

# What's Happening to the International Trading System?

## *Shared Interests of the US and Japan in the Outcome*

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I intend to cover very briefly six topics today:

1. World Trade and the Diamond Jubilee of the Multilateral Trading System (MTS)
2. Managing the US-China Strategic Competition
3. Whether the World is Dividing into Two Trading Blocs
4. The Current State of US Trade Policy
5. The Evolving US-Japan Relationship, CPTPP and the WTO
6. The Future of International Trade – with Recommendations

I will conclude with some thoughts on what role business can and should play in shaping policy.

### **1. World Trade and The MTS Diamond Jubilee<sup>2</sup>**

The modern history of trade can be readily seen in a few infographics. One picture that captures a lot of information is the world economy viewed as a soccer ball with each country contributing to the surface in accordance with the size of its economy.<sup>3</sup> Share of global GDP is a rough measure of each country's capacity to engage in international trade. The US and China dominate the surface of this image, along with the European Union (when it is viewed as a whole). When the EU's Member States are viewed separately, Japan outweighs any one of the European countries.

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<sup>1</sup> Disclaimer: The views and opinions expressed in this speech are those of the speaker and do not necessarily reflect the views or positions of the Peterson Institute for International Economics (PIIE) or its officers or fellows.

<sup>2</sup> MTS = multilateral trading system.

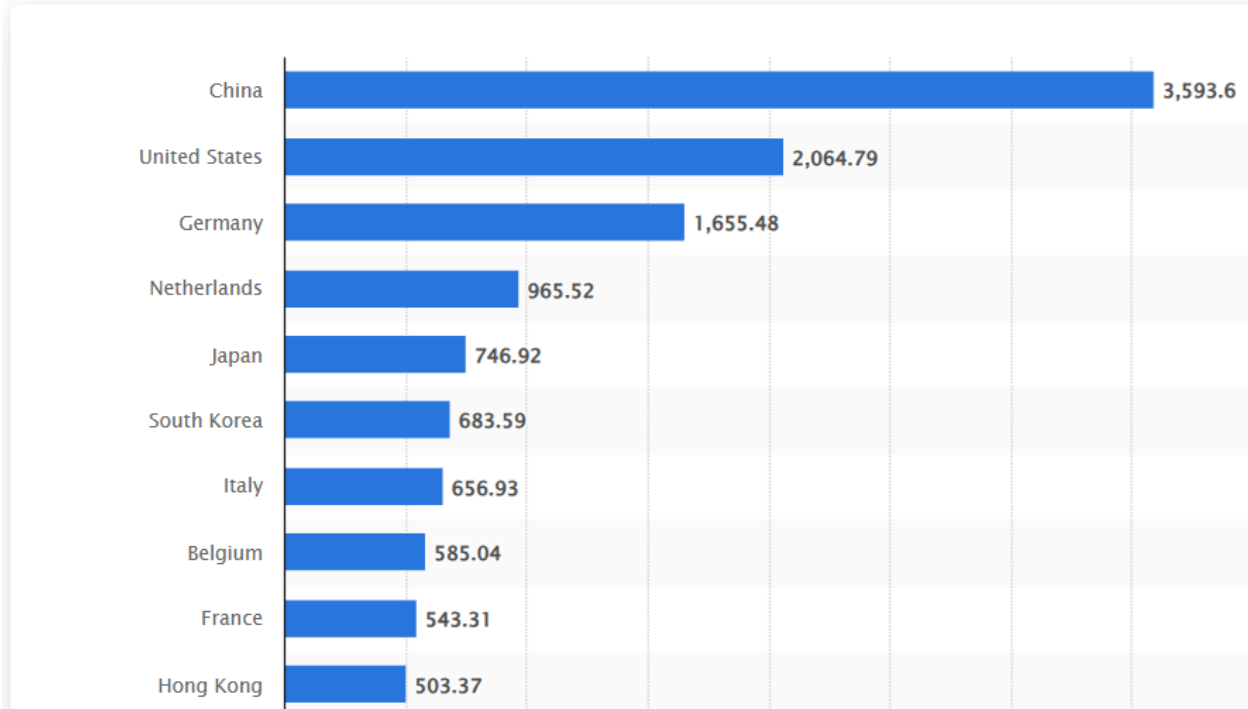
<sup>3</sup> "The \$100 Trillion Global Economy in One Chart." Visual Capitalist. <https://www.visualcapitalist.com/100-trillion-global-economy/>



This translates roughly into exports of goods, for example.

## Leading export countries worldwide in 2022

*(in billion U.S. dollars)*

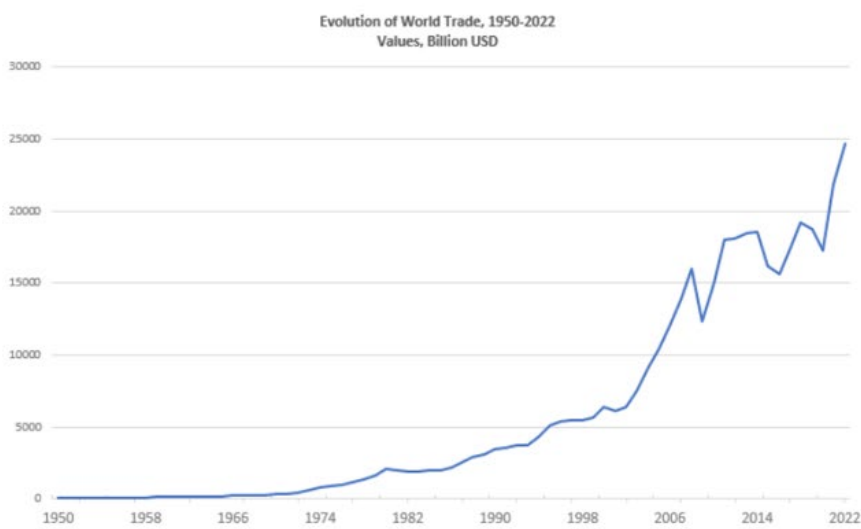
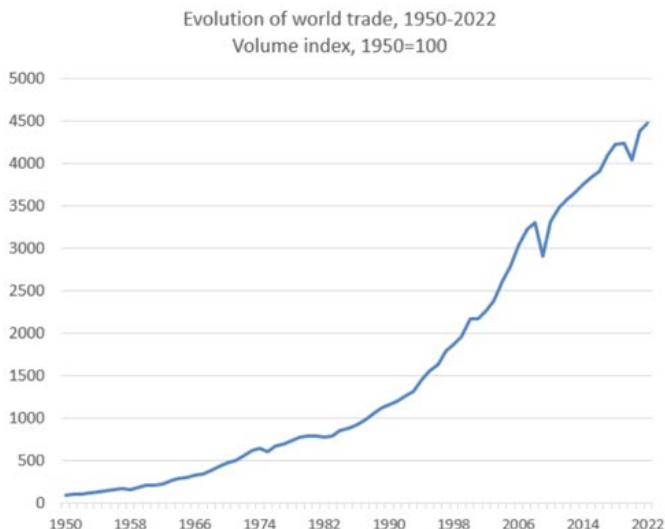


The next images consist of two graphs showing the growth of world trade in goods by volume and value. Both show steep upward curves of impressive growth from just after the Second World War to the present – a period of 75 years.<sup>4</sup> Governments in their collective wisdom, led by the United States, decided to foster international trade by eliminating trade barriers. This enabled unprecedented global economic growth, which along with technological change and investment raised hundreds of millions out of poverty, extended average life expectancies, and benefitted most of the world's peoples.

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<sup>4</sup> "Evolution of Trade Under the WTO: Handy Statistics." World Trade Organization.  
[https://www.wto.org/english/res\\_e/statis\\_e/trade\\_evolution\\_e/evolution\\_trade\\_wto\\_e.htm](https://www.wto.org/english/res_e/statis_e/trade_evolution_e/evolution_trade_wto_e.htm)

These graphs cover the duration up to the present of the multilateral trading system. As



The system was founded 75 years ago, this is its Silver Jubilee year. Japan, along with much of Asia, has been among the strongest beneficiaries of this period of extraordinary economic growth. The idea behind the system is one that Adam Smith, born 300 years ago, first identified. To maximize the benefits of specialization, the available market should be as large as possible. Adam Smith would not have been surprised at the success of Japan as a trading nation, once it enlarged its horizons to world markets with consumer electronics, automobiles, digital cameras, photocopiers, fax machines, and the like.

According to the World Trade Organization (WTO), at present world merchandise trade volume is expected to slow to 1.0% in 2023, a projection revised downward from 3.4%. Part of this slowdown is due to world GDP at market exchange rates increasing by only 2.8% in 2022 and by 2.3% in 2023 (revised downward from 3.2%). Trade and output are being weighed down by several related shocks, including the war in Ukraine, high energy prices, inflation, and monetary tightening. Also a factor is the effects of geopolitical rivalry between China and the United States.<sup>5</sup>

Trade is nevertheless likely to continue to grow. A straw in the wind is that the top two container shipping companies, accounting for 1/3 of cargoes (which in turn account for 80% of world trade), have on order an additional 150 ships. It is anticipated that total container capacity will increase by 12% during 2023/24, with growth in demand estimated at 6%.<sup>6</sup>

Paving the way for world trade growth were a series of eight rounds of multilateral trade negotiations. From 1948 – 1994, the General Agreement on Tariffs and Trade, the GATT, initially

<sup>5</sup> "Trade Growth to Slow Sharply in 2023 As Global Economy Faces Strong Headwinds." World Trade Organization. October 5, 2022. [https://www.wto.org/english/news\\_e/pres22\\_e/pr909\\_e.htm](https://www.wto.org/english/news_e/pres22_e/pr909_e.htm)

<sup>6</sup> <https://www.ft.com/content/c29a373e-4c31-4f48-ac7c-221f1d0652a7>. Financial Times, June 23, 2023.

comprised of 23 members, engaged in extensive rulemaking and liberalization. This was succeeded from 1995 – 2019, by the WTO, initially consisting of 128 members. The WTO has presently 164 members with 24 additional countries seeking membership. The WTO brought about an era of binding dispute settlement, eliminated tariffs on information technology goods, and resulted in an agreement to cut red tape at the border through the Trade Facilitation Agreement.

The outlook has become in recent years cloudy and worrisome. The intended dispute settlement process broke down with a US veto four years ago. Rulemaking ceased to be multilateral. Nevertheless, the WTO still provides much that is of value. Councils and committees are still functioning – national standards are discussed in draft and trade policies of each member are subject to periodic review. Most of the rules are still honored most of the time by most of the WTO's members, but that record is fraying.

There is a leadership gap. Beginning in 2017, the United States stepped back. It had been a driving force of the WTO. To date there has been no full substitute. China is not stepping forward. The EU, Japan, and a number of others, including Australia and Singapore, the so-called middle-grounders, are doing what they feel that they can. But it is not enough.

Frustrated with the inability to make progress with 164 members moving in step, regional and bilateral agreements have absorbed most of the negotiating energies of governments. This has been true for some time, manifested in the EU's multitude of so-called free trade agreements (FTAs), and more recently with the USMCA (updating NAFTA), the Regional Comprehensive Economic Partnership (RCEP), the CPTPP (which will include the UK, and is likely to include China, Taiwan, South Korea, and others), the African Continental Free Trade Agreement (AfCFTA), and the Digital Economic Partnership Agreement (DEPA) as examples.

At the WTO, plurilaterals have been negotiated for the domestic regulation of services, for improving the participation in trade of small businesses, and for facilitating investment for development. Japan, Singapore and Australia are leading the effort in e-commerce negotiations, with an uncertain future at this stage, as there is opposition to their being adopted as WTO agreements. At the same time, the EU, Canada, and now Japan and some others have put into effect a Multi-Party Interim Agreement for dispute settlement (MPIA), for resolving their disputes.

## **2. The US-China Strategic Competition**

According to Henry Kissinger, speaking in November 2019, the US and China were in the foothills of a new Cold War. In November 2020, he opined that the US and China were “now in the mountain passes of the new Cold War”. War, even if cold, affects trade. There is much commentary about whether the two rivals are decoupling their economies and splitting the world economy into two spheres of influence. In one of the most important pronouncements on this subject, US Treasury Secretary Janet Yellen, speaking at Johns Hopkins University on

April 20, 2023, said: “we do not seek to ‘decouple’ our economy from China’s. A full separation of our economies would be disastrous for both countries. It would be destabilizing for the rest of the world.”

There is however a clear strategic decoupling taking place, with a continuing series of restrictions being placed by the US on its exports to China, and efforts to obtain similar export restrictions from America’s allies. Speaking at Hiroshima, on May 21, 2023, at the time of the G7 Summit hosted by Japan, President Biden said “I’m not prepared to trade certain items with China. And when I was asked by President Xi why, I said, “Because you’re using them to build nuclear weapons and other weapons of mass destruction, and I’m not going to do it.” Investment screening aimed at Chinese acquisition of leading-edge technologies is also taking place in Washington and the capitals of its allies.

Jake Sullivan, US National Security Advisor, in a major economic address on April 27, 2023, described this policy in the following words: “we are protecting our foundational technologies with a small yard and high fence.” Expect this policy to be evidenced in a rolling wave of additional restrictions over time.

Decoupling as a whole is not possible, would be damaging to any economy that tried it, and is not in the cards at present, absent some dramatic change in world events. US-China trade hit a record high in 2022 (\$690 billion). It is also true that bilateral trade is easing off in 2023. This is due to the fact that many Chinese imports still bear Trump tariffs (average 3% raised to 19%), and many businesses report diversifying sourcing (with Western governments pushing policies of supply chain resilience and de-risking, as well as a usual suite of macroeconomic factors). US exports to China are declining selectively, for example, due to the fact that US exports of semiconductors and semiconductor production equipment are restricted. In addition, US airplane and auto sales are down and US energy exports are increasingly sent to Europe rather than China.

### **3. Is the World Dividing Into Two Trading Blocs?**

Coordination of allies with respect to restricting exports of some high-technology goods is taking place, and a number of governments and businesses are paying more attention to security of supply. This has been in part spurred by Europe’s experience of excessive dependence on Russia for energy. This does not translate into world commerce dividing in two, centered respectively on a Beijing and a Washington-led trading bloc. No country seeks to choose a more exclusive relationship. China and US markets are each a magnet for trade, countering substantially centripetal forces. Ten of the fourteen IPEF participants have China as their number one trading partner.

Geopolitical alignment has not created a parallel trading realignment. The creation of AUKUS, the Quad, and an alliance to deal with the Russian invasion of Ukraine has not fundamentally altered global trading patterns other than with Russia. The largest trading partner of each of America’s strongest allies in both Asia and Europe, is China. The largest non-

regional US trading partner after the EU is China. Beijing and Washington are more intent on on-shoring than friend-shoring with their respective industrial policy focus being Made in China 2025 and that contained in the US Infrastructure Investment and Jobs Act, IRA, and the Chips Act.

#### 4. US Trade Policy

There are two key concerns for the Biden Administration, one domestic and one international. Prevailing in domestic politics is seen as essential to the preservation of US democracy. An equal challenge exists in terms of geopolitics – due to the rivalry with China. A third, but nevertheless important Biden priority is dealing with climate change. This is a far cry from US trade policy as it existed prior to 2017.

The United States had been for generations the guarantor of the multilateral trading system. That system was based upon equal access to markets and equal access to supplies, first enunciated as post-war aims by Franklin Roosevelt and Winston Churchill in August 1941. It was fostered by creating in 1948 the world trading system, strengthened in 1995, founded on the rule of law, constraining government interference in trade. At the same time, during the first half of that period, eight rounds of trade negotiations swept away most of tariff protection, primarily for the developed countries. The US and Europe went further, with the elimination of tariffs in North America through the North American Free Trade Agreement (NAFTA) in 1994, and the eventual creation of the 27-member European Union, beginning with the Treaty of Rome in 1957.

For US trade policy, everything changed with the shock of the 2016 election, with the rise of US domestic populism. For Democrats, this occurred through the dominance of the progressives. Key policy themes were worker centrism and the freedom of government to regulate in the public interest. For Republicans, the change occurred through the takeover of their party by the America First (Make America Great Again - MAGA) movement. Both parties ceased to support America's embrace of international economic leadership. Neither could abide being in the Trans-Pacific Partnership that President Obama agreed to. The common elements between the two parties' trade policies were the strongly perceived need to deal with China and a willingness to provide protection to domestic industry.

The Biden Administration describes its approach as a break with "old" US trade policy, defined as excessive trade liberalization through free trade agreements (see Katherine Tai's remarks,<sup>7</sup> Jake Sullivan's remarks regarding particularly the harm allegedly caused by reducing US tariffs in the 1990s,<sup>8</sup> and comments that US trade negotiations were entered into on behalf

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<sup>7</sup> "Remarks by Ambassador Katherine Tai at the Roosevelt Institute's Progressive Industrial Policy Conference." Office of the United States Trade Representative. October 2022. <https://ustr.gov/about-us/policy-offices/press-office/speeches-and-remarks/2022/october/remarks-ambassador-katherine-tai-roosevelt-institutes-progressive-industrial-policy-conference>

<sup>8</sup> "Remarks by National Security Advisor Jake Sullivan on Renewing American Economic Leadership at the Brookings Institution." The White House. April 27, 2023. <https://www.whitehouse.gov/briefing-room/speeches->



of US multinational business interests, at the expense of American workers). The Biden Administration concluded that what was needed were industrial policy initiatives regardless of the rules of the multilateral trading system. A thoughtful and clear-eyed description of the shift in US thinking was presented by Peter Harrell, a recent former US National Security Council official at a talk at Georgetown University on June 13, 2023:

*A growing share of Americans—is re-embracing industrial policy to drive a manufacturing and middle-class employment revival here in America. And certain of the policy tools we are deploying to drive this industrial policy cut against rules we have agreed to since the 1990s. . . .The reemergence of geopolitics poses a conceptual challenge to key aspects of the global trading order, particularly to the WTO as a global baseline for global trade. . . . US and G7 policymakers today focus as much on the security aspects of trade as they do on economic efficiencies.*

Specifically, Biden’s policy rests upon the need for freedom of action to deal with trade and investment in relations with China, the need for freedom to use domestic procurement and subsidies to favor domestic industry, while urging its other countries to align their policies with those of the United States, securing the leading edge of technology, and securing supply chains as needed. Friend-shoring would be resorted to where the first set of policies upset relations with needed allies.

Export promotion, long a mainstay of policy to promote economic advancement through commerce, would no longer be mentioned or supported. The sum of the shift in US policy is that trade negotiations of a traditional sort would not be pursued. Signaling this, the Administration allowed Trade Promotion Authority to lapse.

## **5. The Evolving US-Japan Relationship, CPTPP and the WTO**

A centerpiece of the Obama Administration’s pivot to Asia was the negotiation of the 12-nation Trans-Pacific Partnership (TPP). In the 2016 Presidential campaign, Hillary Clinton distanced herself from TPP as negotiated, and Donald Trump promised to cancel it, which he did on his first full day in office. There is every sign that the Biden Administration has no plans to revisit that decision. For the present, the United States will not apply to rejoin TPP, now CPTPP. It rejects tariff negotiations as being part of an “old” approach to trade.

As for the WTO, at one point Trump threatened to leave it, but did not do so. His Administration instead pointed out deficiencies that it saw in the institution – overreach of dispute settlement, members “obtaining through litigation what could not be obtained through negotiation”, frozen outdated relative contributions of market access (a growing lack of

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[remarks/2023/04/27/remarks-by-national-security-advisor-jake-sullivan-on-renewing-american-economic-leadership-at-the-brookings-institution/](https://www.brookings.edu/remarks/2023/04/27/remarks-by-national-security-advisor-jake-sullivan-on-renewing-american-economic-leadership-at-the-brookings-institution/)



reciprocity), and failure to live up to notification obligations.<sup>9</sup> It ended binding dispute settlement for those not making alternative arrangements, and sought to block the appointment of the new Director-General that the other members had agreed to support. The Biden Administration professed its support for the WTO and unblocked the appointment of the new Director-General. It appeared that there would be a major change in policy from the Trump Administration. However, the Biden Administration continued to block the appointment of members of the Appellate Body, preventing dispute settlement from becoming binding under the terms of the WTO Agreements.<sup>10</sup> The Biden Administration also did not distance itself from the national security justification for restrictions on imports of steel and aluminum. In addition, it has not proposed any major multilateral reform initiatives.

With respect to trading relations with Japan, the Trump Administration entered into two trade agreements with Japan in 2019 (one was modest in terms of market access, with tariff concessions covering only 5% of bilateral trade).<sup>11</sup> The trade agreement provided additional market access for a list of agricultural commodities in the Japanese market, and for miscellaneous industrial items from Japan in the US market. The other of the two agreements adopted state-of-the-art commitments on digital trade.<sup>12</sup> Despite the trade agreement, Japan's tariffs on imports from China are much lower than on imports from the United States on a substantial list of products.<sup>13</sup>

During the Trump Administration, the EU, Japan and the US worked on a trilateral basis to address non-market economy practices involving subsidies and state-owned enterprises.

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<sup>9</sup> "Opening Plenary Statement of USTR Robert Lighthizer at the WTO Ministerial Conference." Office of the United States Trade Representative. December 11, 2017. <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2017/december/opening-plenary-statement-ustr>

<sup>10</sup> The Dispute Settlement Understanding.

<sup>11</sup> "U.S.-Japan Trade Agreement Text." Office of the United States Trade Representative. <https://ustr.gov/countries-regions/japan-korea-apec/japan/us-japan-trade-agreement-negotiations/us-japan-trade-agreement-text>

<sup>12</sup> "Fact Sheet on U.S.-Japan Trade Agreement." Office of the United States Trade Representative. <https://ustr.gov/about-us/policy-offices/press-office/fact-sheets/2019/september/fact-sheet-us-japan-trade-agreement>

*The United States and Japan have reached a separate agreement on a high-standard and comprehensive set of provisions addressing priority areas of digital trade. These areas include:*

- *Prohibitions on imposing customs duties on digital products transmitted electronically such as videos, music, e-books, software, and games.*
- *Ensuring non-discriminatory treatment of digital products, including coverage of tax measures.*
- *Ensuring barrier-free cross-border data transfers in all sectors.*
- *Prohibiting data localization requirements, including for financial service suppliers.*
- *Prohibiting arbitrary access to computer source code and algorithms.*
- *Ensuring firms' flexibility to use innovative encryption technology in their products.*

*The digital trade agreement with Japan meets the gold standard on digital trade rules set by the USMCA.*

"U.S.-Japan Trade Agreement Negotiations." Congressional Research Service. November 9, 2022. <https://crsreports.congress.gov/product/pdf/IF/IF11120#>

<sup>13</sup> "TTC, IPEF, and the Road to an Indo-Pacific Trade Deal: A New Model." The Atlantic Council. 2022. [www.atlanticcouncil.org/wp-content/uploads/2022/09/TTC\\_IPEF\\_and\\_the\\_Road\\_to\\_an\\_Indo-Pacific\\_Trade\\_Deal\\_-\\_pdf](http://www.atlanticcouncil.org/wp-content/uploads/2022/09/TTC_IPEF_and_the_Road_to_an_Indo-Pacific_Trade_Deal_-_pdf)

See Table 1 on page 6 for a comparison of tariffs faced by US and Chinese exporters to the Japanese market.

They called for enhanced enforcement of notification requirements and attempted to address forced technology transfer (the latter with no agreed outcome). The format was revived somewhat by the Biden Administration but was directed at a joint condemnation of forced labor.<sup>14</sup>

The primary vehicle for current US policy with respect to Asia is the Indo-Pacific Economic Framework for Prosperity (IPEF).<sup>15</sup> It does not appear that IPEF would yield firm commitments that would lead to deeper economic integration among the participants, including between the United States and Japan. No items are said to require Congressional approval, and since Congress has the Commerce Power under the US Constitution, little that is concrete and lasting can be agreed to by the US negotiators.

The “substantially concluded” IPEF Supply Chain Agreement of May 2023 was broadly welcomed by analysts given the supply chain disruptions caused by COVID and by the fallout from the geopolitical rivalry between China and the US. The agreement does not include binding (enforceable) or trade-liberalizing commitments.<sup>16</sup> It relies on exchanges of information and consultations, with soft commitments on supply chain resiliency and de-risking that raise expectations of positive behavior. The Agreement may well have the potential to have a positive impact on trade, but that is unclear. IPEF was not designed as a formal trade liberalization negotiation nor intended by the US as such but is to result in “enabling conditions” for trade. Where policy alignment might have an effect is with respect to access to critical minerals and developed countries’ support for decarbonization in the region.

Also relatively recent, on March 28, 2023, the US and Japan concluded a critical minerals agreement, designed to permit Japanese electric vehicles to qualify for subsidies granted under the Inflation Reduction Act (IRA). It stands mainly as a model of pragmatism to solve a trade problem created with an ally.<sup>17</sup> This agreement, while having a lot in the way of consultative

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<sup>14</sup> "Trilateral Joint Statement from the Trade and Labour Ministers of the United States, Japan, and the European Union on the International Labour Organization’s Global Forced Labour Estimates." Office of the United States Trade Representative. September 15, 2022. <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2022/september/trilateral-joint-statement-trade-and-labour-ministers-united-states-japan-and-european-union>

<sup>15</sup> "Indo-Pacific Economic Framework for Prosperity (IPEF)." Office of the United States Trade Representative. <https://ustr.gov/trade-agreements/agreements-under-negotiation/indo-pacific-economic-framework-prosperity-ipef>

*This framework will advance resilience, sustainability, inclusiveness, economic growth, fairness, and competitiveness for our economies.*

"IPEF Joint Statement for the Trade Pillar, Clean Economy Pillar, and Fair Economy Pillar." Office of the United States Trade Representative. May 27, 2023. <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2023/may/ipef-joint-statement-trade-pillar-clean-economy-pillar-and-fair-economy-pillar>

Its members include the United States, India, Australia, Brunei, Fiji, Indonesia, Japan, South Korea, Malaysia, New Zealand, Philippines, Singapore, Thailand, and Vietnam.

<sup>16</sup> "Press Statement on the Substantial Conclusion of IPEF Supply Chain Agreement Negotiations." U.S. Department of Commerce. May 27, 2023. <https://www.commerce.gov/news/press-releases/2023/05/press-statement-substantial-conclusion-ipef-supply-chain-agreement>

<sup>17</sup> "United States and Japan Sign Critical Minerals Agreement." Office of the United States Trade Representative.

provisions, is designed to have an actual economic impact, due to the qualification for IRA benefits. Among the provisions is an agreement to confer “appropriate domestic measures to address non-market policies and practices of non-Parties affecting trade in critical minerals”.<sup>18</sup>

The US approach is not to enter into comprehensive trade agreements, such as an FTA, a new TPP, or even a broader and shallower RCEP, but to selectively address some positive elements to facilitate trade that it favors, and to discourage trade which it disfavors. It downplays the possibility of obtaining enforceable global rules. It acts inconsistently with existing obligations requiring non-discrimination or national treatment where industrial policy objectives or strategic security interests exist.

## 6. The Future of International Trade – Recommendations (In the Context of US-Japan Relations)

Adam Smith did not get it wrong. It is advantageous for every nation seeking to increase the well-being of its citizens to make the market available for its products (including now services) as broad and accessible as possible, which means trade across international borders that is as open as possible. This policy, giving freedom to those who have something to sell and those who have a desire to buy the opportunity to do so, is the engine of prosperity that the world has in general benefitted from over the last three-quarters of a century.

Adam Smith also recognized that domestic policies would be needed to treat individuals fairly (he addressed the need for reasonable levels of rent for workers, for example) and took into account overriding demands of what we call today “national security”. Openness must be accompanied by care for the distribution of benefits under domestic laws as well as assuaging harms with effective trade remedies. This is not something the US has done well. In the administration of trade policy, trade remedies must be available and be deployed to avoid short-term injury. It must be conceded that trade must operate within strategic considerations. For the US this has become paramount. However, it is imperative that the policy result in a stronger US economy, not a weakened one. In addition, the concerns of allies must be taken fully into account, or the policy will be self-defeating from a national security point of view. In today’s world, trade policy must also take into account sustainability as part of an obligation of stewardship of the physical planet. With all of these social considerations added, international trade must still deliver economic growth, food security, and generally freedom from want.

Japan, the European Union, and until recent years, the United States, a sizeable group of “middle grounders” (mid-sized trading nations, such as Canada, Switzerland, Australia, South Korea, and New Zealand) as well as a number of developing countries (such as Costa Rica, Chile, and Brazil) have emphasized the need for global trade rules, for transparency, and to avoid

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March 28, 2023. <https://ustr.gov/about-us/policy-offices/press-office/press-releases/2023/march/united-states-and-japan-sign-critical-minerals-agreement>

<sup>18</sup> "Agreement Between the Government of the United States of America and the Government of Japan on Strengthening Critical Minerals Supply Chains." Office of the United States Trade Representative. March 28, 2023. <https://ustr.gov/sites/default/files/2023-03/US%20Japan%20Critical%20Minerals%20Agreement%202023%2003%2028.pdf>

backsliding with respect to the level of openness already achieved for international trade. Japan has taken the lead, since the Abe Administration, in supporting efforts to achieve rules for the world of digital commerce. It is a co-convenor (with Singapore and Australia) of the e-commerce negotiations at the WTO, which is styled a Joint Statement Initiative.

Some recommendations:

#### A. A New Ottawa Group

Japan was an active member at the WTO of the Ottawa Group of the “middle-grounders”, which included Australia, Brazil, Canada, Chile, the European Union, Japan, Kenya, South Korea, Mexico, New Zealand, Norway, Singapore, Switzerland and the United Kingdom, focusing on WTO reform. A group of this kind should be convened with membership based upon a common desire to improve the world trading system. Japan could take the initiative of reaching out to like-minded WTO members to begin the process. This would not be to the exclusion of their outreach to the United States and China. But some momentum may first have to be built to attract their and others’ engagement. The group should refer to the Riyadh Initiative on the Future of the WTO (initiated by Saudi Arabia during its G20 presidency) for a list of agreed common WTO principles and then work to expand the area of consensus.

#### B. Strategic Foresight

Geopolitics and national economic interest dictate that the United States and Japan work more closely at bilateral policy integration. A good start would be the creation of a joint strategic US-Japan foresight exercise, identifying the challenges of the future in detail. The EU Commission has celebrated Japan’s leadership in strategic foresight, from beginnings in substance with the Meiji Restoration to having since 1970 “developed a world-leading capacity for foresight”.<sup>19</sup> This process could equally be trilateral, with the participation of the European Strategy and Policy Analysis System (ESPAS). The three should also support the creation of strategic foresight capabilities at the WTO Secretariat, with which to interact on global trade issues. In select areas of common interest, this process can lead to joint policy planning on a bilateral or trilateral basis, with the inclusion of others as common interests permit.

#### C. The Geopolitically Tinged Rubik’s Cube of Trade Policy

The most challenging near-term aspect of trade policy is managing strategic de-coupling, or what EU Commission President Ursula von der Leyen and now others have termed “de-risking”, namely incorporating security interests into economic and commercial interests. Governments have a responsibility to balance a variety of domestic interests and also find a means to cooperate with other nations. The US, Japan, the EU (and to a degree each of its

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<sup>19</sup> "Japan's Global Vision: Tokyo's Evolving Foresight Practices, Indo-Pacific Strategy and EU-Partnership." European Parliament. December 8, 2021.

[www.europarl.europa.eu/RegData/etudes/BRIE/2021/698051/EPRS\\_BRI\(2021\)698051\\_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/BRIE/2021/698051/EPRS_BRI(2021)698051_EN.pdf)

Member States) will have differing assessments of the optimal balance of de-risking, on the one hand, and maintaining and expanding non-strategic trade, on the other. It will be all too easy to see too much of trade in some sense as dual-use. If a product, service or technology does not have any direct military application, providing it may nevertheless strengthen the economic position of another party, or deepen a country's dependence on a foreign source of supply. Countries with aligned interests need to coordinate, and those with opposing interests need to be consulted, to avoid excessive and unnecessary damage to trade and those engaged in it. In most cases, the relevant expertise to make judgments will lie with those engaged in production and trade in any good, service, or technology. The United States and its allies need to take consider a trade policy that has de-risking but also considers the appropriate terms for non-strategic trade with China.

#### D. Japan's Engagement with the US

##### (1) Bilateral Mini-Deals

A major objective should be to improve wherever possible the bilateral trading relationship. The two trade agreements entered into by the US and Japan in 2019 are a beginning. They were termed "stage one" of a broader formal trade relationship presumably for cosmetic WTO-compatibility reasons. This concept however should be made a reality. The stage one agreements located a few tariff lines for liberalization and the digital commerce area for progress on rules. This was followed by the Critical Minerals Agreement. Businesses will know best where commercial priorities lie.

US willingness to deal with trade areas selectively is indicated both by these specific areas for agreements with Japan, but also by the recent agreement between the US and the United Kingdom. President Biden and Prime Minister Sunak announced a few weeks ago at a joint press conference at the White House, a series of mini-deals regarding artificial intelligence, critical minerals, clean energy and security. The agreement with the UK is not an FTA, nor even a proto-FTA, but relies on investment, agreed policy coordination, and collaboration in research.<sup>20</sup> The current US negotiating posture favors mini-deals of this sort. The openness to this form of engagement should be fully explored, as there is much mutual benefit that can be gained between Japan and the United States with this approach, short as it is of a broad negotiation. Mini-deals should be viewed and constructed in a manner that paves the way for a broader bilateral agreement, as well as ultimately for regional and multilateral agreements.

##### (2) Joint Efforts to Improve IPEF

Analysts at the Center for Strategic and International Studies (CSIS) studying the IPEF Supply Chain Agreement have suggested that the political commitments be made enforceable, and that funding be supplied to provide the necessary capacity to assure that implementation

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<sup>20</sup> "U.S.-Japan Trade Agreement Text." Office of the United States Trade Representative. <https://ustr.gov/countries-regions/japan-korea-apec/japan/us-japan-trade-agreement-negotiations/us-japan-trade-agreement-text>

takes place.<sup>21</sup> Also suggested is that for critical minerals the country coverage of understandings should be broadened. Asia Society commentators point to the utility of an early warning system, the creation of a crisis response mechanism to enable governments to collaborate and collectively manage external shocks from outside the IPEF group of countries, establishing joint guidelines for the application of export restrictions, co-investment opportunities to support supply chain resilience, mapping of availability of critical minerals, and other initiatives worth exploring in the context of IPEF.<sup>22</sup>

Most informed observers state that without the US offering market access, the results from IPEF will be limited. Additional efforts should be made to identify means of inducing further international cooperation. Investment, technical assistance, and financial aid may have to take the place of market access in the near-term.

Informed commentators suggest that the IPEF participants make their objectives and obligations concrete rather than just issue statements of agreement-in-principle, and that governments deepen consultations with stakeholders.<sup>23</sup> The USTR is correct that labor and environmental organizations need to be heard. But it is also true that those who wish to provide goods and services across borders or gain access to them have much of the information needed for making informed decisions on structuring negotiations and choosing negotiating objectives. This information is derived from the experiences of those engaged in global commerce, regardless of the size of the company.

### (3) Smoothing the Path for US Re-Entry into TPP/CPTPP, or a Successor “Regional” Agreement

The domestic political environment for the US rejoining a form of TPP is not present nor expected to be present any time soon. Nevertheless, all engagement with the United States on trade issues should be viewed through the lens of whether they improve the prospects for there being a docking mechanism for US to rejoin CPTPP (or a successor agreement) when the political environment is more propitious. Some elements will likely need to be added to secure the US re-docking.

There is likely to be a US decision point on re-entry when China advances in its CPTPP accession process. A cautionary note is needed for those negotiating China’s entry. In my negotiations with Japan on behalf of the US government, my counterparts often cited the Asian saying, “sleeping in the same bed, dreaming different dreams”. It would have been good if this

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<sup>21</sup> "Assessing IPEF’s New Supply Chains Agreement." Center for Strategic and International Studies. May 31, 2023. <https://www.csis.org/analysis/assessing-ipefs-new-supply-chains-agreement>

<sup>22</sup> "Strengthening Regional Supply Chain Resiliency Through the Indo-Pacific Economic Framework (IPEF)." Asia Society. May 2023. <https://asiasociety.org/policy-institute/strengthening-regional-supply-chain-resiliency-through-indo-pacific-economic-framework-ipef>

<sup>23</sup> "What is the Indo-Pacific Economic Framework and Will It Work?" Peterson Institute for International Economics. December 12, 2022. <https://www.piie.com/blogs/realtime-economics/what-indo-pacific-economic-framework-and-will-it-work>

had been more clearly understood when China acceded to the WTO. No country (other than perhaps China) active in the process of China's accession to the WTO would have thought that there was any question that the WTO was based on its members' economies being "market oriented". The disagreement on this point, evident in recent WTO debates and the conclusions reached in the Riyadh Initiative on the Future of the WTO, points to the need to make the basic principles for involvement in the CPTPP crystal clear and explicit.

#### E. The Role of Business in International Negotiations

A well-ordered government relies heavily on those engaged in commerce to provide the information needed to identify national commercial interests and help prioritize them for international negotiations. The American Chamber of Commerce of Japan (ACCJ) has demonstrated that it is well-positioned to advise negotiators who are willing to listen on key subjects involving improving the context in which US-Japan trade takes place. In particular, given geopolitical realities, the input from ACCJ in its paper "ACCJ Principles for Promotion of Economic Security" should be stressed with US national security, trade and commerce officials, members of Congress and the public, as well as Japanese officials and Diet members. The continuing roll-out of additional restrictions on US-China trade with spillover effects on Japan will make these ACCJ-recommended principles of continuing relevance.

Business has an imperative to make sure that its core interests figure into the mix of influences on policy formation, as well as persuading parties to negotiate appropriate international outcomes. Business and national interests are not necessarily identical, but government policy for commerce if not well-informed on the impact on actual commerce is likely to be harmful both to business and national economic and security interests.

The two additional ACCJ-identified areas of focus, the Japan Digital Agenda 2023 and the ACCJ Financial Services Forum White Paper "Re-imagining Japan as a Global Financial Center" are valuable input as well. With respect to the Japan Digital Agenda 2023, this should be extended into adoption within IPEF to the extent possible, mandating free data flows in line with the United States-Mexico-Canada Agreement (USMCA) and U.S.-Japan Digital Trade Agreement (USJDT). With respect to making Japan a Global Financial Center, it is important to continue to press the Japanese government to continue making progress in corporate governance reform as the best hope for it to enhance its status as a global financial center.

#### **Overall Conclusion**

International commerce has always been subject to less predictable conditions to a far greater extent than is true within any single market, whether the EU, the US or Japan. In the case of international commerce, key variables will include:

- continued major power rivalry and potential retrenchment (i.e., onshoring)
- repetitive instances of US-China conflicts, or worse
- waves of repeated instances of strategic decoupling



- continued attempts to diversify sourcing
- continued efforts by China at outreach through RCEP, CPTPP, BRI, AIIB, and bilateral finance
- continued US engagement through IPEF/TTC/Americas, PGII,<sup>24</sup> etc. and
- the effects on world trade from the war in Ukraine

If one accepts that there is a new Cold War already in progress, it must be managed toward détente. For global challenges, global responses will be necessary, particularly with respect to climate change and future pandemics. The capacity for providing international leadership is not solely based on size, but on ingenuity and dedication. Japan has a vitally important role to play.

It is easy to be too negative about the future of international trade. Globalization, as a policy, has ended. Globalization, as a reality, has not. The United States will discover once again (as Japan knows well) that 96% of the world's consumers live outside its borders. Ultimately, market forces resist being contained. Multilateral rules and general trade liberalization made sense for decades and they still do. The trade policy that created global economic growth will return, paired with societal and strategic concerns.

Business can and should make a difference. Peter Drucker, the famous 20<sup>th</sup>-century management consultant, pointed out the responsibility of leaders of corporations to shape the external environment in which they conduct business. He meant this in a pro-competitive sense but indicated that it was not enough to care about the quality of the product that was being produced, but to make sure that public policies were conducive to allowing market forces largely to determine competitive outcomes.

There is a key role for ACCJ to play in shaping that environment, particularly for US-Japan trade and regional trade relations.

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<sup>24</sup> "Partnership for Global Infrastructure and Investment at the G7 Summit." The White House. May 20, 2023. <https://www.whitehouse.gov/briefing-room/statements-releases/2023/05/20/fact-sheet-partnership-for-global-infrastructure-and-investment-at-the-g7-summit/>