VATT-KESKUSTELUALOITTEITA
VATT-DISCUSSION PAPERS

111

INDIVIDUAL TRADE POLICIES IN EU – THE CASE OF CAR MARKETS

Paola Drei

Valtion taloudellinen tutkimuskeskus
Government Institute for Economic Research
Helsinki 1995

Acknowledgements: This paper was written under the kind and careful supervision of Pekka Sinko and Pekka Mäkelä as part of an AIESEC-traineeship program in the Government Institute of Economic Research. I would like to thank Tuula Kulovesi of the Ministry of Trade and Industry for her valuable comments and for her interest in my report. I would also like to thank all the Staff of VATT for their friendship and encouragement during my stay in Finland.

ISBN 951-561-156-3
ISSN 0788-5016

Valtion taloudellinen tutkimuskeskus
Government Institute for Economic Research
Hämeentie 3, 00530 Helsinki, Finland

Painatuskeskus Pikapaino Opastinsilta

Helsinki, November 1995

Paola Drei: Individual Trade Policies in EU - The Case of Car Markets. Helsinki, VATT, Valtion taloudellinen tutkimuskeskus, Government Institute for Economic Research, 1995. (C, ISSN 0788-5016, No 111) ISBN 951-561-156-3.

ABSTRACT: This paper examines the possibilities of EU member countries to pursue individual trade policies after implementation of the single market. Having reviewed the relevant changes in the institutional framework formed by GATT and EU legistlation, we examine the car market as a special case. We find that the single market makes the national quotas ineffective and necessiates their replacement by union level protective measures. However, analysis of the negotiation process suggests that both national and producer interests have significant influence in the formation of the common EU trade policy.

KEYWORDS: EU trade policy, VERs, Japanese cars.

Paola Drei: Individual Trade Policies in EU - The Case of Car Markets. Helsinki, VATT, Valtion taloudellinen tutkimuskeskus, Government Institute for Economic Research, 1995. (C, ISSN 0788-5016, No 111) ISBN 951-561-156-3.

TIIVISTELMÄ: Keskustelualoite kartoittaa EU:n jäsenmaiden mahdollisuuksia yksilöllisen kauppapolitiikan harjoittamiseen sisämarkkinaohjelman voimaantulon jälkeen. Tutkimuksessa luodaan katsaus GATTin ja unionin säännöksissä tapahtuneisiin keskeisiin muutoksiin ja selvitetään EU:n kauppapolitiikan muotoutumista käyttämällä autokauppaa esimerkkitapauksena. Sisämarkkinat vievät pohjan autojen kansallisilta tuontikiintiöiltä ja edellyttävät unionin tason kauppapoliittisia toimia. Neuvotteluprosessin tarkempi analyysi osoittaa kuitenkin, että kansalliset ja teollisuuden erityisintressit vaikuttavat voimakkaasti EU:n yhteisen kauppapolitiikan muotoutumiseen.

ASIASANAT: EU:n kauppapolitiikka, vapaaehtoiset vientikiintiöt, japanilaiset autot.

CONTENTS

1 INTRODUCTION

We have just entered a new era of international cooperation among EU countries. January 1993 was the deadline set by the European Community's 1985 White Paper for completing the single market; in January 1994, the second stage of the process leading to a problematic but still realistic monetary union, has started.

With the implementation of the single market, the relationship among EU member countries has grown stronger and, in almost every economic sector, a common European approach is replacing the former individual national policies. This new internal development in the EC (the world's largest trading entity) cannot be separated from its effects on the international environment. In particular, a question spontaneously arises: with the deepening of the European integration, is there any possibility of a member country to pursue individually tailored trade policies within the union?

Since the most relevant changes that have occurred so far, after the implementation of the single market, concern mainly the industrial product market, I chose to concentrate on the trade of industrial commodities and not to consider services and agricultural trade.

In addition, only trade policies towards non member countries will be considered. In fact, only toward these countries the EC legislation allows member countries to put up trade barriers to protect their domestic industries. Inside the EC, instead, no discrimination is allowed, even if some intra-Community trade barriers, especially technical, are still tolerated. As we will see, one of the first aims of the single market is to eliminate these remaining barriers in the very near future.

In order to find out what the possibilities are for an EU member country to pursue its own individual trade policy in the industrial commodities market, the motorvehicles market, as a particular case, will be examined. This market is traditionally considered of strategic importance for many EU countries and it was found to be a perfect example of the reticence of member countries to open up their markets and to eliminate national trade barriers towards non member countries.

This paper is divided into two parts. The first part describes the institutional framework in which a member country must operate. Since this framework has deeply changed after the Uruguay Round and the implementation of the single market, it is important to underline the differences between the old regulations and the new. In some cases it was hard to determine this difference for two reasons. One reason is that new rules are not yet applied to all economic sectors. Another reason is that some rules are still waiting to become part of the national legislation.

The second part is a case study on automobile industry. The recent changes, which have occurred in the individual trade policies of some member countries in the motorvehicles market, will be analyzed. In particular, all the details about the new agreement between the European and the Japanese car makers are given. The aim is to see how national trade policies have changed, in the automobile sector, since the implementation of the single market and to point out if there is still a possibility to member countries to protect their domestic car market from outside competition. Finally, the appendix provides a classification of the most common trade policy instruments.

2 INSTITUTIONAL FRAMEWORK

2.1 GATT

GATT was established in 1948 in an attempt to avoid the adoption of trade restrictions which had characterized much of trade in the 1930s. Although the General Agreement is a long and complicated document, it is based on few main principles and aims.

The first principle, contained in the most-favoured-nation clause in Article I of GATT, is that trade must be conducted on the basis of non-discrimination. All contracting parties pledged to grant treatment to each other that is as favorable as the treatment they give to any country in the application and administration of import and export duties. Thus, no country can give special trading advantages to another or discriminate against it: all countries are on an equal basis, and they have the same rights in sharing the benefits of lower trade barriers, for instance. A second main principle of GATT, states that, once imported goods have entered a market, they must be treated like domestically produced goods. A third major principle is that, where protectionism is given to domestic industry, it should be extended using custom tariffs, and not through other commercial policy measures such as quantitative restrictions.

2.1.1 Exemptions to GATT rules

The main exception to the general GATT rule against quantitative restrictions allows their use in balance of payment difficulties (Articles XII and XVII). Even then, restrictions must not be applied beyond the extent necessary to protect the balance of payments and must be progressively reduced and eliminated as soon as they are no longer required.

GATT recognizes a dispensation to its main principles. This is the case, for instance, of governments that feel they have no choice but to offer domestic industries temporary protection from imports. The "safeguards" rule of GATT (Article XIX) sets out carefully defined circumstances under which a member country can impose import restrictions or suspend tariff concessions on products that are being imported in such increased quantities and under such conditions that they cause or are likely to cause serious injury to competing domestic producers.

In recent years, some governments have used discriminatory bilateral arrangements- voluntary export restraints- carried out with the intention of avoiding the disciplines of Article XIX. Voluntary restrictions, in fact, are not considered like safeguard measures of the import country and can go more unobserved to the GATT rules. As a consequence, the question of safeguards was an important part of the last International Rounds. It is easily understandable that transparency is a particular serious problem in the case of the safeguards measures. Some progress in identifying such measures is evident in recent years, however, as a result of GATT's Trade Policy Review Mechanism (TPRM). On the basis of the TPRM reports that had been completed by early 1993, a total of 75 bilateral or unilateral restraints were identified covering travel goods, electrical equipment and appliances, footwear, television, machine tools, and other products.

2.1.2 Uruguay Round: a new agreement on non-tariff barriers[1]

Although the original GATT covered a wide range of trade-related domestic policies, governments were left considerable discretion in the administration of such policies. To avoid an inappropriate implementation of these policies, governments found it necessary to clarify their administration and to extend the rules to trade measures not originally or inadequately covered by GATT 1947.

The Uruguay Round, in particular, provides for the termination of measures taken pursuant to Article XIX of the General Agreement not later than eight years after the date on which they were first applied or five year after the date of entry into force of the Agreement establishing the WTO. The agreements reached in the Uruguay Round concern sanitary and phytosanitary measures, technical barriers to trade, anti-dumping, customs valuation, preshipment inspection, rules of origin, import licensing procedures, subsidies and countervailing measures and safeguards. As a result, a WTO Member applying a non-tariff measure is required to follow precise guidelines to make the system transparent and predictable, as well as provide procedural guarantees for exporters. The Uruguay Round agreements on non tariff measures will apply to all WTO members. They will have a multilateral status, ensuring a global coverage of the rules. The administration of countervailing/ antidumping measures has been clarified by:

- greater and more detailed disciplines on the conduct of investigations
- establishing the criteria to terminate an investigation
- providing interested trade partners with full notice and a right to present evidence
- clarifying the criteria used to determine injury to the domestic industry
- requiring more detailed public notice and explanation of determinations
- establishing that a "sunset" clause of five years applies to measures, unless a determination is made that, in the event of the termination of the measures, subsidisation/dumping and injury would be likely to continue or recur.

2.2 New protectionism

The GATT Agreement defines the most-favoured-nation clause and introduces the principle of non discrimination as one of the cornerstones of the present international trading system (Article I). Despite this statement, many nations have applied discriminatively non-tariff trade barriers against the exports of specific countries,

[1] For a complete overview see *The results of the Uruguay Round of Multilateral trade Negotiations, published by GATT*, December 1994.

pushing international trade more and more away from multilateralism and free trade, toward bilateralism and more restricted trade. There is no wander that observers of international trade are doubtful about a fast shift to free trade. This new subtle form of non-tariff interventions on trade is generally called "new protectionism". Its common traits are:

- recourse to quantitative measures;
- selectivity;
- bilateralness;
- invisibility.

The proliferation of dumping and countervailing duty actions, the impositions of quotas and the use of even less transparent procedures such as government procurement policies, local content requirements, complex tariff valuation processes have all been examples of the stresses that have been placed on the liberal trade regime.

These problems and negotiations to resolve them have centred on the United States, Japan and the nations of the European Union, since they together represent the major markets in the global economic system. They have all, at one time or another, restricted imports in different degrees. As long as the importing country is, at least pro forma, willing to act within the framework of GATT, such stronger measures may be taken either:

a) by referring to the escape clause of Article XIX, or

b) by applying Article VI which allows retaliatory measures against "unfair" trading practices (antidumping, countervailing duties).

The EU member moreover must refer to the common external trade policy and respect the Community decisions when there has been an agreement for a common approach towards non member countries.

2.3 EU External trade policy

The commitment of the EU to free multilateral trade is shown by the membership of all its member states of GATT. One of the main principle of GATT is that there should be no trade discrimination against member of the organization. This implies that the most efficient producer should supply the market regardless of the country of origin of the good or service. Regardless of this principle the EU operates on the basis of discriminating against non member countries by the operation of the CET (Common external tariff). GATT has therefore had to develop rules to take account of trading blocs such as the EU. Thus, regional trading blocs such as the EU are not illegal under GATT rules, but they are against the spirit of GATT principles.

Since 1962 the Council of Ministers gave the Commission power to put up a common external trade policy. Relations between GATT and the member states of the Union are therefore mainly the responsibility of the Commission which in turn is checked by the Council of Ministers. Negotiations on the various trade rounds of GATT are conducted by the Commission on behalf of the Union.

The EU has also many trade agreements with non-members (the EEA agreement, for instance, with the other European countries). There are also Associate Membership agreements and preferential trade agreements with the Less Developed Countries (LDC) such as the General System of Preferences (GSP) and those with African, Caribbean and Pacific countries (ACP agreement, carried out by the Lom convention). The Commission also participate to the Multi Fibre Arrangement (MFA) which regulates trade in clothing and textiles between the developed and developing countries.

2.3.1 The Common Commercial Policy

The Common Commercial Policy (CCP) of the EU was first established by the Treaty of Rome in 1957. The aim of achieving a common external tariff and the wider ambition of closer economic and political integration brought the EEC to have a Common Commercial Policy toward the rest of the world. In short, the Treaty of Rome envisaged common rules for the conduct of trade by the EEC and a common negotiating position vis--vis third countries and international organizations such as GATT. The key provisions of the CCP are contained in Articles 110-116 inclusive. Article 110 contains the following statement:

By establishing a custom union between themselves, member states aim to contribute, in the common interest, to the harmonious development of world trade, the progressive abolition of restrictions on international trade and the lowering of customs barriers.

The really key article, the cornerstone of the CCP, is Article 113. It sets out the important rule that:

The CCP shall be based on uniform principles, particularly in regard to changes in tariff rates, the conclusion of tariff and trade agreements, the achievement of uniformity in measures towards the liberalization of export policy and in measures to protect trade such as those to be taken in the case of dumping or subsidies.

The principal ingredients of the Common Commercial Policy have been a Common Customs Tariff (CCT), whose level has been negotiable with other members of GATT and a Common classification of goods for customs purposes (customs nomenclature). This classification consists of common rules for customs valuation, rules for suspending or reducing customs duties, rules of origin, and rules whose purpose, as defined in Article 113 of the Treaty, is to ensure that uniform principles should be applied, essentially in the same manner, in all EEC member states in their trade relations with non member states. The Article in question lists some of the issues where such uniform principles or rules should apply. They include tariff amendments, existing import quotas, protective commercial measures (including antidumping cases and those involving subsidies), export policy, and the negotiation of international tariff or trade agreements. Without the elements of CCP mentioned above even the narrowest commercial and economic aims of EEC would be difficult to achieve.

Given the EEC's preponderant share in world trade, the EEC institutions have had to assume a major role in shaping the international trading order. The CCT was set in 1957 "at the level of the arithmetic average of the duties in the four customs territories covered by the Community". Agreements on reductions in the CCT have been reached during successive rounds of the GATT's negotiations. Among these, the Tokyo Round, phased during the 1980's, reduced the CCT nominal level to about 6 percent while the Uruguay Round brought its level to 3.8 percent.

It would not be correct to assume that a single rate of duty applies to each product imported under the CCT. Depending on the country in which the good originates, alternative rates may be applied, or duties may be suspended or reduced. Thus, for many products the EC has got two sets of duties: *autonomous duties*, which arise from the averaging of the initial customs duties; and *conventional duties*, which have been negotiated and bound under GATT. In trade with GATT members or other trading partners receiving MFN treatment, conventional duties are applied unless the autonomous rates are lower.

2.3.2 Individual trade policy within European Union

A common approach

Article 113 of the Treaty of Rome requires, as noted earlier, that the CCP should be administrated according to "uniform principles", implying that the rules governing trade with non-member countries should be essentially the same in each member state.

With regard to tariff amendments, once the CCT was in full operation (January 1968), the right of member countries to adjust their tariff rates automatically became restricted. In fact, since than, tariff changes can only be made through the Council and with the agreement of all members. Changes in rates are negotiated internationally by the Commission, mainly through GATT, where it speaks on behalf of the Community as a whole.

Antidumping measures are taken at a Community level as well. Since 1968, when administration of antidumping legislation passed from individual member states to the Commission (supervised by a consultative committee of representatives of member governments), there has been a steady increase in the complexity of the applicable rules and procedures. In broad terms, EU antidumping rules follow the provisions of Article VI of GATT. Following GATT principles, the EU imposes antidumping duties only in cases where EU industries have been injured by the import of "dumped" products. Products are defined as been dumped if they are sold at a lower price in the export market (the "export" price) than in the home market (the "normal" value).

Independent trade policies

Before the implementation of the Single Market a common approach on non-tariff barriers had proved to be hard to achieve, since member states had been very reluctant to renounce to this instrument of protection. The main instrument individually applied by EU members were quotas and VERs.

National protectionist trade policies were allowed by the EU dispositions of Article 115 of the Treaty of Rome. This Article set out the conditions to fulfil in order to raise national trade barriers against a non member country and in order to prevent imports from outside the Community, entering via other EC countries. In fact, national import quotas (or VERs) would be ineffective in the absence of any mechanism preventing indirect imports in other member countries. For this purpose, the country imposing the quota had first to ask for permission from the Commission to require "free circulation" licenses for a particular product. If the Commission granted the request, a trader's application for a license could be refused only with its permission. In each case, the member country had to prove economic justification in support of its application. A part of the test of Article 115 is here quoted:

"In order to ensure that the execution of measures of commercial policy, taken in accordance with this Treaty by any Member State, is not obstructed by deflection of trade, or where differences between such measures lead to economic difficulties in one or more of the Member states, the Commission shall recommend the methods for the requisite co-operation between Member States. Failing this, the Commission shall authorize Member States to take the necessary protective measures, the conditions and details of which it shall determine" (...)

This Article had been enlaced by the governments of member countries to protect national products such as cars, consumer electronics and textile. Between 122 and 222 measures have been granted annually in the 80s. Thus, Article 115 applications were an indicator for domestic quotas and VERs protection towards non member countries and captured major national protectionist activities within EC. The legal provisions of Article 115 remain nowadays in force. However, the Single European Act provides no scope, as from January 1993, for any internal trade measures against imports from external sources. The number of new Article 115 restrictions authorized has fallen from 119, in 1190, to 48, in 1991, and 8 in 1992.

The Single European Act

The Single European Act of 1986 provided the legal and institutional framework for deepening the EC integration process, establishing "an area without internal frontiers in which the free movement of goods, persons, services and capital, is ensured". Under the Act, the scope of qualified majority voting by member states in the Council was extended from agricultural and commercial policy to virtually all the issues relating to the Internal Market. This enabled progress to be made on deregulation and harmonizing national trade policies.

In order to build up the Internal Market, member countries pledged to abolish all intra-Community trade barriers by the end of 1992. While the Communities' bilateral restraint agreements on textiles and clothing under the MFA remain in force, national import quotas within the system were abolished with effect from 1 January 1993. In certain sensitive areas (such as the banana sector, the fisheries sector, cars, steel), the Commission carried out a plan to replace national quotas with an europewide limit that should disappear in a certain number of years. National import restrictions, are not compatible, in fact, with a concept of an integrated European Market.

National excise taxes on certain tropical products (coffee, tea, cocoa) are not scheduled for harmonization. Five member States maintain coffee taxes with ad valorem incidences of up to 100 per cent in 1991. Italy quadrupled its rates in January 1991, giving rise to protests within the GATT system.

Where common technical regulations exist, any EC or third country products meeting requirements may circulate freely within the single market. In the absence of common rules, goods qualify for free circulation throughout the EC whenever they conform to regulations valid in any of the member States. In areas of health and safety, harmonization of technical rules or the demand of essential common requirements has been preferred to mutual recognition. Implementation into national law of new directives laying down essential requirements has, however, proved difficult, and the establishment of supplementary norms has taken longer than predicted. Technical barriers may thus continue to affect intra-EC trade in certain areas, including machinery, for some time.

3 THE MOTOR VEHICLES MARKET

3.1 The effects of the Single Market

Before the implementation of the single market, the car market was a good example of the limited intra-Community trade. According to Tully (1990), the car market suffered from enormous competitive handicaps, because of limited cross border trade. He states that quotas wouldn't have hurt so much if buyers in high-priced protected nations, such as France, could have bought a car in, say, Belgium, where Japanese competition made all cars cheaper, and could have brought it home.

In theory such cross-border trade was the foundation of the Common Market. But in practise a second barrier kept the markets separate, until January 1993. It was the so-called "block exemption", that is an exemption to EC competition law granted to the car industry in 1985 for ten years. The exemption allowed manufacturers to impose highly restrictive agreements on all their dealers (that's why it was called "block"). Under it Peugeot, Volkswagen or Ford of Europe could prevent their dealers from taking on a second brand. According to car makers, the block exemption helped consumers by requiring that all dealers performed repairs. Consumers could benefit from that, but they also wanted lower prices.

To gain the block exemption, the various car industries pledged to hold prices for the same cars selling anywhere in Europe within a band of 12 per cent. According to a 1989 survey by the European Consumers' Organization (a Brussels-based research and lobbying group), automakers used blatantly to violate those terms. It was found, in fact, that prices for identical models often varied by 60 per cent across Europe before taxes. On average, cars in Denmark used to be 45 per cent cheaper than in Spain or Italy. A compact Citroën AX costed $1.500 (or 19%) more in France than in the neighboring Belgium.

Given the big price difference, it could have been simple to look for the lowest pre-tax price, then to pay the value added tax at home, before registering the car. But the block exemption did not allow that. It prohibited dealers in one country from advertising in another. It also restricted companies from buying, for instance, 1.000 cars at a time in Denmark and reselling them in France. Another example: in Denmark, manufacturers demanded that their Danish dealers gave first priority to local customers, and arranged deliveries so that the dealers had few cars left for foreign buyers.

Approval of the EC's Single European Act (SEA), in 1986, brought new challenges to Member States determined to continue protecting their domestic automobile companies from Japanese competition. Under the terms of the Act, all Member states were obliged to remove restrictions on the movement of goods within the Community by the end of 1992. This concerned also the "block exemption". Since numerous EC governments did not impose quotas on auto imports from Japan, this obligation would enable Japanese firms to export vehicles to the protected EC countries, via non-restricted Community markets. In addition, of course, completion of the Internal

Market raised the prospect that Japanese transplant factories would produce cars in one EC country (United Kingdom, for example), and then freely ship them to other EC countries (France and Italy, for instance). Thus, national measures affecting trade with nonmember countries were not efficient anymore and had to be abolished. In certain sensitive areas (such as the banana sector, the fisheries sector, cars, steel), as noted before, they were substituted by Community measures.

3.2 A new agreement

Some EC countries have for many years curbed imports of Japanese motor vehicles by pressuring Japan to adopt voluntary export restraints. The representatives of the car industry had been demanding, during the years preceding the implementation of the Single Market, that existing bilateral national quantitative restrictions had to be substituted by some Community measures "equally restrictive". The EC and Japan agreed on July 31, 1991 to replace the different national restrictions by a restriction on overall sales of Japanese cars, off-road vehicles, light commercial vehicles and light trucks in the EC between 1993 and 1999. According to the compromise reached in 1991 (a "voluntary trade restriction"), annual ceilings are imposed on imports of Japanese cars. Within this quota, the European Union and Japan set out annual national ceilings for markets which were considerably protected before 1991.

Although the Community has reached an understanding with Japanese producers that imports will be completely liberalized after a transition period ending in 1999, according to Gros (1992) "it is likely that Japanese car imports will *de facto* remain limited to their present level if the Community industry faces difficulties by that date".

The Japanese share of the EU market is allowed to increase from 11 per cent in 1991 to 16 per cent in 1999. The agreement is "voluntary" for a reason: it would be strictly illegal, both under the open-border policy of 1992 and GATT rules, if the EU imposed an import quota on Japanese cars. While, if a country "spontaneously" renounce to export a greater amount of cars, the *pro forma* of respecting the international laws is safe.

3.2.1 The context of the agreement

The European Automobile Industry

Six firms or group of firms accounted for the great majority of western European car production in 1990. These firms, in descending order of output, were: the Volkswagen Group (Audi, Seat and VW); PSA (Peugeot, Citroën); the Fiat Group (Fiat, Lancia, Alfa, Innocenti and Ferrari); the General Motors Group (GM/Opel,Saab); the Ford Group (Ford, Jaguar); and Renault. The size of these and other car-makers in western Europe varied considerably, and included not only European-owned producers but also subsidiaries of American companies and, more recently, the local operations of Japanese car firms as well.

Growing concerns over their international competitiveness encouraged many European car-makers in the late 1980s to press for arrangements to secure public protection from greater Japanese competition through the 1990s. The most determined to call for protection were, of course, those firms whose competitive positions were weakest and who therefore felt most vulnerable to the challenge from Japan. More than any other figure, Peugeot Chairman Jacques Calvet openly and vigorously required such protection. Calvet called for strict limits on Japanese auto firms' participation in the European Community after the projected completion of the internal market at the end of 1992. Joining Calvet in calling for substantial protection were, among others, Fiat Chairman Gianni Agnelli and Renault CEO Raymond Levy.

Not all car-makers in Europe during the late 1980s required protection from Japanese competition, however. Perhaps more notably, the German luxury car specialists Mercedes, BMW and Porsche believed that they could effectively compete against Japanese makers even in a unified EC market, and worried about the implications of protectionist moves in Europe for their own vehicles sales in Japan, and especially America. In addition, they were joined by fellow German producer VW. Carl Hahn, VW's Chairman, understood that Japanese producers represented a major challenge to VW, but opposed restrictions part because he believed that the rigours of the open market ultimately would strengthen VW and the rest of European auto industry. The British Rover Group had previously entered into a strategic alliance with Honda, and later sold 20 per cent of its equity to that Japanese producer. With this relationship in place, Rover refused to join those pressing for protection.

Japanese conquest of the EU market

Japanese automobile exports to Europe remained insignificant until the end of the 1960s. During the 1970s, however, Japan's exports and market shares rose considerably in many of the markets of the Community. Indeed, by 1980 Japanese auto firms had gained enormous shares in EC markets such as Belgium (24.7%), the Netherlands (24.6%), Denmark (30.9%), Ireland (30.8%) and Greece (42.9%).

Rising Japanese exports to Europe encouraged many governments to have policies designed to limit the numbers of imported Japanese cars. In 1975, for example, Britain obliged Japan to limit its auto imports to 11 per cent of the UK automobile market. Two years later, the French government decided to put a ceiling on Japanese car imports of just 3 per cent. Spain and Portugal later restricted Japanese market share to 1 per cent and 14 per cent, respectively. Italy had implemented measures to limit Japanese imports since 1954. According to this bilateral agreements, Japan could have a small share of Italy's automobile market (less than 2 per cent). These five nations - together with West Germany, which in 1981 made an informal agreement to limit Japanese auto imports to no more than approximately 15 per cent of the local market - would continue to impose quantitative restrictions throughout the 1980s.

By the end of the 1980s Japanese firms had slightly increased their market share. In the period from 1980 to 1989 Germany passed from 10.4 per cent to 15.2 per cent, Italy from 0.14 per cent to 1.41 per cent. The market share slightly declined instead in UK (from 11.9 per cent to 11.3 per cent) and France (from 2.9 per cent to 2.8 per cent). Indeed, in 1989 Japan held roughly one tenth of the overall EC market, supplied almost entirely by exports which numbered some 1.23 million vehicles.[2]

The post-war development of Japan's motor vehicles exports to the Community encouraged Japanese foreign direct investment (FDI) in the EC first to support and, later, to boost this trade. Japanese car-makers began to invest directly in regional sales and distribution offices from the 1960s. From the early 1970s they began to establish their own motor vehicle assembly operations in Europe. The threat of increased protectionism and other factors motivated Japanese car-makers to expand their direct investment into local manufacturing in the Community starting in the 1980s.

Although some EC Member States remained wary of the prospects of major Japanese auto plants within their country, the advent of the Thatcher government led the British authorities to encourage Japanese FDI in the United Kingdom through a variety of state incentives beginning in the early 1980s. Nissan was the first Japanese firm to profit of Britain's overtures when, in 1984, Japan's second larger car-maker concluded an agreement with the British Government to establish a production facility in England. Honda followed Nissan's decision and started its own project to set up a British plant (with Rover) in 1985, followed by an Isuzu initiative (with GM) and a Toyota direct investment in the UK in 1987 and 1989, respectively[3]. This British FDI policy would carry important implications for Community negotiations with the Japanese in the early 1990s.

3.2.2 The different phases of the accord

The Japanese automobile challenge to the unifying European Community led to long, complex and often bitter negotiations involving numerous players from EC and Japan. The MITI (Japanese Ministry of International Trade and Industry) officials represented the Japanese side in bilateral talks. Bilateral negotiations on the European side were led by the Commission's Directorate General for External Relations (DGI), the Internal Market and Industry (DGIII) and, to a lesser extent, the Competition Directorates General (DGIV). Moreover, each government sent representatives to the Council of Ministers, the Community body which held formal power over the actions of the Commission. The process which ended in the EC-Japan auto accord took more than three years to complete.

---

[2] These dates refer to "Financial Times" 26 September 1991.

[3] Nissan, also directly invested in Spain and Toyota in Germany (with VW) during the 1980s, but well before the end of the decade it had become clear that Japan's major car-makers had chosen the UK as the principal country of their manufacturing activities.

The first phase

The initiative to revise Community policy towards Japanese automobiles came from the Commission when they realized that the internal market would require major changes in the car market policies of numerous Member States.

Despite the central role of the Commission in initiating this first stage of the process, however, the critical direct and indirect roles of member states soon become apparent. The positions of these states initially divided into four principal groups. Least influential in this process were the six states without significant domestic auto industries: Belgium, Denmark, Greece, Ireland, Luxembourg and the Netherlands. These states would gain little, if anything, by limiting Japanese cars in the EC after 1992, but chose to remain largely silent throughout the long process. According to M. Mason (1994), probably hoping to profit afterwards of the help accorded to their EU partners.

The UK held a second position. It did no longer represent the interest of a domestic auto industry and decided to host the local subsidiaries of the American firms Ford and General Motors and also the newly arrived and growing Japanese plants of Nissan, Toyota, and Honda. In their talks with the Commission, UK representatives favored complete freedom for Japanese transplants to produce and ship their goods throughout the Community while they asked for some kind of restriction over auto imports coming from Japan. The so-called "Latin 4" of France, Italy, Spain and Portugal were home to very important car makers which felt strongly threatened by Japanese competition. The German government represented a fourth position during the first stage of the process. Even if they were conscious of the possible future leading role of Japan car industry, they opposed controls on Japanese cars, relaying on their own capacity to face the Japanese challenge.

During the first phases Fiat, Renault and especially Peugeot were hard to convince to find a suitable accord with Japan. Later on, they were also joined by the representative of VW. In fact, even the German had started to consider Japanese competition too dangerous after the spread of the new Japanese luxury line such as the Acura (Honda), the Infinity (Nissan), and the Lexus (Toyota).

On October 1990, the heads of the four cars producers Agnelli (Fiat), Calvet (Peugeot), Levy (Renault), and Hahn (VW) met to find a common position which they intended to communicate to the Commission. Agnelli, Levy and Hahn called for a transition period of ten years before Japanese auto exports could gain unrestrained access to the Community, together with limits on Japanese transplant production during this period. But Calvet's request to find tougher measures made the meeting broke up.

The second phase

Unsuccessful in their effort to build up a common position in this October meeting, Fiat, Renault and VW chiefs chose to keep holding a common position in the future meeting. They created, in February 1991, a new organization (l'Association des Constructeurs Europens d'Automobiles) and decided to make decisions by majority rather than by unanimous vote as it happened in the previous Association. Calvet, realizing that, alone, he could no longer block the decisions of the other industry members, decided not to join this new association.

This new Association easily managed to agree on a common position towards the Japanese. They asked for a transition period longer than last time, for clear limits on Japanese transplant production; they also called for a division of market growth between Japanese and European producers, a decrease in Japanese volume if the market contracted, and a Japanese market share of about 15 per cent by the end of the transition period.

At a national level, the "Latin 4" constituted a 'blocking coalition' to prevent any accord which they considered too soft towards Japan. Specifically, these member States, largely following the interests of their domestic auto firms, demanded a minimum seven-year transition period from January 1993, changes in the agreed import level if the market fell and they strongly pressed to include Japanese transplant production in any final accord.

In Germany, where concerns about Japanese competition were growing, the government spoke in favor of most of the demands set forth by the common Latin front but, apparently, refused to put specific limit on the Japanese transplants. The British government, for its part, publicly stated its opposition to any control over Japanese transplants in the Community, but it also expressed its willingness to support restrictions on Japanese auto imports. The Japanese, on their hand, firmly reacted against any clause that aimed to limit the number of cars which could be produced by the Japanese transplants.

A compromise was found when the Cabinet of the EC Commission President Jaques Delors suggested to find a link between levels of transplant production and Japanese imports in the Community. That is, to find out a way to include in the restrictions towards Japanese cars, the cars produced in Europe. In exchange, the Commission agreed to drop a number of other outstanding issues. For instance, the possibility of an access to the Japanese market which was a measure sometimes advocated by EC Members. To persuade the French to go along, the Commission promised future financial assistance for the restructuring of France's auto industry.

3.2.3 The results of the agreement

The "Elements of Consensus"

The agreement consisted of a bilateral document, the so called "Elements of Consensus", which set forth a series of goals and measures concerning Japanese motor vehicles in the EC to the end of the decade. The Commission and the Japanese government found three common goals: first the "progressive" and ultimately, "full liberalization" of the EC motor vehicles; second "avoidance" of EC market "disruption" by Japanese vehicle exports, and third, a Japanese "contribution" to enable EC manufacturers to attain "adequate levels" of "international competitiveness" by the granting of a "transitional period" during which Community markets would remain regulated. To achieve these goals, the two parts involved had to set out the Japanese participation in the EC vehicles market. First, the Commission pledged to ease relevant national restrictions and measures taken under Article 115 of the Treaty of Rome, and would abolish these restrictions and these measures no later than 1 January 1993. Second, the two sides agreed that Japan should have imposed a ceiling to its exports to the EC as a whole and to each restricted EC market till December 1999. Specific export levels were provisionally set out for the 1999 calendar year. These levels, however, were based on market forecasts, and both sides agreed that changes in market conditions would bring revisions in Japanese export limits. Third, the document addressed the issue of the Japanese transplants in the Community. In one part of the document, the Commission claimed that the EC would impose neither "restrictions on Japanese investment" nor controls on "the free circulation of its products in the Community". At the same time, however, the Japanese promised to take into account that concentrated sales of motorvehicles in specific national markets would create "market disruption" and frustrate the EC efforts to attain international levels of competitiveness.

The conclusive declarations

Finally, and very significantly, together with the Elements of Consensus the document contains the conclusive declarations of the EC Vice President, Frans Andriessen, and those of the MITI Vice Minister, Eiiche Nakao. Andressen stated that the Commission adopted the "working assumption" that Japanese European transplants would produce, for sale in the Community, roughly 1.2 million motorvehicles by the end of the transition period. Nakao, on his hand, did not deny this assumption directly, but reminded Andriessen that the Commission had promised not to restrict Japanese investment and European transplants production in any way.

The Commission's working assumption on total transplants sales in the Community, together with estimates of total Japanese exports contained in the Elements, suggested that Japan would capture roughly 16.1 per cent of the total EC automobile market by 1999.

The different interpretations of the agreement

Conclusion of this historic accord did not put an end to disputes over the Japanese penetration of the EU market. On the contrary, conflicting interpretations of the accord provoked disagreements between the contracting parties. On one side stand some of the Latin hard-liners, who insist that the accord contains strict upper limit of 1.2 million vehicles produced at Japanese transplants through the 1990's. Not surprisingly, Peugeot's Calvet is the strongest supporter of this view.

Opposed to this viewpoint are the British and Japanese Governments. They claim that the agreement in no way restricts either the operation of Japanese motor vehicles factories in the Community nor the movements of products within the EU made at these plants.

Although these two points of view stand in contradiction, according to Mason (1994) "the text of the accord together with commentary by those who drafted it, does indeed place implicit (though somewhat vague and ambiguous) limit on the Japanese transplants". First, because the text includes language warning Japanese car-makers from concentrating their European transplants sales to the five restricted market during the life of the agreement. Second, the declaration of Frans Andriessen about the 1.2 million units sold by the end of 1999, suggests the possibility of an informal agreement limiting Japanese firms to that level during the life of the accord. And third, some Commission representatives made clear that, in interpreting the accord, the Community could compensate for the Japanese transplant production above negotiated levels, by reducing Japanese auto imports into the Community.

The target ceilings for 1995

The European Union allowed 1.105 million cars to be imported directly into EU from Japan in 1995, under the terms of an agreement reached between the European Commission and the MITI on march 31, 1995, when the expected total demand for cars was 13.276 million. But a "reassessment meeting" was planned for the autumn to correct, if necessary, the forecasts. The market has in fact developed much less rapidly then expected and estimates of total demand had to be downwardly revised. In this context, the Commission and MITI negotiators reached the following agreement:

1) total demand for 1995 should be 12.946 million vehicles, only 1.7 per cent more than 1994
2) the volume of Japanese direct exports to the fifteen countries of the EU is to be limited for 1995 to 1.071 million vehicles
3) the quotas for the five limited markets are: France 88.700 vehicles with 1 per cent predicted growth of the market; Italy 55.300 vehicles with a market growth assessed at 2.2 per cent; Spain 40.400 vehicles with a 2 per cent predicted contraction of the market; Portugal 32.800 vehicles with 13 per cent expected contraction; the UK 182.700 cars with a 3 per cent expected growth of the market.

This agreement must also apply to the new EU members: Austria, Sweden and Finland. On this regard, the Japanese Automobile Manufacturers Association (JAMA) expressed regret that "these three nations whose market were until now free, are to be included". The European Commission has revealed that this year's target ceiling for the new member countries has been set at 112.000 vehicles. Table 4.1 shows the Japanese car market share in 1989 and 1995 together with the forecasts for the market share in 1999. The last column includes transplant production.

	Japanese market share through imports 1989	Market share ceilings on Japanese exports 1995	Anticipated Japanese market share through imports 1999	Total anticipated Japanese market share 1999
France	2.8 %	3.9 %	5.3 %	7.0-11.0 %
Italy	1.41 %	3.1 %	5.3 %	7.0-11.0 %
UK	11.3 %	8.5 %	7.0 %	20.9-26.9 %
Spain	-	3.8 %	5.3 %	12.1-16.1 %
Portugal	-	11.6 %	8.4 %	16.5-21.5 %

Table 4.1 Japanese car market share in 1989, 1995 and anticipation for 1999

Source: Internal Commission documents and European Commission

Although limited to 993.000 vehicles (for 12 member states), direct Japanese export did not exceed 818.000 vehicles in 1994. Guy Crauser, the European Commission negotiator representing the EU in the Tokyo talks, has suggested that "this year, Japanese exporters will once more probably encounter problems in reaching the levels of exports that have been authorized". This is the result of the current strength of the Yen, and that Japanese motor manufacturers are not expected to launch any new models before the end of the year.

4 CONCLUSIONS

The implementation of the single market brought about relevant changes in the trade policies of EU member states. The removal of all technical barriers on EU internal trade have made impossible for member states to continue to raise trade barriers in order to protect national industries. The restricted import products would enter their countries via non restricted markets.

Under the pressure of the member states which had mostly profited from the protection allowed by international treaties and agreements, the Commission decided to replace national quotas of certain goods by EU quotas. These quotas should disappear after a transition period but they could also be renewed if the Community faces difficulties by that date.

In this paper, I analyzed more closely the car market. In this market there has been a shift from national negotiations to exclusively EU negotiations and national quotas have been replaced by a Voluntary Export Restraint (VER) to the Community as a whole. This VER have taken a peculiar form. In fact, the agreement on the import of Japanese cars, reached in 1991, looks more like a "gentlemen agreement" rather than a voluntary export restraint and is deliberately vague and ambiguous in its terms. Different interpretations have been given to the question whether transplant production is included in the annual ceilings, and what will happen if EU car makers will not be able to compete with the Japanese without the quotas by the end of the 1990s.

Analysis of the negotiation process and outcome in the car market suggests that individual nations' interests strongly influenced the course of the negotiations. The Commission at times managed to find out a compromise between the different interests by using threats and reward and also by using its privileged position of intermediary. Yet member governments and the chiefs of the major European car industries retained a decisive power over the agreement: only when a common position among the car makers was found, the Commission was able to precede in the talking with Japan and its position reflected the "car industries" point of view.

Even if the national level protectionist measures have become largely ineffective in EU, the car market example shows that strong political pressure over the Commission during the negotiations still provides a way to pursue national trade policies. As national policies have traditionally reflected the views of local industry, it seems that in today's Europe industry pressure groups are to some extent able to directly influence the formation of EU trade policies.

REFERENCES

Calvet J. (1991) *Thank God for quotas*, "European Affairs", 1991 Dec, Vol. 5: 6, p. 68-72.

Cope P. (1988) *The Anxieties of the Motor sector*, "European Trends", 1988, n 4.

Corden W. M. (1992) *International Trade Theory and Policy*, Edward Elgar.

El-Agraa A M. (1990) *The Economics of the European Community*, University Press, Cambridge.

European Report, various issues.

Flam H. (1993) *Ec members fighting about surplus, VERs, FDI and Japanese cars*, "Journal of International Economics", n 36 (1994): 117-131, North-Holland.

GATT (1994) *Guide to GATT: Law and Practice*.

GATT (1994) *The Results of the Uruguay Round of Multilateral negotiations.*

Gros D. (1992) *A Note on EC Trade Policy after 1992: The Effects of Replacing Existing National Import Quotas by Community Quotas that are "Equally Restrictive"*, Weltwirtschaftliches Archiv, Vol. 128, n 1.

Krugman P., Obstfeld M. (1991) *International Economics*, Harper Collins Publishers.

Lehmann JP. (1992) *France Japan, Europe, and industrial competition: the automotive case*, "International Affairs", n 68.

Lutz J. M. (1994) *To Import or to Protect? Indistrialized Countries and Manufactured Products*, "Journal of World Trade", Vol. 28: 4, p. 123-146.

Mason M. (1994) *Elements of Consensus: Europe's Response to the Japanese Automotive Challenge*, "Journal of Common Market Studies", Volume 32, n 4.

McDonald F. and **Dearden S.** (1992) *European Economic Integration*, Longman.

Montagnon P. (1990) *European Competition policy*, Chatam House papers, Pinter Publisher London.

OECD 1993 *Obstacles to Trade and Competition*.

Oxley A. (1990) *The Challenge of Free Trade*, Harvester Wheatsheaf.

Perry K. (1994) *Business and the European Community*, Made Simple Books, Butterworth-Heinemann Ltd.

Preusse H. (1991) *Voluntary Export Restraints-An effective Means Against a Spread of Neo-Protectionism?*, "Journal of World Trade", Vol. 25:2, 5-17.

Salvatore D. (1992) *National Trade Policies*, Greenwood Press.

Schuknecht L. (1990) *The political economy of EC protectionism: National protectionism based on Article 115, Treaty of Rome*, "Public Choice"n 72: 37-50, 1991.

Tsoukalis L. (1993) *The New European Economy*, Oxford University Press.

Tully S. (1990) *Europe Hits the breaks on 1992*, "Fortune", 17 december 1990.

APPENDIX: CLASSIFICATION OF TRADE POLICY INSTRUMENTS

International trade deals with the flow of goods and services that are exchanged from one country to another. International trade is now universally considered as an important stimulus to growth in developed countries and to economic development in developing countries. In order to promote free trade, the most important trading nations in the world have decided to regulate many aspects of trade in manufactured goods by international agreements. Most nations, however, make autonomous decisions about trade in manufactured goods. These policies consist of restrictions in the free flow of international trade.

The most important type of trade restriction has traditionally been the tariff. More recently, however, non-tariff trade barriers have become more important because national governments made use of them very frequently as an instrument to protect national economies. Since we are focusing on the available means to national governments to pursue individual trade policies within the framework of EU, it is important, first of all, to examine the meaning and importance of each type of possible trade restriction. We will follow the classification proposed by Salvatore (1992).

1 Tariffs and subsidies

A tariff is a tax or a duty levied on the traded commodity as it enters a national boundary. An import tariff is a duty on the imported commodity, whereas an export tariff (or export tax) is a duty on the exported commodity. Developing countries use export tariffs to raise revenues because they are easy to collect. On the other hand, industrial countries generally impose tariffs and other trade restrictions to protect their usually labour intensive industries, while they use instead income taxes to raise revenues. Tariff can be ad valorem, specific, or compound. An ad valorem tariff is a tariff that is expressed as a fixed percentage of the value of the traded commodity. A specific tariff is expressed as a fixed sum per physical unit of the traded commodity. Finally, a compound tariff is a combination of an ad valorem and a specific tariff.

An export subsidy is a payment given to a firm or individual that ships a good abroad. Like a tariff, an export subsidy can be either specific (a fixed sum per unit) or ad valorem (a proportion of the value exported).

2 Non-tariff trade barriers

2.1 Quantitative Restrictions

Quotas

A quota is a direct quantitative restriction imposed by a nation on the quantity of a commodity allowed to be imported or exported. Import quotas are used by industrial countries to protect their agriculture, to stimulate the import substitution of manufactured products and for balance-of-payment reasons.

Quotas, as the other types of quantitative restrictions are generally prohibited under GATT rules, except if applied on a non discriminatory basis to overcome temporary balance-of-payments problems (Article XII).

Voluntary Export Restraints (VERs)

A voluntary export restraint is an arrangement under which an importing country induces another nation to reduce its exports of a commodity "voluntarily", under threat of higher general trade restrictions when these exports can damage a domestic industry.

National governments of industrial nations have negotiated VERs to exports of textiles, automobiles, steel, television sets, and other commodities from Japan and many developing nations.

According to a survey of OECD[4], there are three broad types of actions that are named voluntary export restraints. They change according to the degree to which the governments of both exporting and importing countries are involved in the introduction and administration of the agreement:

1) Direct agreements or understandings between governments regarding the volume of exports. If these are formal agreements they are classified as Orderly Marketing Agreements (OMAs). These types of agreement are not truly "voluntary" as they cannot be uniterally eliminated or modified by the government of the exporting country.
2) Government sponsored arrangements among exporting firms that constrain exports below a predetermined ceiling. An arrangement of this kind sponsored by the government of the exporting country is a classical example of a voluntary export restraint agreement.
3) Agreements or arrangements among exporting firms to limit exports undertaken without government involvement. They are made most likely under the pressure of the importing country's government.

---

[4] OECD 1993 *Obstacles to Trade and Competition.*

In the last two decades voluntary export restraints have become an important non-tariff barrier to international trade because they have allowed nations to save at least the appearance of continued support for the principle of free trade.

2.2 Other non-tariff barriers

Export Promotion

A domestic measure undertaken to encourage exports is the so-called export promotion. There are export credit agencies that facilitate and promote national exports through export credits and guarantees of privately financed transactions.

The Arrangement on Guidelines for Officially Supported Export Credits (the Consensus Arrangement) adopted by twenty-two members of OECD in 1978 limits competitive subsidisation of exports by setting minimum allowable interest rates and maximum repayment terms for officially financed and subsidised export credit.

Safeguard Codes and Escape Clauses

These codes and clauses are included in the Article XIX of GATT that provides temporary import relief or "safeguards" for domestic producers injured by import competition.

The measures undertaken in application of this Article consist mainly of ad valorem duties, quotas, minimum import price, suspension of imports and increased tariffs.

Technical, Administrative, and Other Regulations

These restrictions include safety regulations for automobiles and electrical equipment, health regulations for the hygienic production and packing of imported food products, and labelling requirement showing origin and contents.

Although many of these regulations have legitimate purposes, some are thinly used to restrict imports. They can become, therefore, one of the most subtle form of internal pressure to purchase domestic goods rather than imports.

3 Counter measures

The aim of counter measures was to protect a country from the unfair trade policies of an external country. Far from their first purpose, they are often applied as an instrument to raise national barriers to the free flow of goods.

Antidumping Investigations (AD)

The AD investigation is undertaken by an importing country in response to a claim that a foreign firm is selling a commodity at "less than fair value". When it is proved that dumping has occurred and national firms have been materially injured by imports, custom officials can automatically levy an additional import duty equal to the dumping margin of price discrepancy. Antidumping measures are authorised under Article VI. This Article lays down the circumstances in which contracting parties can take antidumping measures as well as the form these measures may take. Article VI was enlarged by antidumping code concluded at the end of the Kennedy Round and revised in 1979 following the Tokyo Round. The Uruguay Round, very recently, set out the new procedures to follow to apply an antidumping duty.

Countervailing Duty (CVD) Investigation

CVD investigation (regulated by the same Article of the AD investigations) is undertaken by an importing country when it is given evidence that a foreign government is subsidising exports to the nation. It generally consists of an additional import duty to offset the subsidy.

Quid pro quo Foreign Investments

These investments refer to foreign investments induced when the importing nation threatens to undertake protectionist legislation. The exporting country will invest in the importing country in order to avoid the protectionist policy held by the importing country.