

**CLOSE-UP**

# P rotectionism? There is Another Way.

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World recession, coupled with Europe's growing trade deficit with Japan, raises serious questions. Those attracted to short term protectionist policies run the risk of lapsing back into the economic nationalism of the thirties, with all its implications. Yet 20 million unemployed in Europe—and the numbers are still rising—must make us realize that we are at the crossroads. The chairman of the British-Japan Parliamentary Group, Sir Julian Ridsdale, in this article, recognizes signs of an understanding that Japan must seize the initiative and take seriously the problems of her trading partners... in order to preserve the existing free trade system.

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## rotection vs. Free Trade

In the 1930s, faced with similar problems, governments of the day turned to protection and economic nationalism. Some still look to such solutions, especially those in the left of politics in the European Community who seek immediate solutions, for what we regard in the

United Kingdom as problems of competitiveness, which we in the long term have got to correct. France and Italy have already taken the protective road; France to Poitiers. Such a course, much to our disappointment in the U.K., will make the establishment of a common industrial policy in the Community that much more difficult and that much longer to achieve.

Britain, as a member of the Community, as a country which exports 30% of her G.D.P., is, like Japan, dependent on the free trading system.

This was underlined by Prime Minister Thatcher in her visit to Tokyo in September last year.

“All the advanced industrial countries, and especially Japan and Britain, depend on the free trading system. Your country's success has been particularly helped by

the openness of those markets to your goods.

"For the world trading system to continue and to prosper, markets must be equally open, one to another. This principle would be true at any time of high unemployment in the major industrialized countries."

As I have already said, I realise the long term problem is one of competitiveness, nevertheless in the short term, with extremely high unemployment in the U.K. the imbalance of trade with Japan and West Germany in particular makes the achievement of the long term aims of the multilateral trading system, built up so carefully after Bretton Woods, that much more difficult.

With the European Community as a whole, U.K. trade in 1981 showed a surplus of £25 million in a total trade of £21,000 million.

On manufactured goods the deficit with West Germany between January and August last year was £2,119 million. With Japan in the same period there was a £1,412 million deficit.

In 1981 on visible trade with Japan, the U.K. ran a deficit of nearly £2 billion; the U.K. sold only £0.69 billion goods to Japan, against imports from Japan of £2.5 billion. The deficit with Japan was eased by invisibles, and with Germany by oil exports.

Nevertheless, the picture that emerges is that the U.K. is running extremely high deficits in manufactured goods with both Germany and Japan. With high unemployment, short term policies that promise protection are that much more attractive.

However, those of us who over the years have supported post-war multilateral Bretton Woods trading policies know that protection does not provide a lasting solution to industry's problems, since it merely slows up the readjustment process, encourages the inefficient use of resources and encourages retaliation measures.

In the present situation we are doing our best to sustain the multilateral trading system, and at the same time make industry more competitive.

These intentions as far as Margaret Thatcher's conservative government are concerned were made clear by the Foreign Secretary Francis Pym in the debate on the Queen's Speech on November 4.

"What we must strongly resist," he said, "is the temptation to believe that the creation of barriers, the retreat into isolationism, could ever be the right answer to the problems. That path by reducing efficiency and the ability to compete will make us all—producers and consumers alike—worse off in the long run.

"The Government want the problem solved not by increasing barriers all round but by reducing them. The reduction of barriers is a high priority objective of the Government.

"On the broader financial front, where we have seen so many recent shocks, it is important to make the point that the Bretton Woods institutions have served the world well since their establishment after the war. They have adapted to meet the changing circumstances of the world economy.

"In the present atmosphere of uncertainty over international economic prospects, they have a vital role to play.

"Now is not time to pull up the roots of institutions that have served us well in the hope that something more

vigorous and more adapted to today's world will spring up in their place. Neither must we assume that the institutions can best tackle the problems of tomorrow with the methods of yesterday. They must be constantly reviewed. They must be reinforced if necessary.

"We shall uphold the competence and political independence of the International Monetary Fund. We shall work for a constructive and orderly evolution of the international monetary system. The Government believe that the institutions must be effective and have the resources necessary to carry out their tasks. Their integrity must be respected. They must remain non-political."

This speech underlines the commitment of a government that believes in a free economy and the multilateral trading system.

This was reinforced by the leader of the House of Commons, John Biffen, in winding up the debate, when he said, "The alternative to open trade is the crippling regionalism of the 1930s with its fortress of tariffs and quotas and its downward spiral of trade. The world of the 1980s with newly emerging economies and transferable technology, cannot afford trade-exacerbated divisions between north and south, the oil rich and those without, the newly industrialised countries and the developed world."

It is important for our friends in Japan and West Germany to appreciate these commitments. They are very different from the French road of protection to Poitiers. However, it is going to need a great deal of wisdom and cooperation from those who support the Bretton Woods world, to preserve and keep it through this difficult period of recession.

I sincerely hope this will be the right road for future Euro-Japanese relations especially over the next 10 years, in spite of the difficulties emerging from France and Italy, and those on the left in politics.

Now is the time for all those who believe in free economies, and the multilateral trading system established after Bretton Woods, to unite and come to each other's aid, and show practically, by international action how we can solve the serious problems of recession and unemployment that face us.

## Japan's Role in the 1980s—Sustaining Two-Way Trade?

Yet the big question that still remains, having stated all these good intentions, is that Europe's trade deficit with Japan rose to over £12 billion in 1980 with a huge growing imbalance continuing in 1981 and 1982, as has been the pattern with the U.S. as well.

However, neither the U.S. nor Europe is alone with such an imbalance. The newly industrialised countries of

Asia have also found it difficult to conduct a balanced two-way trade with Japan as have Europe and the U.S.

As Leslie Fielding said in his article (see July '82 issue), "Europe's trade imbalance with Japan is not unique. It is not due to entrepreneurial decline or some mysterious collapse of industrial flair...peculiar to the EC. Our experience has been shared by most of Japan's trading partners, other than those which supply energy and raw materials.

"Today Japan has become the most powerful industrialised country after the U.S., accounting for 10% of World G.N.P. A more positive role is consequently hoped for from Japan in the 1980s than in the 1960s in sustaining two-way trade and away from her self-sufficient economic behaviour of past decades.

"It could prove increasingly a source of international strain for the Japan of the future to remain an importer, chiefly of raw materials, energy and certain foodstuffs, self-sufficient in most other respects, yet an exporter of finished goods to her GATT partners down a largely one-way street."

I do not believe this will happen, because if it did, the international trading system would break down, and the protectionists have their way. But trade is about giving as well as taking, and this is why so many of those who have been watching the Japanese scene over the years, realise how crucial the choice of economic policies facing the Japanese government is at the present moment.

Will the £4.5 billion injected into the economy recently be enough to stimulate demand? What is the Japanese government going to do to overcome its huge percentage of deficit financing?

Will this problem be overcome soon? When it is, will a further stimulus be given to home demand and larger investment policies undertaken overseas, especially in those countries which are good customers for Japanese manufacturers like the U.K.?

Such action would improve the imbalance, by improving competitiveness and therefore make it easier to export to Japan.

Faced with similar situations in their time, other countries like Britain, the U.S. and West Germany have found it necessary in order to be good partners in the international trading community, not only to try to buy more from countries in imbalance, but to increase their investments abroad as well.

In Britain, for instance, U.S. investment alone accounts for more than 1,000 of the manufacturing companies, compared to 200 from the Federal Republic of Germany and only 24 from Japan itself. I hope the investment by NEC, the largest yet made by a Japanese company in the U.K., who started operations in September last year in their semiconductor plant in Scotland, may be the start of a much larger investment drive. For it is only along such roads that we can sustain the multi-lateral trading system.

Yet, Japan over the past 20 years has set aside 17% to 20% of her G.N.P. for private capital investment and this is a much higher ratio than the 10% or so set aside in Europe or the United States.

Yet, Japanese entrepreneurs have been bold in taking risks in the development of new products, in capital investments to develop new markets, and in investment

to expand overseas markets.

Protectionists continue to point out that in the sixties, to reach the position she has reached today, Japan relied on strong protective policies and minimal defence spending compared to the U.S. and Europe.

Really it was a combination of all these factors, along with Japanese special skills that led to a huge gap opening between not only the competitiveness of Japanese and European industries, but also between the U.S. and Japan as well, particularly in automobiles, electronics and machine tools.

Of course, Japan has other advantages in her favour. The share of scientists, engineers and skilled workers in her labour force has been on the increase far more than in Europe and the United States.

In November 1981, when I was speaking in Tokyo at the European Symposium organised by the Minister of International Trade and Industry, I warned of the damages of inaction to correct the surplus. I was taking into account the growing pressure of protectionism caused by unemployment, against the background of Japan's own protective policies in the sixties, which helped build up her competitive position.

I feel these things must be said because however many businessmen we send to Japan without an expansion of demand in Japan, their efforts will not earn a great deal of reward.

Yet, both sides must face the facts. Let us take into account the lessons of history and build constructively for the future in a spirit of forward looking co-operation.

Without this spirit the future trend of Euro-Japanese economic relations will lead us to increasing measures of protectionism and strain, beginning in a small way, and gradually increasing in their intensity.

## The Future

Yet there is another way for us to tackle the problems of unemployment, inflation and world recession. Let us together build on the institutions set up at Bretton Woods, and encourage international cooperation, not economic nationalism.

Nowhere is this more important than in the field of nuclear energy, the fuel of the next millenium. Costs of reactors are becoming so large that no one country can sustain such a huge investment programme.

International cooperation is vital and will probably by force of circumstances take place very soon. Let us follow this example to build up other measures of co-operation.

In the next decade, the principle export items from Japan to Europe will probably shift away from manufactured goods towards the exchange of technology and capital investment.

This will follow the example set in the nuclear field.

In the meantime I hope help will be given to correct the present imbalance, especially with the U.K., by the buying of such items as military equipment, aeroplanes, and helicopters.

Obviously industry to industry talks are of the utmost value to ease the present difficult situation. This has been shown clearly over automobiles, then electronics and now machine tools. This cooperation to correct the present imbalance will obviously continue in other industries as well, until we move to a better long-term trend, with an improved balance in trade in the future, heading toward the exchange of technology and capital investment.

In this respect, governments could help by sketching out a ten-year programme of probable developments. At least such action would bring hope to large numbers of unemployed in Europe, now numbering in the EC some 20 million, and show what is being done by international action to overcome the present recession and unemployment. Perhaps this could show a possible pattern for joint ventures in Europe, and how in machinery, the main exports will shift to more specialized and electronic applied machines.

I hope joint projects with European countries in the developing world will increase considerably. Will the IMF or World Bank be able to finance the export of major nuclear plants to the developing world, where the cost of oil has been such a crippling blow to the developing countries and occupies such a large item in their £300 billion indebtedness?

I also expect to see an increase in exports from Europe to Japan in the sphere of oil exploration and more practically in engineering projects aimed at the rebuilding of the Japanese archipelago.

This is a long-term forecast, but in the short term, in the U.K., which is but an average example of what is happening in other European countries, industrial activity has continued to languish at a level around 16% below the peak of production achieved in the summer of 1979. This excludes the extraction of oil and gas.

Contrary to expectations export volume of manufactured goods fell by about 7% between the second and third quarters of 1982, underlining the vulnerability of the U.K. to prolonged recession in the rest of the OECD (Organization for Economic Cooperation and Development) nations.

Import penetration which normally saps the benefits to U.K. manufacturers of any recovery in domestic demand is already manifest, despite the absence of a revival in the U.K. economy.

The trade balance in manufactured goods swung from a £475 million surplus in the first quarter to deficits of £194 million in the second quarter, and £283 million in the third.

Moreover it is in intermediate and capital goods where import volumes have shown the most substantial rises; increases of 8% to 9% respectively were recorded comparing the third quarter of 1982 with the first three months of the year, suggesting that the susceptibility of the U.K. economy to foreign products is more broadly based than in the past, and giving further ground for concern that despite sterling depreciation the initial upturn may be both delayed and muted.

All this of course gives further fuel to protectionists, and underlines the need for quick international action, from Japan and West Germany particularly, if we are not to lapse quickly into the economic nationalism of the thirties.

However industrial stagnation should not extend into 1983. Improved real personal incomes, lower nominal and real interest rates, lower oil prices, lower inflation and lower growth in the world economy are expected to lift output through most of the year. There is room for growing optimism, as is being reflected in the City of London.

Nevertheless in spite of this recovery, unemployment rates will continue to be extremely high. If we are to keep protectionism at bay, this puts on the international community an obligation to study the future of work in this technical age. An unemployment rate of 20 million in the European Community and still rising is a most disturbing trend. International action and understanding of a high order are needed to face up to this challenging problem.

I hope we shall find this a new trend in the future. It would be idle of us not to warn of the dangers of protectionism. We are at the crossroads. Summits are not enough. We need discussion and action at all levels.

I find, in the political sphere I move in, a belief that Japan should seize the initiative, and should take the problems of the EC and the U.S. as seriously as they deserve, and should consider what more she can do to preserve the existing free trade system.

Some indications, such as the creation of the "Office of Trade Ombudsman," show that there is an understanding of the problem. But much more needs to be done on a macro-economic scale, if we are to prevent the slide to confrontation and economic nationalism which threatens us all.

Protection does not provide a lasting solution to industry's problems. The right approach must be to restructure at home—we have been doing this painfully in the U.K.—and then consulting at the international level, since interdependence is the key to the multilateral trade system. And states must bear in mind the need to have compatible overall aims and policies so as to keep the system going.

In this recessionary period, this consultation is even more vital, not only between governments at all levels, but particularly between politicians and civil servants, as well as industry to industry consultation. This trend is happening, and I hope will grow even more over the next few years.

Yet above all there is the need for political understanding. As we move forward along these lines to solve the problems of recession, let us not lose sight of the political and strategic role Japan and Europe play in maintaining the balance of power and peace.

Culturally we have much to exchange with each other. Friendship between Europe and Japan is not a tradeable commodity. It is precious and unique. Those of us who visit Japan know how much is done over the years through individual friendship and trust.

Let us continue to cultivate those individual friendships at all levels. Great oaks from acorns grow. It is vital we keep faith with the statesmen of Bretton Woods. ●