

# US-Japan Automobile Trade Negotiation in 1995 — the Analysis on why Japan became assertive toward US negotiators

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## 1. Introduction

The US-Japan relationship has long been the most important diplomatic relationship for the Japanese government.<sup>1</sup> Of course, security and defense issues are important in this relationship, especially when the fight against terrorism continues. However, an economic relationship has also been playing a major role because the United States is still the largest trading partner for Japan. United States and Japan share a long history of trade negotiations since 150 years ago when the first US-Japan trade treaty was signed.

In this paper, I will discuss the US-Japan negotiation over an economic issue. I take up especially the 1995's negotiation between the USTR (United States Trade Representative) and the MITI (Ministry of International Trade and Industry of Japan)<sup>2</sup> over automobile trade

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1 Unfortunately, the converse may not hold true.

2 Even though MITI is now called Ministry of Economy, Trade and Industry, I will maintain the usage of MITI in this paper because the agency was then called MITI when the negotiation took place.

issues. I will first describe the historical background of this negotiation. Then, I will look at the process of the automobile negotiation along which I will contrast this negotiation with past negotiations because in this 1995 auto case, it has been said that Japan side took stronger stance than before. I will analyze the reasons behind this change of Japanese negotiators by looking at changes in their BATNA (Best Alternative To a Negotiated Agreement),<sup>3</sup> their organizational structure, and other issues. I will also analyze the reasons why US failed to reach a favorable agreement with Japan this time. Finally, I will explain what makes this kind of economic negotiations difficult.

In 1995 auto negotiation, although both sides finally came to a conclusion, the outcome of the trade negotiation is considered as a failure.<sup>4</sup> It was not an agreement at all. As the Japanese press put it, the outcome was seen as “the color of Tamamushi (the name of insects whose color is very complex and cannot easily be determined)” - so ambiguous that it can be interpreted in many (different) ways.<sup>5</sup> Probably in order to save negotiators’ faces and to alleviate the constituents’ dissatisfaction, US domestic news on the consequence of the negotiation and that of Japan did not coincide at all.<sup>6</sup> While US side reported they agreed with Japan on numerical target, Japan side claimed that it never reached such an unreasonable agreement. Their conclusion was not an agreement, but was just a document which could

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3 BATNA is introduced in p. 100 of the book “Getting to YES” by Fisher and Ury (1991).

4 Bhagwati with Sakamoto. “Taidan (Talks) - about Japan-US auto negotiation.” Tsusuan (International Trade and Industry) Journal, December, 1995, p. 10.

5 Kitaoka, Shin-ichi. “Nichibei-kankeishi no Shiten-kara (From the view point of the history of US-Japan relations).” Tsusuan Journal, December, 1995, pp. 14-15.

6 By reading the newspapers in two countries, I was convinced on this. The newspapers referred are Nihon-Keizai Shimbun, New York Times, and Financial Times in June 1995.

be interpreted in two different ways. But if we look at the final draft, it is obvious that US side gave in.<sup>7</sup> American economist, Professor Bhagwati of Columbia University, asserted that the final document of agreement is rather disadvantageous to the United States while most of the American public believed that the negotiation was successful because most of the public blindly believed what Kantor said.<sup>8</sup> Why did US negotiators fail this negotiation?

My analysis claims the reasons of failure as follows. There are four reasons why US side failed to reach a mutual consistent agreement: 1) US stuck with the positional negotiation, 2) US failed to recognize the change in Japan's increased negotiating power, which came from the shift in Japan's BATNA, 3) US failed to recognize the change in the internal organizational structural change in Japan, and 4) US negotiators always viewed Japanese negotiators in stereotyped image.

I will not claim that Japan "succeeded" in this negotiation. It was not a "success." It was just that Japanese negotiators did not give in their interests for the sake of maintenance of the US-Japan relationship. I claim that the negotiation was a failure mostly because of US side's misguided strategy. Negotiation is not a zero-sum game. There aren't always winners and losers. Ideally, if a negotiation succeeded, both sides win. Successful negotiation is more difficult than failure. Why? Because it takes two, both sides, to make it successful, but it takes only one to make it a failure. In this case, the United States Trade Representative was the "one."

Here is an excellent episode which shows the validity of my argument. It took place in Geneva right after the said "agreement" on June 28, 1995.

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7 The point was made by Kitaoka (1995), *ibid.* p. 14.

8 Bhagwati with Sakamoto (1995), *ibid.* p. 10.

Mr. Sakamoto, Tsu-san Shingikan (MITI negotiating chair, Vice Minister for International Affairs), responded the question from the Japanese press: “We [USTR and MITI] agreed that we won’t agree.” A question followed from the press, “Did Japan side win in the negotiation?” Mr. Sakamoto posed a little to think about the question and then gave an answer: “To say the least, we did not lose.” which made press people laugh.<sup>9</sup>

Mr. Sakamoto’s response includes the points I made earlier. The negotiation was de facto failure because it was not “an agreement.” It is not that Japan won, but that MITI did not give in.

Before getting into the detailed analysis on the reasons of failure in 1995 US-Japan automobile negotiation, it is worthwhile to look at the background information, especially a historical one.

## 2. Background and History

The automobile negotiation is one of the major topics in long-lasting US-Japan trade negotiations. These trade negotiations include textiles, steel, TV sets, VCRs, machinery, semiconductors, and automobiles and auto parts.<sup>10</sup> US-Japan trade negotiation has been going for more than thirty years.<sup>11</sup> Among these, automobile trade has been always a primary issue because of the strength of US labor union (UAW) and the size of its trade.

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9 Ishii, Hayato (Kyodo: Press member), “Goui Happyou mo Koushouno Ichibubun-Mouretsuo datta America Gawa no Houdou Senryaku (Announce of agreement as a part of the negotiation — Very Strong American Press Strategy).” *Tsuusan Journal*, February, 1996, pp. 22-23.

10 MITI, *Tsusho-hakusho* (White Paper on International Trade). 1989.

11 Itoh, Motoshige, *Zemina-ru Kokusai Keizai Nyuumon* (Seminar: Introduction to International Economics). Tokyo: Nihonkeizai Shimbun Sha, 1989. p. 247.

## **2-A. The history of automobile negotiation**

Automobile issue became one of the main trade issues in early 1980s, and it continues to be a primary issue for more than 15 years.<sup>12</sup> At first, Japan gave in easily to the strong US position by restricting the number of Japanese cars imported to US. (This is called a VER, or voluntary export restraint.) Then, Japanese automakers shifted their strategy from direct export to the combination of export and transplant production, and supplied US market with the combination of low-price transplant products and high-priced luxury imported-products using the brand names such as Lexus (Toyota), Infiniti (Nissan), and Acura (Honda). Because of increased transplant production, the auto parts trade increased from Japan. Also, despite of quantitative restriction on the automobile trade itself, monetary value of US Automobile import from Japan did not decline because of YEN appreciation and of quality upgrading of the Japanese car import. (Unit price of imported car went up.)

### **Automobile trade issues in 1980s**

In 1981, facing the strong opposition from US auto industry to Japanese car import, Japanese government adopted a compromising strategy. It introduced VER (Voluntary Export Restraint) in response to US government's request. This VER is a trade policy in which an exporting country (in this case, Japan) "voluntarily" limit the number of goods exported to the importing country (United States) according to the request of the importing partner.

At the same time, Japanese automakers began opening transplant facilities in the United States, and continued to take increased shares of the US auto market from the US Big Three auto manufacturers. During

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12 Nihonkeizai Shimbun Sha. (eds.) Document: Nichibei Jidousha Kyougi (Japan-US automobile negotiation). Tokyo: Nihonkeizai Shimbun Sha, 1995. p. 18.

the 1980s, while the Japanese Government maintained voluntary export quotas of 1.6 million units and later 2.3 million units per year,<sup>13</sup> Japanese automakers increased total unit sales in the US by opening seven plants there. In the same period, US domestic producers had to close the same number of plants.<sup>14</sup> Through the 1980s, Japanese automakers accelerated their shift from a strategy of direct exports to the US toward a transplant and exporting luxurious-car strategy.<sup>15</sup> Reasons for this shift included the post-Plaza appreciation of the Japanese yen after 1985; the success of Honda and Toyota in managing transplant production in the US during the 1980s; American dealer requests for Japanese commitments to the US market;<sup>16</sup> and the proliferation of US trade restrictions such as local content requirements.<sup>17</sup> Japanese autos manufactured in these transplant facilities deprived the US Big Three automakers of much of their market share in the 1980s. At one point in the early 1990s, Honda even surpassed Chrysler and briefly became the number three seller in the US market.<sup>18</sup>

### **Automobile trade issues in 1990s**

Despite the Japanese “voluntary” export restraints, the US was

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13 See Tomiura (1995) p. 206. According to Mr. Ichiro Sakata, a MITI official, this voluntary restraint was not very limiting because the 2.3 million units allowed in 1985 were so big that the number accounted for almost 20% of the US automobile market. (Author's personal interview on July 20, 1995.)

14 Tabb (1995) pp. 115-117. The seven plants are Honda's Marysville plant in Ohio, Nissan's plant in Tennessee, Toyota's plant in Kentucky, Mitsubishi's plant with Chrysler in Illinois, and Fuji Heavy Industry and Isuzu's plant in Indiana; this data from Japan Automobile Manufacturers Association is cited in Gyoten (1994) p. 104.

15 See p. 70 of Hart (1992).

16 Hart (1992) p. 251; also, personal interview with Sakata on July 20, 1995.

17 Thomas R. Howell and Alan William Wolff, “Japan” in Howell and Wolff (1992), p. 121.

18 All the data here can be found in Japan Automobile Association, Jidosha Handbook (Tokyo: JAMA Press, 1994).

unable to reduce its trade deficit with Japan in the 1990s.<sup>19</sup> To make the matters worse, there remained a huge amount of automobile and auto parts trade deficit. Parts trade increased because of the transplant strategy of Japanese firms. Also, monetary value of automobile trade remained high both because of YEN appreciation and because of unit value increase from the product upgrading of Japanese cars. For example, of the \$59 billion bilateral trade imbalance between the US and Japan in 1993, the imbalance from car and car-parts accounted for 60%, for a total of \$36.5 billion.<sup>20</sup> So, the United States began to urge Japan to take stronger actions to eliminate this trade imbalance.<sup>21</sup>

In January 1992, US President Bush (Senior) visited Tokyo to pursue the goal of reducing trade deficit with Japan by promoting the sales of US cars in Japan.<sup>22</sup> President Bush invited executives of the US Big Three automakers to accompany him on the trip. These executives did accompany the US President, but then they made their own agreement with Japanese manufacturers independently of the US Government. Their Japanese counterparts “agreed to a goal of increasing purchases of American auto parts by \$10 billion between 1990 to 1995.”<sup>23</sup> Thus, indirectly, US negotiators were successful in gaining an indication from Japanese automakers that numerical targets would

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19 From here, I am simply summarizing the opinions expressed in the press. I do disagree the validity of these statements as an academic economist. In principal, trade deficit with one trading partner means nothing. US trade deficit (against all the trading partners) remains high because of low savings rate among US households.

20 Nigel Holloway, “Cars Hold the Key,” *Far Eastern Economic Review*, Oct. 13, 1994, p. 20.

21 As an academic economist, I feel that this statement is not “economically correct.” Trade deficit between two countries does not matter at all whereas global trade deficit may matter in the long run.

22 This statement is also incorrect in terms of economics. This is a summary of the press opinion, not mine.

23 Dryden (1995), p. 375.

work. In the recent book about USTR, Dryden put it: “The Bush administration had added more grounds for future trade negotiators to argue for results, rather than just promises, from the Japanese.”<sup>24</sup> US political pressure also led Japan to tighten its voluntary export restraints on automobiles, reducing the ceiling down to 1.65 million units in 1992,<sup>25</sup> causing some Japanese car dealers in the US to go out of business.

On the Japanese side in the 1992 negotiations, at first MITI officially refused to agree with US negotiators’ demands for numerical targets in the name of opposition to managed trade. Tokyo’s negotiators were under great domestic pressure not to agree to “managed trade” on car parts,<sup>26</sup> and refused to set import quotas or even targets for specific sectors.<sup>27</sup> On the other hand, some Japanese politicians thought that Japan should repay the US for moral debts owed after World War II, and insisted that Japan should somehow accommodate the US. It was the then Prime Minister Kiichi Miyazawa who thought that Japan should not worsen the relationship with the United States. Miyazawa even called the CEO of Toyota individually and tried to convince Mr. Toyota.<sup>28</sup> This pressure sometimes caused MITI to adopt points of view different from those of Japanese automakers. For example, at the time of President Bush’s 1992 trip to Japan, MITI began to press Japanese automakers to raise prices, to lengthen model cycles,

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24 Dryden (1995), p. 376.

25 Larry Armstrong and Karen Lowry Miller, “Japan’s Sudden Deceleration: Is Detroit Winning Back Share - or Is Tokyo Giving It Up?” Business Week, June 8, 1992, p. 26.

26 Tokyo negotiators tried to avoid the same mistake they made in an earlier failed negotiation about semi-conductor trade, which gave an impression to the US negotiators that Japan had confirmed numerical targets.

27 Awanohara (1993), p. 96.

28 Nihonkeizai Shimbun Sha (1995), p. 19.



and to decrease their working hours in order not to increase market shares in the US car market.<sup>29</sup> At first, Toyota refused to bow to MITI's pressure; but, finally, it followed other Japanese carmakers that wanted to avoid losses from US activation of its "Super 301" trade-protection law. In the end, Japanese automakers sought ways to compromise with the US Big Three auto manufacturers by making promises to purchase US car parts and cars. Therefore, during Bush's trip, the five top Japanese car makers - Toyota, Nissan, Honda, Mitsubishi, and Mazda - announced purchase plans for US auto parts and US automobiles from US manufacturers.<sup>30</sup> It was successful in a sense that both US and Japan sides could avoid the trade war. But it was not successful in a sense that this way of solving trade issues — MITI intervened the private business and cooperated "managed trade" — left a scar in the history of US-Japan trade negotiations.<sup>31</sup> What kind of a scar? The next phrase by a US negotiator Jeffrey Garden, Vice Minister of Department of Commerce, ITA (International Trade Agency) represents the point: "Why MITI says 'No' now [in 1995 negotiation] after having done a lot of managed trade until today? Without a 'voluntary plan' (= numerical target), we cannot agree."<sup>32</sup>

## 2-B. A Prelude to 1995 negotiation

In 1993, the new Clinton Administration in the US also picked auto and auto-parts trade as the main topic for trade negotiations (so-called framework talks, or *kazo-kyogi*) with Japan. The Clinton Administration took a tougher stance than had its predecessor (the Bush Administration). President Clinton may have decided to use auto trade

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29 Personal interview with MITI official Ichiro Sakata on July 20, 1995.

30 Awanohara (1993, p. 96) and Do Rosario (1993, p. 80).

31 Nihonkeizai Shimbun Sha (1995, p. 19).

32 Cited in Nihonkeizai Shimbun Sha (1995, p. 20).

issues to help him for the 1996 Presidential election.<sup>33</sup> (And it seemed to work, right?) He claimed that “unfair” Japanese trade practices were a threat to American economic welfare, and demanded that Japan accept an import program with numerical targets for purchases.<sup>34</sup> The goal of US trade negotiators seemed to have shifted from restricting exports to forcing Japan’s market to open. Even though Japan has no tariffs or quotas on cars and car parts, the Clinton Administration argued that Japan’s market was “in fact closed” by its automakers’ system of exclusive dealerships.<sup>35</sup> Japanese critics responded that the US Big Three carmakers already had twice as many outlets in Japan as did all European carmakers combined, but sold fewer cars because of lack of right-hand drive models and the larger size of US cars.<sup>36</sup> (Since I was driving a car in the US when I was a graduate student in the US, I can compare the width of the roads between US and Japan. We have narrower roads in Tokyo than the ones in the US cities. Tokyo roads are narrower than even the ones in Boston, where the roads are relatively narrower in the US. In Boston, compared with California, aren’t there many Volks Wagen “compact” cars? I do not want to drive a 1994 model of Ford Taurus on the road in Tokyo because it is too large although I would drive a 1997 model of Taurus because it is compact.) When these 1993-1994 negotiations between the US and

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33 Dornbusch (1995, p. 20).

34 “Ignorant Armies.” *National Review*, June 26, 1995, p. 20.

35 Howell and Wolff (1992, p. 122).

36 Various sources talks about these issues; for example, see various MITI (currently METI) pamphlets: “Is Japanese Car Market Closed?” June 1995; “Fact Sheets Regarding US-Japan Auto and Auto parts Issue” June 1995, and the “Dear Mickey” advertisement in the magazine *THE ECONOMIST*, June 24, 1995, p. 63. The similar statements were made also in the TV interview of Trade Minister Hashimoto (then) on “Chikushi Tetsuya’s News 23,” broadcasted on TBS Television on June 28, 1995 in Tokyo.

Japan failed to achieve any conclusions, US President Clinton decided to enter the US-Japan auto negotiation of 1995.

### **3. The process of the auto negotiation**

The main negotiation between USTR and MITI took place at United Nations building in Geneva from June 21 to June 28, 1995. I will explain below the process of the 1995 negotiation by paying attention to three stages of negotiation: prenegotiation phase, the negotiation table, and post negotiation. There were three agenda in this negotiation: deregulation of auto parts market, liberalization of Japan's *keiretsu* dealership, and voluntary purchasing plan by Japanese automakers. Because US-Japan easily came to an agreement on first two agenda but not on the last one, most of the 1995 negotiation was about whether Japanese government can affect Japanese automakers so that they will publicize such a voluntary purchase plan. MITI strongly refused to come up with voluntary plan while USTR claimed that the plan is the key in the negotiation and they won't agree without those plans including numerical figures.

#### **US pre-negotiation Phase**

Before he left for the main negotiation in Geneva, Ira Shapiro, General Council (legal adviser) of USTR, engaged in unofficial pre-negotiations with US auto industries — representatives from Big Three auto makers, industry association for auto parts, and UAW.<sup>37</sup> The purpose of this prenegotiation is to get a consensus about the extent to which the US side (as a whole) can concede. Shapiro could not reach an agreement with US auto industry on the day before the beginning of the Geneva table, but he became confident because he felt that he could manage to let the industry understand with his “secret” concession plan

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37 Nihonkeizai Shimbun Sha (1995, p. 16).

with Japan.<sup>38</sup>

### **Japan pre-negotiation Phase**

The relationship between MITI and Japanese auto industry has been very close and the both parties kept contacting each other before and during the negotiation.<sup>39</sup> Thus they do not seem to have any formal meetings as pre-negotiation. But it is true that both sides meet frequently to discuss how they will face the issue together. And it is told that this informal pre-negotiation was conducted with a strong leadership of MITI.<sup>40</sup> MITI had been advising auto makers not to publicize voluntary plans before MITI, and they agree to follow MITI advice.<sup>41</sup> This was to keep consistency inside Japan (between the government and industry) that Japan would not concede to the unreasonable request from US.

### **Pre-negotiation Phase: Secret meeting in the Halifax**

Six days before the Geneva negotiation table, pre-negotiation among three negotiators took place in the suburbs of Halifax, Canada where the Summit was going on. The members were Ira Shapiro (USTR), Sakamoto (MITI), and Watanabe (MITI, the Director General of the bureau of machinery information industry). The main topic here was about the 'voluntary plan' of Japanese auto manufacturers. The voluntary plan discussed here was not about a mere numerical target, to which MITI had been opposed. Japan side changed their attitude from no voluntary plan at all to admit voluntary plan by automakers. US side changed their attitude from that voluntary plan should include

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38 Nihonkeizai Shimbun Sha (1995, p. 17).

39 Interview with Yuki Sadamitsu on April 19, 1997.

40 Nihonkeizai Shimbun Sha (1995, pp. 81-110).

41 Nihonkeizai Shimbun Sha (1995, pp. 81-110).

numerical amount of auto parts purchase by Japanese makers to that voluntary plan should not necessarily include numerical target as long as it ensures the implication of future increase in auto parts purchase.<sup>42</sup>

Later, both US and Japan sides revealed the usefulness of this secret meeting at Halifax as follows. US government official: “The usefulness of the meeting was the fact that we came to know that five Japanese automakers were preparing their voluntary plans.” MITI official: “We came to know that US government got upset by WTO filing of Japan and that they are also serious about sanction on June 28.”<sup>43</sup>

### **Geneva negotiation Table**

In 1995, for more than two years, the argument between US and Japanese governments had been totally apart. US side claimed that Japanese market was closed and unfair whereas Japan side rejected US argument as the irrational claim for “numerical objective.”<sup>44</sup> On May 16, 1995, US government publicized the sanction list for Japanese luxurious car like Lexus and Infinity.<sup>45</sup> Then, Japanese government filed a suit in WTO panel in response to the sanction list. Since US set the deadline for the sanction, both sides agreed to meet before the deadline to seek for mutual beneficial outcomes. That was a week length of the Geneva negotiation from June 21 to June 28, 1995.

The fact that US publicized the sanction list for Japanese luxurious cars may be considered as a creation of *ripeness*, which is a considerably well-studied concept in the negotiation studies. But this is

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42 Nihonkeizai Shimbun Sha (1995, pp. 24-30).

43 Nihonkeizai Shimbun Sha (1995, p. 30).

44 Nihonkeizai Shimbun Sha (1995, p. 15).

45 Nihonkeizai Shimbun Sha (1995, p. 15).

not a natural ripe. This artificial making of ripeness surely created resentment in Japan-side negotiators. This creation of ripeness not only did not work well, but also lead both sides to invite an escalation in the negotiation.

In the Geneva table, there were three agenda in this negotiation: (1) Deregulation of Japanese repair parts market, (2) Opening Japanese “Keiretsu” dealership, and (3) The increase in the purchase of US made auto parts by the Japanese automakers. A US negotiator Jeffrey Garden, Vice Minister of Department of Commerce ITA (International Trade Agency), told the press that all of these three agenda were very important and US side could not miss one.<sup>46</sup> In fact first two agenda were almost agreed by both parties, the key issue in the Geneva table was the third one, about the purchase of US parts by Japanese makers. This final agenda was the most difficult and the center of the dispute because this is the main point which the Japanese government wanted to avoid a concession. The agenda was clearly against the principles MITI adopted this time: ‘No government intervention into business’ and ‘No numerical target.’<sup>47</sup>

After the first day of the Geneva table, MITI Director (Automobile Division) Atsushi Ooi stated that it was unacceptable for Japan side with “numerical target” in any kind and that there was still a large gap between US and Japan. On the other hand, US negotiators responded to his statement that they agreed with Mr. Ooi about the large gap between US and Japan but that US side did not request “numerical target” and would do anything to reach an agreement.

At night, four of the both sides’ negotiators got together to attend an unofficial meeting to discuss with *Honne* (the Japanese word meaning the real thought and true intention, the situation when you say “I mean

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46 Nihonkeizai Shimbun Sha (1995, p. 18).

47 I will write more about the MITI negotiation principles later in this paper.

it”). In this *Honne* unofficial meeting, both side succeeded to gain the feeling of future settlement by talking each other honestly.

Unable to reach an agreement in the first four day deputy-level negotiation, both Mickey Kantor (Trade Representative, US) and Ryutaro Hashimoto (Trade Minister, Japan) arrived in Geneva to seek for the final settlement at the Ministerial-level on June 26, two days before the activation of the sanctions.

Hashimoto revealed the “Global Vision” (= voluntary plan) created by Japanese automakers but he added that the plan should accord with the WTO rules, not the US Section 301 rules. Kantor requested the numerical figures in the plan but Hashimoto refused to do so. Here, Japan clearly conceded somewhat, but US side still stuck to numerical figures.

Finally, the agreement was reached in the following manner. Hashimoto gave Kantor the voluntary plan of five Japanese automakers, but did not include the numerical amount of purchase from US parts makers. Instead of giving the final numerical figures to the US side, Japanese side gave the back ground information such as the one that Toyota aims the local contents standard according to NAFTA standard. This allows US side to calculate the estimated figures of the purchase of US made parts by Japanese makers. Still Kantor had to negotiate with Washington D.C. and ordered spokesperson Ann Rusato (Luzato?) to create two documents for both “agreement” and “rupture” cases. After getting consent from Washington, Kantor went into the final negotiation table with Minister Hashimoto. Resolution document was worked by both Shapiro and Sakamoto. When Kantor picked up the document and told them that was fine, Hashimoto also looked at it and then they shook hands at 11 am June 28, 1995.<sup>48</sup>

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48 Nihonkeizai Shimbun Sha (1995, pp. 64-72).

## Post negotiation - Press release

Even though, in the main negotiation, I asserted that the negotiation failed mainly because of US side negotiators, I would argue it was Japan side who did not work well in the after-negotiation phase. I will explain why chronologically.

After the press conference, the world press people shared a strange feeling about the final document. “Is this a real agreement document?” The official document was a full of blank. There was no numbers which Kantor claimed that US must have gotten from Japan. Moreover, at the end of those blanks, the remark said, “Minister Hashimoto stated that Japanese government had nothing to do with the estimated figures here because the estimated figure exceeds the responsibility of the government. Minister Hashimoto also stated that this estimation is solely done by USTR.”<sup>49</sup> This document itself was fine, but Japan side negotiators were not successful in the follow-up phase.

US negotiators were very good at justifying their outcome and succeeded in convincing most public that they were successful in achieving numerical target while Japan side did not protested the misguided US statement which was beyond the scope of the negotiation.<sup>50</sup> US negotiators emphasized that the agreement included numerical targets and claimed that the agreement was result oriented. Furthermore, they handed in the reference document titled “agreed fact sheet” which could be interpreted as the agreement with Japanese negotiators. But it was obvious that there was not strong Japanese opposition to the fact sheet until Secretary General Igarashi officially stated that American document was just an estimation by only US side on the following day.<sup>51</sup> I believe Japan should have announced the

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49 Nihonkeizai Shimbun Sha (1995, p. 75).

50 Ishii (1996, pp. 22-23).

51 Ishii (1996, p. 23).



opposition to the US press release sooner.

#### **4. Why Japan side became assertive?**

In the 1995 negotiations, MITI of Japan took a strong stance against numerical targets and the MITI negotiators kept refusing to concede. I will give several reasons below why Japan could take more assertive stance than before.

##### **4-A. Internal change in Japan**

This Japan's assertive stance was fostered by a major change in the Japanese congress. The Liberal Democratic Party, which had governed Japan from 1955, lost its majority in the Japanese Diet first time since then in 1993, and the new leader Morihiro Hosokawa from the Japan New Party became the prime minister. "Deregulation" was a slogan of the new Hosokawa Administration, and this slogan helped win Japanese public opposition to the "managed trade" proposal of the US negotiators. It was the Prime Minister Hosokawa who first said "No" to the United States:

"For these twenty and thirty years, both US and Japan have always concluded trade negotiations with ambiguous outcomes. It was a general perception of the public that it was Japan who, at the final stage, concedes from 'foreign pressure.' Because of this, it is true that both of our frustration have been accumulated. My view of new US Japan relation is that the relationship needs to be the equal one between two adults (rather than the unequal relationship between an adult and a child). I mean, in a such relationship, both of us should say what we have to say and should agree with only what we want to agree and should not agree with what we cannot agree."<sup>52</sup>

After the Hosokawa administration, Liberal Democratic Party (LDP) regained its political power and took the cabinet back.<sup>53</sup> But this time, there was a generation change in LDP and younger politicians at LDP know that public supported Hosokawa's view that Japan should say 'No' when necessary. Minister Hashimoto must have been one of those young (then) people.<sup>54</sup> He also had a strong leadership. Such forceful leadership of the new Trade Minister Ryutaro Hashimoto (LDP) strengthened MITI's tough stance against the US position.<sup>55</sup> Japanese academics also supported MITI's point of view by publishing many books and articles with macro-economic arguments in support of the stance by MITI.<sup>56</sup>

In 1995, there was also internal change in MITI personnel, too. Both of the main negotiating positions, *Tsu-san Shingikan* (The Negotiator, Vice Minister, of the Ministry of International Trade and Industry) and *Tsu-shou seisaku kyoku cho* (The Director General of trade policy bureau) were replaced by Sakamoto and Hosokawa (a different guy from the former prime minister) who are familiar with GATT rules and were also critical to MITI's weak stance at the semiconductor negotiation in 1986. Director level also strengthened the assertive stance of Japanese negotiators. Newly assigned director of Americas Division of MITI, Masakazu Toyoda, has been regarded as "tough negotiator" by US side because he did not compromise on the

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52 The statement was made by (then) Prime Minister Hosokawa on February 11, 1994. This is the author's translation from the original Japanese citation in *Nihonkeizai Shimbun Sha* (1995, p. 181).

53 This political regain by the LDP was not fully utilized because in order to get the majority in the diet, the LDP had to form a coalition with the Socialist Party whose head, Mr. Murayama, had become the Prime Minister.

54 In my view, ...

55 Interview with Ichiro Sakata on July 20, 1995.

56 To name a few, see Motoshige Itoh (ed.) (1994).

principle of 'No numerical target.' This strong stance was fostered by his background as a multilateral negotiator in OECD. Although he now works for "Americas" division, he had never lived in the US, and he had been working in Paris for the Organization of Economic Cooperation and Development. As a result, he does not foster the idea that US-Japan relationship is most important and that economic issue should not prevent from keeping such a "good" relationship.<sup>57</sup>

These legislative and administrative changes in Japan contributed to the changes in Japanese negotiating styles from compromising to rather assertive.

#### **4-B. Role of WTO (World Trade Organization)**

Helping to press both the US and Japan towards a settlement in 1995 was a new multilateral mechanism for resolution of trade negotiations and disputes, the World Trade Organization (WTO). The existence of WTO obviously contributed to the strengthened Japan's BATNA or alternatives to a non agreement case. Of course, both Japan and the US were members of WTO, and both threatened to take complaints about the other to this new regulator of world trade. But it was well known to both sides that the resolution of WTO dispute panel will be favorable to Japan, and the existence of WTO is a source of increased negotiating power of Japan side, not of US side.

Here's a brief summary of what's happened over WTO. The Japanese said that they would go to the WTO against any unilateral US imposition of tariffs on Japanese luxury cars. For its part, the US threatened to take Japan to the WTO for its invisible trade barriers - cartel-like dealings and business-government collusion - which shut US auto parts out of the Japanese market.<sup>58</sup> However, according to Clyde

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57 Nihonkeizai Shimbun Sha (1995, p. 33).

58 Borrus with Javetski (1995, p. 35).

Prestowitz Jr., President of the Economic Strategy Institute, US negotiators seemed to realize that the WTO would probably not favor the US because many WTO members were against unilateral trade sanctions by the US, and many others saw Japanese-style collusive practices as important tools for their own economic development.<sup>59</sup> The threat of WTO intervention seemed to pressure both Japan and the US, especially USTR, away from trade war.

Also, there was a reason why Clinton administration could not push Japan harder in this WTO issues. According to Anderson (1996), there was an atmosphere in the Clinton administration that many people felt this way, “How can the administration disregard the WTO after a big effort to create them?”<sup>60</sup>

#### 4-C. Japan's other alternatives than WTO

Other than a filing in the dispute settlement in the WTO, Japanese side was preparing an alternative list when the negotiation failed. It was now proved that MITI was preparing the case of breakdown in the negotiation. It was reported that the Director General (trade policy bureau) Hosokawa had been visiting prominent politicians in order to do *Nemawashi* — unofficial consensus building system in Japanese society, to make potential opponents understand the possibility of drastic change that can be expected. The number of the politician visited by MITI officials was over thirty. So MITI was surely expecting the possibility of failure in the agreement.<sup>61</sup>

Well then what were the alternatives? In response to the 100% imposition of the tariff on Japanese luxurious car, Japan side prepared two alternatives: 1) Subsidizing Japanese automakers, and 2) retaliation

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59 Borrus with Javetski (1995, p. 35).

60 Anderson (1996, p. 30).

61 Nihonkeizai Shimbun Sha (1995, p. 58).

to US export to Japan.<sup>62</sup> The first one includes new-law making of subsidization to automakers. This aims to alleviate the weakened management of auto manufacturers. The second one is not necessary agreed by the all people in Japan, but it was the imposition of the 100% tariff on the products mainly imported from U.S. such as airplanes, beef, orange, wheat, and a certain type of chemical products (which is produced mainly in Arkansas). Even some of the MITI officials with strong stance toward US pushed this possibility, Minister Hashimoto was so prudent that he opposed to the idea of retaliation with violation of WTO rules.<sup>63</sup>

Finally, it turned out that MITI even prepared an unrealistic retaliation possibility in financial market. Set aside the feasibility of the retaliation plan, it was a massive sales of US bond held by Bank of Japan into the market. If that option had been possible, the massive sales would reduce US bond price and thus would lead to high interest rate in the US market which would have given a huge damage to the US economy.<sup>64</sup>

By preparing those alternatives, Japan side gained a negotiating power. At least, they knew what they would do in the case of breakdown. Because of these contingency plans, Japanese negotiators did not hesitate to insist their merits and interests rather than just to give in.

## **5. Why US made the negotiation failure?**

As I said in the introduction section, I view the main negotiation was a failure mostly because of US side's bad strategy. I will give four reasons for that. Let's look at them one by one.

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62 Nihonkeizai Shimbun Sha (1995, p. 59).

63 Nihonkeizai Shimbun Sha (1995, pp. 59-60).

64 Nihonkeizai Shimbun Sha (1995, p. 60).

### 5-A. US's position - numerical target

The first reason is that US took positional stance rather than that of principle-based negotiators. Even though Japan tried to cooperate with US side in order to seek mutually benefit outcome by giving the concessions on several points such as deregulation in automobile inspection system, US negotiators insisted on numerical target until the last minutes. I wondered if those negotiators (most of them are lawyers, by the way) have ever read *Getting to YES*. No matter how hard Japan side tried to convince US side in practical aspects, Mickey Kantor did not seem to listen to anything other than numbers. This stance was a typical of positional negotiators. The situation was exactly like the positional negotiation described in Fisher and Ury: "The more you try to convince the other side of the impossibility of changing your opening position, the more difficult it becomes to do so."<sup>65</sup>

The validity of the USTR's position is doubtful, too. Fisher and Ury also pointed out the importance of objective criteria.<sup>66</sup> USTR's request or position doesn't seem to fit with the objective criteria. The request of numerical target in the trade for a particular good is clearly a violation of the GATT rules.<sup>67</sup>

In contrast with the USTR negotiators, Japanese side tried to stick to the principle negotiation method. The MITI Negotiator Sakamoto wrote about the "principle" about one year after the Geneva negotiation table.

The most important point to us in the US-Japan automobile negotiation was in our stance to try to stick to the "principle"

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65 Fisher and Ury (1991, p. 5).

66 Fisher and Ury (1991, p. 8).

67 Tominaga (1996, p. 23).

based argument. We wanted to amend the “conventional perception” — whether it is good or bad — which was formed through a fifty-year long US-Japan trade negotiations after the World War Two.<sup>68</sup>

Sakamoto contrasted the “conventional perception” and the “principle” as follows. The Japan side “conventional perception” says that we will lose if the US sanction is conducted even if we stick to the principle of the negotiation. The US side “conventional perception” says that US bluff will surely lead to the Japan’s last minutes concession and that once if we convince MITI, we can affect Japan’s auto industry no matter how hard is the request. The consequence followed those “conventional perceptions” has lead the one-sided agreement in the semiconductor negotiation which is regarded as success of the USTR and the failure of the MITI. Japan’s “principle” in this auto negotiation, according to Sakamoto, was two folds: 1) The principle of the non-intervention of the government to the markets and 2) The principle of the multilateral trade negotiation, which is represented by the WTO.<sup>69</sup>

### **5-B. Failure in recognizing the change in Japan’s negotiating power**

It was true that Japan had conceded a lot more than they should have in its negotiating history. But this time, Japan did not have to concede because their BATNA had changed. They now have a better alternative than before, thus Japan has more negotiating power. As Fisher and Ury put it in their book, *Getting to YES*: “There is power in developing a good BATNA. ... [A] fundamental way to increase your negotiation power is by improving your walk-away alternative.”<sup>70</sup>

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68 Sakamoto (1996, pp. 22-23).

69 Sakamoto (1996, pp. 22-23).

70 Fisher and Ury (1991, p. 183).

As I explained in sections 4-B and 4-C in this paper, MITI prepared their alternatives well before the negotiation itself begins. There were two types of alternatives: One is to save automakers from the US sanction and the other is the retaliation to US trade. With the combination of the first alternative and the WTO filing, Japan succeeded in preparing a good BATNA. Because the first one is legitimate with respect to external standards, whereas the second option of retaliation was not a “good” alternatives.<sup>71</sup> Fisher and Ury explained the importance of external standard of legitimacy as follows:

There is power in using external standards of legitimacy. You can use standards of legitimacy both as a sword to persuade others, and as a shield to help you resist pressure to give in arbitrarily. ... Convincing the other side that you are asking for no more than is fair is one of the most powerful arguments you can make.<sup>72</sup>

Because of the birth of WTO in 1995, Japan got a support from external standards. US's action (creating fear of unilateral sanction) is clearly violation of the GATT/WTO rules, Japan's argument that Japan will not discuss under US trade law section 301 is legitimate. Of course, if US really put a sanction on Japanese import, it might have hurt Japanese industry in a short time, but Japan knew that Japan can subsidize those losses to automakers before they get support from the other member countries in WTO and the dispute settlement mechanism of WTO will be in favor of Japan. Thus Japan's alternative was firm and created negotiating power.

The problem of US negotiators was that they did not seem to fully

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71 In this sense, Minister Hashimoto was correct since he opposed to the second opinion.

72 Fisher and Ury (1991, p. 183).



regard these increased power in Japan as important. The reasons why US side could not appreciate these changes in Japan's alternatives may be partly because of its positional negotiating stance (see section 5-A), partly because of stereotyped image of bowing Japanese (see section 5-D).

### **5-C. Failure to understand Organizational change in Japanese government**

There were two organizational changes in Japan side. One is in politics. The other is in the Ministry of International Trade and Industry. These changes made Japan side take a different way of negotiation. USTR negotiators failed to capture those internal changes and therefore this ignorance led them to a failed outcome in the negotiation.

Political change was facilitated by the new trend in Japanese politics in 1990's. As expressed in the section 4-A, there was a generational change from old LDP members to new politicians. The new trend in politics allowed MITI to focus on economic interests, rather than to focus on "maintaining good relationship with United States."

With a help from political climate change, the Japanese government, especially MITI succeeded in changing their negotiating stance from the past. MITI allocated those people who have more international background and who are critical to the past semiconductor agreement with US in the important negotiating positions before the Geneva negotiation. One of those people is the chief negotiator Sakamoto. He, looking back the negotiation, stated as follows:

"In the past, Japanese government unnecessary intervened to the market mechanism through the various concessions [with United States] such as semiconductor agreement, VER in automobile, and Voluntary purchasing plan of auto parts. In this year's [1995] Japan-US automobile negotiation, we took a strong stance that we

should make such a negotiating pattern — Japan side concede in fear of Section 301 [in US trade legislation] — an end.”<sup>73</sup>

#### 5-D. Stereotyped image of Japanese negotiators

The final reason of US failure in the auto negotiation is the one related to culture, gender, and personality type. It is the stereotyping with which US negotiators were obsessed. From the past experience of semiconductor and 1992 automobile negotiations, US negotiation members could not wipe off the image of bowing-Japanese.

The prominent trade economist (and one of my mentors at Columbia economics department)<sup>74</sup> Jadish Bhagwati pointed to the prevailing stereotyping against Japanese as follows:

In fact, many of these cultural stereotypes are invoked much too readily to mark the Japanese as exotically different when, in fact, their differential behavior can be explained by differences of economic situation.<sup>75</sup>

There still remains the way of thinking in US political system that harder negotiating stance will bring something out from Japan. And it is important for Japan side to negate such factors in the future negotiation.<sup>76</sup>

The executive of Japan *Kei-dan-ren* (Japan Business Entities Association) Miyoshi also pointed out the US problem of wrong perception toward Japan and Japanese business. He claims that US side did not

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73 Bhagwati with Sakamoto (1995, p. 12). (Translated from Japanese by the author.)

74 The author studied international trade at Columbia University's Ph.D. program.

75 Bhagwati (1991, p. 28).

76 Bhagwati with Sakamoto (1995, p. 11). (Translated from Japanese by the author.)

seem to understand the changes happening in Japan's business government relationship.<sup>77</sup>

Nikkei Shimbun Sha (1995) also pointed to the same point:

In the first half of the automobile negotiation, U.S. side could not sweep off the idea that "MITI will compromise if we push hard" from the past experience especially semiconductor negotiation. This obsession was one of the main factor that made the negotiation difficult due to perception gap between US and Japan. Also the obsession made US side fail to grasp the timing of the internal change in MITI's stance.<sup>78</sup>

With all four reasons above combined, the negotiating strategy taken by United States turned out to be wrong. But those are not only reasons for the failure. Compared with non-economic negotiations, negotiation in economic relations has a different kind of difficulties in it. (Of course I understand there are also different kinds of difficulties in conflict-resolution type negotiations — such as escalation, military action, emotions etc.) I will explain some of those difficulties embedded in the economic relations in the next section.

## **6. Difficulties of Negotiation in Economic Relations**

In the final section of this paper, I want to conclude by stating particular reasons why economic negotiations can be difficult.

The general problems in economic negotiations are in the difficulties in recognizing true merits of the parties. Compared with the international negotiations over territories, it is harder to identify the interests to the countries or negotiators in the negotiations in economic

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77 Miyoshi (1996, p. 28).

78 Nihonkeizai Shimbun Sha (1995, p. 33).

relations. This difficulty comes from both lack of knowledge of negotiators in economics and from the non-zero sum nature of economic issues.

First, many economically wrong opinions are prevailing in public opinions and policy makers, and thus among negotiators. One of the most prominent academic economist Paul Krugman (who was at MIT and moved to Princeton) expressed this point in his 1996 book targeting for general readers as follows.<sup>79</sup>

They [Pop internationalists - people who talk about international economy without knowing basic economics] all offer a view of the world .... of international trade a an arena of ... “win-lose” competition among nations. And they all contain little or nothing of what economists think they know about international trade.

Through participating public debate, Krugman became aware that “most basic truth about international trade had been driven out of public discussion.”<sup>80</sup> People “might think they know a lot about economics but had never been exposed to the real thing.”<sup>81</sup> Many people do not know economics. How can they know merits from trade without knowing basic international trade textbook? Without knowing the expected outcome, how can they negotiate over the issue?

A good example is VER (Voluntary Export Restraint) which many people consider as US’s success. But if you take an intermediate microeconomics course at any college,<sup>82</sup> you will know that the idea

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79 Krugman (1996, p. viii in the introduction).

80 Krugman (1996, p. x in the introduction).

81 Krugman (1996, p. xi in the introduction).

82 I teach this in my international trade course at School of Commerce, Waseda University.

that VER is good for US is wrong. VER is not the best option even in order to achieve the same (wrong) goal. Import restriction can collect the economic rent, but voluntary export restraint cannot collect such money. It gives money to the Japanese automakers. This kind of wrong policy is prevailing because policy makers don't know economics. Without having sufficient information, the negotiation in economic issues is a difficult task.

Second, economic issues are typically non-zero sum types. But most people have difficulties in understanding the non-zero sum nature of the issue. This clearly relates to the point made in the first point. As the negotiation theory encourage people to seek integrated approach rather than distributive approach, it is important, but difficult for many people to get away from the wrong idea about the "win-lose" approach.

Books on negotiation theory such as *Getting to YES* and *Negotiation Theory and Practice* emphasized the importance of mutual gain. For example, Jeff Rubin explained the notion of "enlightened self-interest" as "it may be possible for both to do well,"<sup>83</sup> and Mary Parker Follett introduced the concept of "integrated approach. ... a solution has been found in which both desires have found a place, that neither side has had to sacrifice anything."<sup>84</sup>

Difficulties in understanding non-zero-sum type are explained as follows. Mary Parker Follett described the requirement of the integrated approach as "a higher order of intelligence, keen perception and discrimination, more than all, a brilliant inventiveness."<sup>85</sup> It is easier to fight than to suggest a better way because, in order to fight, you don't have to think (just react), but in order to come up with better options,

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83 Breslin and Rubin (eds.) (1991, p. 4).

84 Breslin and Rubin (eds.) (1991, p. 14).

85 Breslin and Rubin (eds.) (1991, p. 16).

you have to be wise (be proactive and creative). Also, as Bazerman explained in his paper, human has a fundamental bias toward the fixed-pie assumption.<sup>86</sup> Thus, the most difficult part in the negotiations, I think, comes in this part: negotiators' intelligence. "Intelligence" includes knowledge. It is important to know that people have a tendency to think that a pie is fixed. To become inventive, you have to know you should be inventive. But all those things are very difficult to achieve.

Thus, all these things combined, it makes difficult to seek good consequences from the negotiations in economic issues. And I realized that economists share the responsibility to make public more "intelligent."<sup>87</sup>

## 7. Conclusion

In sum, my analysis revealed why MITI took more assertive stance than before and how US failed to capture Japan's change. I claimed that US failed the negotiation for its own sake. But does this mean US lost at all? Maybe not so. President Clinton won the 1996 election not only because of the consequence of negotiation of course, but I am sure USTR and President Clinton succeeded in the follow-up phase when they explained the results to the press. Also, the fact that Mickey Kantor pushed "numerical target" until the end of the negotiation may have contributed to a large appreciation of YEN in the summer of 1995. (from 100 per dollar to 80) This Yen appreciation surely helped the US economy and worsened Japanese exporting industry. And it is true that Japan has still been in recession while US experienced a boom in late 1990s.

There is a saying in Japanese: "*Niku wo Kirasete, Hone wo Tatsu*

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86 Breslin and Rubin (eds.) (1991, p. 200).

87 I should bear this in mind because I am teaching economics at the University.

(While allowing the opponent to cut your body, you cut into his bone.)” — meaning that purposefully lose at small battles to achieve winning in the large war. This 1995 automobile negotiation somewhat looked like that. If that is a case, it is not always a good idea to win in the negotiation.

But I am sure that from this negotiation Japan has achieved something valuable for the future. For the US and other countries in the world now know that Japan may say 'No' when it is needed. And I hope the result of this negotiation will contribute to the perception amendment in the US negotiators from that Japan will easily give in at the last minutes to maintain the relationship to that Japan is an equal partner who can refuse to agree.

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