
2 Unravelling Trade: Global Institutional Change and the Pacific Economy

JOHN GERARD RUGGIE

Whoever invented the old schoolyard saw that sticks and stones but not words have painful consequences must have led a very sheltered life. Much the larger number of us, I suspect, responded to the power that words wielded in our schoolyards *with* sticks and stones. An analogous situation exists in the international trade arena today, where the power of words to evoke virulent, even if not as yet violent, actions seems exceedingly high. That potential is particularly great in the Pacific, in part because it is the fastest-growing region and the one that can boast of the largest number of new entrants into the tournament of major economic players. The end of the Cold War, which had muted the intensity of trade disputes in the past, can only exacerbate this already menacing situation.

The chief verbal demons the force of which we must learn to exorcise are the terms 'free trade' and 'protectionism'. If they are allowed to continue their privileged role in framing public and to some extent even academic discourse concerning international trade, then any relevant remnant of the GATT-based (General Agreement on Tariffs and Trade) trade regime is doomed, and with it world economic stability. Contrary to what liberal economists would like us to believe, free trade in the sense of unrestricted trade has never been GATT's mandate. Commenting on the negotiations for an international trade charter in 1947, Jacob Viner wrote: 'there are few free traders in the present-day world, no one pays any attention to their views, and no person in authority anywhere advocates free trade' (Viner 1947, p. 613). Even for the relatively more liberal United States, the international edifice of the 'open door' had to accommodate the domestic interventionism of the New Deal. No country

anywhere was prepared then—or at any time since—to subordinate domestic stabilisation to free trade.

At the same time, the GATT-based political regime for the governance of international trade relations sought to ensure that domestic interventionism did not reproduce the mutually destructive consequences of the inter-war period. Out of those twin concerns emerged an institutional compromise that I have elsewhere described as ‘embedded liberalism’ (Ruggie 1982, 1991a).¹ Unlike the economic nationalism of the 1930s, the international economic order would be multilateral in character; but unlike the liberalism of the gold standard and free trade, its multilateralism would be predicated upon domestic interventionism. Domestically this was a compromise between the major societal groupings (agriculture, labour and capital), as well as between export-oriented and import-competing industries. And it was a compromise between the legislative branch, which retained the right to authorise trade negotiations and to ratify their results, and the executive branch, which was given the right to conduct trade policy. Internationally it was a compromise between the United States, where domestic stabilisation measures remained the least comprehensive and systematic and the most constrained by opposition, and the European states, where rejection of liberal orthodoxy was universal but the objects of economic protection varied widely among the left, right and centre of the political spectrum.²

Once negotiations on post-war commercial arrangements got under way seriously in the context of an international conference on trade *and* employment, the principles of non-discrimination and tariff reduction were affirmed, but so were safeguards, exemptions, exceptions and restrictions—all designed to protect the balance of payments and a variety of domestic social policies. The proposed charter for an all-encompassing International Trade Organisation became internally so inconsistent that it is difficult to say just what sort of regime it would have given rise to. In any case, the US Senate refused to ratify the charter, it being too intrusive

¹ A more detailed discussion of the origins and characteristics of the embedded liberalism compromise may be found in Ruggie (1982, 1991a). See also Ikenberry (1992). I adapted the term from Polanyi (1944). In it, he developed a distinction between ‘embedded’ and ‘disembedded’ economic orders: ‘normally, the economic order is merely a function of the social, in which it is contained...Nineteenth-century society, in which economic activity was isolated and imputed to a distinctive economic motive, was, indeed, a singular departure’ (p. 71).

² This was true even in Great Britain, where Labour sought to institute systematic national economic planning, which in all probability would have entailed deployment of discriminatory instruments of foreign economic policy, while the Tories remained committed to imperial preferences, which were inherently discriminatory in character (see Gardner 1980, ch. 1). In Scandinavia the overriding objective of domestic economic policy was the achievement of full employment (Paavonen 1983).

for some and not activist enough for others, as a result of which a far smaller domain of commercial relations became subject to the international regime than would have been the case otherwise. Among the most important areas excluded were the regulation of commodity markets, restrictive business practices, and international investments—the absence of which has severely plagued the international trade regime in recent years. The more traditional concerns of commercial policy—tariffs, quotas and the like—were addressed by the GATT, which the United States quickly helped to form and joined by executive order.

The GATT made obligatory the most-favoured-nation rule but a blanket exception was allowed for all existing preferential agreements (a United States concession to Britain), and countries were permitted to form customs unions and free trade areas (United States encouragement to Western Europe). Moreover, quantitative import restrictions were prohibited but were deemed suitable measures for safeguarding the balance of payments—*explicitly* including payments difficulties that resulted from domestic full employment policies. They could also be invoked in agricultural trade if they were used in conjunction with a domestic price support programme. The substantial reduction of tariffs and other barriers to trade was called for but it was *not* made obligatory, and it was coupled with appropriate emergency actions, which were allowed if a domestic producer was threatened with injury from import competition that was due to past tariff concessions. The Agreement also offered a blanket escape from any of its obligations provided that two-thirds of the contracting parties approved—the United States availed itself of the opportunity to exclude its entire agricultural trade from international scrutiny. Lastly, procedures were provided to settle disputes arising under the Agreement and for the multilateral surveillance of the invocation of most (though not all) of its escape clauses. The principle of reciprocity was enshrined as a code of conduct to guide both tariff reductions and the determination of compensation for injuries suffered.

If we use this actual historical compromise of embedded liberalism as the baseline for assessing the conduct of international trade relations today rather than the textbook models, then much of what has passed for protectionism in recent years must be sifted through rather carefully and the real stuff separated out from what may be little more than creative adaptations of the embedded-liberalism framework. That task is taken up in Part 1 of this chapter. The more problematical shift towards strategic unilateralism in trade policy on the part of the United States is addressed in Part 2.

Using this historical baseline also helps to contextualise and therefore hopefully to understand better certain new features of international economic transactions. The creators of the trade regime presupposed several key institutional parameters when they constructed the regime within which movement towards freer trade and away from protectionism had reasonably stable meanings. Three of these institutional assumptions, in particular, have become increasingly undermined over time: (i) that the

major impediments to international economic transactions are point-of-entry barriers or government cheating; (ii) that the typical international economic transaction consists of the exchange of tangible products supported—or literally serviced—by the attendant invisibles sectors; and (iii) that international economic transactions are conducted at arms-length and take place between disjoint and unrelated national economic units. As discussed in Part 3, changes in these institutional parameters have eroded the efficacy of the trade regime and its most common adaptive forms, but in a manner that free-trade/protectionist rhetoric does little to elucidate.

If, however, the language of free trade and protectionism is not up to the task of expressing the resultant problems fully, how then should they be depicted? I take a stab at this question in the conclusion.

1. The new protectionism

Today, the post-war compromise is at risk in the area of international trade (see Bhagwati 1991a). But free-trade/protectionism rhetoric does little to clarify the nature of the risk. For twenty years now, liberal internationalist commentators have cried wolf. For twenty years now, they have been detecting a 'disastrous isolationist trend' in US foreign economic policy, warning of 'the first real international trade war since the 1930s', and reminding us that 'trade wars could become full economic wars, precisely as they did under similar international conditions in the 1930s' (Bergsten 1972). If imminence fails to materialise over such an extended duration, however, then it is worth exploring whether there may be something amiss, not in the world of actual state behaviour, but in the model of state behaviour that analysts are bringing to bear on it. That, at any rate, is what I intend to do.

The facts of the matter regarding the so-called *new* protectionism are straightforward and beyond dispute—the referent being various forms of administered and negotiated non-tariff restrictions on imports. For example, a recent GATT study reports on the bilateral voluntary export restraint arrangements (VERs) known to have been in effect at the end of 1987. The product categories affected include textiles and clothing (71 arrangements outside the Multifibre Arrangement); agricultural and food products (58); steel and steel products (52); electronic products (23); automobiles and transport equipment (20); footwear (15); machine tools (13); and miscellaneous (25). 'The majority of the arrangements protect the EEC market or the market of one of its member States, followed by the US market; these two account for just over three quarters of the measures listed. The arrangements mainly limit exports from Japan (38 arrangements), the Republic of Korea (35), the EEC (15) and Taiwan (13)' (GATT 1988, ch. 7). In addition, many of the countries subject to voluntary export restraints also faced anti-dumping and countervailing duty actions. Lastly, it is clear that the use of mechanisms of this sort has increased over the years.

In short, it is not the facts themselves but what they signify that is at issue. To assess what they signify, let us look first at the quantitative dimension of the issue and then at the alleged problem of coercion and discrimination that it raises.

How much? Of what?

Quantitatively there is overwhelming evidence that among the Organisation for Economic Cooperation and Development (OECD) movement towards greater international openness by an economy is statistically closely associated with governments expanding their domestic role via adjustment and distributive policies—and that openness overrides virtually all other domestic economic and political differences among them in doing so (see Cameron 1978). Thus, as trade barriers have come down governments have become more active in managing the consequences. That much is almost axiomatic. Furthermore, in managing the consequences of greater openness generally speaking ‘governments merely attempt to mitigate the negative effects of trade liberalization on specific industries and not to offset them entirely’ (Blais 1986, p. 210).³ As a result, despite the recent proliferation of instruments of the ‘new protectionism’, the markets of the industrialised countries are more open today than they were only a decade ago (GATT 1988; United Nations Conference on Trade and Development (UNCTAD) 1989).

This apparent anomaly has led the distinguished international economist Jagdish Bhagwati to puzzle why ‘the growth of protectionism appears significant but its consequences do not’ (Bhagwati 1988, p. 56). Judith Goldstein, in an exhaustive study of all statutory restraints imposed by the United States since the 1950s, documents the same puzzle: while access to the institutions of administered protection has been progressively eased, and while these institutions have been increasingly pressed for protectionist measures, they ‘have not become increasingly protectionist over time’ (1986, p. 179; 1988).⁴ In point of fact, there is every evidence to suggest that they are not intended to be protectionist in the conventional sense of the term (see also Finger 1981; Finger et al. 1982; Nelson 1987, 1989; Aggarwal et al. 1987; Morici & Megna 1983; Yoffie 1983). (The

³ Andre Blais (1986) examined the impact of a country’s economic size, level of affluence, rate of unemployment, and the presence of left-wing parties in its electoral system—and all were outweighed by openness in determining the level of industrial subsidies, thereby confirming the findings in Cameron’s study, which focused on public expenditures.

⁴ Goldstein examined the invocation of five statutory provisions to restrain imports into the United States: escape clause, anti-dumping, countervailing duties, adjustment assistance, and unfair practices related largely to patent claims.

corresponding situation in the European Community (EC) admittedly is more complex.)⁵

But within the embedded-liberalism framework, there is no anomaly to begin with: in terms of its overall balance of political objectives, this was how the trade regime was expected and designed to function. It is free-trade rhetoric that has produced the anomaly. From the vantage point of the embedded-liberalism compromise, the bulk of the 'new protectionism' may be seen instead as norm-governed institutional adaptation to a very different international competitive environment than existed in the past.

The embedded-liberalism baseline also suggests a critical difference between such instruments of administered protection as VERs, anti-dumping and countervailing duty investigations, and the like, and the more pernicious form of 'managed trade'. Most instruments of the so-called new protectionism do not seek to fix bilateral or overall market shares, but to slow down or limit the rate of increase in imports in the attempt to give domestic industry time to adjust to a new competitive situation. Moreover, they tend to be of limited duration: as Aggarwal and his colleagues show, the longevity of these instruments exhibits distinct patterns which largely reflect industry structure, and the majority are not permanent (Aggarwal et al. 1987).

What is euphemistically described as 'managed trade', however, does constitute a serious deviation from the norm. Under it, instead of merely limiting adjustment costs, governments in essence, and sometimes explicitly negotiate market shares. The controversial side-letter to the 1986 semiconductor agreement between the United States and Japan, which promised the United States a 20 per cent market share in Japan within a five-year period, is a case in point (Prestowitz Jr, 1988, ch. 2). The Multifibre Arrangement is another.⁶ But 'managed trade' by far remains the exception to the rule.

In sum, within the embedded-liberalism framework, the puzzle posed by the new protectionism is no puzzle at all.

Coercive discrimination?

Let us turn next to the allegedly coercive and discriminatory treatment that VERs and other such 'orderly marketing arrangements' are said to embody. Exporters typically act under the threat of worse to come if they

⁵ As Martin Wolf has put it, the EC 'is not only itself a discriminatory trading arrangement, if looked at as a collection of separate countries, but is embedded in concentric circles of discrimination' (1987, pp. 56–7), consisting of a variety of preferences and restraints. *The Economist* (1991a), reports a less than flattering GATT study of Community practices.

⁶ The Multifibre Arrangement started on the VERs side of the ledger, but over time it has shifted to the 'managed trade' side—from embedded liberalism to illiberal protectionism (see Aggarwal 1985).

fail to reach agreement with the importing country—hence, the accusation of coercion if not outright relapse to the rules of the jungle.

Two counterarguments come to mind. First, it is well known by now that VERs and like instruments typically transfer the scarcity rents produced by government intervention in the importing country to the *exporter*, and that they are paid by consumers in the *importing* countries. Paying off exporters at the expense of one's own consumers is a very odd form of international coercion—indeed, so odd that Japanese automobile manufacturers decided unilaterally to impose such an arrangement on themselves as they shifted their efforts in the United States from selling medium-priced models to capturing the luxury market from European exporters!

Second, those who charge coercion typically ignore the fact that not only the threatened unilateral but even the existing *multilateral* alternative to VERs would leave exporters *worse off* than VERs do. As Hindley has pointed out, 'for most countries confronted with a request for a VER the alternative, should they refuse, is not unrestricted trade but an Article xix emergency action [under the GATT]. In that event, the exporting country will find itself faced with a tariff on its exports or by formal quota restrictions on them with the quota rights going to importers...rather than to exporters. In either case, the profits of the exporting industry will be reduced...' (Hindley 1980, p. 321). What is more, unlike the case of VERs, there is no effective time limit on how long Article xix safeguards may remain in force; as noted above, VERs generally do have such a limit at the end of which they either expire or must be renegotiated. Finally, no country claiming injury under Article xix has ever had its claim challenged. In any practical as opposed to a purely rhetorical sense, therefore, the charge of coercion is specious: the exporting industry typically gets a better deal under VERs than it would under the legally prescribed, multi-lateral alternative (Hindley 1980; see also Ono 1991).

The charge of discrimination is somewhat more complex. That these measures are discriminatory cannot be questioned; it is the very reason they are invoked. The real issue, however, is whether VERs or the legally permissible alternative, again Article xix under the GATT, do more collateral damage to the trade regime. And it is not obvious that Article xix should be preferred on those grounds. Article xix permits alteration or suspension of past tariff concessions in a non-discriminatory manner provided that interested parties are consulted. But it is clumsy. Precisely because of the necessity to apply it in a non-discriminatory manner, the invocation of Article xix is likely to affect innocent bystanders adversely—bystanders who are not causing injury to domestic producers in the initiating country. Thus, it may require widespread and lengthy renegotiation or even trigger retaliatory suspension of past concessions.

Finally, to retort that Article xix action, nevertheless, is to be preferred on principle because that is what the GATT calls for while VERs are 'GATT-illegal', simply will not do. It is a perfect example of what Robert

Aliber in another context sardonically described as 'sacrificing the state to save the constitution' (Aliber 1986, p. 120). No rational government can be expected to follow that precept when well-established and apparently acceptable alternatives are available. Moreover, the term 'illegal' is itself problematical in this context. The trade regime is at least as much a political institution as it is a set of legal prescriptions. As such, the intersubjective appraisal by states of one another's actions based on the normative understandings among them count at least as much as legally prescribed rules and procedures. And even in strictly legal terms, Hindley makes an excellent point in dismissing criticisms of VERs on the grounds that they violate the law: 'A much better analogy is the out-of-court settlement of civil legal actions, a procedure whose outcome is constrained by the law, but which both parties to the dispute expect will leave them better-off than undergoing the expenses of the full judicial process. No legal system will collapse as a result of such agreements (on the contrary, if there were no such agreements collapse would be very much more likely)' (Hindley 1980, pp. 331-2).

Let me summarise what has been said thus far. The multilateral trade regime has changed in many ways over the course of the post-war era as is only to be expected. Among those changes are the invention and deployment of mechanisms, which in a literal or formal sense may well be 'illegal' within the GATT. Nonetheless, I have resisted the notion that these mechanisms demonstrate a resurgence of protectionism. Of course countries cheat: they always have; they always will; and their propensity to cheat is likely to be higher in hard times. But there are sound reasons to reject the 'new protectionism' paradigm. First of all, it views the trade regime from a free-trade baseline. But that view is historically inaccurate and fundamentally distorts the nature of the post-war institutional compromise. Second, it has to dismiss as anomalies the most interesting and widespread innovations in the international trade regime, innovations that seem reasonably consistent with the actual shape of the post-war institutional compromise. Third, those who subscribe to the 'new protectionism' paradigm repeatedly expect governments to follow prescribed collective procedures even when those procedures cannot possibly yield collectively desired outcomes. Not surprisingly, governments rarely oblige. Fourth and finally, condemning all such practices with the single opprobrium of 'protectionism' makes it impossible to identify those specific practices, such as negotiating market shares under 'managed trade' arrangements, which do violate and corrode not only the letter but also the spirit of the post-war institutional compromise, and which should, therefore, be controlled.

2. Aggressive unilateralism

No matter what the economic inefficiencies and bureaucratic inanities of the 'new protectionism' may be, then, within the embedded-liberalism framework many of its instruments appear relatively benign and, indeed, are part and parcel of the techniques by which the multilateral trade regime functions. But can the same be claimed for the alleged 'aggressive unilateralism' (Bhagwati & Patrick (eds) 1990) in recent US trade policy? If inter-war bilateralism was the evil that energised the creation of the post-war multilateral trade regime, then unilateralism must be even more noxious.

The chief culprit here, of course, is the amended Section 301 of US trade legislation (Omnibus Trade and Competitiveness Act of 1988), especially the so-called Super 301. Under this provision the United States asserts the right to act as accuser, judge and jury in assessing unfair trading practices by others, and to impose punishment on those it finds guilty. It is clearly GATT-illegal, even under the creative and sophisticated standards of 'justified disobedience' that Robert Hudec has devised (1990). And the potential for deleterious and even destructive consequences for the international trading order is high.

It is worth examining the reasons for Super 301, however, before speculating about its adverse impact. Three stand out. One is the macroeconomic policies of the first Reagan administration, which produced record budget and trade deficits. Super 301 is no cure for that problem, as the Congress should have known if it did not. In any case, thus far the provision has not been invoked by the United States towards that end.

A second reason is precisely the fact that most instruments of the 'new protectionism' have had such a minimal impact. Super 301 imposes more severe constraints on the discretion of the executive branch than did its predecessors because in the past it was executive-branch discretion that buffered protectionist demands. Now, it has been an article of faith among students of trade policy that the executive branch is more 'enlightened' than the Congress in these matters. But keep in mind that it was Congress that mandated executive-branch discretion in the first place, thereby giving itself the opportunity to be responsive to constituency demands while at the same time avoiding serious damage to the international trade regime. By the mid-1980s Congress felt that the executive branch had become too passive.⁷ Thus, it altered the strategic balance between the two branches.

⁷ According to former ITC chair Paul Stern, even during the record-breaking trade deficits under the Reagan administration, 'less than 1 percent of total U.S. imports were actually challenged as unfair under U.S. laws. The volume of U.S. imports affected by anti-dumping and countervailing duty investigations as a percentage of total imports amounted to only 0.2 percent in 1987, 0.4 percent in 1988, and 0.2 percent during the first half of 1989. Even in the cases where the

The third reason for Super 301 can be put simply: Japan. Even though the amendment is expressed in universalistic language and three 'unfair' traders were identified in its first year of operation, it would never have been adopted were it not for Japan.⁸ Specifically, the provision is aimed at removing Japanese policies and practices which the United States claims have kept the Japanese domestic market relatively sheltered against foreign competition and thereby contributed to the seemingly permanent \$40–\$50 billion annual bilateral trade imbalance in favour of Japan.

I enter this realm with great trepidation for it is utterly treacherous terrain for the uninitiated. Experts argue vehemently about even the most basic of facts: for instance, is Japan's level of manufactured imports substantially below what would be expected of a country its size and level of industrialisation, or does it fall within the margin of error?⁹ And the US Congress has never been known to exhibit great skill in economic analysis, and surely had some cause/effect relations and orders of magnitude wrong.

In these infelicitous circumstances, the safest move for me is to take refuge once again in the embedded-liberalism compromise. According to Richard Cooper, in neo-classical theory intra-industry trade is viewed as less socially profitable than inter-industry trade, all other things being equal (Cooper 1980, especially pp. 75–6). And yet governments in successive GATT rounds have encouraged the liberalisation precisely of intra-industry rather than inter-industry trade. The result has been that specialisation is achieved not by countries abandoning whole industrial sectors, but 'mainly by individual firms narrowing their product lines' (Blackhurst et al. 1977, p. 11). There are, of course, straightforward economic reasons why intra-industry trade should have grown throughout the post-war era having to do with similarity of production structures and the existence of scale economies among the major capitalist countries. But there are also strong political reasons why the governments of those countries would have wanted to encourage such trade among themselves. As I have argued at greater length elsewhere, the domestic social and political adjustment

U.S. International Trade Commission (ITC) and Department of Commerce (DOC) made affirmative determinations, the average dumping duty applied in 1987 on dumped or subsidized goods was 1.2 percent. In 1988, the average was 3.7 percent; in the first half of 1989, the figure was 1.4 percent' (Stern 1990, pp. 192–3).

⁸ Brazil and India were named in the initial US review largely because they led the Third World group in the Uruguay Round that opposed US initiatives to liberalise the services. Brazil has since been dropped from the list.

⁹ The 'damn right it's too low' end of the spectrum is occupied by the so-called revisionists, Chalmers Johnson, Clyde Prestowitz, Karel van Wolferen and James Fallows (see Fallows et al. 1990; Johnson 1988b). For extensive empirical evidence which concludes cautiously that 'yes, on the whole and to date, that tendency exists' see Lincoln (1990a). The margin-of-error position is taken by Saxonhouse (1983) and Leamer (1988).

costs of intra-industry trade are lower, the international vulnerabilities are fewer, and yet all the while it offers gains from trade. In a word, intra-industry trade is more compatible than inter-industry trade with the objectives of liberalising internationally while safeguarding domestic stability—the essence of the embedded-liberalism framework (Ruggie 1982).

This puts ‘the Japan problem’ in a somewhat clearer light. As is documented in Lincoln’s recent and detailed empirical study, Japan imports least precisely in those areas in which it exports most, so that its level of intra-industry trade is at or near the bottom in virtually every industrial sector (Lincoln 1990a). Moreover, granted that Japan is resource-poor and therefore needs to import raw materials, it nevertheless exhibits a much stronger preference than any other resource-poor industrialised country for entirely unprocessed or the simplest refined forms of raw materials imports. And on the manufactured exports side, Japan exhibits a far higher level of export concentration in selected high value-added products than its competitors. Finally, while the lowering of formal trade barriers according to both theory and the historical experiences of other industrialised countries should have led to the substantial erosion of this pattern, evidence suggests that the disparities between Japan and the rest in some instances actually have widened over time (Lincoln 1990a).¹⁰

Leave aside for the moment the questions of *why* Japan exhibits this pattern of ‘unequal trade’ and *how* it is maintained. It is indisputable that, at least in *this* sense, ‘Japan is a great economic power that does not play by the same rules as the other great economic powers’ (Krugman 1990a, p. 44). Moreover, whatever its cause, Japan’s trade posture poses fundamental *political* problems for other governments: ‘The fact that intra-industry trade has become a normative pattern of behavior for other countries means that Japan’s failure to conform imposes adjustment costs on the industries of other countries that they do not expect to bear’ (Lincoln 1990a, p. 60). And, of course, it also imposes adjustment costs on the governments concerned as they struggle to accommodate the displaced industries—or face, in van Wolferen’s words, ‘a gradual loss of industrial capacity’ in key sectors of their economies (1986–87, p. 288).

To call this ‘protectionism’ on the part of Japan, however, gives too much credit to the concept and not enough to Japan. It is not a matter of Japan ‘cheating’ on the formal GATT rules. Japan’s tariffs are low, its quotas are few, and its outright rule violations are no more frequent than those of other industrialised countries. The structure of Japan’s trade is

¹⁰ Peter Drucker has described Japan’s posture less generously as a form of adversarial trade. ‘In adversarial trade the seller’s goods displace the goods produced by the manufacturers of the buying country without any compensating purchases from that country’ (1986). The structure of Japan’s trade in this regard contrasts starkly with Germany’s, another heavily export-dependent economy. The comparison may shed light on the argument, and thus deserves systematic study by economists.

simply, and importantly, different from the established norm around which the international trade regime revolves.

This difference, in turn, poses a fundamental dilemma for all other members of the trade regime, which the United States has sought to resolve in part by means of Super 301: how does one overcome a structural asymmetry by institutional means that require symmetrical quid pro quos? The long and desultory experience with US–Soviet conventional force reduction talks in Europe suggests that it cannot be done; those negotiations succeeded only after the Soviets unilaterally made major asymmetrical concessions (before the Soviet empire collapsed altogether). Similarly, there simply are no GATT means available to get from ‘here to there’ on the asymmetrical structure of Japan’s foreign trade, given the GATT norm of reciprocity.¹¹ Super 301, then, may be seen as an attempt by the United States to evolve clumsily and, as always, inconsistently a tit-for-tat strategy intended to induce the structure of Japanese trade into greater harmonisation with its trading partners (see Axelrod 1984).

In the event, Japan was not moved to retaliate against the United States when targeted by Super 301, or even to bring action against the United States within the GATT. Though Japan refused to negotiate formally under Super 301, it sought to defuse the issue by reaching several accords with the United States under the framework of a so-called Structural Impediments Initiative. Even more strikingly, a major Japanese newspaper poll reported that 85.9 per cent of respondents in part, or fully, favoured acceptance of US demands!¹²

The real danger of Super 301 is that it may prove politically difficult to contain its use to these strategic purposes, that it will become a sledgehammer rather than Carla Hills’ crowbar. But surely the first steps in avoiding that possibility are to understand the strategic purposes the leg-

¹¹ In opposition to Super 301, Bhagwati points out that ‘[o]bjectionable trade practices not in violation of GATT’s rules [e.g., structural impediments] must be dealt with by negotiating what are called new ‘disciplines’, where acceptance of a new obligation by one country [e.g., Japan] must be paid for by an equal concession from the other’ [e.g., the United States] (Bhagwati 1989a, pp. D2). But politically, that’s not a solution; it is a restatement of the problem.

¹² A *Nihon Keizai* poll (*Los Angeles Times* 1990) reported: ‘[T]he process of working out the [Structural Impediments Initiative] accord has uncovered an astonishing degree of sympathy for the United States here [in Tokyo] and support for its advocacy of a more open Japanese economic system’ (p. D2). In addition to the views expressed in the public opinion poll, editorials in Japanese newspapers ‘were overwhelmingly for reform’ (p. D2). The reason is fairly straightforward: the same practices that have kept imports out have kept domestic prices high. A joint survey by the US and Japanese governments confirmed in 1989 that 84 of 122 products surveyed were on the average 41.7 per cent more expensive in Japan than in the United States. ‘Only in the case of consumer electronic products, where U.S. manufacturers have dropped out of competition, were prices lower in Japan’ (*Los Angeles Times* 1989).

isolation is intended to address, and then to devise viable multilateral measures that alleviate its dangers.¹³ Neither end is well served by the free-trade/protectionism rhetoric that has tended to frame criticism of Super 301 to date.¹⁴

3. Parametric change

Far from representing an extreme and limiting case, the resort to strategic unilateralism, on the contrary, may be a sign of things to come—*not* because countries are becoming more protectionist, but because parametric changes in the world economy increasingly are eroding the efficacy of the available multilateral arrangements. Three such changes pose particularly difficult challenges to the trade regime: the growing significance of domestic structures as an international trade issue; the growing magnitude of the services which are not easily captured by existing conceptual or institutional templates; and the process of globalisation, which makes past means of compensating for economic openness increasingly irrelevant.

Domestic structures

One of the curious and long-forgotten features of the post-war international economic regimes is that their terms of reference were drafted in such a way as to accommodate the possible membership of state-trading nations—specifically the Soviet Union. That feat was achieved, however, by simply requiring state-trading enterprises in their external purchases and sales to behave like private economic units: ‘solely in accordance with commercial considerations’, according to Article xvii of the GATT—which is to say, in response to factors such as price, quality, transportation costs, and other terms of purchase or sale.¹⁵ Thus, the potential

¹³ The ultimate compatibility between unilateral and multilateral outcomes would not be unprecedented. The original Section 301 of the Trade Act of 1974 also contained important elements of unilateralism. At the same time, it ‘encouraged the United States to make greater use of the GATT dispute settlement process...[O]f the sixteen GATT complaints filed by the United States between 1975 and 1985, eleven complaints arose out of section 301 investigations’ (Bliss 1987, p. 45). On the interplay between unilateral and multilateral measures during the Reagan administration, see Lincoln (1990a, ch. 6) and Prestowitz Jr (1988).

¹⁴ A notable exception is Hudec (1990). Hudec offers the provocative and potentially productive suggestion that the United States’ trading partners hold it accountable to its own (new 301) standards, in the attempt to increase the demand all around for more collectively legitimated mechanisms.

¹⁵ The words were taken almost verbatim from the ITO Charter, which the Soviets had had a hand in drafting (see Viner 1947; Feis 1947). For the corresponding assumptions on the monetary side, see Mikesell (1947).

international incompatibility of domestic structures was assumed away. And the post-war economic regimes were designed to remove or lower point-of-entry barriers such as quotas, tariffs, and various forms of (currency) exchange restrictions, as well as deliberate acts of cheating such as dumping. Discriminatory barriers were to be removed altogether, and the obligation to move towards greater openness in the rest was broadly defined by what I have called the embedded-liberalism compromise.

What has happened as point-of-entry barriers have been progressively lowered or eliminated, however, is that the impact of domestic institutional arrangements on the volume and structure of international economic transactions has become more salient. In some measure the problem has always existed. Even the US and the West European economies have always differed in terms of their precise balance and form of state–society relations. But those institutional differences gave none of them a permanent competitive advantage *vis-à-vis* the others and thus posed no threat to the overall economic relationship among them. Besides, the differences have decreased over time. Agricultural subsidies have become more divisive in recent years. But here the United States finds itself in the odd position of having obtained a GATT waiver long ago to exempt its own extensive domestic price support programmes and now having to suffer the consequences of the EC's common agricultural policy. In any case, a quid pro quo deal that would also provide some relief to European and American consumers, as well as to commodity-exporting countries, may yet be achieved in the current GATT round.

The problem case on today's agenda is Japan. Japan's domestic structures are widely perceived to be different from those prevailing in other advanced capitalist countries: its labour markets, capital markets, production arrangements, and distribution systems, to name but a few. The experts disagree sharply and deeply on whether these differences are due to cultural, bureaucratic, or electoral factors. And there are disagreements on whether the differences are declining, as liberal economists tend to believe, or are more permanent features of Japanese society. Without waiting for expert consensus on the final truth of the matter, policy-makers in the other capitalist countries have come to hold the view that these differences give Japan unfair trade advantages. In the United States, politicians feel additionally disadvantaged by the differential structure of domestic interest aggregation, which is far more transparent in the United States and thus puts them constantly on the spot, and by the differential access to the two political systems enjoyed by foreign lobbyists and interest groups. To the extent that Japan comes to serve as a model for the newly industrialising countries in Asia–Pacific and elsewhere, for China, and even for the former East European socialist countries and the Soviet Union, this problem would multiply manifold.

But the highly charged case of Japan—with its Japan-bashers in one corner and the Chrysanthemum Club in the other—merely masks a more

fundamental problem that would be with us even if Japan were not. Now that formal trade barriers have been reduced to insignificant levels, domestic policies and practices that shape the structure of foreign trade *ipso facto* are taking centre stage in the international trade regime. And if they diverge systematically and substantially among countries, an international political problem exists. As it stands, however, the GATT regime is designed 'to maintain a balance of [external] concessions and obligations, not to restructure nations' (Kalla 1986, p. 95). Yet harmonising the international effects of divergent domestic economic structures is what the international trade game increasingly is about. Once again, there are no easy multilateral means to get from here to there. Unless such means can be devised, unilateral ways of trying to resolve the problem are inevitable.

Tangible invisibles

What is called trade in services used to be the 'invisibles' appendage to merchandise trade: shipping, insurance, and the like, as well as tourism. Today the list is longer, the magnitude much higher and services are 'traded' in their own right. In addition to all of the old items, they now include information services, professional and business services, personal services, construction, consultancy and cultural services (see Kakabadse 1987, ch. 1). Their magnitude has reached somewhere between one-fifth and one-quarter of total world trade, although because of definitional and statistical anomalies the balance of world services imports and exports routinely is off by as much as \$100 billion per annum (Shelp 1986–87). The growth in traded services is accounted for by a combination of factors: technological developments, especially the informatics revolution; domestic deregulation, particularly of capital markets and the telecommunications sector; and the fact that both manufactured products and primary commodities embody ever greater services inputs, ranging from data processing to bioengineering.

The institutional problem posed by this increase in traded services is not quantitative, however, but qualitative. The GATT was designed for merchandise trade: tangible manufactured products and commodities that are exported and imported across national borders. Invisibles were basically left uncovered by the GATT; the only service explicitly mentioned in its articles of agreement is trade in motion pictures—the GATT's Hollywood clause.

Traded services have been a central concern of the current GATT round. At the time of writing, agreement remains elusive; and throughout the negotiations to date, all of the major players have shifted their positions on various occasions, thus making specific predictions difficult. Preliminary indications are, however, that a services agreement will mark only the end of the beginning of a very difficult chapter in trade diplomacy. At best, it likely would bring into the conventional GATT framework *that portion* of services *which fits* the conventional trade

framework (see *The Economist* 1990a; Stokes 1990a; Bhagwati 1991b; *The Economist* 1991b). But that portion is relatively small compared to a whole that cannot yet even be adequately defined. And a number of disputatious issues lurk beyond. It is these that concern me here.

First of all, because the concept of services has no well-established place in economic theory, its definition has tended to be ad hoc and arbitrary: the residual activity not included in agriculture, mining and manufacturing. Attempts to define services more theoretically have focused on the fact that they are non-storable and, therefore, require simultaneity of provision and use. But this insight has simply generated endless lists that can be endlessly argued about rather than a finite and universally agreed upon set (see Shelp 1986–87; Berg 1987; Riddle 1986; Kakabadse 1987; Giarini (ed.) 1987; Bhagwati 1987). With tongue only half in cheek, *The Economist* has proposed defining services as ‘Things which can be bought and sold but which you cannot drop on your foot’ (1985). But architectural plans, computer disks and magnetic tapes, not to mention Big Macs in Moscow and Budapest, in fact, can be dropped on one’s foot. What this ambiguity means is that, unlike the case of merchandise trade, in traded services the very definition of the concept itself remains subject to strategic behaviour by governments. There is no reason to expect that political contesting over definitions will cease once a GATT services agreement is reached.

Second, governments regulate their domestic service industries more rigorously than most other economic activities (Shelp 1986–87; Berg 1987). Entry into many services such as law, medicine and accounting is strictly licensed; governments frequently reserve the right to approve the charges of utilities which in many places still include transportation and telecommunication; financial institutions, including banks, insurance firms and securities traders, are subject to prudential supervision; and in many countries the state still owns outright certain service industries. Most of these regulatory objectives and instruments were not designed with trade in mind, but under a GATT services agreement they potentially could become targeted as illegitimate, non-tariff barriers. The probability of such conflicts arising is even higher if the service is provided, not on the spot, but via telecommunications transmissions—which arguably represent more of cross-border transaction. The principles of national treatment, non-discrimination and transparency that a services agreement presumably would include might alleviate some of these difficulties. But the list of exceptions that governments will insist on is certain to be long and highly asymmetrical across countries, thus providing ample scope for international trade disputes.

Third, many of the providers of services themselves are undergoing profound and rapid redefinition, posing additional conceptual and regulatory puzzles for governments (*The Economist* 1990b, p. 33). Banks trade stocks; securities firms retail checking accounts; and telephone companies issue general-purpose, revolving credit cards. Thus, the classical distinc-

tions among financial institutions, and between financial institutions and the informatics sector have become quite blurred, 'and the consequent increase in competitive inequities has given an international dimension to what has traditionally been a domestic concern' (*The Economist* 1990b, p. 12; see also *The Economist* 1990c).

Fourth and finally, it turns out, in any case, that relatively few such services are actually 'traded' in the sense we normally understand that term (Bhagwati 1987; Riddle 1986, especially ch. 9). This problem itself comes in several parts. Insofar as the defining characteristic of the provision of services is that production and consumption need to take place at the same time and in the same place, in many instances the ability to provide services depends on the establishment of local affiliates. To that extent, however, trade in services at a minimum implies a right of establishment, and at the limit it becomes indistinguishable from foreign investment. Neither constitutes trade. And both are more intrusive.

But assume for the sake of the discussion that this first part of the problem is satisfactorily resolved. A related question immediately arises: access of what or whom? In merchandise trade, the factors of production and the consumer stand still while the finished product moves. Ball-bearings and bananas cross frontiers, from producer to consumer, passing through customs along the way. In traded services, it is more likely that the factors of production do the moving while the product is fixed by location. To that extent, trade in services amounts to provider-mobility across borders (Bhagwati 1987). No economic theory explains, however, why mobile factors of production should include US banks providing services in South Korea, for example, but not South Korean construction workers offering their services in the United States.

As is obvious from the ongoing Uruguay Round, there is petty protectionism aplenty to be found in the services negotiations—not the least of which is on the part of the United States, which foisted the negotiations on its reluctant GATT partners in the first place. But even if that were not so, the underlying structural issues in traded services are so difficult that serious political conflicts will emerge no matter what. And some of these conflicts will have little enough to do with 'trade' as we traditionally understand it, let alone 'free trade' or 'protectionism'. A new and different conceptual framework is necessary, therefore, before significant progress in the institutional realm can be expected.

Moreover, once again conflict focused on the Asia-Pacific area may be higher than elsewhere in the industrialised world. Regulatory environments in general are more opaque there, thus inviting the imputation of worst-case motivations. Moreover, if past experience from direct foreign investment and patent protection is any guide, then in Japan at any rate such new institutional mechanisms as the right of establishment are likely to prove extremely elusive in practice, thereby inviting external pressure if not retaliatory measures. Using the precedent of direct foreign investment is not encouraging: 'Compared with Japan, no other industrialized country

has so adamantly denied multinational corporations access to domestic markets' (Encarnation & Mason 1990). As for patent protection, the most egregious case offered up by Japan is the integrated circuit. Texas Instruments, its inventor, applied for a patent in Japan on 6 February 1960; it was granted effective 30 October 1989! By then Japanese firms accounted for 90 per cent of all sales in Japan, and 40 per cent of the market world-wide. In memory chips, Japan by 1989 accounted for 70 per cent of the one-megabit market world-wide, and over 90 per cent the the four-megabit, the most advanced memory chip in production (Hayes 1989; Sanger 1990a).

Globalisation

A third core institutional assumption of the post-war economic regimes was the notion that international economic transactions take place at arms length between distinct and disjoint national economic units. Its efficacy has been severely challenged in recent years by the phenomenon of globalisation.

Much has been written about globalisation, and nearly as much has been dismissed as 'globaloney'. Milton Friedman, as is his wont, has put the negative case most categorically: 'The world is less internationalized in any immediate, relevant, pertinent sense today than it was in 1913 or in 1929' (Friedman 1989). Friedman contends that the divergence between the price of the same good in different countries that became distinctly pronounced after the Great Depression has remained in place despite steadily decreasing transportation costs, thereby 'demonstrating vividly how powerful and effective government intervention has been in rendering the law of one price far less applicable after 1931 than it was before' (1989, p. 10).¹⁶

Be that as it may, a truly remarkable expansion of the 'borderless economy' (Ohmae 1990) has occurred in the increasingly extensive, diverse, and denationalised institutional links that have been forged among firms and within markets across the globe. Illustrating the poverty of conventional concepts, this phenomenon typically is described as 'offshore' production and 'offshore' markets, as if they existed in some ethereal space waiting to be reconceived by the economic equivalent of relativity.

The rapid growth in trade among the industrialised countries from the 1960s on was marked, as we noted above, by intra-industry specialisation, whereby trade took the form of simultaneous increases in exports and

¹⁶ Friedman also adds that immigration has slowed to a trickle compared to the nineteenth century. In a controversial paper published some years ago, Kenneth Waltz advanced an argument very similar to Friedman's, using as his measures of internationalisation (i) the size of the external sector of the major economic powers relative to their domestic economies, and (ii) the degree of inter-sectoral specialisation reflected in their trade patterns (Waltz 1970).

imports within the same industrial sector. A closely related phenomenon has been the growth of intra-firm trade, or the rise of 'the global factory' (Grunwald & Flamm 1985). Led initially by the automobile and consumer electronics sectors, components production by multinational enterprises has become fragmented across a vast array of countries, exploiting the shifting advantages of different production locales. The resultant trade in intermediate products is largely intra-firm trade or at least trade among related parties. As is the case with traded services, intra-firm trade does not exist in conventional economic theory, hence no uniform and universal statistics on it have been collected. But the available evidence on US manufactured imports suggests that somewhere around half originate with wholly owned foreign affiliates or related parties abroad; that this kind of trade is growing more rapidly than the standard stuff; and that it is less sensitive to such macroeconomic factors as exchange rates (see Little 1987; Helleiner 1981).

International financial markets are even more closely linked and their magnitude is even more impressive. Total world trade amounts to some \$3 trillion a year. International capital markets turn over at least \$75 trillion, and foreign exchange transactions now exceed \$100 trillion. Moreover, whereas capital movements historically reflected business decisions to finance trade or to establish production facilities abroad, 'it seems apparent that the dominant proportion of the investment funds actually in movement internationally today reflects instead decisions concerning portfolio holdings...shifts among holdings of various kinds of intangible assets' (Roosa 1982, p. 4). In addition, securities firms are establishing branches in the world's major financial centres (Spero 1988-89). As a result, since 1980 foreign equity trading in the United States has increased at an annual rate of 19 per cent to reach \$384 billion by 1988, and US purchases of foreign equities rose 30 per cent per annum to reach a total of some \$151 billion (Wayne 1989). And numerous other financial instruments that did not exist only a decade ago are now traded internationally in rapidly expanding volumes.

The 'global office' is a more recent and still more modest phenomenon, to date consisting largely of firms moving certain routine 'back office' tasks offshore. Thus, Citibank does some of its financial data processing in Jamaica, American Airlines processes ticket stubs in Barbados and the Dominican Republic, while New York Life processes claims and McGraw Hill magazine subscription renewals in Ireland (Lohr 1988).

Finally, this globalised segment of world production, trade, and services is becoming progressively denationalised not merely by location but also institutionally. Cross-investment and other forms of inter-corporate alliances are becoming increasingly common, thereby blurring the distinction between domestic and foreign producers and products (Reich 1991a, especially Pt 2).

For the purposes of this discussion, two international political consequences of globalisation merit particular attention. The first concerns the predicament globalisation has put governments in. Government policies may have made possible the emergence of this offshore world in the first place, through favourable tariff provisions and the liberalisation of capital markets, for example. But globalisation, in turn, has created numerous policy problems for which governments have proved unable to devise effective responses.

Globalisation constrains the ability of governments to pursue independent macroeconomic policies; even Japan is reported to have become afflicted by this problem (Sterngold 1990a, 1990b). Moreover, as a result of globalisation certain aspects of trade policy have become virtually metaphysical in character—as when the US International Trade Commission finds itself confronted with anti-dumping charges brought by a Japanese firm producing typewriters in the United States against an American firm importing typewriters into the United States from its offshore facilities in Singapore and Indonesia!¹⁷ At the very least, as the multinationality of firms has increased, governments have become conflicted not simply by the traditional import/export-dependent industry preferences, but also by newer demands for ‘strategic trade policy’—demands for government action to secure access to foreign markets and to vindicate other norms of fairness in international trade under threat of home-country retaliation for failure to comply.¹⁸ On the finance side, the global offshore world exists largely in a regulatory void, which has even some of its promoters concerned: ‘national systems of supervision and regulation—to say nothing of tax and accounting policies—that were created many years ago were not designed for a marketplace of world-wide dimensions in which firms with differing charters and national

¹⁷ The case involves Brothers Industries Ltd, a Japanese concern assembling typewriters in Bartlett, Tennessee, and Smith Corona, the US concern doing the same offshore. Adding another element of globalisation, Smith Corona is owned 48 per cent by Hanson PLC, a British group (Reich 1991b; Sanger 1991). Sanger’s story also points out that Chrysler inadvertently may have filed an ITC claim against *itself* when it charged Japanese firms with dumping minivans in the US market—one of the vehicles covered by the definition is made for Chrysler by Mitsubishi. The Brothers Industries request subsequently was denied, the firm not being enough of a domestic producer to claim injury.

¹⁸ Helen Milner’s case studies of selected US firms in the 1920s and 1970s, and a cross-sectional comparison of US and French firms today suggest that the more extensive the multinationality of firms becomes, the less likely they are to demand protection and the more likely they are to resist it, even if their industry is under pressure from import competition. At the same time, she points out that these firms may increase demands for ‘strategic trade policy’. Some of the most advanced industrial sectors, including semiconductors, commercial aircraft and telecommunications, exhibit this pattern (Milner 1988; Milner & Yoffie 1989; Yoffie & Milner 1989).

origins compete head-to-head with each other around the clock and around the world' (Corrigan 1987, p. 2; see also Ohmae 1990; and Spero 1988–89).¹⁹ And novel financial instruments, which are designed to reduce or diversify risks for individual firms and investors, at the same time can increase the system-wide transmission of destabilising factors such as stockmarket crashes.²⁰

In the absence of a solution to the eroding efficacy of standard national policy instruments through more effective international policy coordination, for example (of which there is as yet little sign), we can expect governments to try to find more unconventional ways to cushion their domestic economies from unexpected shifts and swings in currency values and import levels. Indeed, the liberalisation of capital markets is central to any explanation of the recent increase in the 'new protectionism' in trade (Bhagwati 1988, p. 71). But cross-border corporate ties and market forces now are undermining the efficacy of that well-established domestic compensatory move as well.

Orthodox economists welcome this development on the assumption that it will increase economic efficiency while decreasing government intervention. In point of fact, however, it may have just the opposite effect. If the relatively benign option of the 'new protectionism' ceases to provide effective relief, then there is no telling what measures governments might turn to in exasperation. Such a move would not be 'correct' or 'efficient' by the standards of economic theory, but governments in the industrialised countries are elected by their constituents, not by the keepers of the economic faith. The very success of uncompensated liberalisation—or disembedded liberalism, if you will—could generate precisely the kind of economic nationalism that embedded liberalism was designed and was able to contain.

There is a particular Japan/Asia–Pacific angle to this story as well. Not surprisingly, it concerns whether Japan's pattern of globalisation conforms to the general pattern or is distinct and possibly detrimental to the multi-lateral trading system as a whole. The basis for this concern is Japan's rapidly expanding foreign investment in the East and Southeast Asian region, reflecting the need to source offshore as a result of the appreciation of the yen and rising domestic labour costs. Indeed, since the Plaza Agreement of 1985 realigning the yen and the dollar, that investment has risen from less than \$2 billion per annum to nearly \$8 billion projected for

¹⁹ Steps have been taken to coordinate the supervision of international banking, but international securities trading, and the international banking and securities clearance and settlements systems are weak and vulnerable.

²⁰ Empirical studies of the 1987 stockmarket crash find, however, that direct international linkages, that is, cross-border equity investment, do not explain the worldwide decline in equities markets; what was transmitted was panic, and cross-border investment is not necessary for that to have occurred (Bennett & Kelleher 1988; Aderhold et al. 1988).

1990 (Sterngold 1990c; Sanger 1990b); and Japanese manufactured imports from the region increased by some 200 per cent from 1985 to 1988 (*The Economist* 1990d).

There is a benign reading of where this could lead to, and one not so benign. In the benign variant, Japan's investments would contribute to the industrialisation of the entire area and lead to its active participation in the multilateral trading system. In the less benign variant, Japan merely expands its own industrial structure over a more broadly based manufacturing platform, stretching from South Korea to Singapore. The home-country sourcing preference that Japanese multinationals have exhibited to date would remain in place, and Japan's imbalance in intra-industry trade with the rest of the industrial world would continue unabated. As one study of this phenomenon has concluded, Japanese firms 'are tightly controlled by the respective parent company, procure their equipment mainly in Japan and own and operate mainly Japanese machinery' (Kreinin 1988, pp. 540–1).²¹ If this less benign scenario were to materialise, the European Community would likely respond by turning more decisively inward and the United States by turning its bilateral free-trade areas into more airtight trading blocs.

4. Conclusion

When US policy-makers sat down with their foreign, largely British, counterparts to negotiate the post-war economic regimes, the practices they sought most to banish from the repertoire of international trade relations were various beggar-thy-neighbour policies—and for the United States, British imperial preferences—together with exclusive currency blocs and other restrictive practices in the monetary realm. Put positively, they sought to institute the principle of economic openness. A return to pre-World War I *laissez-faire* liberalism was not a viable solution, however, no matter how much the New York banking community and some export-oriented industries agitated for it, because between the two wars governments throughout the industrialised world had become subject to new domestic political demands and constraints. Thus, the post-war economic regimes were designed to achieve progressive liberalisation internationally without, however, subordinating the domestic economy to the

²¹ Kreinin's work is a comparative study of procurement practices by Japanese, European and US multinationals in Australia. Japanese multinationals operating in the United States imported over \$71 billion worth of goods into the United States in 1987, overwhelmingly from Japan, while exporting \$21 billion—the difference being roughly equivalent to the size of the US trade deficit with Japan that year (Lehner & Murray 1990). Of course, it is possible that Japanese firms simply have not yet matured as transnationals, and that over time this pattern will change—an argument made by Bhagwati (1991a, pp. 30–2).

strictures of external parity; and to allow for and even facilitate governmental intervention in the domestic economy, without, however, triggering the mutually destructive consequences of inter-war practices.

For what they were designed to achieve, these regimes have performed remarkably well. They have contributed to an expansion of international trade and capital flows that is historically unprecedented in its magnitude and duration. They have withstood the most severe economic dislocations the world has experienced since the Great Depression. They have accommodated and even facilitated the emergence of new entrants such as Japan and the Asian newly industrialised countries, whose pace of evolution from relatively poor countries to newly and even leading industrialised countries also is unprecedented in recent history. Lastly, the institutional adaptations invented by countries by and large have been designed not to gain unacceptable unilateral advantage but, at one and the same time, to respond more effectively to the changing international economic environment without abandoning the fundamental normative understandings that animated the regimes in the first place.

Yet still the trade regime is in trouble today. In part the trouble is rhetorical in origin, and that part ought to be solvable without undue difficulty. It concerns the irrelevance of much of free-trade discourse in deciphering the meaning of the so-called new protectionism. Practices that arguably fall within the *actual* post-war institutional compromise, which I have termed embedded liberalism, must be distinguished from instances of illiberal protectionism if total obfuscation and rancorous debate is not to destroy what is left of the trade regime. Their difference lies, as suggested above, in their intent and result. To claim that governments have tried to achieve effective protection via VERs and similar instruments makes it necessary to assume that they are either stupid, or perverse, or both—so bad a job would they have done for so extended a period of time. The instruments of ‘managed trade’, on the other hand, which are designed to fix or allocate market shares, are clearly violations not only of the letter but of the spirit of post-war norms and, therefore, should be resisted and undone.

A second part of the problem is more institutional in character and also more difficult to solve. The major institutional changes that have taken place in the domain of trade have pushed domestic economic structures to centre stage. That is true of the decline of formal trade barriers, the growth in global service transactions, and the phenomenon of globalisation itself. But GATT was designed to achieve a balance of *external* rights and obligations, not to achieve *internal* restructuring. Moreover, it is in any case impossible to achieve symmetrical results by symmetrical means from asymmetrical starting points. Now, no one can oppose the recommendation that GATT be strengthened. But in the meantime, governments can be forgiven if they do not stand by and watch entire industrial sectors collapse while negotiations go forwards. Moreover, it makes as much if not more sense, in the light of our discussion also to strengthen the policy harmonisation roles of the OECD. Much as in the arms-control field,

greater transparency would result on which mutual and balanced confidence measures could be built, leading ultimately to more serious negotiations on a multilateral basis concerning the adverse external effects of asymmetries in domestic structures.

A third part of the problem is fundamentally intellectual in character, and it may be the most difficult to resolve. The construction of the post-war regimes and their operation for many years was sustained by a broad, quasi-Keynesian consensus on what made the public economy tick (Ikenberry 1992). That consensus, of course, has long since been shattered, and none has yet taken its place. No comprehensive and systematic reconstruction of the post-war economic regimes is conceivable without such a consensus.

But even partial reform will require major intellectual stretching by the economics profession. Not being trained as an economist, my characterisation of what is needed perforce is unschooled and may be off the mark. It seems to me, though, that to understand institutional change in the global economy ultimately will require a model of the global economy that treats it as an entity in its own right: a non-territorial, decentred yet singular space-of-flows, which exists alongside the various national spaces-of-places that we call national economies. These conventional spaces-of-places will continue to engage in 'external' economic relations with one another, which we will continue to call trade, foreign investment, and the like, and which are more or less effectively 'constrained' by the state. In the model of the global non-territorial space-of-flows, however, which needs to complement the national-economies model, 'exterior' relations become internal transactions, and the state is endogenised. I am sure that this is a difficult challenge, but in the long run it should not be insuperable.

I am somewhat less sanguine about the ability of mainstream economists to come to grips with the issue of Japan, not because it is inherently more difficult, but because there is so much more at stake for the profession itself. If the 'revisionist' Japanologists are even partially right, and if the theory of scientific revolutions *à la* Kuhn has any bearing on this matter, then economists would be the last to admit that Japan represents a different type of capitalist economic formation. And before so doing, they would be expected to go to some lengths to ignore or discount contrary evidence, invent circuitous logics to account for anomalies, and deploy a variety of rhetorical strategies to discredit the opposing position. The recent strategic trade policy debate, in fact, exhibited some of these patterns, but in the end it successfully raised related issues and is, therefore, a welcome development irrespective of who ultimately proves right or wrong (see Richardson 1990a; Cohen 1990). Understanding the domestic economic structure of Japan, and thereby helping to attenuate the inevitable trade disputes with Japan that lie ahead, will require similarly detailed empirical studies, informed by models of strategic rationality, and which explicitly test for, not simply assume, what Albert Hirschman has called the 'mono-economics' claim that pervades the conventional theory (Hirschman 1981, ch. 1).