one of the reasons for applying discriminatory treatment against Japan.

The imposition of export standard and non-standard settlement methods is also partly attributed to the excessive competition reason. The overseas market development reserve system is originally aimed at providing favorable treatment to those who pioneered the development of new overseas markets and protecting them from excessive competition by late-comers—though in reality all exporters are given favorable treatment in proportion to their export performance.

b) It may be rather strange that the excessive competition reason comes to the fore not only regarding exports but also imports. The excessive competition reason is cited for a defence for all measures including import deposit, IQ, and AIQ systems; the unpublication



of quantity limit of imports under the IQ systems; and the import standard and non-standard settlement schemes.

There is a side that it is unclear: trade restrictions have to be introduced because trade will fall into excessive competition if left as it is, as insisted by the authorities concerned; and, since restrictions are introduced, this is proof of excessive competition. This is a vicious cycle. On the export side various kinds of benefits are given in support of export industries, for instance, tax incentives, subsidized interest rates (short-term loans and deferred payment credits) and the like. These measures make exports more profitable than sales to domestic markets and induce excessive competition in export activities. As import quota system exists there may arise excessive competition among importers who try to obtain import quotas and thereby earn premiums. Such being the case trade restrictions motivated by the prevention of excessive competition might better be abolished.

Furthermore, since trade restrictions tend to function in favor of large business at the sacrifice of medium- and small-sized enterprises, there is the presumption that big businesses have exercised pressure on the authorities into the introduction of restrictive measures on the pretext of preventing excessive competition. If such is the case, then the matter should be left with the anti-monopoly policy with no resort to trade restrictions.

However, it cannot also be denied that there is a constitutional element in Japanese enterprises that is apt to give rise to excessive competition. For instance, there are too many small enterprises. With a low ratio of owned to total capital, they rely on borrowings from outside sources and consequently have no financial cushion in case of a downturn in sales. Small margins and large turnover is their motto. They are good at making a profit by forestalling their competitors. They lack character and initiative and blindly follow other enterprises who have succeeded. Changes are needed in the philosophy of business behavior. Without such changes, it will be impossible to prevent excessive competition whatever attempts are made on the aspects of exports and imports. In this connection it might be a problem worth of examination as to whether the activities of trading firms which are unique in Japan constitute one of the causes for excessive competition in trade.

Measures as stated below will present themselves in order to cope with the problem of excessive competition. a) Direct and selective restrictions and incentive measures in the field of both exports and imports intensify excessive competition and therefore should be abolished as far as possible. Too rapid growth of exports on one hand, and, on the other, shopping around and the resultant boosting up of prices by importers should be regulated indirectly by overall adjustment measures; b) In order to prevent excessive competition and thereby to maintain orderly marketing it is better to establish floor prices for exports and ceiling prices for imports only when they are needed and to watch for their observance rather than restricting exports and imports quantitatively.

#### D) *Propensity to Bargain*

Japan's trade liberalization made its first rapid progress from 1960 to 1963. This might be regarded as a spurt in order to move into GATT Article XI and IMF VIII status country. Liberalization made another spurt from 1969 to 1971. This was prompted with a view to first bringing the liberalization of trade and capital to completion rather than revaluating the Yen, since large surpluses of international payments have been accumulated. However,

from 1964 to 1969, the pace of liberalization has been extremely slow and delayed. During this period residual import restrictions were maintained for so long with few positive motives, placing some industries under a state of over-protection.

Anyway, it must be said that Japan's trade liberalization has been too slow. There might certainly be circumstances that the above mentioned intermediate period fell on the time of Kennedy Round tariff cut negotiations and that Japanese government was too busily occupied in those negotiations to give attention to trade liberalization. Another reason for such slow tempo of Japan's liberalization might be found in the cautiousness of the authorities mentioned earlier.

As other causes for delayed liberalization of trade the following can be cited:

a) No voluntary and positive action is taken unless pressure is exerted from foreign countries. Once a certain target has been established under foreign pressure, great progress is made. Foreign pressure, or one target or another help arouse public opinion and thus persuade vested interest groups to accept trade liberalization. The authorities concerned hardly dare to proceed with liberalization unless such opportunity is given.

b) There is an opinion that Japan's non-liberalization or restrictions of trade is not particularly disgraceful if their degree is not stricter than those in other countries. Therefore, Japan lacks incentives to proceed with liberalization irrespective of what other countries may do, or to take the lead in a global liberalization of trade.

For instance, in July 1969 an estimation was made that damages Japan suffers from nontariff barriers imposed by the United States is bigger than those the United States suffer from nontariff barriers which Japan imposes. Or again, there is a view that since the number of items under residual import restrictions were reduced to 40 at the end of September 1971, the same as that in Germany, there is no longer need for further liberalization. Furthermore an argument is made that all advanced countries are protecting their agricultural industries and that Japan's agricultural protection through residual import restrictions alone might have a trade inhibiting effect less than those due to a waiver by the United States or the variable surcharges imposed by the EEC. In other words they try to justify Japan's non-liberalization of trade not by the basis of economic rationality but by comparison with other countries.

c) There are a considerable number of items on which it has become already unnecessary to retain residual import restrictions and other nontariff barriers. Notwithstanding, there is a tendency that the authorities have maintained them to bargain for the removal of other countries' restrictions against Japan. This is a result of the fact that multilateral or bilateral negotiations at the GATT are centered around balancing concessions offered by one country to its negotiating partner by equitable concession from that partner. It may be a bad influence of the foreign economic policy of the United States which insists on reciprocity. Since August 1971, Japanese import liberalization is to be bargained for American removal of import surcharges. In short, the philosophy is that Japan is prepared to participate in an international trade liberalization but does not dare to lose alone. This is that trade liberalization is taken as loss on the basis of the mistaken philosophy that exports are gains and imports losses.

In short, the above three attitudes might be called together "propensity to bargain." In reality, unless this view is abandoned, the reductions or removal of nontariff barriers will not make progress. This is because nontariff barriers cannot be subject to bargaining negotiations since their effects cannot be measured and, therefore, they cannot be com-

pared each other.

Unless the mistaken philosophy that exports are gains and imports losses is abandoned and a shift is made to a philosophy that the removal of nontariff barriers works for national interest in order to optimize resources allocation, to eliminate deviation between private and social costs and to maximize social gross product, there will be no solution to the nontariff barrier problem. Japan which has ample surplus of international payments should set such an example.

#### E) *Outlook for the Removal of Nontariff Barriers*

Japan can reform all its trade restrictive measures if it has the intention to do so. Therefore, there exist no such difficulties as the government cannot negotiate trade liberalization with other countries because state governments or other agencies have the power to do so. Availing the opportunity that the favorable trend of its trade (or current) balance had established itself, Japan proceeded with a substantial removal of nontariff barriers by September 1971 in order to meet the demand for the stabilization of domestic commodity prices, to evade pressure for revaluation of Yen or, then, to avoid a large scale revaluation of national currency. The necessity of changing the trade philosophy has at last come to be keenly felt and there is a tendency towards gradual reform. However, the recent introduction of import surcharges by the United States and the revaluation of Yen are feared to cause a delay in Japan's trade liberalization for some time.

a) The number of items under the residual import restrictions had been reduced to 40 (28 agricultural, 3 minerals and 9 industrial items) by the end of September 1971. Some ten additional items (6 or 7 agricultural and 3 non-agricultural items) are expected to be liberalized from import restrictions by the end of March 1972. However, there is no knowing what will happen next. This is because the remaining restrictions are all "hard core items" which are very difficult to liberalize. However, once the philosophy has been changed, the majority of these items can be shifted to the tariff system including tariff quotas, surcharges, and the like.

b) Among state trading goods, agricultural products except rice might well be shifted to tariff systems as soon as possible. The same can be said of some of the exempted items. However, the government would not dare to touch these items on the pretext that state trading and exemptions are legal in the GATT rules.

c) The IQ system will be retained though the number of items under the system will be substantially reduced. The AIQ will be abolished in a not distant future (probably by the end of March 1972) with all the items shifted to the AA. The AA system might also better be abolished. However, this may depend on a sharp reduction of IQ items and their easier identification.

d) The import deposit system might better be dismantled because it has already been made ineffective with the deposit ratio reduced to zero. However, the government will probably retain it on the ground that the system inflicts no harm.

e) The systems of standard and non-standard settlement will be retained for both exports and imports, though minor modification in the form of extending the time limit from the present four months to six months will be made for import standard settlement. It may be said for justification that foreign exchange control cannot be relaxed with a view

to controlling short-term capital movement.

f) Export tax incentives will be abolished sooner or later though there will still be some complications.

g) It might be better to abolish the system of export interest subsidization, even though it has no effect since the subsidization ratio has been reduced to zero.

h) There is a tendency that measures might be newly introduced or strengthened to favor import credits. However, the action might better be avoided.

i) The majority of voluntary export restraints Japan has introduced for the "excessive competition" reason in spite of no pressure exerted by foreign countries might better be dismantled. However, there is a fear that they might rather be intensified on the ground that orderly marketing needs to be strengthened. Those voluntary export restraints which have been introduced in the face of accusations by foreign countries might better be shifted to export floor price systems. In fact, moves toward this direction are evidenced.

The outlook for other minor nontariff barriers has already been dealt with in the preceding section and will not be repeated.

In conclusion:

- 1) Japan might be able to abolish as many import quota schemes as possible and shift to a simplified system which will have only tariffs as trade barriers. But how should progress be made towards that direction?
- 2) It is more advisable to abolish such tricky measures as tax incentives or interest subsidization and leave all the adjustment of exports and imports to overall adjustment measures. But, how should conditions be changed to allow Japan to shift toward that direction? There arises in this regard an aspect which cannot be solved by internal measures alone and requires international action.

## VI. GLOBAL PROGRESS

What sort of a way can be found to cause a global advance toward the reduction and removal of nontariff barriers?

1) As regards Japan, our examination has mostly been made not from the viewpoint of whether the reduction or removal of nontariff barriers is negotiable with foreign countries, but from the standpoint of whether the action is desirable from economic rationality and, therefore, whether it should be proceeded even with unilaterally. This is the correct viewpoint.

It might be said that it is wrong to examine the matter from such viewpoint as it is negotiable because they are within the authority of the central government and not negotiable because they are outside its authority.<sup>10</sup> This is equal to abandoning the attack on the nontariff barrier problem from the outset. Similarly, the viewpoint that, judging from their legal status *vis à vis* GATT or other international or bilateral agreements, they need not be discussed if they are legal and only discussed if illegal is incorrect. It only reduces the nontariff barrier problem and does not serve for the purpose of expanding world trade. Rather the amendment and removal of irrational points in the GATT or other international

<sup>10</sup> Gerard and Victoria Curzon, *Hidden Barriers to International Trade* (bibliography 2), p. 10.

agreements themselves should be sought.

Furthermore, no fruitful results can ever be expected from the way which is designed to bring about the reduction or abolition of nontariff barriers through bargaining in accordance with the principle of reciprocity to seek equitable concessions from trade partners. Nontariff barriers can hardly become a subject of bargaining since they are not measurable in their effect, not comparable each other and differ from each other by country in the motivation and interest. Their reduction or dismantlement could not be carried out by any means other than such across-the-board formula in disregard of equitability of their effects or reciprocity as attempted originally by the Kennedy Round negotiations.

In short, the dismantlement of nontariff barriers is impossible unless various countries advance toward the direction of their voluntary abolition for national interest in order to rectify the distorted resources allocation and to assure the maximization of gross social product. Such changes in philosophy are fundamental and earnestly desired for the solution of this problem.

2) All countries should abolish nontariff barriers which are direct and selective restrictions on trade as soon as possible and shift to the tariff system (including tariff quota schemes which are in line with price mechanism similar to it, or fixed import surcharges). If it is possible to measure the tax equivalent effect of nontariff barriers, there is no reason why a shift to tariff systems is impossible. If it is not possible to measure such effect, it might be well to permit countries to levy or raise tariffs in the extent that they can feel safe or secure by doing so. It might be unavoidable even if this might raise temporarily the tariff barriers to some extent. However, after some time has elapsed it will be proven and recognized through the experience that tariffs of high rates are unnecessary. Then it might be well to set about a Kennedy Round type tariff cutting negotiation, taking an appropriate occasion. This method, as suggested by some experts, is worth thorough consideration.<sup>11</sup>

3) The ideal is that trade barriers should be confined to tariffs and that the adjustment of international balance of payments left with overall adjustment measures. However, the reality is that the overall adjustment measures *per se* do not work promptly and effectively with a tendency that some countries have unfavorable balance while others favorable balance for a prolonged period. Hence the difficulties in removing nontariff barriers and fears that they might instead be increased. Therefore, more urgently needed than anything else is the streamlining of the international monetary system and foreign exchange rates in which overall adjustment measures can function promptly and effectively. If they say that it can be managed by a minor modification of the existing adjustable peg system, the rules for their administration will have to be clarified, for instance, regarding the criteria for determining fundamental disequilibrium, and the obligations of the United States, which is the central reserve country. Though it is not necessarily clear what sort of cooperative relation does exist between the GATT and the IMF, how can the trade liberalization be negotiated at GATT as the center and be promoted by means of tariff cuts or reduction and removal of nontariff barriers without regard to the international monetary situation? It should be remembered that if the latter is in a state of confusion the liberalization of trade can only regress.

4) The establishment of only the rules of free trade that will assure a static optimal

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<sup>11</sup> Curzon, *ibid.*, p. 63.

Harold B. Malmgren, (bibliography 7), p. 66, 70.

resources allocation is not enough. Comparative costs of various countries change as time goes on. Measures have to be provided which would realize and promote a dynamic and long-term optimal resources allocation. The protection of infant industries is justified from such dynamic viewpoint. Such being the case, instead of protecting and maintaining mature and declining industries, assistance for structural adjustment aimed at stimulating and assisting the shift of resources to industries which have comparative advantage ought to be approved internationally.

In order to have each country promote this task as a kind of international obligation, they should be required to establish a fund for structural adjustment assistance to use a fixed percentage (say 0.5%) of its gross national product for this purpose. If this structural adjustment is realized smoothly and in a substantially large-scale, most of the need for each country to restrict imports or raise tariffs will disappear and thereby the necessity for voluntary export controls will cease to exist. Furthermore, such structural adjustment is absolutely necessary to open markets for manufactured and semi-manufactured imports from developing countries.<sup>12</sup>

5) The establishment of an international code or uniform criteria is desirable. If such code or criteria is produced, many nontariff barrier problems will be solved. The international code for antidumping is one good example. If a uniform criterion is given for determining market disruption, troubles concerning import restrictions or voluntary export restraints will be reduced. An international criterion concerning the conditions of deferred payment exports is also desired. The untying of aid to less-developed countries is important. All troubles concerning industrial and safety standards, disease control, food sanitary regulations, measuring systems and customs valuation will mostly disappear if international uniform criteria are established. Furthermore, the necessity of an international code on direct foreign investment or the international enterprises has come to be recognized.

Though the desirability of the establishment of an international code or uniform criteria concerning these matters is clear, the very work of preparing them involves considerable difficulties. Such being the case, pending such code or criteria are produced and considering the fact that it is not clear which country's criteria are now the best, each country should of course refrain from abusing its criteria in such a way as to deter international trade, and trouble, if any, should be solved through negotiations.

6) Such an attempt to reduce by half the present levels of tariffs in the advanced countries does not present an attractive target when the time and labor required are compared with an expected result to be brought about. Rather, a more realistic solution is a Multilateral Free Trade Arrangement that the majority of advanced countries abolish all their tariffs at one stroke. And, at this occasion of the formation of MUFTA, all nontariff barriers should also be removed across the board. As exemplified by the experiences in the EC and EFTA, it is possible. There only remains a choice as to whether we proceed to an outright formation of a gigantic MUFTA involving almost all advanced countries in the world, or, in case this is difficult, by a roundabout way to first form some number of small groups comprising several countries which have closer interests with each other and then at some opportune time form a free trade arrangement between these groups. It might be worth while to examine which method is more realistic.

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<sup>12</sup> Kiyoshi Kojima, *Japan and a Pacific Free Trade Area*, Macmillan, London, 1971, p. 12-6.

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