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The Trilateral Commission was formed in 1973 by private citizens of Western Europe, Japan, and North America to foster closer cooperation among these three regions on common problems. It seeks to improve public understanding of such problems, to support proposals for handling them jointly and to nurture habits and practices of working together among these regions.

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The speech of Joseph Nye opening the session on U.S. international leadership provides a useful analytical framework in evaluating the Clinton Administration’s performance in international affairs. The comments of Karen House and Tom Foley offer sharply different perspectives on President Clinton.

A global perspective informs WTO Director-General Renato Ruggiero’s speech on globalization and the multilateral trading system.

A global perspective also largely informs the Tokyo meeting essays by Bill Emmott, Koji Watanabe and Paul Wolfowitz, published separately in a volume entitled Managing the International System over the Next Ten Years—with excerpts included here. The authors were asked to reflect on the challenges, over the next ten years or so, of managing the international system and of democratic industrialized societies in that system. This project was in large part inspired by the Trilateral Commission’s need to re-examine the utility and outlines of a “Trilateral” approach to management of the international system, given remarkable ongoing changes in the world as we look ahead toward the next three years of our work.

We are impressed with the generally positive character of the broad changes in the world since in the Trilateral Commission was launched in the early 1970s. These largely positive changes do not mean that leadership in the broad international system is no longer needed. In some ways the need for leadership (for management with the broad interests of the system in mind) is intensified—and it is changed. The Trilateral countries remain in an important sense the “bedrock” of the wider international system. But the “glue” among our countries has weakened. The welcome end of the Cold War has reduced the urgency of Trilateral cooperation for our political leaders. The welcome spread of democratic governance and market-driven economic growth has blurred the old distinction between the “First World” and others. As relations with other countries become more mature—and power more diffuse—the leadership tasks of the Trilateral countries need to be carried out with others to an increasing extent. The 1997-2000 triennium of the Trilateral Commission needs to reflect this more complex context and the opportunities it provides.
Forging a Partnership with the New Asia

The world today is almost unrecognizable from that which existed when the Trilateral Commission was formed in 1973.

There is no longer a single defining factor of international politics. In place of the Cold War is a hodgepodge of economic and political issues, overlapping one another, blurring the traditional boundaries between the subnational, the national, the regional and the global. The pace of technological advancement has so compressed space and time that ever more issues and players compete for our immediate attention. Global free market forces have pervaded every aspect of economic life, bringing prosperity and growth even as they constrain the ability of governments to manage national economic policies.

Obviously, the complexity we now face is different from that which shaped our way of thinking for over four decades. With the growing number of issues and actors, traditional notions of economics, security and national sovereignty are increasingly called into question or even flouted outright. One would think that after Francis Fukuyama announced the end of history, the important questions would have been handily resolved. Instead, vigorous debates are going on about the place of cultural values, growth-oriented policies, the role of the state, and the role of the market in promoting human welfare. In the arena of politics, speculation is rife as to whence the next major conflict is likely to come.

Amid all these changes, a major testing ground will be Asia.

Asia has now joined the ranks of North America, Western Europe and Japan as an engine of world economic growth.

Asia, of course, is not so uniformly industrialized or democratic that it would constitute a true and comprehensive third side of the Trilateral Commission. In fact, its success poses something of a conundrum. Can the Asian miracle be replicated elsewhere? Is there an Asian model of development? Is there a set of Asian values that underlie the region's stunning performance? Or is it simply a matter of mobilizing capital and labor inputs in sufficient quantities?

The diversity of Asia allows no easy answers. Every explanation besets a counter-argument. All that can be agreed on is that the rise of Asia is the biggest event of the late 20th century. Even if we allow for the recent drop-off in Asian growth rates, or a downward revision in the GDP based on purchasing power parity (as the World Bank did for China last year), the economic weight of the region will still be considerable, thanks to its enormous and ever wealthier population. For the rest of our lifetimes, at the very least, the impact of developments in Asia will be felt far beyond its shores.

The Distracting Values Debate

Asia's economic resurgence has led to a newfound confidence. Pundits such as John Naisbitt foresee an increasing assertiveness of Asian identity, and prominent Asian leaders are making a case for the importance of Asian cultural values for economic growth and development. A growing number of influential thinkers, led by Samuel Huntington, ascribe to culture a significance that surpasses even traditional economic and political factors.

This is actually a replay of a debate in political science circles that took place a few...
decades ago, when American academics were assessing the development chances of Third World countries. The difference is that this time the cultural explanation is receiving a wider audience in policy circles.

The trouble with culture and values, as the debate on political culture the first time around showed, is that they are so hard to pin down.

In this world of interdependence and globalization, I suppose the assertion of values as an explanatory variable can be reassuring to some. But it is difficult to tell how much of, say, Asia’s economic success can be attributed to values or to the right policies and institutions. What's more, nations do not always fall neatly into the civilizational slots assigned them.

When the concept at hand is so vague and impractical, yet is presented as the major force that will lead to future conflict, it can hinder us from taking a constructive approach towards one another. Rather than a clash of civilizations, the true clash may be a clash of dogmas.

I think we should recognize the values debate for the distraction it is and focus on ways to build bridges among us. The world has a vital stake in the future of Asia. Our common interests will be better served by concentrating on that which binds us together, by identifying areas where we can cooperate for mutual benefit. It is our duty to prove that the champions of cultural and civilizational rifts are wrong.

**Coming to Terms with Asia’s Growing Clout**

More substantive challenges face the international community as it attempts to come to terms with Asia’s growing economic—and inevitably political—clout. There seems to be an odd mixture of optimism and apprehension in the West over the prospects of an Asia ascendant. I tend to see the challenges as opportunities in disguise. The trick is to approach them in the right frame of mind, to keep things in perspective.

Keeping things in perspective can be hard, but it is necessary if we are to continue on the right path. Seeing skyscrapers spring up from rice paddies and fields of rooftop satellite dishes can easily lead one to take for granted the glowing projections about Asia in the 21st century.

But there is no greater hype about Asia than the label "economic miracle." To paraphrase an old showbiz saying, it took the East Asian countries decades to become overnight successes, and plenty of toil and tears to pull off the miracle.

A miracle is by definition an unnatural phenomenon. As such, it should not be expected to last indefinitely.

Admittedly, it is heart-warming to see institutions such as the World Bank use boom-year figures to extrapolate Asia’s growth up to the year 2020, because that would make Thailand the 8th largest economy in the world by that time.

But when we consider how hard it is to forecast accurately even the next five years in this fast-changing world, such academic exercises can lull us into complacency. In between World Bank projections of Asian economic dominance, we should also take into account the predictions of the doomsayers. Andy Grove of the Intel Corporation says only the paranoid survive, and I think that's an appropriate sentiment to bear in mind as we sail into the uncharted waters of the new millennium.

Whether and how quickly Asia fulfills the prophecies made for it will depend on how it strikes a balance between sometimes conflicting priorities.

**State and Market**

One example is the balance between the state and the market. Many governments are paranoid, but not quite in the way Andy Grove meant. They want the benefits of opening up their economies, yet balk at the prospect of surrendering control to the vagaries of the market. As globalization intensifies, as market forces and technology strip away the ability of central authorities to control flows of
capital and information, governments still attempt to cling to the old certainties.

In Southeast Asia, we see evidence of this ambivalence. At one level, the region is heading towards greater economic openness and integration. The ASEAN Free Trade Area, which is on track to be completed by the year 2003, will make ASEAN a market comprising some 470 million people. The ASEAN members are firmly committed to AFTA, because they recognize that delay or backtracking means AFTA will be made redundant by APEC and the WTO. ASEAN's competitive edge and credibility depend on AFTA staying one step ahead of the game.

At another level, there is evidence that not all countries in the region are quite ready to let the market decide. While Thailand has become a regional hub for the automotive industry without state direction, countries such as Malaysia and Indonesia have invested heavily in national car projects, and Malaysia is promoting a huge Multimedia Super Corridor designed to attract hi-tech companies in an Asian version of Silicon Valley. Such efforts may well turn out to be successful in the long run, but more importantly, they show that despite what proponents of the borderless world say, governments are not about to go quietly into the night.

This ambivalence about giving market forces free rein is part of a larger trend. Mainstream liberal thinkers, including Robert Kuttner and even George Soros, are increasingly questioning the gospel of free-market capitalism.

But in economies newly emerging from the constraints of central planning, laissez-faire is the order of the day. In Asia, unfettered market forces are creating new wealth and prosperity. At the same time they are also creating new problems, of widening income gaps, of environmental degradation, of unsustainable resource use.

**Dilemmas of Growth**

This presents another dilemma for Asia. The very factors that will make East Asia an economic colossus pose challenges for long-term growth. This is the world's most populous continent, with almost 1.3 billion in China alone. The latent energies of this mass of humanity are only beginning to be tapped, as governments open up their economies and compete for foreign direct investment. As the developing countries' manpower enters the world labor market, it forces earlier industrializers to upgrade their production structure to stay one step ahead, in a kind of economic domino effect.

The upside to all this is that incomes will rise, as will demand for goods and services. This will in turn spur trade and investment, within Asia and with the world. Barring catastrophic upheavals, Asia will become the preeminent economic center of the world, even if actual growth rates fall short of those in the late 20th century.

The downside to Asia's growth is the strain it will exert on the environment and the earth's resources. This can in turn lead to international frictions.

Neo-Malthusian predictions, of course, are nothing new. The population bomb scare of the 1970s was eventually proven wrong (or premature, depending on how one looks at it), thanks to scientific advances and the green revolution. Current thinking, though, has it that the limits of sustainability are quickly being reached. Not only is the population growing, industrialization and its side effects are on the verge of outstripping the earth's ability to repair itself. This sort of argument comes not only from dyed-in-the-wool tree-huggers, but increasingly from mainstream research.

Among the most pressing issues for Asia is water. A recent UN report noted that only 0.007 percent of the earth's water is readily accessible for human uses, and that water use has been growing at more than twice the rate of the population increase during this century. With the world population expected to increase from 5.7 billion now to 8.3 billion by 2025, with more water needed for agri-

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Culture, irrigation and industry, and with a growing proportion of consumers, the strain on water resources can lead to more frequent international disputes over water rights. The Asian Development Bank estimates $80 billion to $100 billion will be needed over the next five years to lay an acceptable foundation for a water infrastructure in Asia.

Moreover, as arable land is increasingly converted to industrial use, grain production in rapidly industrializing economies may not be able to keep pace with demand. Likewise, the demand for energy will surge as Asia’s newly affluent adopt Western lifestyles, with TVs, refrigerators, computers and cars.

Already, trade in non- or semi-renewable resources has burgeoned as wealth spurs demand for such commodities as timber, oil and gas, and even endangered animal species believed to have medicinal properties.

These developments will play a key part in determining foreign policy, as nations seek to secure supplies and supply lines. Poorer countries, which tend to also be the most abundant in natural resources, will have little choice but to comply with the demands of the market.

**Trilateral Countries and Asia’s Development**

This is one key area where the West and Japan can make a useful contribution. Asia’s industrialization has come at a high environmental cost, and this is one of the most serious obstacles to sustainable development. As early industrializers, Western governments are familiar with the growing pains of rapid development, and have worked out ways to manage resources and even undo decades of damage. A growing environmental movement is gathering strength in Asia, and companies from America, Europe and Japan are well-placed to address their concerns. As Asia seeks to clean up, so can environmental management companies.

There are other areas, such as information technology, where our interests coincide—where the strengths of the Trilateral countries can help Asia’s development, while themselves benefiting in the process. Let us not be sidetracked into giving tangential issues more importance than they deserve. It is not in anybody’s interest to attempt to remake others in their image, as the only response will be resistance. As interaction and interdependence increase, a certain degree of convergence will occur naturally. Let us remember that diversity is healthy for the survival of the species. Let us find mutual benefit in our diversity, and learn from one another, for only by doing so can we grow together into a community that transcends all boundaries.

Anand Panyarachun, former Prime Minister of Thailand, is Chairman of Saha-Union Public Co., Ltd.
The Future of the Asia Pacific Region: Japan’s Approach

Japanese Foreign Minister Yukihiko Ikeda spoke to the Tokyo meeting. The following text is based on the simultaneous English interpretation of his speech.

This meeting is having discussions under the very interesting theme of Asia Pacific community-building. I would like to talk on three topics. One is regional cooperation in the Asia Pacific. What should be the desirable way of cooperation? Second are some of the instabilities within Asia Pacific. Third, as we think of the future for this region, is the very important factor which is China. What may be the prospects of China? Also I would like to, by and by, touch upon what should be Japan’s approach in its diplomatic affairs within the Asia Pacific.

Regional Cooperation

ARF. The first thing I should mention is that, in order to maintain peace and stability in Asia Pacific, the presence of the United States is indispensable. To complement the U.S. presence here, we need endeavors such as ARF and other forums for dialogue.

In this region, different from Europe, we do not have established institutions comparable to the NATO or the OSCE. In the near future, I don’t think there will be any multilateral security arrangement that would substitute for such bilateral agreements as the U.S.-Japanese security arrangement. But the efforts of dialogue and cooperation in the security area are increasingly important.

The role played by ARF is remarkable. Last year, and this year as well, I have had the pleasure of attending the meetings of the ARF. The ARF will be going on a step-by-step basis. Confidence-building measures will come first, and then we will move on to the stage of development of preventive diplomacy, and then move on to elaboration of approaches to conflicts. We are starting with the first stage right now: confidence-building amongst the countries of this region. Since we have little experience when it comes to multilateral security collaboration, for us, the foreign ministers of different countries, to come together in itself is critically important. Last year we saw very frank and meaningful dialogue on regional affairs. We also had three working-level meetings: one on confidence-building, a second on PKO, a third on search and rescue. We have seen approval of many specific and concrete recommendations.

It was impressive that China has been very active in the ARF. In the past, China has been asserting itself on matters for which its interests are involved; but for matters for which their own interests are not involved, they were just smiling—like the Japanese in the past—and saying nothing. But in the last year’s meeting, the Chinese were very active and positive and forthcoming in giving their views on matters outside of their direct interest. Together with the Philippines, China has been co-chairman of the working group on confidence-building. ARF will continue to play a very important role in the future.

APEC. On the economic front, APEC has been playing an increasingly important role. From the 1970s in this region we have seen the economic taking-off of the newly industrialized countries and then the ASEAN countries and China. We have seen a chain-reaction of industrialization and high economic growth. There has been a gradual liberalization of the market, and I think APEC has been instrumental in this regard. APEC has been articulating “open regionalism”; it is a forum which is open to the outside.
We have seen regional integrations in many parts of the world. Japan has never participated in such integrations. But for Japan, APEC is very important. It is an open regional framework and I believe we are expected to play an important role.

APEC is a forum to discuss economic matters, but it also gets into some political matters, because on the occasion of the APEC leaders' meetings, we have increasingly seen side meetings to discuss political matters as well. Many bilateral dialogues have been promoted in parallel with the APEC meetings, which I believe is conducive to creating stability for the whole world.

ASEM. The relationship between Asia and other regions is very important. The ASEM (Asia-Europe Meeting) was held in Bangkok last year. In the foreign ministers meeting held in Phuket, the meeting in Bangkok, and the second foreign ministers meeting held in Singapore this year—I had the pleasure of participating on all these three occasions. In the triangular relationship between North America and Europe and Asia, the weakest link—between Asia and Europe—has been strengthened with this ASEM endeavor. ASEM comprises not only economic but also political discussion, as well cultural exchanges. I am sure ASEM will become an even more important forum.

The Bangkok Meeting was the first occasion where the former suzerains and the former colonies participated on an equal footing, and I believe it was a quite impressive and historic occasion. There have been many follow-up meetings ever since the first meeting of the ASEM. As was mentioned in this year's meeting, we will be able to see clearly ahead of us a bridge between Europe and Asia.

Japan is a member of Asia but also a member of the industrialized nations. So we do share certain values with Europe. This unique position of Japan should be fully utilized; so we hope to play a useful role in further deepening mutual understanding between Asia and Europe.

Instability Factors
Let me now turn to some of the instability factors we see within this region. Potential destabilizing factors include problems concerning energy, environment and food, which may become the bottleneck of regional economic development in the medium to long run. But since this will be touched upon in the afternoon session, I would like to focus on instability on the political and security fronts.

Korean Peninsula. The deepest concern for peace and stability in the Asia Pacific is the Korean Peninsula, where troops continue to confront each other across the DMZ. Four-party talks have been proposed by the United States and the ROK. We believe that direct dialogue between the North and South is of great importance. Therefore we welcome the fact that the briefing on the four-party meeting was made earlier this month, and hope that the talks are realized as soon as possible.

The question of the nuclear weapons development program in North Korea not only poses a serious problem to the security of Japan and Northeast Asia, but also has major implications for the international nuclear non-proliferation regime. Under close coordination with the United States and South Korea, Japan is actively involved in KEDO activities and is soliciting the understanding and support of Asia Pacific and European countries.

Military Expenditures. Another topic is that, although the Cold War has ended, Asian countries' military expenditures are on the rise, and there are concerns that an arms race is going on in this area. I do not believe this has gone that far yet. I believe this is only an effort to modernize weapons that have become old-fashioned. These countries are using their military expenditures to modernize their weaponry, commensurate with the increase in the national budgets that has been caused by their increase in income. Therefore we do not yet need to be concerned about an arms race; but we would like to closely watch how the situation evolves.
Territorial Problems. The third destabilizing factor is conflict and rivalry over territorial issues. There are territorial problems that involve Japan; and as you are well aware, there were some situations that were of concern last year. Unlike in Europe, we do not have any institutionalized mechanism for dispute resolution, but through such fora as ARF, dialogue must be promoted. For example, in the case of the South China Sea, we hope that the ARF meeting could become a trigger to promote consultations between the parties involved. This kind of framework of dialogue is being established and we are beginning to see a beacon of hope. Regarding territorial problems that involve Japan, it seems that there are some nationalist elements on the rise when you look at public opinion both in Japan and the neighboring countries concerned. Although each nation has its own positions that cannot easily be given up, we need to be careful not to allow those disputes to lead to regional instabilities.

China
Finally, I would like to touch upon China. Needless to say, China is eminently important for the future not only of the Asia Pacific but of the whole world.

Needless to say, Japan's basic policy toward China is to support China's reform and opening-up policy. We will maintain this basic policy and encourage China to become a constructive partner of the international community. It is from this perspective that we are supporting the early accession of China to the WTO. We also welcome that China's attitude to multilateral regional cooperation, such as APEC or AEO, has become more constructive.

This year reversion of Hong Kong will take place. The whole world is keeping an eye on this. Japan considers that maintenance of free and open systems, which are supporting Hong Kong's prosperity under the rule of law, is crucial. We think that this will benefit China, too. It is important that Hong Kong's role as a financial center will be maintained under the "one-state, two-systems" policy. We are paying great attention to this.

Trilateral relations between Japan, the United States and China will be of great importance. Friendship needs to be promoted among these three nations. Although there were difficulties in U.S.-Sino relations last year, we are seeing improvements. Japan welcomes this. There were also problems between Japan and China last year, but with mutual efforts, we hope this situation can be rectified. Later this month I will visit China. This year happens to be the 25th anniversary of normalization of relations between Japan and China. Mutual visits by heads of states will be planned in the future in order to promote Japan-China relations. There were some problems in recent years. The problem of the Senkaku Islands has subsided for the time being. Over nuclear tests in China we had tentatively halted grant aid to China. However, we shall discuss the resumption of grants to be offered by Japan to China during my visit in China this month.

Some people say that when U.S.-Sino relations improve, then "Japan-bashing" will change to "Japan-passing". China and the United States will go over Japan and enhance their direct relationship. We don't think that would be true. We are of great importance as a bridge between the two; and at the same time, in the international community as a whole, all three countries have their own roles to play. They have their own obligations to fulfill in order to insure the betterment of the international community. So we should not think of U.S.-Japan-China relations as a triangle in which this side has improved and that side has deteriorated, or this side has increased in significance and that side has been reduced in significance. It's not a zero-sum game. We believe that this should be a plus-sum relationship. The general improvement of the triangle will contribute to the international community. China, which has major clout in this area, must be engaged as a constructive partner. Japan and the United States need to cooperate with each other to involve China as a constructive partner.
WINSTON LORD

The United States and the Asia Pacific Region

"The United States remains an indispensable factor of any new configuration for peace, security and economic growth in the Asia Pacific"—that's the Foreign Minister of Singapore speaking. It could have been almost any other leader in this part of the world. "No region in the world is more important to the United States than the Asia Pacific, now and in the next century"—that's a quote from me; but it echoes a widely held view, a bipartisan view, in Washington.

The ascending priority of the East Asian region for the United States was reflected in President Clinton's first term through rhetoric and overseas trips. (His first trip after the election was to our two democratic treaty allies of Northeast Asia; and his first trip after his re-election was to our other three democratic treaty allies in Southeast Asia.) Also through lifting APEC to the summit level, through maintaining our force levels, through engagement with allies and the building of regional architecture, he sought, working with others, to build a Pacific Community. In the early months of the second term, you've already had the Secretary of State visiting Asia. The Vice President arrived in Japan today. We will have the Secretary of Defense, the Chairman of the Joint Chiefs, the Secretary of the Treasury, all coming to this region in the first few months, underlining its importance.

But, frankly, there are challenges, some generic. For example, the Defense Budget Review will be coming to a head this summer. I am pleased that the Secretaries of State and Defense have already preempted one of the key outcomes: namely, they have affirmed that our force levels will remain at roughly a hundred thousand, which is absolutely essential—not the magic figure, but the maintenance of that presence—for our whole policy in the region.

Another challenge remains the Congress. There is bipartisan support with respect to our force levels and our policy generally in this region, certainly toward Japan. But we face, as we do on a global basis, micro-management, special interests, restrictive legislation. Then there is the question of resources for foreign policy, which have been declining in recent years to an alarming degree—a fifty percent cut in our international affairs budget over the past ten years or so. Here, I think the President and the Congress have finally realized that enough is enough; and that's important in Asia—not so much for aid, because of the dynamic economies, but for maintaining our diplomatic presence and for supporting multilateral institutions.

Finally, and most dramatically and most recently, there are these alleged campaign finance scandals, with a heavy Asian focus. As someone who was personally involved in all the policy-making of the last four years in Asia, I saw absolutely no evidence that this had any impact on policy, and there has been no evidence so far in the investigations. But that begs the question: how about the future, whatever the results of the investigation? And, frankly, already there is tremendous preoccupation in Washington with these investigations, with gathering information, with answering questions—which is taking intellectual attention away from the substance of policy, at a minimum, and which has killed or is delaying key personnel appointments, many of them relevant to this region. Of course, the more fundamental question is: will it have an impact on the substance of our policy? The jury is out on that. I would like to think we will pursue our national interests.

* * *

Now, let's go to the specifics. Four years ago, in my Senate confirmation hearings, I laid out ten specific goals for American foreign policy in this region—if you will, Lord's Ten...
Commandments. In staccato form, they were: global partnership with Japan; stopping the nuclear threat and moving toward peace on the Korean Peninsula; positive engagement with China; deepening our ties with an expanding ASEAN; normalizing relations with Vietnam; promoting an independent Cambodia; strengthening APEC; building regional security dialogues; spurring cooperation on global issues; and promoting our values. I would submit that the record over the four years is quite good on most of these objectives. Of course we made mistakes. We also made some course corrections, stylistic as well as substantive, as we went along. Of course, inevitably, most of these issues are works in progress. So, let me take each in turn—given the time limits, in brushstroke form—to bring the challenges up-to-date and to give crisp policy prescriptions.

**Japan: Update Global Partnership, Prevent Revival of Tension over Okinawa and Trade**

We begin as we must, and should, with our relations with Japan—the most important probably in the world, certainly in this region. The policy prescription now, to update what has truly become a global partnership, is to prevent the revival of tensions over Okinawa and trade. Our partnership is, I think, the strongest it's been in a half century, in the wake of the President's very successful 1996 trip—thanks to our global cooperation, regional cooperation and bilateral efforts. But to maintain this situation is going to require efforts by both sides.

On the Japanese side, on the security front with respect to Okinawa, stronger efforts by the government are needed to stress the importance of this alliance and our presence to the Japanese national interest and the regional interest—as opposed to coalition politics and the dangers that can present. On the economic front, it is important that the economy be stimulated by domestic demand and not go back to an excessive focus on export drives. Moreover, there is the strong need for reform, for deregulation, for implementation of past agreements. And more generally, it is time at last for Japan to take steps, and say they’re taking steps, in their own national interest—not because of gaiatsu (foreign pressure).

The United States has its own policy imperatives. For all the objectives in the region, we have got to maintain our engagement, our presence—that's a given. More specifically on the security front, continued sensitivity to Japanese and Okinawan concerns is required, without affecting our capabilities. On the economic front, bilateral negotiations remain necessary but the United States needs to move increasingly toward multilateral forums like APEC and WTO. And, generally, we need to meticulously consult with our Japanese partners on all the issues I am going to be discussing.

The Japanese fear of U.S. preoccupation with China this year, with summit meetings, I think should never have been there. We are, after all, fellow democracies and we're allies, unlike with China, as much as we want to engage China. The danger now, with what is happening in Washington, is that Japan won't have to worry about excessive dealings with China for the wrong reasons.

**Korea: Launch Genuine North-South Dialogue and Negotiations**

I've heard in this meeting some criticism of U.S. policy toward North Korea. All I would say is that, for $25 million a year, the United States has stopped the most urgent security challenge—not only in Asia but in the world—when we came into office four years ago. Many people forget the atmosphere in 1993 and 1994 when the North Koreans were on the verge of presenting a genuine threat on the nuclear front. We froze their nuclear program completely. It has to be dismantled before they get nuclear reactors. The so-called nuclear capability, at most, is one nuclear device. It's not going anywhere. They've got to reveal it before they get key parts for nuclear reactors. So, I think that's a pretty good deal. Meanwhile, just in recent weeks, we finally got the North Koreans to sit down for a briefing for possible peace talks on the peninsula.
So, my policy prescription here, updating what we had four years ago, would be to launch genuine North-South dialogue and negotiations. This is very difficult for three reasons: first, the historic hostility and mistrust on both sides; secondly, the North Korean decades-old strategy of dealing with the United States over the heads of our Korean allies; and thirdly, the domestic scenes in both parts of the peninsula. The brutal, opaque, volatile regime in the North is beset by economic crisis, and there is a decline of the Kim Young Sam government in the South because of scandals, which in turn tempts the North Koreans.

U.S. policy should consist of maintaining vigilance, deterrence, firmness with the North, continuing to make clear to Pyongyang that it must deal with South Korea; keying the pace of our ties with North Korea to that principle, while maintaining solidarity with Seoul, not letting its domestic politics jeopardize that process; and pressing ahead with the four-power talks, where the fundamental trade-off will be confidence-building measures and reduction of tension by the North in exchange for economic assistance by us, by South Korea and Japan. We should maintain close coordination with China, with Russia, and other interested parties. And we need to do a much better job of contingency planning—either for the bad news of implosion or a military incident, or for the good news of reunification and what that means for U.S. force levels.

**China: Advance Bilateral Relations in the Face of Tough Domestic Scenes**

China has received, correctly, a great deal of attention in our discussions the last two days. This is the most critical, the most complex foreign policy challenge for the United States in the coming decade. My prescription here is to advance bilateral relations in the face of very tough domestic scenes. Our tactic is engagement; our strategy is integration. I've worked on Chinese affairs for twenty-five years (ever since I preceded Henry Kissinger into China in 1971), and I will tell you that this is the most difficult mood and the most difficult regime that we've had to deal with during that entire period.

Why is that so? First, there are some generic historic reasons. The Chinese have had very little experience in dealing with the outside world as equals. For four thousand years they were number one—everyone else irrelevant or tributaries. For one hundred and fifty years, they were humiliated by foreigners. That complicates their attitude. Then you've got the phenomenon, always delicate, of an emerging power adjusting to a status quo superpower.

More specifically, you have many other reasons why they're difficult to deal with. They're rising in economic and military strength and reflecting that in increased nationalism, which is being used (along with political repression and raising standards of living) to maintain Communist Party control. In a period of transition, no leader can afford to look soft on America on sensitive issues. Also, the Chinese have watched what happened in the former Soviet Union, and they have concluded that too much political freedom will threaten their party control and their territorial control. In addition, they're suspicious—either alleged suspicions or genuine suspicions—that the United States is out to contain China, divide China, subvert China.

Having said all that, I want to emphasize that the Chinese genuinely want good relations with the United States, at least for the next couple of decades until they grow stronger—for obvious economic reasons and also for geopolitical ones, because it's still useful to have the "far barbarians" balance off the "near barbarians" who are historical antagonists.

The mood is equally difficult in the United States. The bipartisan consensus of several Administrations has been frayed by Tiananmen Square, by the end of the Cold War, and by Chinese behavior. And there's a tendency now in certain quarters to demonize China, to have it replace Moscow as our enemy. And now, of course, you have these allegations of improper, illegal financial influence, etc. There
is therefore a massive debate taking place in the United States on our China policy. I think this is inevitable; I think it's actually healthy; but I also think it's terribly distorted. Containment is put forward by some, but this assumes that China will be hostile and aggressive. We should not assume that, any more than we should assume that China will be benign and cooperative. Containment would be a self-fulfilling prophecy, turning China into an enemy. It would divert diplomatic, political and military resources of the United States. It would forfeit Chinese cooperation on many issues. And, unlike against the Soviet Union during the Cold War, we would be totally alone. Many of our friends and allies are preoccupied with rising Chinese power, but they don't want direct confrontation. So we'd not only be acting on our own and therefore be ineffectual, we'd have tremendous frictions with Japan, with Korea, with Europe, and with many others.

Therefore the Clinton Administration is pursuing comprehensive engagement. Its conceptual framework for the long term is to work with others to integrate China in the regional and world institutions—have the Chinese accept, but also help shape, norms and rules and institutions. Give China a stake in being cooperative rather than aggressive. If you will, tame any possible adventurous impulses through interdependence and self-interest. Thus we seek to expand areas of cooperation—which don't get attention in the media, whether it's regional security (Korea, Cambodia, or Central Asia), or arms control (extending a Non-Proliferation Treaty or a nuclear test ban), or working together at the UN, or cooperating on new global issues (like the environment, crime, terrorism, drugs, and refugees). At the same time, of course, we have some serious problems that we have to work to narrow, or at least contain the fallout. They include human rights, trade, proliferation, Taiwan and the very important wild card of Hong Kong. I will fearlessly predict that Hong Kong will go either extremely well or extremely badly or somewhere in between.

Now, engagement does not mean rolling over for the Chinese. In addition to seeking cooperation, it means advocating your values. It means tough negotiations, whether on the WTO or anything else. It means threatening the largest trade sanctions in trade history in order to get proper implementation of the intellectual property rights agreement. It means imposing sanctions, whether well-advised or not, when the Chinese transgress on proliferation issues. And it means sending aircraft carriers into the Taiwan Straits. Engagement also means keeping your powder dry, shoring up your alliances (such as the President's trip to Japan and his trip to Australia and other allies) and maintaining our force levels.

**Adjust to ASEAN's Expanding Size and Clout**

The fourth area is ASEAN, the single most under-appreciated area out here in U.S. domestic coverage. If I had the time I'd go into some other astonishing figures with respect to its trade importance—half the world's shipping goes through Southeast Asian lanes—and the growing collective importance of ASEAN. My policy prescription here is to adjust to an expanding ASEAN, expanding with respect to size and with respect to clout and cohesion.

With respect to size, it faces real challenges, political and economic, as its original members are now joined by Vietnam and three more countries (including Burma)—generally more repressive and less affluent than the "tigers" they're joining. With respect to the challenge of adjusting to ASEAN's clout, it's getting to be a little bit like it has been at times with the EU. You can't negotiate with it while they're making up their minds and their positions, but once they've got a collective position, you can't negotiate with it. So, we welcome ASEAN's greater strength. We should and must deal with it collectively as we have, both in a bilateral sense and in the regional institutions, where they've taken the lead. We should also maintain our strong bilateral ties to try to affect the course of ASEAN policy decisions—Indonesia being the one perhaps most likely to be dis-
torted by our domestic debate. We also, of course, must maintain our assets of interest to ASEAN and other Asian countries, namely an open market and our military presence.

**Vietnam: Put Meat on the Bones of Normalization**

Vietnam is one of the major achievements of the Clinton foreign policy of the first four years. It is also the most quiet achievement, because of a very nervous White House about political backlash, always exaggerated by the White House. What we’ve done has actually been widely supported. In the process of normalization, gradually, we’ve served the highest policy goal of information on missing-in-action. We’ve also served our regional security interest, our economic interest, our interest with respect to drugs and refugees, our geopolitical interest, and also our interest in healing the wounds of that bitter war.

So, my policy prescription here is to put meat on the bones of normalization. We have problems with the still vocal, but highly exaggerated opposition in the Congress among some special interest groups. We’ll also have problems as we get more deeply involved with Vietnam, as we have with China to a certain extent—the classic debate about how you deal with a repressive political system when you have so many other positive interests at the same time. But Vietnam has major incentives to move ahead with us, both geopolitical and economic. And we have some specific policy steps we can take in the next couple of years that could advance this process: getting our ambassador out there, setting up a consulate in Saigon, negotiating a trade agreement, MFN, Export-Import Bank credits, other commercial agreements, military-to-military exchanges, and cooperation on issues such as drugs and refugees.

**Cambodia: Help Maintain Domestic Peace as Elections Approach**

Cambodia represents a stirring panorama of movement away from the killing fields (thanks to UN, international, ASEAN, U.S., and Japanese support): violence is way down; free elections; the return of four hundred thousand refugees; removal of That, Chinese and Vietnamese outside influence; some progress in economics and toward a civil society; and massive Khmer Rouge defections (they’re down to banditry). My prescription is to help Cambodia maintain domestic peace as it moves toward the ‘97 and ‘98 elections.

Inevitably the Cambodians face problems, and they’ve had some setbacks, given the magnitude of their challenges and their historic backdrop. These include growing corruption; suppression of dissent by opposition politicians, journalists, etc.; and now increasing tensions between the “odd couple” running the coalition. They’re close to civil war at times; and as they head toward the elections in ‘98, the two Prime Ministers have figured out there’s only going to be one Prime Minister. U.S. policy must be one of “tough love” toward the coalition partners: don’t expect miracles given the magnitude of their challenges and the distance they’ve traveled; try to offset the media focus on their shortcomings; maintain our diplomatic, economic, and non-lethal military assistance; help them build a civil society; but at the same time, and quietly, caution coalition leaders against corruption and repression and against coalition in-fighting; and as elsewhere, closely coordinate with Japan and ASEAN and China and others.

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As we deal with key bilateral relations, we should at the same time maintain the momentum of building a Pacific Community—working on regional institutions and functional challenges. Some of what the Administration has been doing in this field, working with the countries represented in this room, will have some of the most lasting impact. Over the long term we want to move increasingly toward multilateral approaches to economic, security, global and value issues, but the U.S. presence and our bilateral ties will remain key for the foreseeable future.
APEC: Define a Broader Agenda while Delivering Practical Results

The single most important community-building mechanism, of course, is APEC. We've had a good discussion of that today. The President lifted APEC to the leader's level in Seattle in '93. This was crucial: we now have an annual summit meeting of the Asia Pacific leaders, which has broader implications. The bold trade liberalization target dates have been set.

The prescription here is to define a broader agenda while delivering practical results. It's not a choice between the vision of free trade by 2010 and 2020 (which we should be moving toward), the very setting of that date has implications already in freeing up trade) and something else. We have got to deliver practical benefits for businesses, which are the ones building the Pacific Community above all, and have governments get out of the way. So we have to work on both fronts. But APEC is at a crossroads in its definition—not only of its membership, but of its agenda. Increasingly, as trade ministers handle the business of trade negotiations, what are the foreign ministers going to talk about? What are the leaders going to talk about? It is important to make it worthwhile for the leaders to meet every year.

ARF: Move from Promising Beginnings to More Concrete Progress

The building of regional security architecture has the same potential long-range significance we see with APEC. Unlike previous Administrations, the Clinton Administration has encouraged regional security dialogues—not as a mask for withdrawal, but rather on top of the foundations of our alliances and military presence; supplementing them, not supplanting them.

My prescription here is to move from promising beginnings to more concrete progress. In just three years, the ASEAN Regional Forum has included all the major actors, including Europe. It helped to calm down a South China Sea conflict a year-and-a-half ago, showing its potential. Sensitive issues are already being discussed and confidence-building measures are already being developed. But we need more concrete confidence-building measures. We need freer and less stilted exchanges among foreign ministers. And we need to define the agenda once again.

Furthermore, the ARF is a rather ungainly (although inclusive) organization of twenty countries. It doesn't really feel suited to tackle Northeast Asian problems in any depth. So, I hope the "track two" academic approach to Northeast Asia—involving the two Koreas, Japan, China, Russia and the United States—can be turned into an official track to focus on Northeast Asian problems, now that the North Koreans look like they're going to join the four-party process.

Elevate Global Issues on Bilateral and Multilateral Agendas

In the next century some of the key issues are going to be global issues, as the huge population and resource pressures take hold out here, and as other issues like drugs and refugees, crime and terrorism unhappily persist. My prescription here is to elevate these issues on our bilateral and multilateral agendas. We already have a very remarkable common agenda with Japan, as I've mentioned, and there's tremendous potential here working with China. The Vice President will be stressing that in China in a few days. China recognizes its need on the environment, for example. Moreover, it recognizes the need to work on other problems, such as terrorism (which they've seen in their West) and drug trafficking (which they've seen on their South).

On the whole, however, regional efforts on these issues are rather fledgling. They need to be beefed-up and related to global efforts. I would recommend that APEC get even more serious about environmental issues and other global questions related to economics, and that the ASEAN Regional Forum (and the Post-Ministerial Conference related to it) tackle security-related global issues like terrorism, crime and drugs. Working together on these topics...
has two advantages: it's the only way to resolve these issues, and it also gives you positive agendas for bilateral relations and regional mechanisms.

**Promoting Our Values:**
**Surmount the Current Distracting Debate**
Finally, the tenth commandment: promoting our values, human rights, democracy. This is the central issue with respect to building a Pacific Community. It is also the most misunderstood. My prescription is to surmount the current "distracting" debate (as former Prime Minister Anand of Thailand put it yesterday) about the clash of values. Promoting these values has a traditional place in U.S. foreign policy under any Administration—of course to be balanced off against our other interests. It is required for domestic and Congressional support, but it is also fundamentally pragmatic, because it forwards our other interests—economic and security interests, for example. The fact is that open societies do not produce refugees or attack each other across their borders or practice state terrorism. So there is a very practical edge to doing this. But it must be done without arrogance and without an annoying missionary zeal, with respect for other cultures and histories and stages of development. Of course it's better if it's done multilaterally—but frankly we get very modest help from our European, Japanese and other friends. Of course it should be done above all, if possible, by indigenous groups, non-governmental groups—they are growing in importance and we should support them.

The current debate about the clash of values is fundamentally distorting, and indeed it's demeaning to both sides of the Pacific. It suggests that the West does not care about family or discipline or community, or that the East does not care about individual freedom and liberty. The fact is the trend in Asia is toward open societies. The fact is there are universal aspirations, and it's racist to suggest otherwise. The fact is that in developing economies in the modern world of technology, information, the Internet, computers and satellites, you cannot have for very long, in my view, open economies and closed politics. You can't have investment without the rule of law. You can't attack corruption without a free press. You can't advance complex economic reforms without dissent and debate. And you can't expect people to adjust to painful transitions without accountability and incorruptibility among their leaders.

Let me close with a quote that I fully agree with, from a distinguished Asian observer: "If we in Asia want to speak credibly of Asian values, we too must be prepared to champion those ideals which are universal, and which belong to humanity as a whole. It is altogether shameful, if ingenuous, to cite Asian values as an excuse for autocratic practices and denial of basic rights and civil liberties. To say that freedom is Western, or un-Asian, is to offend our own traditions, as well as our forefathers, who gave their lives in the struggle against tyranny and injustice. It is true that Asians lay great emphasis on order and societal stability. But it is certainly wrong to regard society as a kind of false god, upon whose altar the individual must constantly be sacrificed. No Asian tradition can be cited to support the proposition that in Asia the individual must melt into the faceless community." That's a quote from a speech by Anwar Ibrahim, the Deputy Prime Minister of Malaysia.

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On the foundation of our alliances and our military presence, through diplomatic and economic engagement, with the patient building of regional economic and security architecture and the promotion of freedom, we're seeking to build, in conjunction with others, and while respecting diversity and individual identities, a more secure, prosperous and free Pacific Community.

Winston Lord, former U.S. Ambassador to China, was Assistant Secretary of State for East Asian and Pacific Affairs in 1993-97.
Commenting after Winston Lord’s speech was Michael Armacost, former U.S. Ambassador to Japan and Undersecretary of State for Political Affairs, who is now President of the Brookings Institution.

I don’t disagree fundamentally with anything that Winston Lord has said. Let me mention three things that occurred to me as I listened to him speak.

The President’s Sustained Involvement is Fundamental

I read carefully Win’s testimony when he was confirmed in 1993. I thought it was a very good road map for our policy in Asia. I was not infrequently critical of the Administration, but invariably the criticism occurred when the Administration deviated from the road map that Winston laid out. As Joe Nye acknowledged yesterday, we had a somewhat ragged start in ’93 and ’94. Happily, we’ve done a better job of positioning ourselves for the next four years.

If we’re going to exploit the opportunities which we now have, the most important thing is that the President engage himself in a sustained and consistent way in the management of the key relations in the region. The episodic, rather sporadic involvement of the last four years won’t do. The relationships are too important; the responsibility cannot be delegated.

This is true for two reasons. First, we all know that China is a hierarchical society which is going through a political transition. If we are to have an authoritative strategic dialogue, it must be conducted at a Presidential level. This is not a matter that can be pawned off to others. Secondly, we Americans are going through one of those introverse phases in our history—not isolationist perhaps, but we are preoccupied with internal matters. Only the President has the bully pulpit from which he can explain the stakes we have in relationships as important as those with Japan and China, and elicit support for the difficult trade-offs that will be required to keep those relationships under control.

Those of you who know Americans well realize that in dealing with China we have a special problem. Historically, attitudes toward China have been extremely volatile in our country. We go through pendular swings from abject cynicism to naive sentimentality. Overlaid on that fluctuation of public moods, there is now the problem of special interest politics. We have an incredible array of groups that feel passionately about China, most of them negatively. The environmentalists worry about the high sulfur content in the fuels Chinese use; the labor unions about the jobs displaced by labor-intensive exports; the Christian Right about the frequency with which abortion is relied upon to control population; everybody has a special agenda. Unless the President articulates a clear strategic concept for managing the relationship, there’s no hope of disciplining this incredible array of special interest groups. So the President’s involvement is fundamental. Is it possible? Surely it’s possible. Is it likely? I haven’t a clue.
Concentrate on Fundamentals in Economic Relationship with Japan
The second point is: it's important that we maintain the focus on fundamentals in our economic relationship with Japan. We've gone through a period that's been relatively quiet with Japan for the last eighteen months on trade, and the last twelve months on security matters. That's largely a result of the fact that the trade statistics have been moving in the right direction. Japan's trade surplus with the world has been coming down; and its trade surplus with us was declining until recent months. It's very unlikely that those conditions will continue. With the yen where it is, and with the prospect of relatively slow growth in Japan over the next year, I would be very surprised if our bilateral trade deficit with Japan didn't grow, perhaps quite dramatically. And those are the conditions in which it usually is difficult to manage not only trade, but security relations as well.

So I hope we can concentrate on the fundamentals. The fundamental problem for us, of course, is the imbalance between consumption and savings in our own society. Everybody who studied Economics 101 knows that if you consume more than you save, you must make up the difference with imports. So however assertive our trade policy, we can merely rearrange the composition of our deficit. We can't reduce it unless we get a hold of our problems at home. We have made, I think, quite impressive progress in the last few years in reducing the "dis-saving" of government (we haven't done so well in raising household savings). But I don't believe there are any grounds for complacency for Americans, because I fear the President took a pass on the budget this year. The expenditure cuts he proposes are mainly back-loaded to the point where nothing much happens until after he's finished his term. And it's difficult to imagine the Vice President, who will confront opposition from his left for the 2000 nomination, being more courageous on these matters than a President who's just been reelected and faces no further campaigns. The Republicans meanwhile were battered on the budget issues last year and, therefore, are not displaying much courage on these issues either. So there is a danger that we could lose momentum on this very important issue which will ultimately be decisive with respect to our management of trade with Japan and others around the world.

The fundamental challenge for Japan is precisely the subject we heard discussed yesterday: administrative and regulatory reform. I was very encouraged by the briefings I heard yesterday. When I was posted to Tokyo in the late '80s, there was a lot of talk about deregulation, much of it based on the Maekawa Report. The calls for deregulation were phrased in terms of the need to harmonize Japan's industrial structure and business practices with those of its trading partners. That was music to American ears, and I'm sure to European ears; but when one thought about it, it was difficult to imagine Japanese politicians going out and making a strong case for such dislocative adjustments in order to mollify foreigners. What we heard yesterday was: administrative and regulatory reform are needed in order
to preserve the competitiveness of Japan’s economy, the prospects of future economic growth, the avoidance of irrelevance as a financial market. These are substantial interests, real interests; it’s not difficult to imagine Japanese politicians expressing those interests with real conviction, or Japanese voters embracing such ideas with real enthusiasm.

So that’s encouraging. At the same time, we all know that “he who initiates the draft, controls the law.” In Japan, when one moves from general principles to specific proposals, invariably one must rely on the repository of knowledge and experience that is in the bureaucracy. The principles that we heard adduced for regulatory reform—international comparability, transparency, reliance for managing supply and demand upon the market (rather than upon visible hands in Kasumigaseki)—have to be translated into detailed proposals by the administrative class, many of whom perceive them as an attack on their source of power. I believe there will, nonetheless, be progress on these issues, but it’s going to be a difficult and time-consuming struggle. It’s important for foreigners to position themselves in a way which encourages the proponents of regulatory reform, while insisting on outcomes that result in genuine national treatment of our own companies.

Cultivating Friends Bilaterally is Vital for Multilateral Coordination

A final comment. It’s extremely critical for us to achieve some balance between cultivating bilateral relationships and approaching problems multilaterally. Very often I find in discussions at home that people treat bilateralism and multilateralism as alternatives. Back in 1993, when we discovered the Korean nuclear problem was more acute than we had thought, anybody who reflected on the problem understood that we couldn’t orchestrate an effective strategy without the help of China, Japan, South Korea and others. Unfortunately, through absent-mindedness or a lack of strategic thought, we allowed our relations with each of those countries to atrophy to the point where it took much more time, and was more difficult than would have been necessary, to organize a multilateral effort. When you think about Korea today, you can imagine a scenario either of implosion and collapse or perhaps of a “soft landing.” We will cope more readily with the consequences of collapse if we work together with other countries in the region. If it’s a soft landing, it’s inconceivable we could orchestrate the necessary financial support without coordination among our friends. That requires that we cultivate our friends, and so I believe we should start with that task.

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If we can remember some of these things, it seems to me the prescriptions that Win laid out very thoughtfully will be more easy to manage.
JUSUF WANANDI

Building the Political and Security Underpinnings of Community

Let me congratulate the three authors on the paper prepared for us today. It is a very balanced paper. Take a closer look at the proposals put forward there, especially on the role of the Tri lateral countries towards this part of the world.

Balance of Power, Concert of Big Powers, Community

Well, with the end of the Cold War and the realization that economic growth and dynamism alone are not sustainable without a security underpinning, thinking has been going on in the region about what kind of security arrangements should be established in the future for the Asia Pacific part of the world. (I would rather talk about the "Asia Pacific" because, especially from the political security perspective, it's much more valid to talk about an Asia Pacific encompassing North America than about only "Pacific Asia" or "East Asia.") Three ideas have been discussed.

The first is a balance-of-power arrangement. But this idea is criticized because experiences in Europe have shown that a balance of power alone cannot be sustained, cannot be stable over the longer term.

The second idea is a concert of big powers or great powers. Four have been mentioned in this part of the world: the United States, China, Japan and Russia. Some even put ASEAN into this concert of powers. But there has been a lot of criticism of this idea because there is not yet any concert, and to wait for a concert definitely will take a lot of time. And basically, it is against the grain of historical development: countries would like to have a more democratic arrangement established, and issues not decided by only the few.

The third idea is that a community be established for the Asia Pacific. I endorse the paper's main thrust that efforts concentrate upon how to build a community for the Asia Pacific region in the future. It will take some time; we are just starting.

Balance of Power Plus Institution-Building

There will be a mix of elements of what has been existing before in this whole development of the region. The first element is the presence of the great powers. There is a certain element of a balance of power already; that has to be accepted, and is a fact of life for the region. Here, the United States' presence, including its military presence, is vital. The main bilateral alliance making this possible is the U.S.-Japan alliance, which is vital to the region as well. There are some problems on the Chinese side, but I think that will be overcome in the discussion to come in the future.

The second element is institution-building, which the paper has dealt with at length. The first institution is ASEAN, for Southeast Asia. We soon expect ten members, in the middle of this year. There will be some difficulties for ASEAN for sure. First, the process of decision-making will get more complicated with three new members, including Myanmar. Second, the development of AFTA (ASEAN Free Trade Area) is going to be more complicated, because we have then to face a two-tier membership in that respect. And third, we will be clobbered by Tri lateral countries because all ASEAN will look like Myanmar. But the decision has been made, because the leaders think that this is an historic moment, that the ten Southeast Asian countries should be together and we are not going to postpone it anymore. We tried to get Myanmar as a member twice before—in '67 and in '72—and she declined.
The trend in Myanmar is still very uncertain, whether she would like to become isolationist or not. A strategic decision has been made in ASEAN to bring Myanmar in. It is now or never, with all the consequences thereof. In the foreign ministers meeting in Singapore last month between ASEAN and the EU, this has been thoroughly discussed, and I think both sides have come to the conclusion that both sides have to do something about Myanmar. We have a plan in ASEAN to lay down a roadmap for political as well as economic development in the assistance to Myanmar to be established.

The second institution is APEC, for the greater Asia Pacific region, which will be discussed later.

The third among these institutions for the region is the ASEAN Regional Forum. This has been very newly established—three years ago. It has now a very large membership of twenty members, ten Southeast Asian and ten dialogue partners of ASEAN. Therefore the process will be slow, but it has to be admitted that this is the only regional institution we have.

For the first few years in ARF we are stressing confidence-building. Some measures have been agreed upon and are being implemented. One is an annual regional seminar on security developments among officials. Second is the exchange of officers of the defense establishments, as well as cooperation between the presidents of the national defense universities and institutes—they have just decided on that in Beijing. Of course another one is the so-called Defense White Books to be published. Fourth is to encourage everybody to actually endorse the existing non-proliferation regimes for nuclear, chemical and biological weapons, as well as the registration of conventional weapons.

We are just starting with a second-track effort to propose to the ASEAN Regional Forum how to proceed on preventive diplomacy. In the medium term, it is hoped that the ASEAN Regional Forum is also going to become a conflict-resolution mechanism. There is in this respect a decision on peacekeeping that has gone quite far. There will be a seminar at the end of this month in Kuala Lumpur of the trainers of peacekeepers in the region. Search-and-rescue coordination in the region has been established, and there will be disaster relief operations as well. It is only the beginning, and you have to bear that this will be a slow process.

There is a lacuna in this ASEAN Regional Forum, and that is dialogue and confidence-building in Northeast Asia. We are now talking about the possibility of the ASEAN Regional Forum moving into confidence-building for Northeast Asia. We are discussing and consulting whether or not it is appropriate at this stage to have North Korea included as a member of the ASEAN Regional Forum.

Last but not least among the institutions is the ASEM process between Asia and Europe. Some of the programs established last year in Bangkok are now starting to be developed and expanded, including businessmen meetings and foreign ministers meetings. There will be economic ministers meetings to work out some of the programs established in Bangkok last year.

In all of this confidence-building and institution-building in the region, the second-track approach and effort has to be recognized. The second-track is non-governmental, although government officials have been included in a private capacity. The idea is to give some input—ideas as well as pressure—to the governments on cooperation in the various fields.

The last element of this community-building effort is strengthening the global multilateral institutions. What was said yesterday by Renato Ruggiero on the WTO is valid as well in the political security field. One part is to strengthen the UN-led collective security system, to build a stronger regional cooperative system to support Chapter VIII of the UN Charter and to cooperate with the UN as a whole.

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Europe has just come to the scene in the form of ASEM.

What then can the Trilateral countries really contribute? Japan and the United States are very much part of the region and therefore they are involved in all of the efforts of community-building that have happened so far. Europe has just come to the scene in the form of ASEM. So there are regional institutions in which everybody can cooperate to support the idea of community-building in this part of the world.

The economic part is a very important part of the development of the region and in the development of security in general. This afternoon there will be more that can be discussed on how to develop cooperation in the economic field. But the political security part must not be forgotten. In ASEM we have laid down that political cooperation between Asia and Europe has to be pursued further. We can learn—we are very new—what other parts of the world have been doing in cooperative security efforts and common security efforts.

Jusuf Wanandi is Chairman of the Supervisory Board of the Centre for Strategic and International Studies, in Jakarta.

Yuan Ming

The Importance of Politics and Strategic Vision

My experience three years ago here in Hotel Okura with this distinguished group still stands very fresh in my mind. At that point the excellent report An Emerging China in a World of Interdependence was discussed, and I've got to tell you it was very well-received at home too. China, as my French friend said yesterday, doesn't want to be a schoolboy sitting in anybody's classroom—but China wants to learn. An Emerging China in a World of Interdependence got a lot of attention at home. Several discussion groups were formed affiliated to different departments of the government and paid a lot of attention and concern and discussion how China could cope with this kind of strategic idea.

I think this new piece—Community-Building with Pacific Asia—is excellent. It will take some time for me to really digest all the richness of this report but I want to mention a couple of points.

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First of all, it's very important to emphasize the importance of politics. This is really the time to think about politics very seriously and cooperatively, collectively. It will really shape the future of the world, of the region, in the twenty-first century.

We have got to notice the phenomenon that new leadership is emerging in the region. The World War II veterans—that kind of leadership—are passing from the scene. The new leadership lacks the kind of experiences of their predecessors. Also they are not the kind of leaders who can use personal charisma to lead their people. So facing that kind of chal-
lenge, how could they work cooperatively and collectively? It's a challenge. Really, it's a challenge.

A famous American politician said, "All politics are local." This is shown in many capitals in the region. Leaders get blocked by all these domestic issues and it's very difficult for them to communicate very directly without any kind of hesitation—very open, very frank discussion, face-to-face dialogue. There are too many restraints for them to do so. So how to make some breakthrough and suggestions for them? We have got to think about it. Leaderships are too busy to think deeply, and we have really got to help them. So it's very important for this report to mention the importance of politics. It's really a strategic consideration.

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The second point I want to make relates to the emphasis on community-building. It seems to me it's a step further from the 1994 Trilateral Commission report, An Emerging China in a World of Interdependence. From a Chinese perspective, I will say it's a step forward to put this policy of engagement in a more concrete and healthy way. Of course, the question is how.

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My third point is the crucial importance of U.S.-Japan-China relations. I have got to say at this moment a lot of suspicions hang on from a Chinese perspective towards both the United States and Japan—especially relating to the U.S.-Japan security treaty. A lot of talks were going on and a lot of different ideas are being expressed, but so far no consensus has been reached. It's not a good sign. So, how to solve this very crucial and difficult problem still remains a big challenge. Maybe we'll start some exercises of trilateral meetings.

Bilaterally, U.S.-China relations are the most crucial and important issue at this moment. Though we have a lot of difficulties right now, it seems to me the historical legacy is still there. We Chinese always say Americans are too arrogant, very self-centered, very self-righteous. On the other hand, I would say as Chinese we also have our cultural legacy and we also have our self-righteousness. But how to overcome those kind of things and develop and build up something new for the new world? We've got to think about it.

In talking about U.S.-China-Japan relations, we have got to think about what Russia is thinking and what Korea is thinking. It is very important to shape some new U.S.-China-Japan relationship. We couldn't do that without suggestions and help from the Russian side and from the Korean side.

* * *

Just a few words on China. Later on we'll have more, so I'll just talk very briefly. China is now going through a transitional period, no doubt about it, but this is not a transition from the Deng Xiaoping period to the post-Deng Xiaoping period. The post-Deng period started a couple of years ago. This transitional period is from the command, planned economy to a more open, market economy. This is a real challenge, especially reform of the big state-owned enterprises.

This year, there are coming two very crucial issues for China. One is the transition of Hong Kong and the second is the CCP's Fifteenth Party Congress in the fall. These are very high concerns on our domestic political agenda.

* * *

I have just a couple of ideas off the top of my head after reading all those excellent suggestions in the report. First, I think this report should be used to brief the leadership, because it really contains a lot of constructive ideas and thoughts. We have to make full use of it. Secondly, we should use this report for the NGO dialogue—to open more dialogues and meetings with the people concerned. There are a lot of thinkers in the region. To invite their concrete ideas and suggestions would be very helpful. Thirdly, educating the younger generation is very important. Now, more and
more young people are interested in business, mainly because the world changed. At my university, Beijing University, the most brilliant students now don't want to go to the Department of Political Science and Department of International Politics. They want to join the Business School and the School of Management. And this is not only in China. When I travel around the region, that's everywhere. The good news is that so many dynamic, brilliant young people want to jump into the sea of business and are doing beautifully. But on the other hand, I really worry about the future if they totally concentrate on business and management without enough political sense and strategic vision. Then how could they shape the future of the world? So I think for the education of the younger generation, we've got to broaden their vision. Let me say this report could be teaching material for the younger generation—especially the brilliant young students in the business school and the school of management—and give them some sense of the importance of politics.

I have some reservations about this report on the Taiwan issue. In the report, there are some suggestions about possible visits by democratically elected Taiwanese leaders to the Trilateral countries, although not in their official capacities. I do have concern about this. At the moment this issue, Taiwan, is something really serious. And we've got to be very, very careful of that. Think about Mr. Lee Teng-hui's visit to Cornell. It was not in his official capacity but it raised such a noise. So if we think about this in concrete terms, we've got to be very careful.

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I am delighted to be here as a guest from a non-member territory. The world has changed greatly since the founding of the Trilateral Commission in 1973, especially in the past eight years. Maybe it is time to re-examine Trilateralism or at least the definition thereof.

My remarks will relate primarily to China. I will also say a few words about the other major players in the Asia Pacific community.

Where is China Today?
This century has proved to be one of continuous upheavals for China. It began with the defeat of China by eight foreign powers. In 1911, the Ching Dynasty was overthrown. This was followed by Chiang Kai-shek's attempt to unify the country. He led several Northern Expeditions to defeat War Lordism. Then came the invasion by Japan in 1931, which led to the Sino-Japanese War in 1937. After its termination in 1945, civil war broke out culminating in the founding of the People's Republic of China in 1949. The country hoped better days had finally arrived, but hope was once again dashed. Numerous cruel political campaigns in the 1950s and 1960s were followed by the ten mad years of the Cultural Revolution, which must rank as one of the greatest human tragedies of the 20th Century.

In late 1978, an upheaval of another sort quietly began. For once, finally, it has been for the betterment of China. In terms of its social impact, the economic opening initiated by Deng Xiaoping is no less an upheaval than the overthrow of the Ching Dynasty in 1911 or the arrival of the Communist regime in 1949.
Every one of the billion plus lives has been affected.

So in the past 18 years, China has marched forward in the right direction. It has moved from being the most leftist country in the world to one on the far right. Look at where China has come from: before 1978, China made Stalin look as if his middle name was Reagan, and Khrushchev like his middle name was Thatcher. Raw capitalism is no longer found in any of the Trilateral countries. Yet it pulsates in China. In some ways, the Chinese economy is more market-oriented than most Western European countries represented here. As a percentage of total GNP, the government in China is smaller than in much of Western Europe!

Economic reform soon spread to social and political reforms. But the most significant change is of ideology. Somewhere along the line, a fundamental conversion has transpired—quietly. Many who know China realize that she is today no longer an ideologically driven country. Economic development has taken center stage; and as a result, with the exception of a few areas, pragmatism has replaced idealism. One can argue that, after all the terrible upheavals, the ruling party has lost all legitimacy to rule. If the leaders want to regain it, they must give the Chinese people better livelihoods. A prolonged economic downturn may mean social unrest and trouble for the rulers.

Given where China was only 18 years ago—a totalitarian state with a completely centrally planned economy—what has happened since then is nothing less than amazing. Although China is now more market-oriented than many countries in the West, she still lacks—in some cases completely—the necessary social institutions. Until very recently, things such as a civil service system, a central bank, commercial and other laws, and regulatory bodies—to name just a few—were all missing. None of these can be organized, let alone perfected, in a short period of time. Often the old systems must be torn down first, and resistance from different sectors of society is inevitable.

Nothing is more difficult to overcome than entrenched concepts deeply rooted after some forty years. Take, for example, the abolition of the price control scheme. It took about ten years and many failures. But it was finally accomplished, peacefully, under Premier Li Peng, who is supposedly not known for his reform policies.

With all the changes—economic, social and political—there are serious dislocations in almost all areas of society. While some of these spell opportunities for businessmen, they are nevertheless very unsettling for all concerned. Given what has already been achieved, I argue that reforms in China could not have gone any faster without seriously running the risk of the society imploding—and social unrest which would make Bosnia look like child's play!

The changes in China, especially the economic ones, did not go unnoticed by the West. Indeed the assertion that China is now a powerhouse was not first made by China. Western media told her so! In late 1992, the *Economist* published a 19-page article on the rise of China, which started a trend. Somehow, through many pieces, the economic strength of China has come to be perceived as an economic threat, and this economic threat has somehow been translated into a security threat.

America and Europe were the first to recognize China's economic prowess, but Japan was the first to formulate a comprehensive thesis of the "China Threat." Is this a reflection of the differences in the way the West and Japan look at China?

In the past 150 years, China has been the "Sick Man of East Asia." Now, for the first time, she is thought of by the major nations as a world power. She is like a farm girl, who has never been to the city, all of a sudden thrust onto the stage on Broadway. How awkward she must feel! By the same token, it can be argued that America in all her history has never had to deal with another 500-pound whatever as a friend. After World War II, every other nation was a client-state either of the United States or of its then opponent, the Soviet...
Union. America has never had to face another superpower or potential superpower on a friendly basis. She too, in this regard, is inexperienced on the world stage. When we have two of the biggest players stumbling upon each other on a shrinking global platform, trouble is almost unavoidable.

Here, allow me to say a word as a businessman with extensive operations in China. Having known the bowels of Chinese society, especially of its state-owned enterprises, I must say that I am not sure China will be a sustained player in the economic field. Once you know their mindset, management, organization, technology, physical and social infrastructure, etc., you may not be as positive on China’s economic prowess.

China’s Relationship with Her Neighbors
The topic of this session is community-building in the Asia Pacific region. It seems to me that today China is not in any community at all. She does not have any sense of belonging; she feels strongly that she must fend for herself, including being self-sufficient in food supply. Look at her neighbors—Russia to the north, Japan to the east, Vietnam to the south and India to the southwest. All of them were enemies not too long ago. Then there is the United States on the other side of the ocean with its military power projection capabilities and intentions towards China at best uncertain.

Yet in China, economic development has become the paramount concern. Only by improving people’s lives will the rulers have legitimacy. Moreover, the Gulf War of 1991 served as a wake-up call to China that warfare is now a technology game. Without economic development, there is no money to acquire technology, and without technology, one cannot have modern weaponry to defend oneself. As a result, China must have peace with its neighbors.

This is why President Jiang Zemin, who visited India last November, will soon go to Russia, where Premier Li Peng was two months ago. Dialogue and mutual visitations between China and Vietnam have been stepped up recently. And for the first time in history, China welcomed the Japanese Emperor to her soil in 1992. Her need and her intention are more than clear.

China’s Long-Term Intention
But are China’s neighbors ready to make peace with her? At the heart of the matter is their suspicion of China’s long-term intention. Most Westerners and Japanese alike still fear that China will one day become a security threat. Why do they believe that?

Some of them say that China is Communist and so must be a security threat. While China’s history since 1949 has been very troublesome, all of her problems have been domestic. At no time has she shown territorial ambition over neighbors. She has not gained a single inch of ground, and has never attempted to do so.

Since 1949, China has fought five border wars. In the Korean War, she was invited in by the North (just as America was invited by the South). In 1962, India invaded her. China ended up taking a lot of land, but voluntarily returned it all. Then there were the three wars involving Vietnam. China was first invited to fight the French. Then during the Vietnam War, China was welcomed by the North (just as the United States was asked in by the South). The last time, in 1979, China wanted to teach Vietnam a lesson, but ended up being taught one.

Then look at China’s longer-term history of relative peace with her neighbors. Given her size, she had many tributary states. China certainly had a lot fewer wars with her neighbors than most if not all European states during the comparable periods. Moreover, although China repeatedly sent its navy to Japan, to Southeast Asia, and all the way through the Indian Ocean to the East Coast of Africa, since the 15th Century, she never colonized anyone as European nations did. Neither is her history like that of Japan, which repeatedly took land from her neighbors—all of Korea and parts of China, notably Manchuria and Taiwan. Indeed, China has been more
peaceful with her neighbors than most if not all other nations.

Others say today that China is a security threat because of her nationalism. But China is not even a nation-state as the term is understood in the West. As the Chinese scholar Lucian Pye once said: China is a civilization which feigns to be a nation-state. Indeed one can argue that the over-emphasis on family is so strong in China that they are almost incapable of nationalism. There is a Chinese saying that a filial son will never be a soldier, or even a policeman. During the height of the Sino-Japanese War, young Chinese were dodging the draft in droves. Only in 1944 did university students begin to join the armed services in any significant numbers. So where is the nationalism?

In times of peace, the Chinese can hardly agree with each other on anything. Sun Yat-sen, father of modern China, bemoaned the fact that Chinese people were like a bowl of loose sand. They simply will not stick together. Many years later, Mao Zedong complained of the same thing. If any images best depict the Chinese people of the past 150 years, they are: "Sick Man of East Asia" and "Bowl of Loose Sand." As a people, China is struggling to shed the former image, but has yet to deal with the latter.

I believe today the West, especially America, is misreading China just as the United States misread Vietnam in the 1960s and '70s. The price for the present mistake, if uncorrected, will be equally severe, if not more so. America thought that North Vietnam was a threat because it was Communist. The fact was that it was, first and foremost, nationalist. China after 1949 was primarily Communist and not nationalist. All Communist regimes liked to export their ideology. However, unlike the former Soviet Union which annexed its neighbors, China never attempted to do so. Now Communism as an ideology is bankrupt everywhere, including in China.

What China wants today is to build up its economy, so she will be able to "rise to our feet"—as Sun Yat-sen once mistakenly thought he had accomplished, and as Mao Zedong prematurely proclaimed on top of the gates of Tiananmen on October 1, 1949. Deep in her psyche, China wants to shake off the affront to her self-esteem of being the "Sick Man of East Asia," rise to her feet and be an equal among the prosperous nations of the world. She does not want to be subordinated to foreign powers (as she was from the 19th Century); neither does she want to have others be subordinated under her. She wants to be a co-equal within the international family of nations.

**Incorporate China**

So what should our posture be towards China? We should do our best to incorporate her into the Asia Pacific community, and indeed the international community. Some would ask: what if your assessment of China's long-term intention is wrong? My answer is the same: rope her in! If I am right and China is shown to be a good international citizen, then we have nothing to worry about. If we make it too difficult for her to get in, we may in fact drive her away. This is a real possibility today.

Even if I am wrong, it is much better during this proving period that China should be under our nose, rather than left outside to her own devices. If we allow her in today, we can always kick her out later. But if we exclude her now, we may be unnecessarily creating an enemy which both sides cannot afford.

Given this, we should as soon as possible bring her into international bodies such as the World Trade Organization. We should also encourage her to participate in all relevant international treaties—relating to weapons non-proliferation, trade dispute resolution, human rights, etc. No one says that this will be an easy process, but it is the only sensible thing to do. We should also incorporate her into international security arrangements.

This is why I believe the April 1996 security reaffirmation between the United States and Japan is fundamentally a wrong move. It is not that I want to isolate Japan. Far from it! That would be too dangerous, for she would rearm in no time, not to mention the devel-
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...development of nuclear weaponry. The United States, and indeed all of Japan's neighbors, should embrace Japan. No one understands this better than China.

But the United States and Japan are not the only two major powers in Northeast Asia. There are now at least three: the United States, Japan and China. The binding of any two will create an inherently confrontational environment. Who is the U.S.-Japan security arrangement against? What do you imagine the Chinese will think? Look at it this way: if the security arrangement were between the United States and China, then what would Japan do? Would we fault her for rearming?

Of course China understands the necessity to keep Japan under the U.S. security umbrella. (Ostensibly for face reasons, China will not openly admit it.) After all, China is much more afraid of Japan than of America. But just try to convince Beijing that the only purpose of the agreement is to keep Japan at bay, and has nothing to do with China! Besides Japan, who is it directed at other than China? North Korea? There are already American troops in South Korea. Russia? Hardly so given her state of affairs.

So given this U.S.-Japan security reaffirmation, one would be naive not to expect China to rearm even faster. Yesterday one of the Japanese participants worried that the Chinese military budget has increased substantially of late. Well, by all accounts, it is smaller than that of Japan, which is meant to be for defense only. (One percent of Japan's GNP is a huge number, which makes Japan's defense budget the second highest in the world in absolute terms!) Why can Japan have a huge military budget and China, which is a sovereign state, cannot have a smaller one? China has a much longer border with potentially hostile neighbors, and a very long coast. She has a renegade province in Taiwan which, in case of an emergency, is an issue which must be resolved. Historically China has never invaded Japan; in contrast, Japan has repeatedly invaded China (and Korea) since, at the latest, the 16th Century. More recently, Japan took Taiwan from China in 1895, Manchuria in 1931, and waged a full-scale war from 1937.

Given the present situation in Northeast Asia, a U.S.-Japan bilateral arrangement will create as many problems as it hopes to solve. Rather, we should have a trilateral security arrangement which includes China. Yoji Funabashi of the Washington Bureau of Asahi Shimbun, in a November 1996 article, proposed what he called a 2 + 2 + 2 formula. In essence, his suggestion is that the Foreign Ministers and Defense Ministers of the three countries—the United States, Japan and China—should regularly meet together. This can be a first step.

Is such a trilateral arrangement possible? It will not be easy, but I believe it is doable. Back in 1993, China was watching the then new Clinton Administration. Unfortunately, the United States decided on a wrong policy, which most Americans today would admit. It will be a lot tougher now after four years of a stormy relationship, but I still believe it can be done. After all, there is another foreign relations team in the new Clinton Administration.

The bilateral security agreement between the United States and Japan is originally a product of the late 1940s and 1950s. But the world has changed, and Northeast Asia has changed. China is no longer the same as it was forty some years ago, and we must accept her as she is today. She has been moving in the right direction for at least eighteen years. Not incorporating China into the Asia Pacific community will only be to our own peril. China is a 500-pound something—whether teddy bear or grizzly bear the West does not know. So what do you do? As I often say: if you are locked in a cage with a bear, the safest position is to hug it! (The same is true dealing with Japan.)

While building the trilateral security arrangement, we must keep Russia and Korea informed in order to minimize suspicion. In the longer term, this arrangement should be enlarged to encompass a six-power pact. Call it the North Pacific Treaty Organization (similar to NATO), which will comprise the United States, Canada, Japan, China, Russia and the united Korea (or
South Korea, if the Peninsula is not united in the near future).

Some may ask: who will be the enemy? The answer is: there is none, and there should be none. Maybe this will be the new form of security arrangements in the increasingly multipolar world. By being partners with each other and everyone, we insure that everyone plays by the same mutually agreed rules. We are each watching out for everyone else. In this new paradigm, words such as "alliance" lose their meaning. There will be no "alliance" because there will be no "enemies." It is more appropriate that we think of each other as partners working for the common good. This will be the ultimate community-building.

The 20th Century will soon be over. As we look back, I believe it will be marked by two human experiments. The first was Communism, which has failed even before the century is over. The second is how to get out of Communism while maintaining economic growth. If the transition out of Communism fails—be it in Russia or in China—it will wreak havoc on the entire world in the next century. Let us make sure that we help rather than impede Russia and China as they struggle to join the world community. Both countries are trying hard. I believe China has a better chance. I have operations in both, and so have a useful perspective on each.

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Southeast Asia
Now let me briefly comment on each of the other major players in the Asia Pacific region, starting with Southeast Asia. The major trend there is in fact community-building. This is amazing indeed, for only a few decades ago, that part of the world was diagnosed to be terminally ill! Yet against all odds, a number of Southeast Asian countries have maintained relative political stability and, in the process, achieved economic success. Now out of this political backwater rises a strong spirit of community-building. They are forging a mode of cooperation which is in some ways exemplary.

While the same form may not work for other regions, it has so far done well for Southeast Asia. Just consider: ASEAN, APEC, ARF, ASEM, plus all the Track II activities.

As to challenges for Southeast Asia, political succession must be high on that list. Many countries will face the issue in the coming few years, such as Indonesia, Malaysia, the Philippines, and maybe even Singapore.

Korea
Korea will in the coming decade remain a sensitive and important area. While foreigners are increasingly talking about the possibility of reunification, my Korean friends tend to shy away from the subject. They prefer to speak of a "less confrontational Korean Peninsula." The experience of Germany with reunification has scared the South Koreans.

Although no one in Japan talks about it, they must be uneasy about a unified Korea. China probably also prefers to keep the status quo of a divided Korea. Nevertheless, I get the impression that China might have accepted the eventual collapse of North Korea now. North Korea has been a friend of the Chinese, but has increasingly become a nuisance, if not an embarrassment. After all, China has already established a relationship with the Republic of Korea.

Reunification of Korea will have far-reaching ramifications on Northeast Asia, if not all of East Asia. A key element will be the fate of the American military personnel in Korea and, by extension, in Japan as well. What will be the rationale for keeping American soldiers in either Korea or Japan? Will there be another pretense why American GIs should stay in the Peninsula? And if the United States were to withdraw troops, or even significantly cut back the number, what will be the reaction of the united Korea, of Japan, and of China? All this would substantially alter the security equation of Northeast Asia—so the North Pacific Treaty Organization is needed that much more.

Here a side-point which is worth noticing. Whenever I speak with South Korean friends...
on their security situation, they usually start with the relationship with China. But soon their attention turns to Japan, which then dominates the remainder of the discussion. It seems that they are more afraid of Japan than of China, although the latter is a bigger country, is a closer friend with North Korea, and is physically nearer. The interesting question is not whether my friends are correct, it is: why do they have that perception?

Taiwan
Apart from North Korea, the Taiwan Strait must be the most dangerous flash point of East Asia. The determining factor here is one person: Lee Teng-hui.

In the cross-Strait relationship, China is reactive. She does not want to be proactive. China has no intention to regain Taiwan in the near future, and there is no domestic reason for Beijing to use force. Yes, China wants the renegade province to be reunited with the Motherland, but she understands that no one likes a poor relative. With economic development, per capita income in China will one day catch up. When it becomes 20 percent of that of Taiwan (the present differential is 35 times), reunification will be much easier.

Time is on China’s side, and she can wait a long while. Unless seriously provoked, China will do its best to avoid using force. If she is forced to fight to regain Taiwan, she will lose all except the satisfaction of reunification. Capital, technology, human resources—all would flee the island. China would be left with a reluctant, if not hostile province, not to mention the loss of all friends in the international community. This would set back China’s economic program for decades. These consequences are not something that the Chinese relish; but if Taiwan moves too close to independence, Beijing will have no choice but to fight. No Chinese leader will be able to keep power—and that includes the just deceased Deng Xiaoping—if he is weak on issues of territorial integrity. The people will demand it.

I am amazed by my American friends who want China to promise not to use military force. China will never make that promise, unless Taiwan pledges not to move further to independence. (China has clearly stated two other conditions under which she will militarily take Taiwan: social upheaval within Taiwan or foreign intrusion into the island.) The day China makes that unilateral promise would be the day that Lee Teng-hui declares Taiwan’s independence.

Lee has worked tirelessly in the past few years to rearrange Taiwan’s internal affairs to make reunification increasingly difficult. Moving towards democracy is key to that process. The wider the social gulf is between the two sides of the Strait, the less the Taiwanese people will want reunification. Watching all this, China is displeased; but there is not much that she can do unless Lee goes too far.

At the heart of the danger is that Lee Teng-hui does not understand Beijing. As Sun Tze writes in The Art of War: know yourself and your counterpart and you will win every battle. Everything that Lee has done so far suggests that he has very little understanding of how Beijing thinks and works. One of his advisors said to me last summer that Lee Teng-hui was really surprised by the severity of China’s reaction to his Cornell trip in June 1995. Apparently Lee has replaced his senior foreign affairs team with people who think like him. With those knowledgeable about China (or, for that matter, the United States) removed, the situation is that much more serious. I am really concerned that he will push too far, which will force the hand of Beijing. That will be disastrous for all concerned.

In analyzing the Taiwan situation, there are two other players of significance. The position of the United States is relatively clearer, in spite of her policy of “calculated ambiguity” during the missile incident of a year ago. Will the United States come to Taiwan’s aid if civil war breaks out? I believe the United States must keep reminding Lee Teng-hui not to provoke China further, as he has increasingly done even after the missile incident of 1996. There is rea-
son to believe that Lee expects the United States to intervene in case of war. Given his volatile personality, repeated warnings from the United States are very necessary.

The other player which must not be forgotten is Japan. What is her intention vis-a-vis Taiwan? Is there anything involved for Japan other than pure economics? How will Japan develop her sphere of influence? Although I know many Japanese would still like to see Taiwan as one of their colonies, or at least become independent, I trust that Japan today does not have any territorial ambitions. Yet Japan has done precious little to affirm the One-China policy.

**Japan**

Japan is undergoing self-discovery. She has done it before, notably during the Meiji Restoration and the later expansionism which ended in her defeat in 1945. After the War, she gave her full attention to building her economy. But now that she is rich, what is next? What is Japan’s long-term intention other than business? What role in the world does Japan want to play? Is it possible to have in the world today a country as wealthy and technologically advanced as Japan which has no other focus than economics? What will her relationship be with Korea and with Taiwan?

What about her relationship with China? Does Japan want a strong China? Probably not. Though unspoken, that impression seems unmistakable when one speaks with the Japanese. These days there is a debate in the United States about whether America wants to contain China. I am willing to bet that many more Japanese than Americans would like to see China contained.

Yet China represents a potentially huge market for Japanese goods. So Japan is in a dilemma. She is somewhat schizophrenic about China, as she is about many other things. Someone said yesterday in our meeting that Japan feels inferior but also superior. Japanese are the only people I know who have an inferiority complex and a superiority complex in the same person and at the same time. This is indeed a nation of contradictions.

**United States**

Most Asians are of two minds about U.S. leadership: we cannot live with it, but we also cannot live without it. Asians love U.S. products—from Coca-Cola to Steven Spielberg; we envy her technology—from biotech to infotech; we want her markets; and we need her Seventh Fleet. But we do not like America’s insensitivity and bullying.

How does the United States view her own presence in Asia? For economic and security reasons, the majority of Americans want engagement with Asia. I do not believe isolationism is a serious threat, although, as someone said yesterday, America will from time to time be preoccupied by domestic issues.

The issue is not whether America should be engaged in Pacific Asia. Rather, it is the form of leadership which America must assume today. Asia—and indeed the world—is a very different place from that right after the Second World War. In those days, America blew the trumpet and we all followed. But Asia has grown up. This dictates a new mode of leadership. Gone are the days when one speaks and all others listen.

In the new mode of global leadership, the United States will be the first among equals. Her role will be one of a facilitator or a catalyst. At times she will be an initiator or a proposer, although in many circumstances it is much more effective to be a silent proposer—in other words, somehow put the thought in another country’s mouth and let them think that it is their idea. America will have to be a persuader and not a dictator; and if necessary, a mediator or an arbitrator. But at all times, she will have to be a moral leader. This form of leadership is very different from that understood and practiced by the United States in the post-war years.

Can the United States fill that role? I seriously doubt it. The American system is simply too open. Regulations increasingly move the

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society in that direction, and the media ensures that nothing is said or done outside of the public eye. Can there be any quiet diplomacy which, I submit, is necessary? It is becoming increasingly difficult.

There are also too many checks-and-balances: Congress versus the Administration, the Republicans versus the Democrats, and all the interest groups. Can there be one spokesman in foreign affairs? If not, how does the United States exercise leadership in that arena? As one U.S. Congressman said to me, the 535 Members of the House and Senate are like children without adult supervision. When it comes to foreign affairs, this is disastrous. When Americans debate and fight among themselves, all in the open, other countries are totally confused.

The new style of leadership requires much more skill and finesse, but the American system, and indeed American culture, are so unsuited to it. Herein is the dilemma for all of us. This is not to mention the zeal with which many interest groups (to which many U.S. lawmakers belong in one form or another) preach to other countries. They like to impose their own values on other people, and they do it with little or no sensitivity towards others' history and culture. Moreover, in the past four years, there has been no prioritizing of issues. The result is that whoever in the United States shouts the loudest will get the most attention. Her neighbors are totally befuddled. This is not good for mutual trust or community-building.

A strong U.S. President who is interested and engaged in foreign affairs will partially alleviate the problem. Let us hope that we do not have to wait another four years to see that.

Europe
Until the ASEM meeting in Bangkok a year ago, there was no forum for senior-level discussions between Europe and Asia. Since the end of World War II (which also marked, for the most part, the end of colonialism by European powers in Asia), ties between the two continents—both political and economic—have been wanting. As such, the renewed interest of European companies and the recent ASEM meeting can be considered Europe’s rediscovery of Asia. Given the trilateral nature of the world today—North America, Europe and East Asia—this new Europe-Asia nexus should be welcomed.

On the economic front, the two regions are in many ways complementary and should have a closer relationship. It can only benefit both parties. Furthermore, Europe has one advantage over America in dealing with Asia. While Europe respects human rights and operates democratic political institutions similar to those in the United States, Europeans are much less dogmatic. If the United States can be likened to far-right fundamentalists, Europeans are nominally religious. The latter take a much more pragmatic approach to these things. As a result, there is much less friction both on the government-to-government level and on the business level.

Ironically, this approach may prove to be more effective in engendering pluralistic and more tolerant societies in Asia. America tries to directly influence if not change Asian societies, but Europeans create an internal sense of need within Asia for a better society through the building up of a middle class. In so doing, although European countries cannot directly claim credit for the positive changes, they also do not create ill feelings or strain in bilateral relationships. A by-product is that European companies, if they are competitive, will make more money for themselves—and in the process improve the livelihood of many Asians as well as contribute to the liberalization of Asian societies. This is a real possibility in the coming years.

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ASEAN and APEC

As Chair of the Asia Pacific Economic Cooperation (APEC) forum in 1996, the Philippines hosted, quite successfully, the regular APEC meeting that was capped by the annual summit of APEC Economic Leaders, in November last year. And I must admit that, as we labored to bring those meetings to a successful conclusion, participants from the countries and regions represented here—the United States, Japan, Europe—showed a lot of skepticism about the APEC process. The United States hardly submitted anything of significance in its Individual Action Plan (IAP). Japan submitted virtually nothing in its IAP. Europe met us with tremendous skepticism, with doubts so thick they could have been cut with a knife.

Let me then talk about APEC and the process that moves it along, from the perspective of the APEC chair in 1996, and about how important it is to keep this process going in the face of all the skepticism that we encountered. There were very important lessons learned from our turn as APEC chair and as host of the APEC meetings in 1996, lessons that might prove useful to non-APEC members as well. I speak not only as a Filipino, but as someone who represents the region of Southeast Asia as well.

**ASEAN Lessons for Community-Building**

The first lesson we learned about building a community—perhaps the most important aspect of APEC, based on our experience in Southeast Asia—is that each one who pretends to be a member of that community must be prepared to put his own house in order. From this comes credibility, and authority. All of the talk today about community-building in Southeast Asia—or in the entire Asia Pacific region, for that matter—will remain just that, mere talk, if there is no real commitment on the part of each member to try and keep his affairs in order. I say this after having shed a great deal of sweat and blood back in the Philippines helping get our economy back on track. For many years, the Philippines could not but speak with a small voice in the Association of Southeast Asian Nations (ASEAN); we did not have much to say, mainly because we did not have much to show. After we had finally gotten our house in order, or at least partly in order, we were then able to play a more active role and take on more responsibilities not only in ASEAN but also in APEC.

For us, the Southeast Asian countries, the next task in building the Asia Pacific community was to strengthen our subregional association. If we cannot hold together a small group of nations, then I doubt if we will be able to make a significant contribution to the formation and the guidance of a much, much larger group. I remember representing the Philippines in the initial ministerial meeting of APEC in Canberra, Australia. We—the six members of ASEAN then—felt that we were not ready to enter into a large organization at that time because ASEAN was not strong enough. Especially given all the skepticism we encountered these past few years as we strove to build a bigger community—whether it was global, Asia Pacific, or East Asian in scope—we needed to prove that we could get our act together on a subregional scale. In the specific case of ASEAN, we think that it will be able to pull its own weight in the much larger association that is APEC only if ASEAN is given the support to strengthen itself as a subregional group.

In our part of the world (I say this especially to the Europeans), talk is many times different from action. I was reminded by one ambassador that, when you look at Southeast Asia, you must watch not their lips but their hips—where they actually move. In Southeast Asia, in trying to strengthen ourselves, we concentrated on a lot of economic rhetoric. But to tell you very frankly, we did very little about economic cooperation during the first 15, 17,
20 years of ASEAN's existence. The action was in the political sphere. There was a lot of cooperation between governments—you will remember our effort regarding Kampuchea, or Cambodia, in the United Nations. That was an ASEAN-led initiative that was very important for us at a time when we could not make a significant advance in economic cooperation for various reasons. We felt it was important for ASEAN to make a success out of some area, and this happened to be in politics. Political cooperation for many years was not talked about very openly in ASEAN. But in Asia, at least in Southeast Asia, it is not so much the talk that is important, it is not so much the rhetoric that is important, it is the action that is actually undertaken.

The third element in ASEAN which is important in building a broader community, whether in Asia itself or the broader Asia Pacific region, is that we did a lot of homework in getting people together. We did not build ASEAN on the basis of just governments talking with one another. We built ASEAN on the basis of bringing a whole lot of members of what we now call "civil society" directly in touch with one another. As we say, not only our politicians were getting together, not only our editorial writers were getting together, but even our cartoonists were getting together! And so a whole proliferation of people who did not talk with one another, who did not know one another, began thinking together, addressing questions that were very specific to them. A very broad range of contacts enabled peoples to feel comfortable with one another. I think this is very important in our relationships with China and other economies that we are not very familiar with—to make people comfortable with one another by getting them to talk with one another, to think together, to solve various problems together. That's why we have always been insisting on open sub-regionalism. This is an APEC term now, but that is an ASEAN experience. We have always been interested in internally strengthening ourselves first, but always open to the rest of the world. Why did we have to worry about Kampuchea? And why are we worrying now about three other countries coming into ASEAN as fast as possible? Simply because of this—we are interested in opening ourselves to the rest of our neighborhood, the rest of the world.

The ASEAN Countries in APEC
It is important when we talk about APEC that we reflect on the experience of ASEAN, because we who are in ASEAN and who are members of APEC always insist that the types of procedures we are following in APEC should be those that we in ASEAN are comfortable with. This is something that many Europeans never understand. They say, "What kind of organization is this? You come to agreements that are not agreements because they are not binding." But judge us on the basis of results.

APEC's concentration on trade, on investment and on business is very ASEAN—and I think that it is very APEC, and very realistic. For the beginnings of a community, our experience in ASEAN has always been, let's work together on those things that we need not quarrel about. Let's leave for later those issues that divide us in the hope and expectation that, after we have gotten together and resolved a number of problems that are not so difficult to resolve, then we can tackle the more difficult ones. I think it is important that we understand that in building APEC as some sort of a community, we start first with business, we start first on trade, we start first on investment.

Now this is boring stuff. In Manila last year I heard quite a lot of foreign ministers say, "Oh, of course talking about trade and investment, that's not our cup of tea." Half of them were falling asleep most of the time. One of them suggested to the Chair last year that, "Hey, next year, get all of these sherpas to work together, let them come with their statements, let's acknowledge that they did a good job and then let's bring ourselves to a retreat where we can talk very freely just as we have been doing in ASEAN." Yes, we have an economic cooperation meeting, but after we spend some ten
minutes on it, we spend the whole day talking about a whole lot of other things. And there are a whole lot of other things we can talk about informally under APEC which we would probably not advertise to the rest of the world. It is important, based on our ASEAN experience, that we start with trade, we start with investment, we start with those things that we feel very comfortable with—and then we move on forward.

Now what are the results? Insofar as ASEAN is concerned, a result of APEC is that we have decided to accelerate our economic cooperation. Now, instead of only talking about economic cooperation, we are really doing something about it. When we signed the agreement for AFTA in Singapore in 1992, the original deadline was 2008. But after the WTO agreement and after we saw the reality of APEC coming up, we said we are going to move forward our trade agreements to the year 2003. Now in ASEAN there is active talk—led by the smallest economy of all, Brunei—that we would like to get all of this thing done by the year 2000. And surprise of surprises, the two most closed economies in Southeast Asia, that is the Philippines and Indonesia, are saying, look, we’re going to liberalize and we’re going to liberalize not only to the whole of ASEAN, but we are going to liberalize to the whole world by the year 2003. Now that is ASEAN talking, and I think that is the result of APEC, simply because there are pressures that we have gotten ourselves into that have forced us to accelerate the pace at which we should go. Maybe this is not following the Cartesian logic of the Europeans, but the fact is that there is movement.

A lot of people concentrate simply on the ITA (Information Technology Agreement) among the results of the 1996 Manila and Subic APEC meetings. Yes, we have moved the WTO forward with respect to this sector, but more important for us, although this is not advertised, is the framework agreement on development cooperation, again following the ASEAN model of getting people—our traders and our businessmen—together to work out those principles.

Economic development is now part and parcel of the APEC agenda. Running on a parallel track is the ASEAN Regional Forum, where security issues are discussed. President Ramos wanted to suggest during the Subic meeting that, look, we can have our trade ministers talk about trade and investment, but heads of state talking only about trade and investment doesn’t make sense. At some point in time, you must begin talking about broader issues. And I think this is the importance of APEC. If we keep the process going, you certainly have an informal umbrella—we do not want to formalize this—where heads of government can begin talking with one another, not only on economic relationships but also on the broader consequences of broader economic integration.

Two Last Points
There are two last points I would like to make. In APEC we have been subjected to a lot of criticism about the interest on the part of ASEAN to get the Asian economies together. This has been a proposal of Malaysia and we in ASEAN think it is a good idea. It has been always shot down by the United States and, with some difficulties, also by Japan. But we think that getting Asian members of APEC to talk with one another in an informal dialogue would be very important. We do it already because of our relationship with Europe, with ASEM. When we have to prepare for ASEM meetings, then obviously the foreign ministers and the economic ministers of East Asia have to get together. This is a process we must encourage rather than stop. Getting ASEAN in there with Japan and China would make it much more conducive for confidence-building than if you left Japan and China together. We think that ASEAN and the other Asian economies can contribute to the economic dialogue that should go on very intensively—informally, formally—within the APEC umbrella for greater economic cooperation and responsibility in Asia.

Finally, economic interaction within East Asia is increasing at dramatic rates, but we...
cannot forget the financial dimensions. This is one of the biggest concerns we have: we are so economically interdependent, but we have not started talking seriously about financial interdependence. We have given a lot of rhetoric to the importance of financial flows, but we have not started to address this very important issue.

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ROSS GARNAUT

East Asia’s Growth and APEC’s Open Regionalism

Thanks to the Trilateral Commission for inviting an Australian along.

Sometimes we Australians don’t seem to fit very well within any of the established classifications. Our main objection to some of the groups that Jesus Estanislao has been talking about is that we are classified out of them. Of all the countries on Earth, the one which sends the highest proportion of its exports to East Asia isn’t Japan, it isn’t China, it isn’t Singapore—it’s Australia. Of all the countries on Earth, Australia, by quite a large margin, in proportion to its population, takes the most immigrants from East Asia. Not proportionately but absolutely, there are a larger number of schoolkids in Australia learning the Japanese language than in any other country on Earth other than Japan. There are more schoolkids in Australia learning the Indonesian language, absolutely, than in any country other than Indonesia and Malaysia.

We have before us a very good paper from Morrison, Kojima and Maull. I want to take up two issues that are in the paper but need to be taken further. One is the sustainability of East Asian growth. The second is the role of “open regionalism” in APEC and the World Trade Organization.

The Sustainability of East Asian Growth

The issue of the sustainability of Pacific Asia’s growth came up a number of times already in our discussions. In one of the questions yesterday, attention was drawn to Paul Krugman’s skepticism about the sustainability of this growth. There are a lot of blind alleys we can get ourselves into there.

The reality is that East-Asian-style growth persists when a number of conditions are met. There’s nothing miraculous about it. Nine countries in East Asia have now experienced that style of growth at rapid rates. You need high rates of savings and investment. You need a lot of structural flexibility, and a lot of international orientation to get that structural flexibility. You need a considerable use of markets. It’s a silly dichotomy to draw between growth dependent on increases in inputs and growth dependent on increases in productivity, because the two are very closely interrelated. The big difference between the high rates of investment in East Asia (in all nine of the countries which have sustained high rates of growth) and high rates of investment in the former Soviet Union—a comparison made by Krugman—is that the investments in East Asia have been disciplined by a market, and in particular by an international market. That has meant that those high rates of investment weren’t wasted, didn’t lead into diminishing returns.

The whole experience of East Asia has been that once rapid growth has got underway—Jess Estanislao has been part of the successful end of a very long struggle to get it underway in the Philippines—it has lasted. It requires an effective state, a consistent approach to a number of areas of economic policy, to get underway, but once the high growth rates are coming through, it’s much easier to sustain. The process of rapid growth politically vali-
dates itself, reinforces itself. The political headaches once it's underway are suffered more acutely by those who for ideological or other reasons want to knock it off course.

It doesn't go on for ever. Part of rapid East-Asian-style growth is a process of catching up with superior technology and management methods abroad. So as the world frontiers are approached, it slows down. We saw that in Japan in the early '70s. We've seen it successively in Hong Kong, in Taiwan and, in the last year or two, probably in Singapore. We'll see it in one after another of the other countries. But those frontiers aren't reached quickly. There's no general tendency for growth to slow down until those world frontiers of productivity and average incomes are being approached.

If that's our perspective, then we can see that rapid East-Asian-style growth hasn't jumped up on us suddenly. It's been going on now for half a century beginning in Japan, Taiwan, and Hong Kong. We can see it continuing for another half a century. We're probably halfway through the whole process in time; and probably only a quarter through in terms of the increase in output.

The frontiers of East-Asian-style growth are constantly shifting. The success of the advanced countries, the earlier countries in the process, shapes the path of others later on. We've seen that most interestingly by what's happened in Japan through the deep and painful recession of these last half-dozen years. Although Japan's GDP growth has been slow as structural changes continue in Japan, the movement off-shore of labor-intensive processes and rapid increases in imports of labor-intensive manufactures from East Asian countries have continued. That's helped to underwrite the expansion of trade. It's one of the reasons, along with the China boom of the 1990s, why rapid growth was sustained in East Asia right through the Trilateral recession of the 1990s. (East Asian growth stalled in the earlier OECD recessions in the early '80s and early '70s)

So I've got a lot of confidence in the durability of the economic determinants of rapid East Asian growth.

Some different sorts of questions about the durability of East Asian growth have been raised in the course of our discussion—some of them political and security questions. It goes without saying that a major political catastrophe in a large country in the region, in China or Indonesia, would upset the whole process. The descent into war would upset the whole process. But we've discussed that elsewhere.

Other sustainability issues that come up in the Morrison-Kojima-Maull paper are related to food, to energy, and to the environment. Food, if you forgive the analogy, is a red herring. Sure, East Asia's dense population means that as incomes grow, there is a tendency for demand for food to run well ahead of the capacity of limited domestic land resources to supply it efficiently. That reality led Japan, Korea and Taiwan into high levels of agricultural protectionism, which has been one of the big sources of tension in the international trading system over the past two decades. Such protectionism is one way to reconcile limited natural resources with a dense population and rapidly rising incomes. The other and more productive way for the whole world community is free trade. China at the moment is debating whether it will resolve the apparent dilemma associated with limited land resources and rapidly rising demand for food in the Japanese way through protection (which will put it into tension with its trading partners in North America, Australia, and elsewhere) or through free trade. Through free trade, there's absolutely no question that the world as a whole has the resources easily to supply the growing demand for food in East Asia. In fact, it will require very rapid growth in demand for food in East Asia to offset the general tendency for world food prices to fall—as the countries in the area of the former Soviet Union unwind the catastrophe of its agricultural policy through this century, as something similar happens in Latin America, and as India and other South...
Asian countries remove the suppression of agriculture that’s accompanied their policy and planning since Independence.

The dilemma is a bit more acute with energy than with food, but again all the experience is that markets can handle the energy issues if they’re allowed to work. Unlike food, it may be that growth in East Asian demand for energy will lead to some increase in relative prices. So long as this happens smoothly and over time, it’s not going to raise questions of sustainability.

The global commons—the global commons—raises larger questions than the others. We heard some rather sanguine comments this morning about the opportunities for lowering the energy-intensity of growth in China. Sure, there are opportunities for that; but the total growth in energy demand is going to be so large in the large poor countries of Asia now undergoing rapid industrialization—led by China and India—that if there is a greenhouse problem, and there probably is, then it’s going to come under a lot of pressure from this new wave of Asian industrialization. The solution is going to have to involve rational global rules that end up causing emissions to occur in those places where they’re most cost-effective.

Open Regionalism

I think the Morrison-Kojima-Maull paper under-sells “open regionalism.” The paper talks about it as a concept of uncertain definiteness. It actually has a precise definition if you go back through the literature. It’s cooperation amongst countries within a region to reduce their own trade barriers without introducing any discrimination against outsiders. As such, it’s a form of regionalism that’s fully consistent with the multilateral rules. Its evolution in APEC is strongly influenced by the ASEAN experience. ASEAN is comprised of a group of countries that have been unilaterally reducing their own protection levels, tariff levels, rapidly for a couple of decades. That’s led to a considerable expansion of intra-ASEAN trade, very little of it the result of discrimination. There is now some discrimi-
al free trade by 2020. In recent months the British government has articulated a goal of global free trade by 2020. Leon Brittan, Vice President of the European Commission in Brussels, has said that if APEC actually demonstrates that it is going to get there, then Europe couldn't refuse to accept a challenge of that kind. And so by 2020 I can see a process whereby APEC-style open regionalism will have led the WTO and the global community into global free trade.

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ZHU XIAO HUA

A World of Interdependence

I would like to focus on coordination and cooperation in the Pacific region and in a world of interdependence. I believe no country can opt out of the community.

I remember a story I should tell you, when I was in charge of the foreign exchange reserves of China. When I took the position in 1994, the reserves totalled 21.2 billion U.S. dollars; they accumulated year by year, and last month exceeded 110 billion U.S. dollars. I analyzed the accumulation of these reserves. One third came from the surplus of the trade sector, one third from the non-trade sector, and one third from capital inflow. We also analyzed where the reserves went to, the structure of our investment of foreign exchange. Most of it is in America’s Treasury bills. So the reserves created from the surplus of our current account and capital account helped to cover America’s fiscal deficit.

I believe it’s the chain of life. One country’s imbalance covers another country’s imbalance, but in a different field and a different sense. So it’s a world in which we should cooperate with each other, coordinate with each other—not dismiss a member from the family, or dismiss a family from the community.

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I believe you know WTO is a big issue for China, and also for the world. The world needs China; also China needs the world. It’s natural, I believe, that China should be a member of the WTO. Think about reality—the big surplus that China’s trade sector generates, and the big capital inflow into China. The capital inflow went from US$25 billion in 1994, I remember, to US$33 billion in 1995, and then US$42 billion last year. So, I believe, in the WTO and the other regional or global organizations for economic cooperation, China should be a very important member.

There are some disputes between the different groups in the world. Yesterday’s discussion and this morning also reviewed some of them. Some people don’t understand the reality of modern society. We should keep in contact with each other, closely; and not hold hostility with each other. On the economic side, you can see, especially in the Pacific Asia region, cross-investment already taking place. I just mentioned the capital inflow into China. For several years, China has been the number one or two country with the largest capital inflows. Because of the Mexican crisis, China became the number one developing country for capital inflows.

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We should help each other, coordinate with each other, and cooperate with each other. This is not just a principle; you can see it working in real life, especially in the commercial circle. There’s a very famous principle of “comparative advantage.” It should be viewed not just from the economic side, but also from the political side. So I believe a disparity of development means big potential for further development.

In European countries and North American countries, the Industrial Revolution took place
long ago. Then different countries followed the process, and now it is the turn of Asia. The first tide of the “miracle” was Japan. Then the four “tigers” followed. Now maybe five countries—including China and Indonesia and Thailand—followed this tide.

I believe in this world no people can be independent from others. We have mutual interests among us. So we can talk with each other to solve the disputes between us. It’s very easy. I believe the globalization of the economy and high-tech creativity push people together, not separate them from each other.

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One of this century’s biggest events—Hong Kong’s return to China—will occur this July. The declaration between China and the British government in 1984 has determined the transition of Hong Kong. Hong Kong already played a great role in the last decade as a financial center and a business center in the region. Under “one country, two systems,” Hong Kong will keep its independent monetary system, independent tariff system, independent accounting system, and independent legal system. Hong Kong can keep its position in the region, keep its position as a financial, business and transportation center.

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Not only does China need the world; other parts of the world need China. We should cooperate with each other to keep sustainable growth in the region. It’s very important—if we are pursuing sustainable growth in the region—that we solve the population issue, pollution issues, and resource shortages. China, through the last three years, has basically reached its economic soft-landing, keeping high economic growth. Over the last eighteen years, China has had an average annual growth rate of about 9.7 percent. We want to change the development pattern, from greater-inputs-led development to higher-productivity-led development.

The open market policy in China is a very important policy. We want to enter WTO not just to get advantages. We also want to follow the rules of the organization. We know enterprise reform in the state-owned sector is a very important thing for preparation for entrance into WTO. So two years ago, the Chinese government already carried out very important policies to encourage state-owned enterprise to reform—to carry out reform of the mechanism of performance. We are restructuring the industry sector—renovating the hardware and improving the management—to deal with the challenges of an open market. So I believe if we can continue our policies we can reach the goal.

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I believe the Trilateral should include other East Asian countries. Twenty-five years ago, maybe just Japan in Asia could talk with European countries and North American countries. But I believe now the situation already has changed. So the Trilateral discussions should have a wide range of East Asian countries.

When I was in Kuala Lumpur last year for an Asia symposium, some people from Malaysia said, okay, why don’t you move your office from Singapore to Kuala Lumpur. We already prepared convenient conditions for you, because we will become a center for the region. And many Singapore people say, okay, we already are the heart of the region. But some people from other centers say, okay, we should develop our facilities to become the heart of the region. So competition among the Pacific Asian countries has already been created, and they are serious about their further development. I believe the division of labor is needed not just for mass production, but also for coordination and cooperation in the region. So I believe we can do something institutionally to help reach a reasonable goal for the next ten years.

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Community-Building with Pacific Asia

The other panelists in the Asia Pacific community-building sessions in the Tokyo meeting were Charles Morrison, Akira Koijima and Hanns Maull, who together authored the draft report entitled Community-Building with Pacific Asia which served as background for these Tokyo sessions. The report is being revised for publication, and will appear in the early fall. The following excerpt is a slightly modified version of the introductory chapter of the Tokyo meeting draft.

The modern era is a phase of the continuing global spread of the industrial revolution. Starting in northern Europe at the end of the 18th century, spreading to the Americas and Australia through migration, and then to Japan, this revolution brought a remarkable series of inventions and transformed the way people work, live, and travel. Higher economic growth, increased mobility, a tremendous demand for resources, and sharply reduced birth rates are among its major effects. As the industrial era spread laterally into new areas, latecomers could absorb the lessons and developed technologies of the earlier countries, and thus global industrialization seemed to move ahead at an accelerating pace. While many of the newest technologies are still developing in and around the core (the areas we call the Trilateral countries—Western Europe, North America, and Japan), the impacts quickly pulse out from this core, often bringing the sharpest transformations along the frontier.

This revolution has affected political life and international relations, sometimes traumatically. In the core areas, modernization was eventually accompanied by democratic forms of government and the creation of international security communities, that is, groups of countries so closely tied by bonds of economic interdependence and a sense of common values and destiny that war among them has become virtually unimaginable. But even where democracy came after severe internal strife or defeat in war, it has almost always proved an enduring political system, acquiring a degree of public acceptance that no other system has achieved.

In the past three decades, the frontier of the accelerating late industrial revolution has moved beyond Japan to the rest of East and Southeast Asia. The economic take-off of this region, which we call Pacific Asia to distinguish it from the larger Asia Pacific region that includes Australia and North America, is of historic significance for several reasons:

• The pace of economic and social change is faster than for any previous area or era. The Southeast Asian countries and China are going through demographic change, for example, in the course of two to three decades that took a half century in Japan and up to a century in a much earlier era in Europe.

• With 1.8 billion people, the countries of Pacific Asia are much more populous than the original core areas. Of these 1.2 billion are in China alone, which as a single political unit has considerably more people than all the Trilateral countries put together. When fully modernized, this gives it the potential to become the world’s leading country.

• In the developing countries of Pacific Asia, modernization is taking place in societies which have long historical traditions and cultures quite different from those in the West. Most of these countries also have suffered

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1Pacific Asia refers to countries of East and Southeast Asia that border on the Pacific or its attached seas and which have ethnic Asian populations. It thus does not include countries with a dominant non-Asian population, such as Russia, Australia, or Papua New Guinea. We also include in our definition land-locked Mongolia and Laos, as well as Myanmar, the latter because of its Southeast Asian location.
sharp political and social discontinuities as a result of colonialism, giving them again a very different recent history from European countries or their North American offshoots. In Japan's case, economic modernization and political and social fragility combined in the prewar era in a manner that proved explosive to the region. In developing Asia, economic dynamism is frequently combined with political fragility.

- If Pacific Asia joins the Trilateral world as a region of economic prosperity, security, and good government, the "zone of peace" will become dramatically larger. This will give the world enormously greater resources to move forward toward completing a single international community.

These features suggest the importance of the current transformation of Pacific Asia. Although only Japan in Asia is currently involved in the Trilateral Commission, the Commission has historically recognized the importance of Pacific Asia to the Trilateral world. No geographical region has received more attention from the Commission over the years. In 1985, a Commission report examined East Asian Security, and in 1988 another looked at East Asia in Transition. The 1994 report An Emerging China in a World of Interdependence addressed the challenges associated with the rise of Pacific Asia's dominant country.

Why this report? Our report reviews many of the issues examined in earlier reports, but in a rapidly evolving context. In contrast with the 1994 China report, this report returns to the broader region—the developing Asian countries from China and Korea in the north to Indonesia in the South. There have been many changes in this region since the 1988 East Asian report, including sustained higher growth in China, the consolidation of civilian-led democracies in South Korea and Taiwan, the economic stagnation and now food emergency in North Korea, the return this year of Hong Kong to Chinese sovereignty, and economic recovery in the Philippines, not to speak of the end of the Cold War. Some of the major premises of earlier years—that Russia would continue to be a major strategic threat, that Japan would continue to grow faster than other Trilateral countries and might have a GNP equal to that the United States in the early 21st century—now seem remote.

We believe that Pacific Asia has made remarkable progress over this time, albeit not without setbacks, such as that in Tiananmen Square in 1989. The future of the region, of course, depends largely on the peoples of the region. The questions for the Trilateral countries are: What are our interests in the region and how best can we pursue them? In what ways can we assist Pacific Asia in its push for greater economic prosperity, security, and domestic stability? How should we promote our further engagement with the region and encourage a global partnership of the Trilateral countries and Pacific Asia?

In reflecting on the future of the region and its global role, we emphasize two factors of special importance.

The first is the critical role of politics. While economics, particularly the private sector, have been the driving force of economic modernization and integration in Pacific Asia, politics shape the uses of the power acquired through economic modernization. Pacific Asia's ability to sustain growth, to protect its natural environment while pursuing growth, to achieve good government, and to attain a security community ultimately depend upon political leadership.

The second is "community." International relations is frequently analyzed on the basis of power balances. Power balances are obviously still important in the world politics, and in Pacific Asia, but the history of Western Europe and North America also illustrates that politics based on power balances can be transformed with the growth of a sense of community, that is, a sense of shared values, a common understanding of rules to govern behavior without the threat of physical coercion, and ultimately an emerging identity. It is our view that the Trilateral countries should be trying to build communities with Pacific Asia. The diversity of countries, cultures, economies, and interests presents an incredible challenge for community-builders, but diversity also can provide a basis for and enrich a community.
Above all, successful pluralistic communities require tolerance of diversity. The communities that Pacific Asian countries build with each other and with Asia Pacific or European counterparts will not be based on the simple adoption of one set of values over another. Inevitably there will be elements of diversity and elements of fusion, subordinated however to the broader values of peaceful resolution of differences, basic respect for universally recognized rights, and appreciation of the shared interest of all mankind in a sustainable, prosperous, and just existence.

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SECTION 2
GLOBALIZATION AND THE WTO

RENATO RUGGIERO

Towards a New Global Economic Architecture: The WTO’s Role in an Interdependent World

It is useful to recall how far we have come from that feeling of uncertainty which surrounded the setting-up of the WTO—doubts about its ratification, about its political clout, about the working of its dispute settlement system. Furthermore, the message I was receiving in almost all capit-itals when I was appointed was that, after seven arduous years of negotiation and a hard-won success, there was no longer the energy or the will for further big steps at the multilateral level. On the multilateral front everyone seemed exhausted; the mood was for regionalism, and many saw this as the dominant force at least up until the end of the century.

Things have—happily—turned out very differently:

- The WTO dispute settlement system has been a success right from the start. There have already been some difficult tests, and there are some highly sensitive cases under consideration. But I can state that no one—I repeat, no one—has shown any sign of a will to weaken, the system.
- We have also continued to move forward in trade liberalization. After a difficult start on financial services and telecoms, we now have a great success in the latter area—the agreement on trade in telecommunications services reached in February—which will be joined in a few days by the Information Technology Agreement. The importance of these telecoms successes in qualitative as well as quantitative terms is no less than a new round of trade negotiations. On financial services, we are about to resume a negotiation whose prospects are now brighter.
- No one can underestimate the significance of the success of the Singapore Ministerial Conference last December, as the occasion to make a positive political judgement on what

1Editor’s note: On March 26, a few days after the Trilateral meeting, forty governments did indeed agree to implement the WTO Ministerial Declaration on Trade in Information Technology Products (ITA). The ITA will cut customs duties on computer and telecommunications products beginning this July and eliminate them altogether by the year 2000. These tariff reductions will apply to all WTO members. Taken together, the ITA and February deal on trade in telecommunications services cover international business worth over a trillion U.S. dollars per year.
we have built in the first two years and to redefine a very ambitious work program.

Now we look forward, hopefully, to further negotiating success and also to the 50th anniversary of the multilateral trading system next year. It is not hyperbole to say, with one of the leading economic newspapers, that "the WTO is on a roll."

This is the very encouraging background against which I want to talk to you about the role the WTO can play in helping us to understand and to deal with the new realities of the global economy.

The Unprecedented Convergence of Global Interests

As we approach the end of this century we face an important turning point in world politics—and a growing debate about what the new era will bring. Some see widespread instability and conflict, others a world of competing regional blocs, still others a "clash of civilizations." And yet what is most striking about this new era is not the possible re-emergence of global conflicts—the old power-based system in modern disguise—but the unprecedented convergence of global interests. A movement towards borderless trade, free-flowing information, and deep interdependence is fundamentally transforming the way nations and peoples interact.

This is a transformation that is being driven by the most revolutionary of historical forces—the economics of the free market in all its diversity. On the material level, the market economy has helped spawn the extraordinary advances in technology in recent decades—the semiconductors, fiber-optic cables, and communications satellites that are weaving together a borderless world economy from the bottom up. IBM now employs programmers from as far afield as India, China, Latvia, and Belarus—linked through seamless global networks. On the Internet, consumers can plan vacations, conduct banking, and purchase electronic books—all down-loaded without ever passing scrutiny at the border. Whole areas of economic activity are now decoupled from time and space.

But it is at the level of ideas that market economics are most revolutionary. In recent decades we have seen the rise of a remarkable consensus—among almost all countries, from different backgrounds and different levels of development—that open markets are the best approach to economic growth and progress. The moral and material collapse of communism has helped to reinforce this view. So, too, has the change in attitude towards economic development in the developing world. Underpinning this global conversion to free markets is the huge success of the post-war multilateral trading system in providing the essential foundation for five decades of historic growth in world trade. In a sense, the existing international order has to be rethought, not because it has failed, but because it has succeeded beyond our greatest expectations.

Globalization and the Widening Circle of Growth

Out of the ashes of the Cold War era the possibility of a very different world is emerging. Take, for instance, the huge potential that now exists for sustained global growth. It is estimated that the world economy—the global output of goods and services—could easily double by 2020. Even if the world’s population continues growing at present rates, global living standards could rise by almost two-thirds.

Globalization is also spreading the tools of economic, technological and social development. Knowledge has become the essential raw material of the new economy. This new resource is different from the old—land, labor, and even capital—in that it is inherently mobile. Furthermore its capacity for expansion is almost limitless. By linking the world through telephones, computers and satellite links, globalization is bridging one of the most significant gaps between the developed and the developing world, and leveling the competitive playing field. Marx spoke of socialism as the
great economic and social equalizer, yet ironically it is the triumph of the market that is making this dream a possibility.

But perhaps globalization's most powerful influence is the way it is weaving together a world of deep interdependence. In the last four decades world trade has increased 15-fold and global production has increased only six times. In 1995, global trade in goods and services was over US$6,000 billion. Investment has become an even more powerful force integrating the world economy, especially since the mid-1980s. In the last decade annual global investment flows have increased from some US$60 billion to US$300 billion. Behind the increasing importance of foreign direct investment lies a strong push towards firms which transcend borders. Intra-firm trade accounts for about one-third of world trade. Another one-third is accounted for by exports of multinationals to non-affiliates. The remaining one-third takes place among non-multinational firms.

The developing world will benefit hugely from this widening circle of growth. Developing countries account for a quarter of world trade today, compared to less than 20 percent a decade ago, and if current trends continue, this figure could reach 40 percent by the year 2010 and over half by 2020. Foreign investment in developing countries has tripled in the past five years—from about US$33 billion to US$100 billion—though much is still directed towards a dozen or so countries. In 1997, the world's fastest growing countries will be in Asia and Africa—China is expected to grow at 9.7 percent (though the latest estimates are for some slowing), Vietnam at 8.5 percent, Malaysia at 8 percent and so on. Output in Africa as a whole is expected to grow by about 4.5 percent in 1997.

What these numbers demonstrate, among other things, is the accelerating pace of development. It took Great Britain over 150 years to industrialize; the United States accomplished the same feat in less than a century; but the Asian tigers have moved from developing to almost industrialized in a few short years—the most rapid and sustained growth in economic history. In ten years of economic liberalization, more than 2 billion people in India, China and Indonesia have almost doubled their per capita income.

But globalization is also a major growth stimulus for industrialized economies. As developing countries export more, they import more. During the period 1990 to 1995, North American exports to developing Asian economies grew by 13.5 percent per annum, compared to 7.5 percent for exports to the rest of the world. Exports from Western Europe and Japan to developing Asia grew even faster, at 15 and 16.5 percent respectively—about three times the growth in their exports to all of the other regions.

This global economic convergence of policies, technologies and national systems means that the lines separating our different worlds—industrialized, developing, least-developed—are becoming blurred. In linking together our economies through wires, cables, and satellite beams, we are also linking together our interests. And in linking together our interests we are linking together our futures as never before.

The WTO and the Challenge of Managing Growing Interdependence
Globalization is the dominant economic and political fact of our time; and managing our growing economic interdependence is the dominant challenge. Here the multilateral trading system in general—and the WTO in particular—is coming to play an increasingly central role, for a number of reasons.

First, the center of gravity of global politics is shifting increasingly towards economics. For almost fifty years, international relations were carried out in a Cold War world, shaped by the strategic realities of superpower rivalry and nuclear balance-of-power. In the next fifty years, international relations will more and more be played out in the context of globalization, shaped by the new demands of economic interdependence and the rise of Asia and the devel-

In the next fifty years, international relations will more and more be played out in the context of globalization.
The Multilateral Trading System, founded on the principle of non-discrimination, provides an important bridge between developed and developing countries. The process of moving trade rules inside the border has been very much in evidence since the end of the Uruguay Round. Last December in Singapore, WTO Ministers agreed to create a working group to consider whether investment rules should be brought into the WTO, and another group to consider whether the WTO should include multilateral rules on anti-trust and other competition-policy-related policies. The February Telecommunications agreement—which creates an international regulatory framework for the global industry—paves the way for further integration. And much the same challenges will be faced in the upcoming financial services negotiations. Because trade is on the leading edge of global integration, more than ever the WTO will be a key global instrument.

A second major development is that the achievements of the multilateral system and the impressive agenda agreed in Singapore have once again taken the lead over regionalism—lessening the fear that the international system will devolve into an Orwellian world of three or four major regional blocs. Global firms operating in global markets increasingly need global rules—something which regional arrangements cannot provide. Regionalism also loses much of its advantage in an era of borderless trade. Especially in new sectors like telecommunications, information technologies, or financial services, geographical proximity is no longer an issue. Moreover, in a world of overlapping regional blocs, the idea of "preference" is losing much of its meaning. Having agreed to free trade in the Pacific Basin, free trade in the Americas, free trade in Europe, and, as some have suggested, free trade across the Atlantic, there comes a point when it only makes sense to bring these various regional threads together in a single system of global free trade.

The third point is that the multilateral trading system, founded on the principle of non-discrimination, provides an important bridge between North and South, between developed and developing countries. The GATT started out in 1948 with a membership of 23 mostly industrialized countries; today the WTO’s membership stands at 130, eighty percent of which are from the developing world. And of the 28 countries lining up to join, all are developing countries or economies in transition. This momentum for accessions—including emerging players like China, Russia, and Vietnam—is the most tangible proof of the huge gravitational pull of the system for all countries.

Developing countries are also increasingly active participants in the functioning of the system. Between 1980 and 1994 developing countries were involved in less than ten percent of the 120 disputes examined by the old GATT. But in the last eighteen months alone, developing countries have initiated about half of the 69 requests for WTO consultations or panels. And through their important contribution to the Singapore Conference and to the successful negotiations on telecoms and the ITA, developing countries have demonstrated that they are not just active in the system, but indispensable to making it work. In this very
practical sense, we are all on the same side of the negotiating table.

As the first international organization created since the end of the Cold War, the WTO is emerging as a key element in managing this new globalized era. Indeed, this year in particular is proving a remarkable one for the multilateral system, one in which we are laying the foundations of the world trading system in the 21st century. When you add to the Telecoms agreement and the ITA (and the agreement we hope to have in financial services), the encouraging signs of progress on major accessions such as China, the high-level conference to improve integration of least-developed countries in the world economy which is planned for later this year, and the 50th Anniversary of the multilateral system in 1998, it is truly an impressive program. It is also one whose importance is very great for the growth and good order of the global economy.

And looking towards the end of this century, in less than three years' time, we see on the horizon the resumption of negotiations in a number of fundamental areas like agriculture and services.

The Essence of Globalization is Empowerment, not Hegemony

Does this emerging global economic system make an era of world prosperity and peace inevitable? Not if history is any guide. Believing that growing international trade made modern warfare unthinkable, Norman Angell wrote his famous book The Great Illusion in 1911—on the eve of the most bloody conflict in human history. If the twentieth century has taught us nothing else, it is that we should never underestimate the human capacity for allowing the dark to eclipse the light.

What I am suggesting is that globalization is transforming human relations in a way that makes turning away from the international community—retreating into protective nationalism or cultural particularism—infinitely more difficult and immeasurably more costly. More and more, countries are finding that they cannot achieve economic growth and progress without at the same time embracing open trade and investment. That they cannot participate in a technology-driven economy without letting their people have access to global information. And that they cannot expect to enjoy the benefits of the international system without accepting the reality and validity of the rule of law—domestically as well as internationally.

Does this mean that globalization represents the triumph of Western, or even American civilization? One of the main flaws of this critique, heard equally on the Right and Left, is that it ignores the reality of the globalization of culture. It is true that European moviegoers are watching Hollywood films; but American children are also watching Japanese cartoons; and their parents are driving European cars, or dining at Vietnamese restaurants, or reading the works of Canadian novelists. The power of globalization is that it promotes the interaction of civilizations—a cultural cross-fertilization and flowering from which the whole human race can benefit. To assume that the global economy can absorb a China, say, or a Russia, without at the same time being influenced by their civilizations is the height of cultural arrogance, let alone historical naivety.

But more importantly, the critique that globalization is hegemonic—an irresistible force, imposed on defenseless societies—utterly fails to understand the forces unleashed by this revolution. The very essence of globalization is empowerment. By freeing economies, societies, and knowledge, globalization is giving people the power to choose; and by extension, weakening the power of those who might be tempted to control this freedom—whether governments, or intellectual elites, or the media.

In other words, globalization is a reality because millions of people are choosing to make it a reality. Telecommunications is creating a global stage; transport is creating a global village; the Internet is creating a global classroom. From Tokyo to Toronto to Taipei ordinary people are watching music videos,
surfing the Internet, or listening to Walkmen as they commute to work.

In the end, it is the human dimension of globalization which makes it such a powerful force for world peace and world prosperity. Global economic integration is breaking down the barriers, not just between economies, but between people. It is weaving together a web of global interdependence which gives us a shared interest in our mutual prosperity. And it is equalizing the human condition through the spread of technology and knowledge, building a global vision as well as a global economy.

Ever since the time of Adam Smith, the apostles of free trade have held that trade is essentially liberating; that it is a fundamental basis of civilized discourse among nations; and that only if trade is free, can we maintain the foundations of political and other freedoms. It is this ideal which has been a constant dream of the international system—since the time of the Corn Laws, or the League of Nations, or the end of the Second World War. At the dawn of a new era, a new century and a new millennium, we have the responsibility—as well as an opportunity—to turn that dream into a reality. Next year we will celebrate the fiftieth anniversary of the creation of the multilateral trading system. It is important that we mark this event in an appropriately high-profile way, not just for its own sake but to reaffirm our commitment to the system and our confidence in its value for all our futures.

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SECTION 3
MANAGING THE INTERNATIONAL SYSTEM

This section presents excerpts of the essays prepared for the Tokyo meeting by Bill Emmott, Koji Watanabe and Paul Wolfowitz, published separately in a volume entitled Managing the International System Over the Next Ten Years. This project was in large part inspired by the Trilateral Commission's need to re-examine the utility and outlines of a "trilateral" approach to managing the international system looking forward, given remarkable ongoing changes in the world.

BILL EMMOTT

Managing the International System Over The Next Ten Years

The following is taken from the last section of the Emmott essay, headed "The Dangerous Weaknesses of the Trilateral Countries."

Two things, at least, will by now be clear from this essay. The first is that the author considers that the future is defined more by disorder and obscurity than by order and clarity, and that policies must be shaped accordingly to be agile and to deal with a range of potential dangers. The second is that the author considers that the Trilateral alliance has a role to play that is, if anything, even more crucial in this disordered future than it was in the dangerous order of the Cold War.

The motherhood-and-apple-pie conclusion to draw from the above would be that the United States, Canada, the European Union
and Japan must work together to build a shared leadership. But such a view would be more pious than practical, revealing little about actual policy or about challenges. A more helpful approach is to concentrate on the weaknesses of each of the Trilateral members, with regard to the tasks and objectives already outlined. Put simply, if cohesion in the Trilateral alliance is identified as the key objective, it is necessary for each member of that alliance to understand the problems that the other members face in maintaining that cohesion.

**Japan**

This author's view is that in the medium term or beyond, Japan may well face the greatest difficulties in maintaining its position and role inside the alliance. This is not because the present or probable future leadership of Japan, or indeed Japanese public opinion, is likely to desire a break with the alliance. It is because Japan sits on the edge of the region of the world that, at present, looks the most unstable. For that reason, Japan could well be faced with the most difficult strategic dilemmas among the Trilateral members.

The U.S.-Japan alliance remains the cornerstone of Japanese security policy, and is the cornerstone too of American policy in Asia. It remains strong. What needs to be recognized by fellow Trilateral members, however, is that changes within Asia are swirling around this alliance and could readily, in the future, start to erode it.

There are plenty of other ways in which Asia could prove unstable, but China and Korea are the two that could pose the greatest challenges for Japan. A natural aim for a pugnacious Chinese leadership would be to seek to break Japan's links with America. A natural consequence of bloodshed on the Korean Peninsula would be to force the Japanese finally to choose between being pacifists and being truly engaged, in military terms, overseas.

Meanwhile, Japan is undergoing a wrenching restructuring of its economy and, quite possibly, of its governmental system too. Economic stagnation and financial-market slump over the past five years have challenged the political system in new ways and have brought to light deep-seated problems within government of corruption, excessive discretionary power and lack of accountability. A smooth adjustment to these challenges is possible, especially given the currently low level of unemployment, and thus lack of social pressures, enjoyed by Japan. But it is also possible that these challenges could send Japanese politics, and public opinion, in wholly new directions if frustration grows and if external shocks intervene.

The worst mistake, with Japan, would be to take it for granted. The second worst would be to ignore the regional pressures under which it is liable to find itself.

**The European Union**

Currently, Western Europe faces the biggest domestic difficulties among the Trilateral partners. It has the highest levels of unemployment, and the toughest task in reforming welfare states and public finances. Those are its principal weaknesses within the alliance. The European Union continues to be the region where the dangers of a backlash against open trade and investment are the greatest. But there is also a secondary weakness that must be taken into account. This is that the yearning for an independent European voice, in foreign and security policy as well as trade, defined by its ability to be independent of the United States, remains strong.

These weaknesses are liable to make the EU a sometimes baffling, sometimes irritating, often frustrating partner. Yet they should not be overblown. In fundamental terms, the EU does not have a viable alternative strategy to the alliance. It may cavil at it, and seek an independent voice, but it does not look likely to be pulled in any new direction in the foreseeable future. While Japan has to contend with, and possibly accommodate itself to, a stronger China, the EU's main strategic worry is a weak, fissiparous Russia.

The EU's sluggishness in making up its mind
what, exactly, it wants to be reflects the complexity of its task as well as the fact that treaty-based institutions are especially difficult to reform and re-direct. The main concern arising from that sluggishness is that EU expansion is moving far more slowly than NATO expansion, which could give rise to even greater pressure later for further expansion of the military alliance rather than the EU itself. . . .

The real questions about the EU revolve around whether it will become riven by internal arguments, not around its policy towards its Trilateral partners.

The United States
The United States can fairly be described as the hub of the Trilateral alliance, even at the risk of mixing the Trilateral metaphor. As such, its greatest weakness has always been, and will always be, the self-centered nature of its politics. . . .

The United States is more akin to China in its self-centeredness than to Japan or the EU. The self-centeredness of Japan and the EU is tempered by these countries' sense of their own vulnerability. America, by contrast, by virtue of its size and its power, can see itself as the "middle kingdom," in the Chinese phrase, around which the rest of the world revolves. Self-centered policies by the United States have a high chance (or risk, depending on your point of view) of success. That makes them especially tempting. . . .

The importance of this weakness cannot be over-stated. If unchecked, it is liable to make the United States a constant source of challenge to the multilateral rules of law that a globalized economy requires, and to lead it to undermine multilateral peacekeeping and security institutions. It is liable also to lead the United States to confront its partners at least as often as its potential enemies, and thus to risk undermining the cohesion of its own alliances.

There are also strong grounds for optimism, however. They lie, fundamentally, in the broad and powerful countervailing force against such self-centeredness that exists within the United States itself, deriving from the people and the arguments that have given the United States the leadership role that it now holds. Nevertheless America's Trilateral partners must recognize this weakness of self-centeredness, and give those people and those arguments all possible support.

The world that has emerged in the 1990s is one of great promise and of great opportunity. To put that promise and that opportunity in danger by weakening the Trilateral alliance would be folly, grand scale. The position of the Trilateral alliance should be that we must concentrate on making ourselves a strong coalition, but an open coalition—open to the rest of the world, open to the desire of other countries to share our values and to drive forward in the same direction. A strong coalition and an open coalition is necessary to have the agility to deal with the unpredictable nature of the next ten years, and of the future at any stage.

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KOJI WATANABE

Japan in Need of Reform and Trilateralism

Japan finds itself in trouble. The political, administrative, and economic system that enabled its development for the half century since the end of World War II has ceased to function well. Everybody, regardless of his or her political party or economic or social group, has started emphasizing the importance of reform. Yet
no clear-cut image of this reform has emerged so far....

Two national goals have been attained: “growth” (by catching up with the United States) and “democracy” (by creating a rich egalitarian society through the protection of the weak).... The socioeconomic system, which has been centered on attaining the two national goals of catching up to the West and establishing an egalitarian society, has in a sense served its purposes, ceasing to function effectively in a set of new circumstances....

External Implications of Reform
The critical question concerning Japan and Trilateralism is whether Japan can afford to play an increasingly active international role in the face of multiple challenges that need to be met in reforming the domestic socioeconomic system.... Some Japanese might say, “We are preoccupied with mending our own house, so don’t bother us,” or “We cannot afford internationalism in terms of either intellectual or financial resources.”

The process of reform and deregulation will be painful and politically costly. As stated before, since the Japanese system has developed a built-in mechanism protecting the weak sectors of the economy from market competition, a wide range of vested interests are benefiting from the current regulatory system. Various political forces will resist reform and deregulation, and to the extent that reform and deregulation are considered to be linked with foreign interests, there is always the danger of a nationalistic reaction. One can only recall the intense sense of dissatisfaction with and anxiety about the American negotiating style seeking to force the Japanese market open in certain areas.

However, if one analyzes the nature of the challenges and proper ways to meet them, it is obvious that Japan has to be all the more international, all the more engaged and active in the shaping of the international setting within which domestic reform has to take place. Reform must be carried out, not because of foreign pressures, but because without undergoing it, the Japanese economy will lose its vitality and remain stagnant. Without reform, forces of globalization would bypass Japan and make other countries the center of a dynamic Asia.

A case in point is the financial sector and the Japanese version of the “Big Bang,” which is planned to be completed by 2001. The Japanese finance sector has been so overregulated that it is losing competitiveness.... Unless drastic deregulation in the form of a “Big Bang” is carried out, both Japanese and foreign money would shift away from Japan....

In all likelihood, Japan of all industrial democracies is the most in need of reform and deregulation because of the unique role that the government and bureaucracy have played in economic activities. However, the degree of liberalization industrial democracies should carry out must be studied, and the type of regulations most justifiable on certain grounds, like safety and health, should be sorted out. It might be useful for a Trilateral study team to explore the feasibility, cost-effectiveness, and advisability of comprehensive deregulation among advanced industrial countries.

In more general terms, it would be useful to jointly study the role of the state and bureaucracy in the age of globalization. This involves the history, political culture, and political systems of the countries concerned and is a subject of political sensitivity. However, for Japan it might be a useful exercise since never before has the role of the bureaucracy been exposed to such intense criticism.

The Challenge for Trilateralism: A Japanese Perspective
The Japanese penchant has been for globalization; hence Japan has become the only advanced industrial country not to be a member of any regional integration scheme, with the exception of APEC. This is due to the negative memory of the trading blocs of the 1930s and to Japan’s belief that Japanese economic interests are best served by an expanding global market. With regard to APEC, Japan is one of its
strongest proponents for openness. The growth of institutions within single regions (NAFTA or EU) or of institutions including two but not all three Trilateral regions (APEC and ASEM) seems to be compatible with and supportive of Trilateralism. But as a preventive for the emergence of any rivalry among these groupings, the Trilateral process of consultation takes on added importance.

In the early 1990s, after Prime Minister Mahathir of Malaysia proposed the establishment of an East Asian Economic Caucus (in November 1990), the idea of a re-Asianization of Japan found considerable support among Japan’s policy establishment because of the growing importance of East Asia for Japan and because of Japan’s weariness with the United States. The inclination toward Asia was to a considerable extent a product of negative images of the United States—Japan-bashing, a high-handed negotiating style, unilateralism, unreasonable demands such as numerical targets, the perception that the country was in decline, America’s triple deficits and loss of competitiveness. Today, however, while Japanese business interests in the Asian economy, be it in ASEAN countries or China, are still very strong and the shift of production sites will continue on the assumption that appreciation of the yen will resume, enthusiasm for an East Asian community, which is implicitly based on so-called Asian values, has somewhat subsided. This probably reflects two factors. First, with the big trade issues having been resolved without substantial concessions on Japan’s part, the Japanese image of the United States has improved. Second, it became clear that the negative legacy of history still persists—for example, in the form of repeated demands by other Asian countries for apologies about the Pacific War—and that the definition of “Asian values” or the “Asian heart” is elusive.

Against this background, the APEC concept has been promoted to institutionalize regional cooperation encompassing the Pacific Rim nations and to start to take concrete steps to plan integration on the basis of an open, liberal orientation. Japan came to believe that APEC would serve Japanese interests well, since it would not only enhance the mutual integration of Asia and North America but also serve to assure an American presence in Asia.

The formation of ASEM probably greatly satisfies Japan’s desire to be a part of both Asia and the West. By joining ASEM, Japan can associate itself with its East Asian partners, and through ASEM, Japan-Europe relations, the weakest leg of Trilateralism, can hopefully be strengthened.

Trilateralism is the enhancement of a cooperative relationship among advanced industrial democracies which share the common values of basic human rights, democracy, and a market economy and share the responsibility for peace and prosperity of the world because of their degree of influence, either positive or negative, by virtue of their strength....

The binding notion should be that of advanced industrial democracies, not Western civilization. When Japan identified itself as a member of the West, the West meant the West in the sense of East-West divide, not Western civilization. The assumption naturally was that democracy exists outside Western civilization and would prevail because it is the least defective and dangerous system to mankind.

To argue that democracy can take form only in Western civilization is false. We should perhaps remind ourselves that democracy—defined as government of the people, by the people, and for the people—is of relatively recent origin and is still developing....

If those who believe that the clash of civilizations is the major source of conflict preach the strengthening of unity among two parties across the Atlantic to form an exclusive bloc, their belief threatens to become a self-fulfilling prophecy by dividing the world by civilization and bringing about the demise of globalism, which many of us have considered one of the cardinal tenets of Western idealism, one which many non-Westerners wish to share. To preach the Trans-Atlantic Free Trade Agreement and creation of a North Atlantic economic
organization as a counterpart to NATO in the immediate aftermath of the establishment of the World Trade Organization is a human tragedy, and to expand NATO to cover only and all those countries belonging to Western civilization is an attempt to deny the universal nature of democracy when democracy is spreading as never before in one form or another.

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PAUL WOLFOWITZ

Managing Our Way To a Peaceful Century

The world faces a choice not unlike the one it faced at the end of the last century. Depending on how we make that choice, the next century could bring unprecedented peace among the major powers, new-found prosperity for hundreds of millions of poor people, and a great expansion of democracy and individual freedom. But if we manage badly, the next century could eclipse the twentieth as the bloodiest century in human history.

The World Heading Into the Twenty-First Century

Perhaps the single most important phenomenon of our time is the creation of wealth on a scale and at a pace that are unprecedented in history.... This extraordinary wealth creation is lifting hundreds of millions of people out of poverty and creating vast new opportunities for global trade. It has also led to the emergence of a large middle class in a number of countries that previously had none; that, in turn, is at least partly responsible for the triumph of democracy in country after country, including some with no previous history of democratic rule....

Yet while there seem to be great vistas opening before us, it is worth remembering that the end of the last century was similarly a period of exceptional economic growth and great technological progress which generated great hopes for the coming century. The sustained and significant increases in productivity of industrialized countries beginning in the latter part of the 19th century have been called "one of the most momentous developments in modern history." That growth was in part the result of the accelerating pace of scientific and technological progress—with some of the most important innovations of the Industrial Revolution (such as the automobile, the airplane, radios and telephones) just making their appearance—and that progress in turn generated a euphoria about the possibilities of scientific and human progress that was at least the equal of today's excitement about the Information Revolution.

The ends of both centuries have also been marked by great optimism about the prospects for peace as well. If anything, the experience of peace—or at least peace among the major powers—was longer and deeper at the end of the last century than it is in our time....

The 20th century did not, of course, unfold as it appeared to promise. By its midpoint it was already the bloodiest century in history, and a very large fraction of that bloodshed can be attributed ultimately to the failure to deal with the emergence of the new powers—Germany in Europe, Japan in Asia....

Nothing decrees that history will repeat itself, not even in the sense of Marx's famous remark about the two Napoleons: "the first time as tragedy, the second time as farce." But if we are to realize the enormous promise of the coming century, we will have to do a better job of managing the emergence of new powers on the world scene. If we fail, the con-
sequences could be even more destructive than we have seen in the twentieth century because the weapons of war have become even more terrible....

**Implications for Trilateral Cooperation**

There are a number of implications for Trilateral cooperation that flow from the above analysis.

First is the need for the United States to continue to play a balancing role in Europe and, particularly, in Asia.... This ability to assemble ad hoc coalitions against efforts to disturb the status quo may be increasingly important as the Asian security equation becomes more complex over the next two decades.

However, this type of role requires a flexibility that may be harder for the United States to maintain than a position of sustained opposition to a clearly identified threat. Moreover, it is a much more difficult role to explain and defend to the American public....

A second important conclusion is that, since the Western countries taken as a group will still retain the preponderance of economic power for a considerable time, cooperation among them will be important in managing the transition to a new distribution of power. Although the purpose of such cooperation is strategic, the cooperation required is not primarily military....

A third conclusion is that the values which the Western countries share can become an important instrument in shaping the transition to a new distribution of power. A commitment to larger political purposes should be part of the glue that binds the advanced democracies together and allows them to shape a future that can assure their continued safety and prosperity....

A fourth conclusion....is that there is still a need for the basic alliance structure that was created for other purposes during the Cold War. This is particularly true in Asia, even though it is most often in reference to Asia that one hears the argument that those alliance relationships need to be replaced by some new multilateral structure of collective security.... In fact, new multilateral security arrangements have little chance of working unless they are built on the foundations of the strong alliance relationships constructed in an earlier period.... There are important ways, however, in which these Cold War structures can be complemented by new ones that bring together countries that did not have the experience of cooperating with one another or which may even have been adversaries.

**The Need for Public Support**

Maintaining public support in the face of these challenges will not be easy. It will require demonstrations that the members of the alliances are capable of putting longer-term common interests ahead of short-term special interests, demonstrations that will be harder as long as people believe that the threat to the common interests is rather remote or even non-existent. America's allies seem to believe that the United States is behaving like a hegemonial bully, now that it is the sole remaining superpower. The American people, on the other hand, believe that our allies are taking a "free ride" at our expense and that America's relative share of the burden has actually increased since the end of the Cold War when it should have declined. These gaps in perception may be difficult to bridge, but the consequences of a failure to do so could be serious indeed.

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Japanese Politics


COMPLICATED POLITICAL SCENE

SOME OF OUR FRIENDS FROM ABROAD WERE DISAPPOINTED TO SEE THE EARLY DEPARTURE OF PRIME MINISTER HO SorOKA AS HE AND HIS CLOSE ALLY MR. Ichiro Ozawa were considered reformists. Things that have transpired in this country over the past three years certainly have been confusing. There have been three changes of government since Prime Minister Hosokawa’s resignation, but the political situation is still unsettled. The general election of last October, which took place under the new electoral system introduced by the so-called reformists, has further complicated the political scene. Instead of the two-party system and more vigorous policy debate that the reformists claimed the new electoral system would bring, we now have so many political parties that it is difficult for you to remember all of their names. The Social Democratic Party of Japan and the Sakigake Party remain allies of the LDP, but they are not in the coalition government as they were in the first Hashimoto Cabinet. On the opposition side, in addition to Mr. Ozawa’s Shinshinto, we have the Democratic Party, created by defectors from the Social Democratic Party and the Sakigake Party, headed by Mr. Hatoyama and Mr. Kan. Mr. Hata and 12 Diet members left the Shinshinto in December 1996, and established the Taiyo-to. Another small group of former Shinshinto members has left the party and established the 21st Century Parliamentary Group.

Despite the sorry state of the opposition side at this moment, things are not easy for the LDP either. We did not achieve a majority in the last general election, and we are quite short of a majority in the House of Councillors, or Upper House. One of my main preoccupations in recent months as Secretary General of the LDP has been a series of consultations day in and day out with my counterparts in the Social Democratic Party and the Sakigake, two former coalition partners, as well as with the Democratic Party, through which I have been seeking common policy positions.

This painstaking and sometimes tedious process can easily be seen from the outside as political stalemate. Indeed, many skeptics in the media and in business here and abroad have been saying that this Hashimoto Administration cannot achieve the necessary reform. Such analysis has fueled what may be called “Japan pessimism,” which has been so pervasive in this country in the past several months that it can make the “British disease” and “Euro-sclerosis” sound like expressions of optimism. They fondly and nostalgically recall the good old days of “Japan bashing.” Now, these pessimists complain of “Japan passing,” namely that North American and European banks and businesses are passing over Tokyo
RYUTARO HASHIMOTO

Prime Minister Ryutaro Hashimoto spoke to the Tokyo meeting. The following excerpts are based on the simultaneous interpretation from Japanese of his remarks. At the center of his remarks was his resolve to carry through reform in Japan:

You are discussing the reforms, the changes taking place in Japan politically, economically and societally. And I would like to share with you my resolve.

Various countries of the world today are faced with the challenge of responding to globalization of world economies. Japan is no exception. Japan has come to a very big turning-point. In particular, the big challenge is how we can maintain the vitality of the Japanese economy, and how we can augment it.

When these difficulties are identified, the issue is how we can reform ourselves, in adapting ourselves to the new situation. The world is becoming one. People, goods, funds and information are moving freely. The socio-economic system which brought success to Japan in the past is now interfering with the viable development of Japan. We are now cognizant of this point. We need to create a socio-economic system which is in harmony with the rest of the world. We must give a radical review to the Japanese system, so that we can make a commensurate contribution for the development of the world's economy. In the past fifty years after the war, we have built up various systems taking deep root in the Japanese society. To change these systems will entail enormous difficulties. But I am determined that we are going to go through with reform on six fronts: administrative, fiscal, economic structure, financial system, social security and education. We must do it.

The Prime Minister also spoke of Trilateral and Asia Pacific cooperation:

The cooperative relations among these three poles will become even more important in the process of building the structure of a new international order after the Cold War. These three regions represent the area where we share value orientations and systems in the basic way, namely liberal democracy and market economy. And we still hold the overwhelming economic clout in the world. When the international situation is in a state of flux, we are maintaining the most stable relationship of cooperation amongst the three poles.

You are inviting many guest speakers to this meeting from the Asia Pacific region, which gives me enormous pleasure. I have participated in the meetings of APEC. I have made visits to a number of countries within the region. And I have directly felt the vigorous and dynamic economic development of the Asia Pacific region. I am delighted we are increasing the sense of community within the Asia Pacific region. For Japan, regional cooperation within the Asia Pacific region is equally important as its cooperation with developed nations. I hope that these cooperations, together with inter-regional cooperation like Asia-Europe Meeting (ASEM), will contribute to the creation of the new international order after the Cold War.
in favor of other Asian capitals. They even say that Japan has become so useless that our foreign friends will not pay attention to Japan anymore, and, thus, they call this phenomenon “Japan nothing,” a view I strongly oppose.

I am not saying that the doom-sayers have been entirely wrong. Indeed, there have been, and there still are, enough reasons for grave concern about the future of Japan. We do understand the difficulties foreign companies face in dealing with formidable red tape when they do business in Japan. That difficulty has become obvious to Japanese corporations as well. The Japanese telecommunications industry has begun to realize that they were constrained against competing successfully in the international marketplace because of bureaucratic controls. Japanese bankers have started to voice their concern over the loss of their competitive edge because the Ministry of Finance’s long review process blocks them from selling new products before others come up with them, though less ambitious bankers are happy with Ministry of Finance control as they are not “allowed” to go bankrupt. On a macro level, there is very serious concern over Japan’s huge budget deficit with even more serious prospects in the coming years due to lower productivity growth and the heavier fiscal burden of maintaining the social security system as a result of the aging society.

One encouraging sign in this pessimistic atmosphere is that an increasing number of Japanese have begun to accept the notion that something is fundamentally wrong and that in order to survive, Japan does need some basic reforms in many aspects of our society. One of the things that has caused the serious nature of our fiscal condition to sink into the public mind has been the Hashimoto Cabinet’s decision to give transparency to economic data. Before the general election of October of last year, the coalition government decided to reveal the stark economic reality that the accumulated fiscal debt incurred by both state and local governments was 442 trillion yen, a figure as large as one year’s GDP. As a prescription for this situation, we put into our campaign platform a proposal to raise the consumption tax to five percent. The Shintóto pounded on this proposal despite Mr. Ozawa’s earlier commitment to a ten percent consumption tax. In my view, the statistical evidence was convincing enough to the voters. There were no street demonstrations or major voter revolts. Enough voters accepted our message to allow Mr. Hashimoto to continue his task. But, I think the votes also showed they wanted more reform.

Major Reform Initiative
With this background, we have launched a major reform initiative. It is an ambitious proposal to attack six fronts simultaneously, namely, administrative reform, fiscal reform, financial reform, reform of the social security system, reform of the economic structure, and educational reform. Prime Minister Hashimoto made this pledge in his opening Diet speech in January, saying that these measures will lower the magnitude of the annual deficit to a maximum of 3 percent of GDP by fiscal year 2005. The media again criticized us for a lack of focus and strategy in undertaking reform efforts. Again they missed the point. Needless to say, reform efforts are accompanied by pain, and our belief is that such pain should be shared equally by all sectors. There should be no sanctuary, and this includes the agricultural sector and the public works sector. This is understood by our colleagues in the Diet. Politically speaking, diffused opposition is easier to handle than concentrated opposition. There is a Japanese saying that the policeman shouldn’t scare you if you cross against a red light with many other people. Perhaps this “multi-pronged strategy” may be more suited to the egalitarian and consensus-oriented Japanese society.

When the Tokyo stock market dipped in January, the media immediately pronounced that the cause was the dim prospect of our reform efforts. Again, they were wrong. A careful analysis made it clear immediately that...
those stocks that suffered major losses were those of construction companies that would suffer from the inevitable reduction of budget allocation for public works, and those of weaker financial institutions that would suffer from deregulation of financial markets. The stock market sensed "the writing on the wall."

Practical business leaders seem to be reacting to the changing circumstances by starting their own serious efforts of restructuring and downsizing. This is another positive sign. These businessmen do recognize that the days of the bubble economy, when they could seek growth and profit through inflated values of stocks and real estate, are over. They feel that they have to take the heat and make sacrifices. When they do so, they obviously question why some companies can still enjoy warm government protection.

One area that has received the tightest government control and protection is the financial area. Therefore, we felt that we should move vigorously and quickly. The cabinet has already sent bills to the Diet that are designed to reform the financial system. They will strengthen the independence of the Bank of Japan. They will create a new financial industry watchdog independent of the Ministry of Finance, substantially decreasing the regulatory power of the ministry. The Securities Exchange Surveillance Commission, which now belongs to the ministry, will be shifted to the new watchdog. Thirdly, the reform will revise the Anti-Monopoly Law and lift a ban on the creation of holding companies. Perhaps more significantly, in November last year, we announced Japan's version of the "Big Bang" to make the Tokyo market as liberal as those in London and New York by 2001. This will expose Japanese banks to fierce international competition for the 120 trillion yen in aggregate financial assets held by Japanese households. Many assume that some of the weaker Japanese financial institutions cannot survive this competition.

There are still skeptics on the effectiveness of these measures, but I believe it is a positive beginning.

**Representing Society's Pluralistic Interests: Coalition Politics, NGOs**

As we have been struggling to bring about real reforms on many fronts, I have become more aware of the effectiveness of coalition politics. In brief, the monopoly of power of the LDP, while having its merits, brought with it a strong influence of government bureaucracy through the LDP members who have special interest in several sectoral areas. Such influence has been very much reduced through coalition politics, in which other parties bring to bear the voices of pluralistic society on the policy process. I do not believe the measures to reduce the power of the Ministry of Finance could have been taken if the LDP had tried this on its own. Despite some cynical views on our coalition politics, without the cooperation of the reformed socialist party we could not have passed some legislation, such as compensation for the victims of the mercury poisoning in Minamata. Without the help of the Sakigake Party members, the bureaucratic mishandling of the HIV-contaminated blood could not have been revealed.

One positive aspect of coalition politics is the representation of the pluralistic interests of our society. In this connection, I should also mention that there has been a positive development of NGOs and volunteerism in Japan which may have a major impact on the governance of our society. The tragic earthquake in Kobe-Awajishima in 1995 proved to be a watershed for Japan's NGOs and volunteerism when over 1.2 million volunteers and many NGOs played a significant role. Even before the earthquake, these organizations and individuals had started feeling that they should take public interest into their own hands, and they also found that the government bureaucrats simply cannot respond to all the social needs in this day and age. We are trying to pass a bill to facilitate the activities of the nonprofit organizations by reducing the intervention and control of the government bureaucracy in their incorporation process and over their activities.

* * *
I have talked at length about the seriousness of our resolve to carry out the reforms in Japan. I realize that these tasks are not simple, and my colleagues and I feel that we are racing against time. As I mentioned earlier, there is a growing feeling among a large number of responsible Japanese that this may be the last chance to carry out the necessary reforms before we start a serious decline. I believe Japan still has economic and technological strength. We have excellent human resources, and we have a resilience to bounce back from difficulties.

I understand that the Trilateral Commission will meet here in the year 2000. I hope I will be given a chance to speak with you again. It will perhaps depend on whether my colleagues and I are successful in carrying out the reform initiatives I have outlined. It is my sincere hope that we will meet again and together start the new millennium with a more positive and optimistic frame of mind.

Koichi Kato is Secretary General of the Liberal Democratic Party.

TOYO GYOHTEN

The Japanese Economy

Mr. Kato mentioned the pessimism now prevailing in this country. I certainly think he is right. The most fitting word to describe the current situation of the Japanese economy is "hypochondria." (Some of you may wish to contrast it with American "euphoria" and European "paranoia.") Most Japanese people are worried that something is wrong with the Japanese economy, but they cannot be sure that things are moving properly to correct it.

The Real Economy is Clearly Improving

However, the real economy is clearly improving. The GDP growth rate for 1996, last year, was 3.6 percent, which was the highest among G-7 economies. Although support from the government sector was reduced, activities in the private sector are pushing up the overall economy. Household consumption is advancing solidly. Large corporations, particularly in the manufacturing sector, have improved their performance markedly thanks to restructuring efforts and the weaker yen. They are increasing investment and employment. Medium- and small-size firms in the non-manufacturing sector are also enjoying better business. The average annual productivity gain of Japanese industry during the last five years was over 1 percent, more or less on a par with that of American industry.

Next month there will be a tax increase amounting to ¥7 trillion, and further cuts of public works outlays are expected. Fiscal constraint of this magnitude will inevitably have a certain dampening impact on economic activity and slow down growth. However, it is the majority view now that momentum of the recovery will be strong enough to absorb the fiscal drag quickly.

Therefore, it is my view now that the growth rate for 1997, this year, can be sustained at around 2 percent and accelerate again in 1998. All in all, the near-term prospect of the Japanese economy does not warrant pessimism.

Why Such Widespread Frustration?

Then, why is there such widespread frustration? In my view, there are two major factors.

One is the sense of loss which was brought about by the collapse of the pre-eminence of the Japanese economy, as the result of the burst of the bubble in the early 1990s. During the bubble period in the late 1980s, the Japanese economy demonstrated remarkable buoyancy compared with other G-7 economies. High growth, rapid rise of productivity, large current account surpluses in spite of the strong yen, and stable prices all contributed to the image of a mighty economy. Supported by the strong yen

All in all, the near-term prospect of the Japanese economy does not warrant pessimism.
and abundant liquidity, Japanese financial institutions wielded formidable clout in the global market. Supported by advanced technology and innovative managerial techniques, Japanese products such as autos and electronics became a daunting presence in the world marketplace. Not only Japanese but many foreign observers as well came to believe in the invincibility of the Japanese economy. Many Japanese were convinced that the success of the Japanese economy vindicated the validity of the Japanese way of managing the economy and the Japanese way of operating the market. Japan was entirely vanquished by the unwarranted euphoria.

The burst of the bubble (which was in fact an asset deflation) and the ensuing economic distress shattered this euphoria. Japanese had to recognize that the bubble and the following mess were created by policy mistakes and were aggravated by the peculiar features of the Japanese economic structure. The burst of the bubble left corporations, banks and households with deteriorated balance sheets. Economic growth became very stagnant. The government took a series of steps to solve the problem of financial institutions. However the steps were neither decisive enough nor transparent enough to convince the market; and the property market and the stock market remained anemic. The trauma was intensified by the appreciation of the yen, the devastating earthquake in Kobe, and the social instability gruesomely demonstrated in the mass murder by a fanatic religious cult. Meanwhile, our main trading partners, namely the United States and East Asian countries, were making great strides in their respective processes of revitalization and development. The comparison with them made the Japanese economy look senile and unhealthy. All in all the Japanese themselves, and foreign observers as well, came to believe that the economic system of Japan has proven to be inoperative under the changed environment. And yet Japan was not capable of coping with these tribulations.

Another cause of the frustration is the doubt about the health of the Japanese financial industry. Japanese banks are still loaded with bad assets. According to the Ministry of Finance, of the total loan assets of ¥700 trillion held by all deposit-taking institutions in this country, about ¥30 trillion is classified as non-performing. Of course the situation differs greatly between individual banks. There are concerns that some of the weak ones will have to go under. Persisting doubt about the accuracy of data released by banks and the Ministry of Finance on the amount of bad assets, the slow pace of write-offs, and low profitability of banks have raised concern about the viability of Japanese banks.

There are also worries about the stock market. The Nikkei average of stock prices collapsed from its peak at 39,000 in 1989 to 15,000 in 1995. The government took a variety of measures to support the price, including the purchase of stocks with public funds. However the effect of such operations did not last long, and the Nikkei average is still hovering around the 18,000 level.

The more fundamental problem with the stock market is the misgiving about its transparency and fairness. Recurring scandals, including the recent one of the largest brokerage house, have tarnished the clean image of the market. It cannot be denied that there is an impression that the Japanese stock market is still contaminated with insider trading and other misconduct. It is true that the Japanese financial industry has long operated under tight control by the regulatory authorities. The philosophy behind the control was to prevent the failure of financial institutions and thereby to protect depositors and investors. This combined system of protection and control worked pretty well as long as the market was kept apart from the rest of the world. However, the globalization of financial markets, which has advanced rapidly since the 1970s, has made the old system obsolete and inoperative. Cumbersome regulations diminished the attractiveness and the efficiency of the market, and eventually players and businesses started to desert the market. The phenomenon often called the “hollowing” of the Tokyo market became a matter of serious concern and contributed to
the loss of confidence in the future of the Japanese financial industry.

The Drive for Reform

Well, I have explained why Japan is now suffering from a severe case of hypochondria. The Japanese people realized the way they managed the economy was not that flawless. They also recognized that, because of the bonanza provided by the bubble economy, they wasted time to correct the flaws and thereby lost competitiveness. The awakening to our crisis came late. But it did come.

Since last summer a driving power of national scale has been put in motion. The Prime Minister announced his plan to implement reforms in six broad areas. They are: bureaucracy, national budget, economic structure, financial industry, social welfare and educational system. The issue of the reforms was the focal point at the last general election of the Lower House in October last year. And the outcome of the election demonstrated the broad public support of the reforms.

In November the government disclosed its extensive plan for the reform of the financial industry. The plan is based on the three key words: market principles, transparency, and international compatibility. Items included are: deregulation of the management of pension funds; liberalization of international financial transactions; removal of the demarcation between commercial banks and long-term credit banks; liberalization of insurance premiums; introduction of the bank holding company; lowering of the barrier between commercial banks, securities firms, and the insurance companies; liberalization of the security transaction fee; introduction of the mark-to-market accounting system; liberalization of investment fund management; etc. All these measures are expected to be implemented by the year 2001. Furthermore, the Reform Committee of the Liberal Democratic Party announced a week ago its recommendation to front-load several important measures such as the abolition of the securities transaction tax and land price tax and the liberalization of the securities transaction fee.

For the sake of fairness, I should tell you that there are various criticisms and concerns expressed both at home and abroad about the reform plans announced so far. Some argue that the plan is not comprehensive enough. They point out, for instance, that the privatization of postal savings insurance and pensions are not included, although the state-run business is often criticized as engaging in unfair competition against private business. Some argue that the target date of 2001 is too late in view of the rapid development taking place in other major markets in the world. Also, there are some who are worried that the reform effort will be defeated, after all, by resistance and sabotage by many interest groups and bureaucrats who are enjoying the benefit of regulations. There is also a voice of warning that the general public may become less enthusiastic when they have discovered that the deregulation and the increased competition will cause a loss of stability and an increase of risk. Some foreign observers make cynical comments asking how many times they have heard about the Japanese reforms. I believe these criticisms and concerns should not be ignored.

There is no question that the reform now contemplated is probably one of the most major ones in the modern history of the Japanese economy. When implemented it will have a far-reaching impact on the basic structure of the Japanese market and the Japanese way of economic management, at the level of the government, corporations, and households. We should not underestimate the roughness of the road ahead. However, having said that, I tend to believe that this time around the reform will be carried out.

There are three reasons to support my arguments. First, the majority of the Japanese public today is seriously concerned about their lives. They know that the population is aging rapidly. They know the global competition is intensifying. They know the Japanese economy is vulnerable in many respects. On the
whole, they are adequately cognizant that without revitalizing the Japanese economy through reforms and deregulation as proposed, they will have to accept a considerable deterioration of their own living standards in the future. For the first time a sense of urgency has gripped the nation.

Second, politicians came to realize that the current is clearly running in the direction of reform. For the first time the majority of elected politicians are aware that in order to survive as politicians, they have to support the broad agenda of reform. No doubt, many politicians have groups of voters in their constituencies who will lose their vested interests when the reform has progressed. But even those politicians have to accept that the support of the vested interests now will inevitably ruin their popularity in the future.

And last but not least, the ball has already started to roll down the hill. Bills to abolish foreign exchange control, to allow holding companies, to reform the Ministry of Finance and the Bank of Japan, have already been submitted to the Diet. It is certain that the Diet will approve them in a matter of months. More reform bills, including tax laws, will be submitted to the special session of the Diet in the fall. Once implemented the reform incorporated in these bills will make cracks in the old system. It is possible that initial cracks alone may create certain distortions in the market. Money flows may change. Some instability may occur. Nevertheless, the very distortion will make further reforms inevitable and indispensable. A chain reaction will start.

* * *

Let me conclude by summarizing my argument. The Japanese economy is recovering. Although there will be a temporary slow-down in the near future, and although a certain pan demonium will emerge in the financial industry during the process of restructuring, the overall economy will remain resilient. The reform process has already started and will gain momentum as it progresses. The challenge for Japan in the early part of the 21st century will be to consolidate the new framework of the Japanese economy, which is internationally compatible but at the same time original.

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YOSHIKO SAKURAI

Societal Change

I am a free-lance journalist; I am not a bureaucrat or a politician. Therefore my view, naturally, may be very different from those two gentlemen who spoke before me.

I have a viewpoint which is a mixture of optimism and pessimism. I become very optimistic when I look at various specific movements or actions taking place in our society. Let me tell you of some of the concrete examples, which I myself have covered for years.

Government Responsibility, Information Disclosure

The first example is the social and the political changes which surround the HIV issue. In Japan there are about five thousand hemophiliac patients, of which almost 40 percent were infected with HIV because they had to use HIV-tainted blood products for their treatments. In October 1989, a group of fourteen patients, who could not disclose their names or faces (because there was so much prejudice against them, as we Japanese were not very familiar with HIV at that time), brought a lawsuit to the Tokyo local court. At that time, there was almost no attention paid to these people. Years and years passed, up until 1995. Almost everyone in the beginning expected that the plaintiffs would lose this case, because in the past the government’s responsibility for providing
wrong medicines was not recognized by the court. It was always the pharmaceutical companies which were accused of providing the hazardous medicine. But this time, for the first time in history, the Tokyo local court announced that the government is responsible for providing the HIV-tainted blood products to the hemophiliac patients. In addition, a bureaucrat from the Ministry of Health is now being tried for not performing the duty he was supposed to perform. This is also the first time that a central government agency’s bureaucrat is tried in the law court. In the past bureaucrats were accused of accepting bribes or of some personal misconduct, but not a single bureaucrat was accused for not performing his responsibility. Therefore this is also a very new example of how Japanese society is changing gradually. For the first time the government was judged responsible for providing the hazardous medicine. At the same time, the bureaucrat providing the hazardous medicine is being tried. He was supposed to watch over the medical care policies, but he did not.

This court case helped propel another movement, demanding the Information Disclosure Law. Japan is possibly the only advanced country which does not have an Information Disclosure Law. For the first time, the Diet is discussing such a law. If this is realized, the Japanese people will be given, for the first time in the whole history of Japan, the information that they need in order to make the right judgments. In the past, information has often been monopolized by the bigger companies, or the government agencies. It required a tremendous effort for a journalist or a citizen to gain the necessary information. If the Diet passes this Information Disclosure Law, that will change—and that will become a vehicle for the larger change in this society, to make people able to make their own judgments, based on whatever information is necessary.

Citizens’ Groups,
Non-Profit Organizations
Now, as Koichi Kato mentioned, in this change there was a role played by so-called citizens’ groups. Various citizens’ groups supported these HIV patients who were hemophiliac, who were not able to disclose their names and faces because of the prejudice against them. Lots of people helped them and made a strong movement to persuade the Ministry of Welfare to admit its responsibility. These citizens’ groups played a big role as well as in the great Hanshin earthquake of 1996. Also, when a Russian tanker broke down in the Japan Sea, lots of volunteers ran up to the Japan Sea coast and helped the local people in eliminating the oil. With the active roles played by these citizens’ groups, I think the Japanese society will experience another new stage of change.

Mr. Kato also discussed the fact that the Japanese Diet is now discussing the NPO issue—Non-Profit Organizations. If this is realized, societal change will be further promoted, because this would give the chance for each citizen to do something. I think Japanese people are full of willingness to do something for the society, but often they are not familiar with what to do and how to do it. So if the NPO is legalized and if there are many NPO groups coming up, ordinary citizens will be given the chance to participate more actively in this society, to change this society.

Changing Role of Women
Another optimistic element on which my view depends is the changing role of women. Let me tell you my own experience. I became the newscaster for one of the major networks in Japan in 1980. At that time, my TV station was the only TV station which had a woman as an anchorperson. And when I became the anchorperson of this particular channel, people asked me to look very feminine, you know —pretty. Seventeen years since that time, when I now look at the news programs of other stations, each program has women as a central figure in addition to men. Quite often the woman is the central figure emceeing the program. So the role of women and the expectations of women have definitely changed. There is a change from expecting femininity to expecting intelligence, power,
courage, ability to foresee what is really going on. Also, when I became a newscaster, people thought younger women are better. Nowadays, each station says women in their thirties, forties and fifties may be better than much younger women because they have the experience, they have the wisdom to carry out the news program. So the social expectations for women have changed.

Another example which is very personal, shows the changing role of men and women in Japan. My friend, who is a professor of one of the universities, she has two children. One is a boy, one is a girl. She has raised these kids in two different ways. She always told her boy, "You have to be very good at cooking and washing, otherwise no charming woman will come and marry you in the future." She told her baby daughter, "Don't you cry ever, because you are a woman. Women have to be strong because we live longer than men; we are larger in number than men, therefore we carry a greater force to change this society, we have more votes." She jokingly tells this to various friends, but I think she has some truth in raising her two children. When I visit their home, the two kids are beautiful. They are almost adult now, but the boy is able to do almost everything. He does not have to depend on a woman making tea or cooking for him. He is totally and utterly capable of looking after himself. This symbolizes the changing social aspect of Japan.

I have talked to various company executives in charge of choosing the new company employees—i.e., the heads of personnel departments. Often, they say, when we look at the examination tests, the top fifty or seventy are all girl students. Therefore, if we take only the students with very good academic records, the company members will become all women. We can’t do that; therefore we mix. So, Japan is really becoming almost an egalitarian society in that sense. And yet, at the same time, I admit the role of women, the responsibilities of women, are still very limited in this society. So it is from now on that we really change this society through expressing the woman’s viewpoint.

**Regaining the Ability to Think**

Another significant change I see in this society is about bureaucrats. Bureaucrats are the elite of the elite of this society. Often people say that it is not the politicians who make the policies, it is the bureaucrats. Many bureaucrats are excellent, but we also committed many mistakes, pre-war and post-war. We went into a reckless war. Today we see lots of problems in the government agencies—Ministry of Welfare, Ministry of Finance, Ministry of International Trade and Industry. Why is it so? Why do the elite of the elite make these mistakes? I think there are two major causes.

One is the education system. Throughout history the educational system of Japan makes students not think. Students get top positions when they give the expected answers. But look at the issues in the world. How many issues have a set and expected answer? We always have to explore; we always have to think through to find the new answer. Often this sort of ability is lacking in the bureaucrat.

As a nation, Japan has been giving a set answer all the time. Because we were the close ally of the United States, because we had the security alliance with the United States, we simply had to follow the basic course set by the United States. We followed American foreign policies quite closely. The general framework set for Japan made it not necessary for Japan to really think through by herself. We lived this sort of history more than fifty years. In the meantime, our ability to think through, our ability to foresee what is coming up in the future, may become very dull. So we Japanese have to regain the ability to think, and if we do, I think our society will be able to go through the real change.

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SECTION 5
CHANGE IN EUROPE

KURT BIEDENKOPF

European Unification: Changed Conditions Require Simpler, Open Institutional Arrangements

Speaking of Japan, someone this morning said, in my words, a dream fulfilled is a dream lost. And what do you do when a dream is lost? This is also an issue for Europe.

Increased Complexity, Reduced External Forces for Cohesion
Tuesday next week there will be a meeting in Rome to commemorate the fortieth anniversary of the signing of the Rome Treaty. During the last forty years (I will exclude the last three or four because basic changes were beginning to develop) a very impressive historic success story unfolded.

The first point I want to make is that what developed during the last 35-40 years, up to the reunification of Germany and Europe, developed under extremely favorable conditions for West Europe. The bipolar world had two effects, very different ones. First, the common threat emanating from East Europe, from the Soviet Union, developed in West Europe a sense of community. It worked as a force for cohesion among West European nations. Second, at the same time, it kept competition away from West Europe. There was no competition emanating from the Soviet bloc. The United States supplied a protective umbrella which allowed West Europe to allocate resources differently than it would have if it would have had to protect itself, without help from the outside. During the rebuilding of Europe, the Western world enjoyed almost a monopoly on the very productive combination of technological, engineering and scientific knowledge, capital and qualified labor. Until the oil crisis, West Europe had access to very cheap energy and raw materials, and was capable of selling its products—because of its unique position in terms of productivity, etc.—at relatively high prices. Economically speaking, Europe was in the situation of a quasi-monopolist, earning a monopoly rent.

This particular condition has almost evaporated. After 1989-90, Germany was united and East Europe opened up. The military threat from the east is gone, for all practical purposes. At the same time, the economic conditions in which West Europe thrived during these forty years are dramatically changing. World trade until the reunification of Germany and Europe was, for all practical purposes, Western world trade. It is now developing into global trade, which means not only that trading partners and competitors have enlarged in number, but also that the scope of competition has enlarged in quality.

In the Western world, competition took place within a system of common values, and more or less comparable standards of living. Now we have competitive forces arising, especially in the new industrial nations, that are based on different values and different energies, with increasingly favorable conditions. These increasingly favorable conditions include the availability of knowledge and capital throughout the world at almost identical prices, while increasingly qualified labor is supplied at much lower cost to serve this knowledge and capital. Europe is finding itself in a changed—dramatically changed—context, generally referred to as globalization.

What is the basic consequence of these and other changes I cannot elaborate on in the allot-
...there is an effort to replace the vanished external forces that created cohesion with institutional cohesion...
disappearance of the common threat. Another is the expected enlargement of the European Union. Both lead to an increase in the plurality of interests expressed and exercised.

There is an increasingly strong tendency in the European Union to emphasize domestic objectives. To overcome unemployment, it was stated at the last Council meeting, is the most important task of the European Union, not the member-states. I doubt this is the right priority, because I have great doubts it would be possible to solve on a European level what has not been solved on a national or regional level.

Institutions Open to Competitive Processes and Thus to the Opportunities of Complexity

European bureaucracies have reacted to the increase of complexity by increasing the web of institutional and bureaucratic arrangements. Like all bureaucracies, they do not react to increasing complexity by an effort to simplify the solutions, to reduce hierarchies, to institute self-regulating principles. They increase the complicatedness of administrations—and thus forego the opportunities of increased complexity.

These efforts lead to very difficult and increasingly burdensome contradictions within the European development. So the present Intergovernmental Conference and further deliberations on institution-building in Europe will have to concentrate on how to simplify, how to reduce the complicatedness of the present bureaucratic process to be able to better cope with the increased complexity.

I think Europe’s role and future will be decided during the next couple of years very substantially by the way Europe copes with what for German purposes we call die Wende (the change). We speak about die Deutsche Wende when referring to reunification. In reality, this Wende, this change, is a phenomenon which encompasses the entire Western world. This becomes increasingly apparent, especially in Europe but also in Japan. We have to reconsider the philosophical and historical foundations of our institutions and have to organize European institutions in such a way that they are compatible with the different developments in Great Britain, in France, and in Germany, to give just three examples.

The institutional arrangements have to be open. They have to allow competitive processes. Von Hayek once told us that if we don’t know the answer to a very important question, we have to institute a competitive process to find the answer. The European arrangements are very open to competition in the marketplace, but they are not very open to competition when it comes to finding alternative solutions to the problems of institutional arrangements in Europe. Institutional arrangements in social policy, in labor market policy, and other areas are not very open to competition either. This lack of openness to an innovative, competitive process in non-market aspects can defeat the advantages of open markets in the economy.

So, if Europe is to vitalize its energies, and it has a lot of energies, in a way which is sufficient to maintain its present position under conditions of globalization, institution-building will have to be re-directed away from a paternalistic approach towards problems, entrusting governments and the states with the solution of them. Institution-building will have to be open to a competitive process by way of which we will find new institutional arrangements which are better able to solve our new problems than the ones we have inherited from a very successful development during the last forty years.

* * *

That development was based on conditions that no longer exist. The change of conditions has to be reflected in a change of institutional arrangements. Unless we are capable of doing this, we are going to miss the new opportunities.

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The Internal Implications of Economic and Monetary Union

Basic Principles

From its very beginning 45 years ago, the EU has always been essentially a political undertaking and this applies also to EMU. The integration process is a serious, long-term effort by European governments to ensure peace, open and democratic societies, social and political stability, and a proper role for Europe in international affairs.

Along with the original principles, enhancement of Europe's competitiveness and curing "Euroscerosis" seem to have in practice gained importance over the years.

The Maastricht Treaty, concluded in 1991, aims at a common currency, a common foreign and security policy and a common justice and internal policy. In addition to—and closely linked to—this integration-deepening process, an important objective is to open the European Union to new members (to Central European countries in particular) and to enlarge the membership.

EMU itself aims actively to increase monetary, exchange rate and fiscal stability. This is expected to curb inflation and reduce inflationary expectations, lower interest rates, support growth, and eventually improve employment throughout Europe. A common currency is said to be vital for creating a free and efficient single European market for goods and services. The most evident benefits to all European Union countries—not only to the small countries—stem from stability, though the importance of lower transaction costs and better transparency should not be underestimated.

While price and exchange rate stability is the immediate goal of common monetary policy, logic requires much wider and closer cooperation. It is necessary that also fiscal policies be coordinated very closely within Europe. That is the only way of ensuring a combination of low interest rates and low inflation. The aim is to achieve a policy mix that supports the growth dynamics of the private sector, i.e. low interest rates and tight fiscal policy. The greater the credibility of the low inflation objective, the faster this can be achieved and the lower the adjustment costs.

It is important to keep in mind that all the goals of EMU would be imperative to Europe even in the absence of EMU. Low inflation and low interest rates, open and stable financial and other markets, as well as efficient and flexible rules of economic behavior are worthy policy goals under any circumstances. As many of the economic and social problems in Europe are essentially related to the large relative size of the public sector, structural problems with tax and social security systems and subsidy schemes, and rigidities in labor markets, reform of these systems is an important requirement for the efficient functioning of EMU. By the same token, one can see fulfillment of the EMU criteria for public sector deficit and debt ratios as a means of accelerating these necessary changes.

Implementing the single currency is nonetheless a risky undertaking—both economically and politically—primarily due to short- and even medium-term adjustment problems.

Is the Project Realistic?

A steadily increasing number of European politicians have, already a long time ago, decided that EMU is eminently sensible, necessary and possible. Governments and central banks have worked hard to provide the social flexibility and economic credibility necessary for its implementation.

Popular support for the common currency is not however particularly strong in all EU countries. This is a problem primarily because of the critical need to change many traditional
features of European society. Commitment to low inflation now seems to be widely understood and accepted. But the needed fiscal restraint, which demands short-term—and maybe even medium-term—sacrifices by traditional recipients of government transfers, has not received public support in an environment of high and rising unemployment.

Even if these reforms were necessary also in the absence of single currency, the public readily associates such changes with EMU. The basic problem, of course, is how to change the attitudes and the way Europeans in general think. Because that can easily take considerable time, there is a risk that the next few years may see some political turbulence.

Some of our foreign friends, many of them in the United States, have other basic concerns about the viability of EMU in addition to these transitional problems. They wonder whether Europe is at present too diversified culturally, politically, linguistically and economically to be able to conduct a common monetary policy. Labor mobility in Europe is very low compared to that in the United States, and the external shocks that have hit the different EU countries have differed in nature and timing. To them the crisis in the ERM in 1992-93 shows that EU countries still need the exchange rate tool at the national level. They argue that Europe would do well to concentrate on reducing impediments to the free flow of goods, services, labor and capital and return to the single currency project at a later stage or give it up completely.

However, one can ask if the differences between the cultures and social systems of Europe are really so large. What perhaps has mattered more are national borders and related policy differences. Thus the political will to overcome these borders is important. National borders in Europe do not always conform to social or linguistic borders and are in some cases fairly new anyway.

While different regions and countries have varied in their sensitivity to external economic shocks, recent integration developments and changes in the global environment have already changed the situation substantially. In addition, many types of shocks will actually disappear with the onset of EURO—particularly those related to or actually caused by unsound economic or social policies. The exchange rate as a national economic policy tool can readily be advocated from a theoretical point of view and from a large-country and reserve-currency-country point of view. However, practically all European Union countries have learned by experience that for smaller countries it produces more costs than benefits via unstable expectations, speculative attacks, lower credibility and higher interest rates.

As to labor mobility, it is true that it is presently low in Europe, but it will likely increase as social, legal and other barriers are removed during the integration process. Perhaps it is important to emphasize that Europe is in all probability not exactly striving for the degree of labor mobility and the kind of social security structure that we see in the United States.

In short, though Europe may not have been an ideal optimal currency area, the structural effects of the single market and single currency will help to reduce the differences and inefficiencies. In fact, EMU can be seen as a necessary tool for making Europe socially more flexible and economically more efficient.

One outside criticism of EMU has been and continues to be the limiting of common policy principles and “supranational” decision-making power to monetary policy. The major decisions in the area of fiscal policy (or in the area of the two other so-called pillars, common foreign and security policy and common justice and internal policy) will be made by the sovereign states themselves subject to EU-level coordination. This presents a real challenge both to EU procedures and machinery and to member countries’ desire to work together.

The existing excess deficit and convergence program procedures and the in principle already agreed stability and growth pact aim at close coordination throughout the whole range of economic policy. There are many who think...
these are not enough. But on the other hand, there are many who fear that these procedures in fact totally eliminate the room for maneuver in national fiscal policy, too.

The room for national maneuvering can however be expected to be much greater for the euro-member countries with balanced or surplus budgets than for non-member countries with big deficits.

Some critics believe that a federal structure will be an inevitable consequence of a common currency and monetary policy. Analytically, this does not necessarily follow and politically it would be a completely new decision for all the EU countries.

Adjustment Issues
A single currency should start off with those countries that are already credibly aiming and approaching long-term sustainable financial and real economy equilibrium. Monetary and fiscal authorities should have achieved a credible record in promoting stability. The benefits of low inflation without high adjustment costs demand an economically credible start. This again requires—among other things—that the possible Stability Council, comprising finance ministers of EMU Stage Three countries, will be an informal body without any authority to give instructions to the central bank regarding monetary policy. The task of the Stability Council should be to coordinate fiscal policy between euro-area countries, and its discussions with the ECB should be only informal.

A common currency promotes strong restructuring, not only in the public sector and in connection with social security or labor markets, but in the financial sector as well. The pressure for adjustment will accelerate. Introduction of the single currency will tighten and increase competition, as the implicit protection provided by national currencies disappears. The resulting structural changes are likely to be large: a gradual concentration of securities markets in cost-effective, highly liquid exchanges as well as a substantial increase in mergers, acquisitions and even failures among financial institutions are likely to occur. It is important to understand that all these as such healthy and necessary structural changes would come about even without EMU but in that case more slowly—maybe too slowly.

Prospects
What then are the current prospects for Stage Three of EMU? Will it start on time? What kind of a creature will it be? What are the possible implications?

Many countries, even some “core” countries, have not yet achieved sustainable fiscal balance, due partly to cyclical developments and partly to the structural nature of unemployment. At a time when unemployment is high and rising, voters remain unconvinced of the wisdom of monetary union. At the same time, the Maastricht Treaty lays down strict criteria and timetables to be followed during the creation of the monetary union.

Compared to the situation some time ago, the markets seem to be somewhat more sceptical today about a successful start for Stage Three of EMU at the beginning of 1999. However, one should not lose sight of the fact that both politicians and authorities and an increasing number of enterprises already have invested heavily in the project—in terms of both reputation and capital. As time passes, the likelihood of EMU materializing grows steadily.

The understandably strong political preference for early and wide participation in Stage Three may prove difficult to fully combine with strict economic criteria and requirements. Central bankers who aim at medium-term benefits generally have little problem in choosing economic and financial stability as the more weighty requirement in this situation. Politicians should consider carefully the unattractive consequences of reducing the economic credibility of EMU. Economic viability on a permanent basis can be ignored only at substantial economic and ultimately also political cost.

There is a risk that abandonment—or even postponement to an announced date—of Stage
Three could cause uncertainty and turbulence in the financial markets as well as in the political sphere. The further integration of Europe might be questioned; growth and employment prospects could worsen; and the integration of Central Europe into Western Europe could come to a halt. The risk of unfavorable reactions could be expected in respect of currencies of countries on the “periphery” of Europe and of countries in which market confidence has been based on the “borrowed credibility” of assumed membership in the euro area.

It is more likely Stage Three will be launched on time but with only a few and very stable and credible participants. Because expectations in this case would be for the euro to be stable and economic and employment growth rates to be high, market reactions would be positive. However, such an alternative could create political problems between the countries in the euro area and those temporarily left outside. Again, there might be a risk of unfavorable market reaction in countries that had obviously aimed at membership and enjoyed “borrowed credibility” up until final selection time.

It would be crucially important to support and guarantee the necessary political motivation and confidence in these countries so that they would continue their efforts to join the EMU later. Similarly, coordination of monetary and fiscal policies between euro and non-euro EU countries in order to stabilize non-euro exchange rates against the euro is of utmost importance; the required mechanisms (ERM II and tight convergence program procedures) should be put effectively in place.

In the case that Stage Three is made up of a large number of countries, there could be less certainty in the markets concerning its economic and financial stability. The euro era might therefore be initially marked by volatility, rising interest rates and slowing economic growth, which would create both political and fiscal problems. Such problems could also make an early enlargement of the EU more difficult. In this case it would be particularly important to implement monetary policies and the so-called stability pact vigorously, in order to ensure rapid recovery of credibility and stability.

Finally...
Stage Three of EMU is a very demanding project. It is a worthwhile undertaking supported by a large following of knowledgeable people in Europe. It is not however very easy to sell the project to the voters because of the inevitable short-term adjustment problems involved and the present unsatisfactory economic conditions in Europe.

There has been a great deal of criticism of the project. Much of this criticism is understandable: the common currency project entails great risks, particularly in the short term. Nonetheless, it is a very important and essentially well-founded one that deserves our best efforts. At the moment, it would be equally risky to postpone or abandon it. Such a course of action could easily lead to disintegration and moreover leave Europe a permanently less attractive partner for the rest of the world.

Europe must adapt and restructure its institutions in order to become an effective, competitive and equal partner that will contribute to global cooperation and stability. If successful, the euro could challenge the dollar as the world’s reserve currency, but it would at the same time promote worldwide economic growth and development.

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International Implications of Economic and Monetary Union

Two Crucial Issues

The world outside Europe is particularly interested in two issues related to the creation of an Economic and Monetary Union (EMU) in Europe with a single currency (EURO).

1. Will the EURO become a global currency?
   There are several arguments in favor of such an outcome:
   - The market in EUROs will be much larger and deeper than currently is the case for the individual currencies in Europe, including the DM;
   - This size and the improved liquidity will make the EURO a more attractive instrument for both investors and issuers worldwide, both inside and outside Europe;
   - Pricing and invoicing of international trade transactions is more likely to take place in EUROs than now in DMs etcetera; and
   - Central banks, particularly in countries outside Europe and the USA, will keep a higher proportion of their monetary reserves in EUROs than they now do in DMs and other European currencies—provided they consider the EURO as sufficiently stable and strong.

   Question one: Will the EURO become a stronger competitor of the U.S. dollar than now is the case for the currencies in the EMU area combined? The answer is very probably yes. So the EURO will present a challenge to the dollar, though gradually.

   Question two: Will the EURO replace the dollar as the preeminent global reserve currency? The dollar now still represents by far the largest component (60%-70%) of international official reserves. The answer to this question is probably no.

   Question three: Is this global reserve role for the EURO a major goal of the drive toward a single European currency? The answers vary, and are subjective and heavily political. It is clear that the primary goal is to create improvements in economic conditions, especially more stability and economic growth, within Europe. However, on top of this primary objective, several groups in Europe, particularly in France and the European Commission, consider such a global role for the EURO as a reserve currency as a highly desirable outcome. They see economic as well as political advantages in a successful challenge to the supremacy of the dollar. This approach has been a constant factor in French policies. For me personally, however, this has never been a primary goal of the single currency, but rather a likely outcome.

   My conclusion is that the EURO will play a (more) important role as a global currency. The extent to which it will do so is, however, uncertain. It is unlikely to replace the dollar as the number one global reserve, trading and investment currency.

2. Will the EURO become a strong currency?
   I see several arguments in favor of a strong EURO:
   - Initially, a "technical" factor will give support to the EURO. European countries now hold large amounts of their monetary reserves in dollars (U.S. Treasury bonds and bills). After joining EMU, the member countries will see much of their international trade disappear: exports to and imports from other EMU countries will become "domestic" trade, denominated in EURO. After pooling their monetary reserves, the European Central Bank (ECB) and the national central banks, taken together, will need a lower aggregate amount of international reserves (de facto largely dollars). They then will face excess holdings of dollars and are likely to sell part
of their dollar holdings against EUROs. These sales will initially weaken the dollar and support the EURO:

- As mentioned above, the EURO is expected to play a more important role as a reserve currency globally. This implies some shift in the composition of reserves of third countries, from the dollar and other current reserve currencies into EURO. (This argument can, of course, work both ways: if the EURO is perceived to be strong, then both official and private sector institutions in other countries will invest in EURO-denominated assets which, in turn, will further strengthen the EURO. If, however, the EURO is perceived to be weak, then the opposite effect occurs);

- From the beginning of the process (Maastricht), the assumption was that the EURO has to be strong. For domestic political reasons, Germany—needed and needs—to present the EURO in a credible way to its critical population as a currency “at least as strong as the DM,” so that the Germans are willing to give up their own trusted currency; and

- Finally, the new European Central Bank wants to begin its life by establishing credibility and a solid reputation. This implies a strict monetary policy: anti-inflationary, anti-depreciation of the new EURO. The result will be relatively high interest rates and, therefore, support for a strong EURO in 1999.

On the other hand, I should also mention arguments in favor of a weak EURO:

- Certain groups in Europe, particularly several exporting companies in France, and probably in other EMU countries as well, prefer a EURO that is relatively weak or weaker than the DM is today. This implies an (initial) depreciation vis-a-vis the dollar and yen. A similar line of thinking may find support in certain official circles which favor the new ECB to set the EURO/dollar exchange rate initially relatively low to allow European industry a competitive advantage, thereby stimulating economic growth in Europe; and

- More recently, the dominant factor in this debate has become the (perceived or real) expected weakness of the EURO resulting from a larger number of participating countries than was expected earlier, linked with the assumption that several (particularly the newly added) member countries/currencies are weaker than the “hard core” candidates. In concrete terms: the lira (Italy) and, to a lesser extent, the peseta (Spain) and the escudo (Portugal). This outcome is based on the assumption or fear that the convergence criteria of the Treaty of Maastricht for admission to the first wave of EURO members will be interpreted flexibly rather than strictly. This scenario of “fudging” with the convergence criteria (a scenario which I personally oppose) would in all likelihood lead to a weak EURO. Many investors, both from outside and within the EMU area, will shift part of their assets from holdings of bonds denominated in DM, and later in EURO, into third currencies. We have seen this already happening through switches from DM and guilders bonds into assets denominated in Swiss francs, sterling and dollars.

One may convincingly argue that on economic grounds, such a conclusion is unfair or unwarranted in light of the surpluses on the balance of payments of Italy (supported by high domestic savings rates) and the modest amount of international debt of Italy (as a country); these are, however, important perceptions held by the population in Germany and by many traders and investors in New York, London and elsewhere.

Such an outcome of a weak EURO would be bad for the image of the EMU. It is also unattractive for exporters in the USA and Japan: a weak EURO means a strong(er) dollar and yen.

My conclusion is that the outcome of whether the EURO will be a strong or a weak...
currency is uncertain at this point in time. It all depends heavily on the composition of the first wave of EMU participants and on the policies of the new ECB. Both are unknown at this moment. Right now, I see clouds hanging over the EURO in this respect.

**Japan**

Because of the composition of the Trilateral Commission and our meeting here in Tokyo it is useful to address the EURO from the viewpoint of Japan.

It is my impression that Japan does not hold strong positive or negative views about the single currency in Europe. This is understandable: most Japanese are less familiar with all details of the developments within Europe, and they are puzzled by the complex and confusing flow of information about the EMU/EURO. I am not aware of any official Japanese position. Neither do I detect many outspoken views in the business community. I note, however, one interesting and important exception. Toyota recently has taken a strong public position, not with regard to the EMU/EURO in general, but to the composition of its membership. Toyota has stated that it opposes the opt-out of sterling from the first wave of EURO participants. It also has taken the unusual step of threatening that it may shift its next major direct investment in a new car plant in Europe from the UK (where it had built its previous major manufacturing facility) to a continental European country if the UK does not join EMU. As I am personally in favor of sterling joining the EURO in the first wave, I hope that this unusually blunt Japanese message will influence the British decision (but I am afraid it will not). When analyzing the economic arguments for Toyota's attitude, I do appreciate the strength of their point that the risk of substantial exchange rate volatility between sterling and EURO is unattractive if one produces in the UK but intends to sell a large portion of the cars in the EMU area. On the other hand, other economic factors currently favor the choice of the UK over the European continent for a production plant.

The impact of the EURO on the yen may be that it will become less likely for the yen to play an important role as a global currency: it will face two strong alternative global currencies (the dollar and the EURO) rather than only one (the dollar) today.

**USA: Business Community**

Recent press publications reported that a conference organized in New York on EMU/EURO was canceled because of a (perceived) lack of interest from American companies and investors. However, my own extensive experience in the U.S. on this issue is different. It is true that the majority of American companies and investors are not (yet) interested. This is, however, understandable, since they are of moderate size and/or domestically oriented: they have neither production facilities in Europe nor important exports to Europe. For the many larger and/or international American companies and investors, this is clearly different. Although initially after “Maastricht,” in 1992-1994, their interest in the subject was limited, in recent years this has changed. Whereas several American corporations and institutions still assume that the EMU will not happen, it is my clear impression that most internationally active U.S. entities are now devoting much time to the question: What are the concrete implications of the EURO for my company? They have become aware that the impact on their business will be substantial.

My consistent advice to them is: you must take this issue very seriously and, in view of the prevailing uncertainties, you need to prepare three scenarios of the consequences for your specific activities in Europe:

a. There will be no EMU/EURO;

b. EMU with a limited number of currencies/countries in the first wave (up to eight: Germany, France, The Netherlands, Belgium, Luxembourg, Austria, Ireland and Finland); and

c. EMU with a large number of countries in the first wave (eleven: the above-mentioned countries plus Italy, Spain and Portugal).
Today, all three scenarios offer a real possibility. The impact differs, obviously, from company to company, depending on the countries in Europe where they produce and where they sell their products. So, again no general conclusion can be drawn at this moment for the net impact.

My impression is that most U.S. companies take, in principle, a positive attitude vis-à-vis EMU/EURO, for the (logical) reasons that a single currency simplifies their financial operations in Europe, that it reduces their exchange rate risks, and that it reduces their transaction and hedging costs.

Many American companies correctly observe that, whereas the completion of the single market ("Europe 1992") has created one large and open market in Europe for their goods, services and capital (like in the USA), the lack of a single currency continues to present obstacles for real free trade within Europe (unlike in the USA).

Finally, most American companies as well as investors do not like a weak EURO—or, in other words, a strong dollar. This would undermine U.S. competitiveness and the attractiveness of financial investments in Europe (unless a U.S. industrial corporation has large production facilities within the EMU area and does not export to Europe).

USA: Attitude of Authorities
Since World War II, Washington has been consistently in favor and supportive of European integration, both political and economic. On the issue of the single currency, the U.S. Administration has taken a more cautious and almost silent position that ranges from neutral to moderately positive. I consider this a wise approach. Europeans tend to criticize American authorities when they make strong public statements on intra-European matters: "Please do not meddle in our affairs." I admit, however, that EMU/EURO is not merely an internal European issue because it may have an impact on the exchange rate between the dollar and the European currencies and on the international role of the dollar. I quote Larry Summers (U.S. Treasury Undersecretary) who made the typically vague but acceptable comment: "Anything that works out well for Europe will work out well for the U.S." (Wall Street Journal, March 3, 1997) But if one listens carefully in Washington, one can hear two concerns (which, however, are unlikely to become reality simultaneously):

On the one hand, we Americans do not like a weak EURO because this is bad for the American competitive position and exports (this is the dominant worry today); and

On the other hand, we Americans do not like a strong EURO either because this may lead to a replacement of the dollar by the EURO as the major global currency. (This was the dominant worry some time ago.)

Perhaps the most appropriate solution is a balanced, middle-of-the-road outcome: neither a very strong, nor a very weak EURO. Some others in Washington would say: no EURO at all!

A third concern in Washington is that the EMU plan seems to be too ambitious for Europe at this stage, in the sense that the frantic efforts by many European countries to meet the Maastricht criteria lead to deflationary effects, thereby prolonging European stagnation, whereas the United States wants to see higher economic growth in Europe. One can argue, in my view, whether EMU/EURO deserve blame for a number of unpopular measures in Europe that had to be taken anyway, with or without a single currency and the criteria of Maastricht. But all this turmoil now puts EMU/EURO, undeservedly, in a bad light in Washington as well as Europe.

Within this context, I see the remarks made by Ed Truman (Head of the International Department, Federal Reserve Board, Washington) some days ago at a conference organized by the IMF. His comments were surprising in that they were outspoken as well as negative about EMU/EURO: a change of thinking in Washington? He is concerned that too much thinking about coordination of policy within Europe is focused...
on exchange rate policy rather than on more serious issues of fundamental economic policy. Such a shift in focus, he said, would be a step backward, because it would distract attention from fiscal and monetary policy. I think he is factually mistaken on this issue. He also said that EMU could make economic policy coordination more difficult, both internationally and within Europe itself. He may be right indeed that international policy coordination could become more difficult, but more difficult in the sense that Europe—or at least the EMU bloc—may present a stronger countervailing economic-political power to the USA.

Finally, I agree with Truman and others when they doubt that the advent of a single currency in Europe would lead to a global system of fixed exchange rates or currency target zones. I see no evidence that either the USA or Europe would be more willing to take measures toward global exchange rate stability after the achievement of a single currency in Europe, leaving aside the major question whether any official efforts to achieve this global stability could be successful now that international movements of private capital have become so overwhelmingly large. I expect that for many years to come we will face a high degree of instability between the dollar, yen and EURO. The main reason is that large countries continue to give priority to domestic economic and political objectives when setting their policies, rather than to international considerations. This will not change with the arrival of the EURO.

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SECTION 6
U.S. INTERNATIONAL LEADERSHIP

JOSEPH S. NYE, JR.

U.S. International Leadership in President Clinton’s Second Term

Three-Dimensional Chess

I want to talk, first, about how to judge American leadership. You have to have some picture of the way the world is shaped before you can get an understanding of American leadership. The picture of “three blocs” has been properly discredited. “Clash of cultures” also deserves discrediting. But the usual lingo of asking: is the world now unipolar (with the Americans dominant) or multipolar?—is also profoundly misleading.

We need to think of a much more complicated structure of international power, a little bit like three-dimensional chess. On the top chess board, the military board, yes, the world is unipolar. The Americans are going to remain the dominant military power for well into the next century. They’re there now, and their investments in the technology to keep them there are likely to increase.

At the middle level of this three-dimensional chess board, the economic level, the world is already multipolar. The three Trilateral regions are two-thirds of the world economy and China is coming up quickly. This dimension will be quadrilateral in terms of the distribution of power soon after the turn of the century.

At the bottom level of this three-dimensional chess game, the area of trans-national relations that cross international borders out-
side the control of any government (which can include everything from foreign exchange to international terrorists), there's really no structure of power. There's total diffusion of power.

So when you try to understand what's happening in the world, putting it into one dimension is a little bit like using the physics of Newton in an age of Einstein. In other words, we find ourselves in difficulty trying to understand where and how the Americans and others should act in international politics because we often misrepresent the nature of the world.

And in those contexts, the danger is an American government that will try to do too much or too little. Essentially, if it tries to do too much, it will not only arouse resistance in many areas abroad, but probably trip over itself at home. Another way of putting it is: if you get involved in another Vietnam or another Somalia, the domestic reaction may lead you to fail to do the things which are critical for Americans to do. Another way of putting that is: the pursuit of marginal interests too vigorously can lead you not to defend critical interests vigorously enough.

Four Tasks
How would you then address the situation of a power situated like the United States, so that you don't do too much or too little? One first approximation would be to look at the role of Britain in the 19th century. Britain was more powerful than other countries, particularly in its global scale and sea power, but it was also a country which could not control the world. It could do certain things, but not others. In that type of a world system, where one country is much larger than the others but not able to dominate, it seems to me the important things are (1) to maintain the balance of power, which Britain did in the 19th century; (2) to maintain an open international economic system, which Britain also did; (3) to maintain certain rules of the road (we nowadays also call them international regimes, but the law of the sea in the 19th century could be a parallel); and finally (4) to try to mediate and arbitrate and reduce conflicts which could otherwise be destabilizing. If you look at those four principles, those four practices that Britain did in the 19th century, it gives you an idea of what a strategy for the United States might look like.

If you look at the first year of the Clinton Administration, it didn't fill out those four practices very well. On the other hand, if you look at the second half of the first Clinton Administration, I think it did quite well according to those principles. And if you look at the beginning of the second Clinton Administration and in particular at Madeleine Albright's itinerary for her first trip as Secretary of State—Europe, Russia, China, Japan and Korea—that is not a bad itinerary from the point of view of the strategic principles and priorities that I sketched out.

Maintaining the Balance of Power
Let me look at each of those four things in a little bit more detail. First and most important is maintaining the balance of power. It's true, as Renato Ruggiero said in his speech at lunch, that economics is becoming more important. But I would like to remind you all of a phrase that I once put in a Defense Department report: when you forget about security, it's like forgetting about oxygen; you don't notice it until you begin to miss it. Underlying every economic system is a structure of order, and that structure of order rests upon a certain degree of military force and power. In that sense, if we get the balance of power wrong, if we don't understand the relationships among the major powers, we'll quickly find that the economic system will be in great disarray.

If you look at what's happening in terms of the overall balance of power, the greatest questions relate to the rise and fall of powers. There we've seen the fall or decline of the Soviet Union and the continued doldrums of Russia, and the rise of China. How do we deal with this? The first thing the Administration is doing is asking whether its military strategy is properly adjusted for such circumstances. There is

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now a Quadrennial Defense Review, due out in May, which essentially is talking about how we shape the environment through the type of forces we have. There are some debates on trade-offs between forward deployment of American troops and cutting troop numbers so there can be more investment in the new information technologies that go into smart weaponry, but by and large, I think this Quadrennial Defense Review will come out with a strategy similar to what we have seen. If you look at the deployment of American forces globally, you’ll notice about 100,000 in Europe, about 100,000 in Asia, and about 20,000 in the vicinity of the Persian Gulf. They're deployed that way because the view is that those are the three areas—Europe and Asia for obvious reasons, the Gulf because of its critical role in energy—where, if something went wrong, it could profoundly tip the global balance of power.

Europe. More specifically, looking at Europe, it’s important that the Administration is going to continue to support the integration of Europe, which has been a long-standing position, and continue to strengthen NATO. The Administration has been in favor of a European defense identity. It devised the idea of Combined Joint Task Forces, so that NATO forces can be—as the phrase goes—separable but not separate. In other words, some groups of NATO countries may use some sets of NATO forces for peacekeeping or other operations out of the area.

But in Europe the big issue will be how to handle NATO expansion. There’s a debate in the United States and elsewhere asking whether it was a good idea to announce the expansion of NATO when it was announced. That has become largely irrelevant, because to backtrack on that decision now would create considerable disarray and be far more costly than to go ahead. But going ahead requires a careful handling of Russia. In that sense, I think the biggest issue for Clinton in his second term is going to be the management of the Russian relationship in the context of NATO expansion. The early news from the Helsinki summit as we meet in Tokyo seems to be that things may be headed in the right direction. It’s clear that the Russians don’t like NATO expansion. But it’s also clear that there are things that could be done that may make the Russians able to accept NATO expansion as they accepted German unification, which they initially opposed. So one thing to keep a close eye on in terms of the balance of power in Europe is the management of the NATO expansion issue.

Asia. If you look at the balance of power in Asia, you find a lack of institutions during the Cold War. Unlike Europe, where a number of institutions developed, in Asia, essentially, the United States remains the key stabilizer. Another way of putting it is that the forward deployment of American troops helps countries with conflicts (that existed before the Cold War and persist after the Cold War) to avoid such conflicts breaking out into the open, and to avoid the arms races that might accompany them. By and large, I think the presence of American troops is broadly welcomed in most capitals in Asia.

The specific question in Asia relating to the balance of power will be how the United States and others manage the rise of Chinese power. It’s important neither to ignore it nor to exaggerate it. There is a danger among some Americans of becoming slightly hysterical about the rise of China. A good example of a wrong-headed way to think is the lead article in the current issue of Foreign Affairs, called “The Coming Conflict with China.” Handled properly, there need not be a coming conflict with China.

The critical thing the Clinton Administration and Prime Minister Hashimoto did in 1996, when President Clinton was here in Tokyo, was to reinforce the U.S.-Japan Security Treaty, pointing out that it is still relevant for stability in this region, even though the Cold War is over. At the same time, it is important that the Administration, along with Japan, as you heard from Prime Minister Hashimoto this morning, engage China constructively—not to
isolate China, not to lead to a policy of hostility, but to find ways of bringing China as a responsible power into the regional and international system. I think that policy of constructive engagement is proper. I think the Administration is headed on the right track. But the domestic political problems which have risen out of the campaign finance issues, in some cases involving money allegedly related to China, may hobble the President from engaging as positively or as constructively with China as he might like.

Persian Gulf. The third area critical to the balance of power is the Persian Gulf. There Iraq and Iran remain difficult. Holding the balance in the Gulf while trying to advance the peace process in the Arab-Israeli dispute remains the keynote for policy in that region.

Maintaining an Open International Economy
The second major task for a great power that doesn’t have complete control is to maintain an open international economy. The critical question there is to resist protectionism. Every country, every democracy has some degree of protectionism. We’ve seen some of that in the United States, but the most interesting thing—if you go back to the predictions of a half dozen years ago—is that it’s nowhere near as strong as predicted. Patrick Buchanan, the most overtly protectionist of the candidates running in the Republican primaries, rarely got much above 30 percent of the vote.

In addition, it’s important to maintain a stable domestic economy. If you look at the conditions of the American economy and the major efforts being made to bring down the budget deficit (now getting close to a percent and a half of the GDP), you’ll find that there is significant progress by the Administration.

NAFTA and the subsequent rescue of Mexico financially, support for the WTO, the development of APEC, these are areas where the Clinton Administration has indeed followed this principle of maintaining an open international economy. There is an American temperation into unilateralism in areas like Helms-Burton, which relate, notice, to particular political disputes, not to the broader trade issues. There are difficulties there. Nonetheless, in the broader context, the most important thing is that the Administration has stood for an open international economy.

Organizing International Rules and Regimes
The third major task of a great power which can’t control the world, organizing international rules and regimes, is critical. We have seen the extension of the Non-Proliferation Treaty for an indefinite period. We have seen the growth of the multilateral regime on control of missiles. There is now before the Senate a chemical weapons treaty. If you look at other areas—for example in the United Nations and support for United Nations peacekeeping and humanitarian activities—there has been a degree of resistance to paying one’s dues. An arrangement may be reached between the Congress and the Administration on UN dues, but the answers aren’t in yet. In any case, the Administration’s policy is to go ahead and make those payments. On international conventions on human rights, on questions about the environment (where we’re trying to go into tradable permits, which brings a market rationality into this), in a whole series of areas, the Administration is taking a leadership role in that third task as well.

Mediation
The fourth of the four tasks that I mentioned was mediation. There are many instances where the United States is not in a position itself to intervene or to solve a problem entirely, but where the role of the largest power, exercising suasion upon the parties to the dispute, makes a difference. We’ve seen this in the efforts that the Clinton Administration put into the Middle East peace process in the first term—I expect them to continue in the second term. We saw it with the efforts on Bosnia in the Dayton process, for which Richard Holbrooke deserves
great credit—how it's going to turn out is still far from known. We’ve seen it also in less dramatic ways, for example in trying to mediate disputes between Greece and Turkey, or between Peru and Ecuador when war broke out between them, or even between India and Pakistan over the events in Kashmir.

The harder problems in this dimension are the disputes where there is no strong national interest. I think particularly of cases in Africa: what will happen in Zaire, in Burundi? There the best one can hope for is to put together some sort of coalitions internationally, of African states or of others. By and large I think this is an area in which there will probably not be much progress.

Domestic Politics and Internal Preoccupation

Measured against the standard which I’ve used, I think you can argue that the Clinton Administration enters the second term with a quite reasonable strategy for the complex three-dimensional world that I described. The first year of the Clinton Administration may have been off the game, but since then, in the last two years of the first term and at the beginning of this second Administration, they’re probably working pretty close to that strategy.

The key question I’ll leave you with is whether domestic politics will allow the Administration to follow its game plan. Can it implement this strategy? If you look into domestic politics today, one thing you notice is much less bipartisanship than in the past. In the House and the Senate, it’s harder to get bipartisan support for a foreign policy strategy than in earlier years. The second thing you notice is less willingness to devote resources to foreign affairs. Resources are devoted to defense; but when it comes to the budgets of the State Department, or AID, or the U.S. Information Agency, there have been severe cutbacks and a series of quite false economies.

Finally, if you look at what’s happened to American attitudes, they have not become more isolationist—in public opinion polls, isolationism is rejected—but they have become more focused on internal issues. There is an important difference there. Americans are not rejecting the rest of the world, as they did in the 1930s, but they are paying less attention to the rest of the world. Now the Americans are not alone. In 1991, Kurt Biedenkopf, Motsoe Shiina and I wrote a report for this Commission which said that a problem in the years ahead for all three regions was going to be not rejection of the outside, not isolation, but internal preoccupation. That indeed is occurring.

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Karen House

We Cannot Expect Much Leadership from President Clinton

Joe Nye is one of the most articulate Americans on foreign policy issues, as you have just heard here today. However, his vision of American foreign policy is considerably clearer than that of the Administration.

President Clinton’s Weaknesses

In the United States, at least three things have diminished our ability to focus. One is that the simple vision of rivalry with the Soviet Union is gone. The second is that there are many, many more “hits” on the American people about the rest of the world. There are not just three networks that do a half hour of nightly news. CNN bombards you; there’s the Fox net-
work; there's the Internet. There's much more information.

Third, at least in my view, we have a President who cannot cut through that because he lacks a clarity of vision and thus cannot enunciate one that the American people feel is compelling. His vision, to the extent that it exists, has been to indulge the American people in the righteousness of their—to use Bill Emmott's word—self-centeredness. Even his supporters will say that the President is not a man who means what he says—that's become the cliché in America.

So we, sadly, cannot expect a great deal of American leadership at a time when—again to quote Bill Emmott—three very positive things are going on: no war, no country seeming to believe that it can gain from aggression, and the impulse toward freer trade. It's an opportunity for the world—and for U.S. leadership—that is being squandered. And to quote Paul Wolfowitz's paper, it is not a foregone conclusion that the world will stay peaceful, harmonious, Let's-all-get-rich-together. In each of our countries there are people who adapt very well to globalization and who do get wealthier, and other people who do not, and a schism between the two.

You cannot expect a great deal of American leadership because President Clinton is very much like Richard Nixon in his second term. Both of them were willing to do absolutely anything to get reelected, and as we say in Texas those chickens are coming home to roost. (The one difference is that Nixon wanted to be reelected to do something. I think Clinton wanted to be reelected to be something, i.e., President) The Administration is likely to find itself, as it already is, bogged down in: what did the FBI tell whom, and why didn't Janet Reno try to find Tony Lake, and why didn't Tony Lake hear from his staff that the Chinese were trying to buy elections, etc.

No Strategic Vision on China
President Clinton does deserve credit for having gotten NAFTA ratified and for having been far more positive about free trade than he was in his 1992 campaign. But the whole issue of China's emergence, I think, is the critical issue for the next twenty years, and I don't think the United States is remotely prepared to deal with that. As one who thinks it's very important that we talk to the Chinese, I think it is also risky if the President engages in conversations with Jiang Zemin and doesn't really know what he wants to achieve. The consequences of that can be even worse: to have a conversation in which we can put forth no real strategic vision, no long-term view, no real policy.

The Chinese are very unhappy about the U.S.-Japan Security Treaty renewal. They argue that the Americans have been stupid and naive to not understand that Japan intends to re-arm behind this new declaration. If they really believe Japan is a security threat to China, then I don't see how they can be totally serious about the United States making a great mistake. They have to see the United States as something of a deterrent or suppressant on Japanese militarism.

My view of the way the United States ought to operate is to understand that, fundamentally, as at the end of World War II, we have another self-proclaimed rival for superpower status—and that is China. We have to be as consistent and as long-term in our thinking about how to deal with China as we were in our thinking about dealing with the Soviet Union at the end of World War II. The Soviet Union was not the equal of the United States then, and obviously China is not now, in terms of the full range of power. But China will become increasingly more powerful. It does not have to be an enemy. But if we don't find a way—and understand that we don't see eye to eye on everything, and that all of our interests are not the same—I think we risk creating real problems, not just for the United States with China, but for others as well.

The business people in this room will be extremely important in determining future relations with China. What intrigues me is whether the Chinese will be able to translate Western
business greed into political capitulation, or political concessions to China. Most of the business people one talks to are not making money in China, they’re all waiting for the pot of gold at the end of the rainbow. How much will people do China’s bidding to remain investors and businessmen in China? The Chinese, some of them at least, think there are not many limits on Western lust for the China market; and therefore there are very few things China cannot do and still continue to enjoy Western investment.

Wrong Policy on North Korea
The other big immediate issue is North Korea. I personally think it is both morally and politically proper to do everything possible to precipitate the collapse of North Korea. I don’t think the risk that North Korea lashes out diminishes by attempts to prolong its existence and somehow ease it into an accommodation with the South, because I truly don’t think that is very likely. There are those who argue that it’s risky, so let’s just keep kicking the can down the road. I don’t see the utility of that politically, and certainly not morally—leaving people treated the way the North Koreans are treated by their government. The Clinton Administration has kicked the can down the road by saying, “Well, wait five years; we are not able to inspect to make sure there are no nuclear materials being used to create bombs; but it’s difficult to confront them, so let’s just hope for the best.” It’s this kind of let’s-push-all-issues-into-the-future that I think risks a very high price for all of us.

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TOM FOLEY

A Courageous President in a Corrosive Domestic Political Environment

The 1996 Election and the Tradition of Divided Government

The 1996 election was an historic election in many respects. It is the first time since Franklin Roosevelt that a Democratic President has been re-elected to office. It is the first time in over 60 years that a Republican majority in the Congress has been elected to a second term. The election in 1994 of a Republican majority in the House and Senate, after many years (particularly in the House) of wandering in the political wilderness, was connected, in my judgment, with the re-election of President Clinton. That election of a Republican majority in Congress provided a unifying factor in the Democratic Party, so that President Clinton had no challenge at all for the nomination. And there was a general feeling on the part of many Democrats in the country that, with all their dissatisfaction with the Administration, it was desperately important that the government not be unified in a Republican Congress and a Republican President.

We are continuing in a different form a phenomenon that the United States has demonstrated to all of its friends and adversaries since the end of World War II: divided government. For the most part, we’ve had a Republican President with Democratic majorities in the House and the Senate. Now it is a Democratic President with Republican majorities in the House and the Senate. Far from bringing about public grumbling about gridlock, the public actually seems to favor the division of power.
not only the separation of executive and legislative powers that the Constitution provides, but Democrats and Republicans each in charge of one of the branches. Some recent academic judgment is that we get about as much done with divided government as we do with unified government. It would not have been possible for President Bush to have gone into the Gulf War without a significant number of Democrats supporting the resolution. It wouldn't have been possible during the first Clinton Administration for us to have passed NAFTA or agreed to the Uruguay Round outcome if it hadn't been for Republican votes. Indeed, Republican votes were more numerous for NAFTA in the House than Democratic votes.

Corrosive Hatred of a Courageous and Principled President
But there are some deep concerns that the present political environment in the United States is becoming so soured and corrosive that it may interfere with the conduct of our foreign policy and economic policy. You can tell from Karen House's remarks that there are some people who are not great admirers of the President (with the general public, he still enjoys significant majority approval). But I think it goes beyond that. Particularly in the first term, I saw evidence of cultural, political hatred of the President—that could only be compared to the reactions of some during the era of Franklin Roosevelt, when there was so much bitterness, so much hostility and so much division.¹

I would argue that the criticism that Karen has laid on the President is too harsh in almost every respect. In fact, I think the President has shown principle and courage in taking up policies that were politically much more damaging to him at home than was often realized abroad. His support of NAFTA was probably one of the elements in the 1994 defeat of the Democratic majority in Congress, because it alienated organized labor very deeply, one of the fundamental constituencies of the Democratic Party. President Clinton took that on with great energy. The decision to sponsor the Dayton talks and send American troops to Bosnia was a high-risk policy immediately before an election, and could well have resulted in a disaster which could have cost him re-election. The efforts of the President to separate MFN from China policy were subject to harsh criticism in his own party, but I think this was a wise judgment. (Obviously we've been disappointed with the failure of China to be more sensitive to human rights issues.) The President's actions are sometimes objected to not so much in fact, but in motive, that he's doing it for some reason of less-than-committed principle. I think the fact of the matter is that, as Joe Nye has said, particularly in the last two years of his first term, the President's foreign policy has been largely successful, and courageous, and principled. And I think there is no occasion to suggest that his actions in the second term will be motivated by some expediency, some wanting to be liked, some social service policy around the world that has no connection with the fundamental position that the United States has followed for many, many years—to support freedom and democracy, to support stability, to support free-market systems, to support free trade.

Substantial Bipartisanship Needed for Successful U.S. International Leadership
My hope has been that the two parties would display the same kind of bipartisanship that has often marked American foreign policy. With some singular exceptions where great emotion was involved (such as policy in Central America or Vietnam), there has been a remarkable stability to American foreign policy because it has been the subject of large-party bipartisanship and party consensus. Tocqueville once said that

¹I grew up in a small town in Washington state where my next door neighbor and best friend was the son of the Republican County Chairman (and President of the Bar Association and the Polo Club). I was told by my friend never to mention the name of Franklin Roosevelt in his house—his father did not permit it. On the other hand, in my house, every time Roosevelt spoke on the radio, there was a semi-religious gathering of the house.
democracy was the best policy to organize domestic affairs, but in the international affairs of states an aristocracy was the best because it provided the stability, the vision and the continuity that was so needed in international affairs. We don't have an aristocracy in the United States, but the consensus of political leadership in both political parties over a long period of time has provided that degree of stability. It can do so again. But if we see a desire to engage in the kind of blood sports that have been too common in our recent politics—destruction of the other party by fire, by prosecution, by the tortures of the confirmation process—then I fear that it will interfere with American leadership in many key areas.

The most critical ones are China and North Korea. When the President came out of the 1996 election, I think there was a possibility of some very constructive policy toward China (to the great credit of Bob Dole, who kept China from being an issue in the campaign). Now, because of the campaign fundraising investigations (which will go on in the House and the Senate), it may be difficult to proceed with an extension of MFN beyond the yearly basis, which some of us had hoped to see. The analogy now used in some quarters in the United States that U.S. policy toward China is similar to alleged British weakness in dealing with Wilhelmine Germany prior to World War I is, I think, entirely misplaced. There is a problem with Russia as we advance the extension of NATO. A policy toward China of confrontation might well create the circumstance for a warming of Sino-Russian relations, which would not be in the best interest of the United States or its allies and friends.

I still take hope that there are Members in the Congress who will put aside the partisanship that comes when our elections are bitter, and when new elections loom, and restore some of that element of bipartisanship and cooperation which has marked our best times in American foreign policy in recent decades. We really don't have very much of an option, because America will be a player on the stage. There is no likelihood, in Joe Nye's three-dimension chess, that the most powerful military force, still one of the greatest economic powers, and in many respects the country that must provide some acquiescence, if not leadership, to international cooperation, can be irrelevant. I hope the darker view that Karen presents of the President's intentions and character are disproved in coming days. My own strong conviction is that America can have a period of important continued international leadership, in cooperation with its allies and friends. This is required by the circumstances of extremely sensitive, unusual and important times.

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