AMERICA AND THE PACIFIC – 1994 AND BEYOND

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Introduction

I will begin by sketching a picture of the ongoing economic integration in the Pacific Rim. Secondly, I will present some data documenting the tremendous expansion of American exports to Asia, as well as provide an explanation of the factors contributing to this process. As you may realize, American merchandise exports – on a worldwide basis – have grown phenomenally, from $250 billion in 1987 to $450 billion in 1993. Thirdly, I will discuss a "will card" situation that could pose a threat to the continuation of rapid economic growth and economic integration in the Asia/Pacific region. This negative situation is, of course, the *slight* possibility of a complete rupture in U.S.-Japan relations.

Economic Integration in the Pacific Rim

Can you remember when Japan, Korea, China, Indonesia, etc. were commonly referred to as the "Far East", a term which conjures up images of distance, mystery, and impenetrability?

Now, in the closing decade of the twentieth century, these countries could be more accurately referred to as "America's Near West", especially as "California's Near West."

In the 1990's, Japan, Korea, China, Indonesia, etc. are all countries whose markets are becoming "closer" to America, whose markets are becoming less mysterious to Americans, and whose markets are becoming more open to American participation.

This process is occuring as a result of changing technologies, changing ideologies, and changing personalities. Improved telecommunications equipment, facsimile machines, and fiber optic transmission lines are dramatically accelerating the trans-Pacific communication of ideas and data. Advanced aircraft, simplification of customs procedures, and improved airport and seaport management techniques are facilitating rapidly increasing trans-Pacific flows of people and materials. The collapse of communist and socialist ideologies throughout the Asia/Pacific region has led to the opening of markets, the deregulation of markets, and the privatization of inefficiently managed state-owned enterprises. Also, the gradual evolution of national personalities is occuring, in part, as a result of the effects of an American educational experience on thousands and thousands of Asians who have studied in the United States. Upon return to Asia, they become relatively *non-mysterious* customers, partners, suppliers, and competitors for American firms.

The economic integration of the Pacific Rim region – which includes the United States, Canada and Mexico (as the Rim's "East Coast") – is rapidly occuring, primarily as a result of intra-regional capital flows, increased trade liberalization, and privatization trends.[1] These forces have been stimulated by the advance of telecommunications and information systems technology, by the decline of ideology as a barrier to the flow of factors of production and products, by adoption of regional and global strategies by multinational firms, and by the development of regional cooperation groups such as the Pacific Economic Cooperation Council (PECC) and the Asia Pacific Economic Cooperation (APEC) group.[2] Appreciating currencies and rising wages and land costs in the Pacific Rim's capital-surplus countries (Japan, Taiwan, and Korea) and national economic reforms in the capital-deficit countries – especially the major reforms initiated by China, Indonesia, and Mexico – have accelerated the regional integration process. As a result, new private-sector business opportunities between the west and east coasts and the northern and southern rims of the Pacific region are stimulating ever-larger flows of goods, services, capital, technology, and people among these economies. Thus, each of these economies is increasingly becoming affected by policy and market changes occuring in its Pacific Rim "neighbors".

An important indicator of this regional economic integration is the share of the region's total exports that is sold to countries within the region. Between 1970 and 1991, intra-regional exports increased from 56 to 69 percent among the seventeen member countries of the Pacific Economic Cooperation Council (PECC) – which includes all the East Asian economies plus Japan, Canada, the U.S., Mexico, Peru, Chile, New Zealand, and Australia[3].

This intensification of trade relations is occuring as a result of greater flows of capital, technology, services, and people throughout the Pacific Rim. The capital movements include loans and aid, as well as portfolio and direct investments. The people movements include salesmen, workers, tourists, managers, students, and immigrants. All of these trends increase the interpersonal contact between the Pacific Rim nations in a variety of overlapping roles as competitors, suppliers, partners, classmates, and neighbors. This intensification of economic relations between neighbors has increased even more rapidly among the nine East Asian countries in the Western Pacific: ANIES (Hong Kong, Korea, Taiwan and Singapore), the ASEAN-4 (Indonesia, Malaysia, Philippines, and Thailand), and China.

Five trends that illustrate this process are presented below[4]:

1. Intra-East Asian exports have climbed from 26 percent of total East Asian exports in 1985 to 36 percent in 1991.
2. East-Asian exporters have become less dependent on the U.S. market. The share of their exports going to the U.S. dropped from a peak level of 30 percent in 1986 to 21 percent in 1991.
3. East Asian trade became more important to the U.S. The share of U.S. exports going to East Asia rose from 12 percent in 1985 to 15 percent in 1991; the East Asian share of U.S. imports rose from 16 to 20 percent. U.S. exports to East Asia, in volume terms, grew twice as fast (13% per year) as imports from East Asia.
4. East Asian exporters became less dependent on Japan. The share of their exports going to Japan continued their steady, decade-long decline from 18 percent in 1985 to 14 percent in 1991.
5. East Asian trade became more important to Japan. The share of Japan's exports going to East Asia rose from 24 percent in 1985 to 32 percent in 1991. The East Asian share of Japan's imports rose from 27 to 30 percent. Japan's exports to East Asia, in volume terms, grew at about the same rate (12% per year) as imports from East Asia.

Intra-Asian flows of investment, trade, and aid are growing substantially and will continue to do so. The six driving forces underlying this process of economic integration have been: (1) appreciation of the Yen, the NT Dollar, and the Won, (2) democratization, higher wages and land prices, and stricter pollution controls in Korea and Taiwan, (3) elimination of the Generalized System of Preference (GSP) status for Taiwan, Korea, Hong Kong, and Singapore by the United States in 1989, (4) liberalization of trade and investment regimes throughout the ASEAN-4, (5) economic reforms and trade and investment liberalization in China, and (6) economic reforms and trade and investment liberalization in Vietnam and the Russian Far East.

These six forces have been substantially changing national competitiveness, national asset values and the international purchasing power of the PECC countries. In combination, these forces have been propelling waves of transnational direct investments and loans that are reshaping the Pacific Rim's industrial structure and trade patterns, as well as creating new webs of economic and political interdependencies. For example, China has become an increasingly important motor for Asia-Pacific growth. From 1985-92, the share of Taiwan's exports going to China/Hong Kong increased from 8 to 19 percent; the share of Korea's exports, from 5 to 11 percent; the share of Indonesia's exports, from 2 to 8 percent.[5] In 1993, it is reported that $15 billion of actual foreign investments were made in China, up from $4 billion in 1991.[6]

The reason that economic integration in East Asia should be of interest to American business managers is that it signals significant reductions in barriers to the flow of goods, services, capital, and people among the countries of East Asia. This means that American firms doing business in Asia should begin to develop *regional* strategies (as numerous Japanese firms have been doing for years), as opposed to viewing Asian countries as completely separate markets.

American Participation in the East Asian Growth Miracle

Are American firms benefiting from the rapid economic growth and integration of East Asia? Yes, indeed! American merchandise exports to Asia have expanded substantially between 1988 and 1993, growing from $90 billion to $144 billion.

U.S. Merchandise Exports to Asia (Billion $)

Country	1988	1993 (e)
Japan	$38	$56
Korea	$13	$20
Taiwan	$12	$17
Hong Kong	$ 6	$ 9
China	$ 5	$ 9
ASEAN-5	$16	$33
TOTAL	$90	$144

Source: U.S. & Foreign Commercial Service, U.S. Department of Commerce, "Country Marketing Plans" (various years).

This American export expansion can be explained by five factors:

1. Increases in the *price* competitiveness of goods made in America, due to a depreciating dollar and due to the *relative* decline in unit labor costs in the United States.
2. Increases in the *quality* competitiveness of goods made in America, due to increased management emphasis on quality and customer service.
3. Rapid economic growth in markets outside the U.S. and slow growth within in the U.S. market place.
4. Increased "openness" of East Asian markets.
5. Increased commitments being made to international business opportunities by American corporations.

Will American firms continue to expand their exports to Asia? Yes, they will because all five of the trends listed above will continue to be favorable to export expansion. Could anything disrupt this "conventional wisdom" scenario of continued growth and prosperity in the Pacific Rim?

Growing Friction Between the United States and Japan

A frequently mentioned "wild card" that could disrupt Pacific Rim trends would be the complete breakdown of U.S.-Japan relations. (In spite of current rhetoric and posturing the Clinton Administration can be expected to continue to provide MFN to China.) Even though such a cataclysmic event is not likely to occur, it is worth discussing because of the very real disputes that the U.S. – and the rest of the world – have with "Japan's" trade and business practices. It is instructive to remember that Japan is not only out of balance with the United States, it is out of balance with the world, and it has been substantially out of balance for over a decade. That is, Japanese companies and individuals have sold $900 billion more goods and services than they purchased or gave away as official development assistance between 1984 and 1994.[7] This cumulative current account surplus of $900 billion has financed Japanese firms' acquisition of stocks, bonds, properties and manufacturing facilities around the world.

Now that the Cold War is over and the United States is increasing its focus on economic issues,[8] it is asking Japan to restore harmony and balance to the economic relationship. An amicable U.S.-Japan relationship is critical to trans-Pacific economic integration and prosperity. It is also obviously critical to the continued prosperity of countless American and Japanese firms and employees whose lives are increasingly intertwined as customers, competitors, vendors, partners, and investors. Given the importance of friendly relations between America and Japan, it would be logical to assume that America and Japan would take actions to harmonize their complex relationship. However, we are all aware that this has not yet been accomplished in spite of years of studies, special commissions, and expressions of concern. In fact, what we observe is growing friction between the United States and Japan.

As U.S.-Japan commercial relationships have expanded, pernicious emotions of anger, fear, distrust, and disdain have grown even faster, especially in the past few years. A 1993 *Los Angeles Times* study of American opinion leaders titled, "America's Place in the World", reports a number of startling views by prominent Americans about the U.S. – Japan relationship; four of which are presented below:[9]

1. Japan was ranked fourth as the country .... "representing the greatest danger to the United States" (below Iran, China, and Iraq and substantially above Russia, North Korea, and Germany) by the "Influential" respondents. Japan was ranked as the second greatest danger by the "General Public" respondents.
2. The U.S. government should give **top priority** to better managing trade and economic disputes with Japan.
3. Japan is an **unfair** trading partner with the U.S., according to more than 80 percent of the Influential respondents and 72 percent of the General Public respondents (only one in three Influentials branded the EC as unfair).
4. U.S. retaliation for Japan's restrictionist trade practices was supported by 18 to 36 percent of the nine categories of Influential respondents .... "even at the risk of setting off a protectionist trade war".

In Japan, in the meantime, growing numbers of Japanese have become increasingly disdainful of the values of American institutions, the quality and productivity of American managers, and the ineptitude of American macroeconomic policy. The increased frequency of U.S. government requests for Japan to harmonize its social, commercial, and business practices with those of the United States further angers many Japanese. Some resent American interference in what they perceive to be Japan's internal affairs. Others interpret the U.S. requests as the disguised pleadings of a pitiful loser who is seeking an overly large "handicap".

However, both the Clinton and Hosokawa governments recognize that substantial changes in the U.S.-Japan relationship are needed. The recent resolution of the Motorola dispute is likely to be a harbinger of things to come. The U.S. will ever-more persistently request improved access and national treatment for American firms in exchange for continued access and national treatment of foreign firms in the U.S. market. This should not be interpreted as a rise in U.S. protectionism, but rather as an increased interest in obtaining more balanced commercial relationships. This change in U.S. attitude is a natural outcome of the end of the Cold War. The subsequent re-focusing of American policy interests means that it is no longer necessary to offer Japanese firms non-reciprocal access to the U.S. market in exchange for Japan's cooperation on security issues vis-a-vis the former Soviet Union.

Conclusion

The ongoing economic integration in the Pacific Rim will continue in the years ahead. In order to promote this outcome, American and Asian leaders should stop the sterile criticism of each other for being in violation of processes of a theory of "free trade". Economic models being followed by Asian nations should be accepted by the United States as legitimate, not as being "sinful". However, the U.S. should pursue better access to Asian markets in ways that reflect ideas of national treatment, equity, and reciprocity, although some "handicap" modifications should be allowed for countries at different stages of development.

We should remember that free trade is not and should not be an American economic *goal*. Rather, free trade is just the favorite *tool* of economists for stimulating economic systems towards favorable *outcomes*, such as increased prosperity, increased opportunity, and increased equity. Economists believe that free trade helps achieve these outcomes because it promotes increased competition, which, in turn, improves the efficiency of resource allocation and increases choice. The point is that American policy makers should focus their attention on economic *outcomes or results*. If the outcomes or results are *not* desirable, then America needs to adjust its domestic, and perhaps, its international policies.

In order to promote prosperity and harmony, Asia and American leaders should focus their energies on the tasks of actively *managing* tomorrow's inevitable economic competition, cooperation, and conflict in the Pacific Rim. Good management will result in a more balanced Pacific Rim economy and allow for increased bargaining leverage with an expanded and increasingly protectionist European Community. The interaction between dynamic Pacific Rim economic systems can not be left solely to Adam Smith's *invisible hand*, when there are so many governmental and cultural *feet, arms, and legs* involved in the typical Pacific Rim business game.

Notes

1. Five recent studies which provide somewhat different, but complementary, views about the importance of market forces and government programs for regional economic integration are the following: (1) World Bank (1993). *Sustaining Rapid Development in East Asia and the Pacific,* Washington D.C.: World Bank, March; (2) Yamazawa, Ippei, et. al. (1993). "Dynamic Interdependence Among the Asia-Pacific Economics," *Keizai Bunseki* (Economic Analysis), No. 129, March, Tokyo: Economic Research Institute, Economic Planning Agency; (3) U.S. International Trade Commission (1993). *East Asia: Regional Economic Integration and Implications for the United States,* Washington, D.C.: USITC Publication 2621, May; (4) Oman, Charles (1993). *Globalization and Regionalization: The Challenge for Developing Countries,* Paris: OECD Development Centre, July (manuscript); and (5) Bank of Japan (1994). "Economic Growth in East Asia and the Role of Foreign Direct Investment," *Quarterly Bulletin,* February.
2. For a summary of PECC activities, see Mark Earle, Jr. (1992). "PECC IX: Executive Summary," Washington, D.C.: U.S. National Committee for Pacific Economic Cooperation.
3. Pacific Economic Cooperation Council (1993). *Pacific Economic Outlook 1993-1994,* Washington, D.C.: U.S. National Committee for Pacific Economic Cooperation, May, p. 56.
4. These data are from U.S. International Trade Commission (1993).
5. Nomura Research Institute (1993). "Investing in the Pacific," *Asia-Pacific Economic Outlook,* Tokyo: Nomura Research Institute, 4th Quarter, p. 2.
6. U.S. & Foreign Commercial Service (1994). "China: Fiscal Year 1994 Country Market Plan," Beijing: U.S. Embassy, pp. I-4.
7. Organization of Economic Cooperation and Development (1993). *OECD Economic Outlook,* Paris: OECD, December, p. 57 (and various earlier issues).
8. See, for example, President Clinton's introduction to the 1994 *Economic Report of the President* (1994). Washington, D.C.: U.S. Government Printing Office, pp. 3-8.
9. Times Mirror Center for the People and the Press (1993). *America's Place in the World: An Investigation of the Attitudes of American Opinion Leaders and the American Public about International Affairs,* Los Angeles Times, November.

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