U.S.-Japan Competition & Trade in the Global Semiconductor Industry

CASE C (1991-1996)

I. FORGING A SECOND AGREEMENT

The first STA was slated to expire on July 31, 1991. The Semiconductor Industry Association (SIA) and the U.S. Government wanted it extended, but the Electronic Industries Association of Japan (EIAJ) wanted it buried. "When the time comes that this agreement expires, our belief is that we will no longer need anything of this nature," said Tsuyoki Kawanishi, the senior executive vice president of the Toshiba Corporation. Hisao Oka of Mitsubishi Electric and the head of the Japanese semiconductor users committee made a similar comment that, "A new agreement isn't necessary . . . except for political reasons." 1[1]

In the United States, free-trade proponents opposed the extension of the agreement. They argued that it represented managed trade. "This whole thing is nothing more than a government-supported cartel. The semiconductor industry has relied on government protection rather than develop international competitive strategies," said Bryan T. Johnson, a policy analyst at the Heritage Foundation.2[2] However, the Computer Systems Policy Project (CSPP) supported the U.S. semiconductor industry's desire to extend the agreement. Robert Palmer, vice president of manufacturing at Digital and a CSPP member said, "Managed trade is the way of the world. No industrial nation can afford to become totally dependent on another for integrated circuits."3[3]

Although the Bush administration opposed managed trade, it, along with Congress, continued to exert pressure on Japan over various trade issues. But in response to this pressure, many Japanese believed that they should stand up to the United States. A book *The Japan That Can Say No,* written by Shintaro Ishihara, an LDP member of the

Diet created a stir both in Japan and in the United States. Various factions, in the United States and Japan began to position themselves with regard to the agreement. With the approaching expiration of STA, it was obvious to all that the expected 20% foreign share in Japan's market could not materialize. Therefore, in spite of opposition, the second agreement was signed in July 1991. At that time, the 20% "expectation" was included in the formal agreement, with the deadline for achieving this target extended from July 1991 to December 1992. The fair market values (FMVs) were discontinued, and all remaining sanctions were eliminated.

After an interagency review of the U.S.-Japan STA, The United States Trade Representative (USTR) announced that Japanese must improve efforts to open its market. In response, the U.S. and Japan semiconductor industries signed an interim agreement on "emergency measures" to provide greater access to Japan's chip market. That same year, VLSI Research announced that the U.S. semiconductor equipment firms had regained lost market share and achieved market share parity with Japan firms. At the same time that these events were occurring, the semiconductor boom began and the industry faced a sustained expansion. In the fourth quarter of 1992, foreign share increased by 5.3 percentage points and hit the 20% target.

In 1993, the combination of greater R&D efforts, new product development, and increased capital expenditures helped U.S. firms grow their share of Japan's market. SIA figures also showed that the United States had surpassed Japan in worldwide market share, thereby reasserting its worldwide leadership. Japan appeared anxious when its share of world output dropped below the U.S. share for the first time since 1985.

The foreign share in Japan's market, however was not maintained and declined throughout most of 1993. EIAJ and SIA leaders held a joint news conference in Tokyo to reaffirm their commitment to expand access in Japan for U.S. and other foreign firms. The U.S. producers accounted for about three-quarters of the larger 20% total foreign share in Japan.

In 1994, a joint press conference was held in Washington D.C. with vice president Al Gore, secretary of commerce Ron Brown, secretary of energy Hazel O'Leary and other high-ranking officials, announcing an expanded public-private partnership to bolster U.S. leadership in semiconductor technology. Meanwhile, U.S. producers sold $43 billion in chips and American semiconductor companies' capital spending reached $9 billion, about 20% of its 1994 revenue. The U.S. semiconductor industry maintained its worldwide market share leadership of 43.3%, which was headed toward $150 billion in 1995.

During the first quarter of 1995, the foreign share of Japan's market declined but in the fourth quarter rebounded to surpass 29%. For the total year of 1994, the market share number exceeded 20% on an annualized basis for the first time, and the U.S. market share in Japan more than doubled from the 1986 level. On the eve of the expiration of the agreement, the governments announced that foreign share was 30.6% (although in December 1996 the government announced that MITI had provided erroneous data, and that actually the first Quarter 1996 figure had fallen by 2.7 percentage points to 26.9%). Meanwhile, with Ryutaro Hashimoto serving as minister of international trade and industry, MITI publicly declared that "the agreement between the governments has ended its historic mission." In contrast, however, Mickey Kantor of the USTR called for the extension of the STA in October 1995.

II. HEADING FOR A THIRD ROUND

Thus, in early 1996 the American and Japanese chip industries and their governments seemed again to be on a collision course. Although the U.S. government indicated that it was willing to drop the numerical access goal feature of the STA, the U.S. government and semiconductor industry had two important objectives to negotiate with Japan: 1) maintenance of consistent and reliable data that would permit analytical discussion of market access, and 2) a continuing framework that would permit resolution of trade and access issues as they arose. Japan had two primary demands. It wished to replace the bilateral agreement with a multilateral process and it wanted no numerical targets or benchmarks. USTR's Kantor continued to stress the need to negotiate a new agreement, and both sides seemed locked into public positions that could only end in painful confrontation once again.

Questions

Why was the extension of the STA so compelling to the U.S. side? What were likely the primary issues for both the U.S. and Japan? What strategies and arguments could they use to reach a new agreement? With the increasing participation of third countries in the worldwide semiconductor market, should the new STA had included other players in the world? Why? How?

Exhibits

C.1 WORLD MARKET SHARE OF U.S., JAPAN AND OTHER 1982-1995

C.2 FOREIGN FIRMS' SHARE OF JAPANESE SEMICONDUCTOR MARKET 1973 - 1995

C.3 WORLD DRAM MARKET 1977 - 1995

C.4 LIST & RANKING OF THE WORLDS LARGEST SEMICONDUCTOR FIRMS 1995

Exhibit C.1

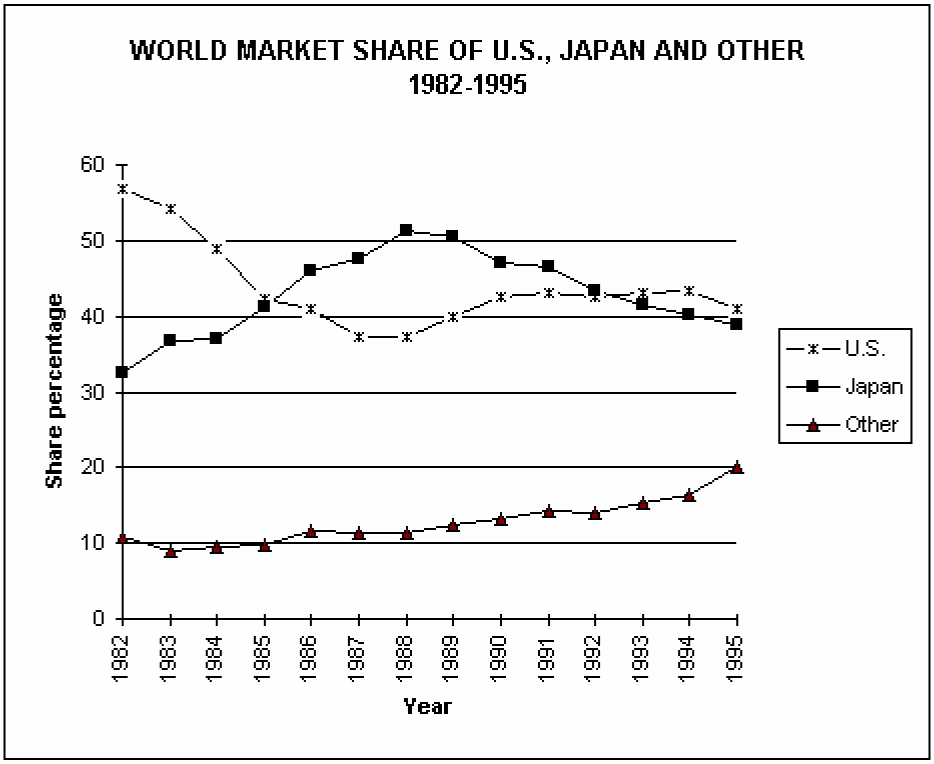

Exhibit C.2

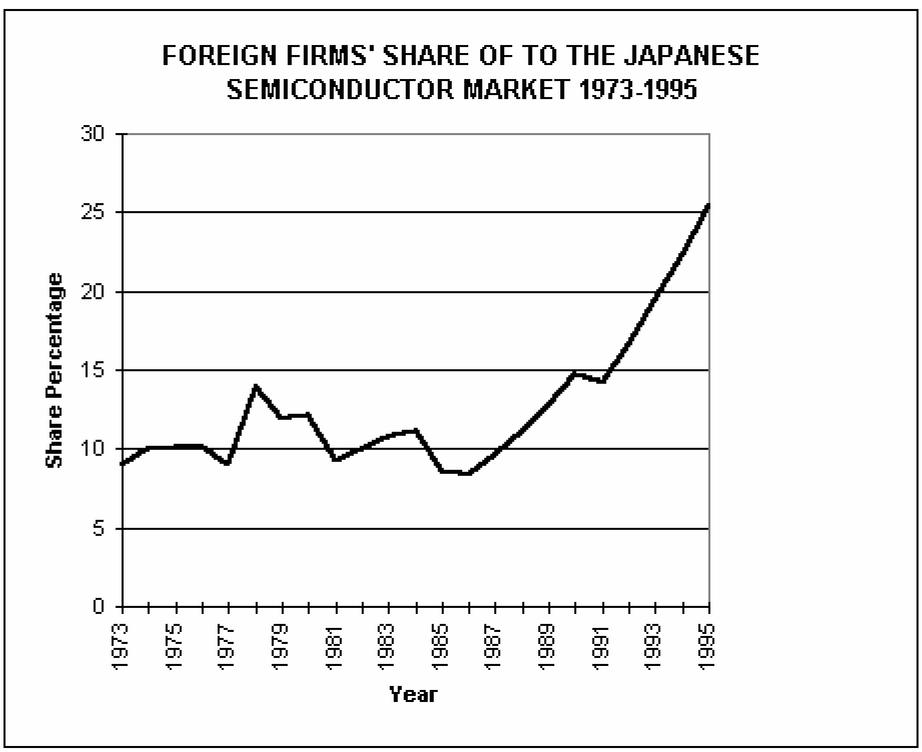

Exhibit C.3

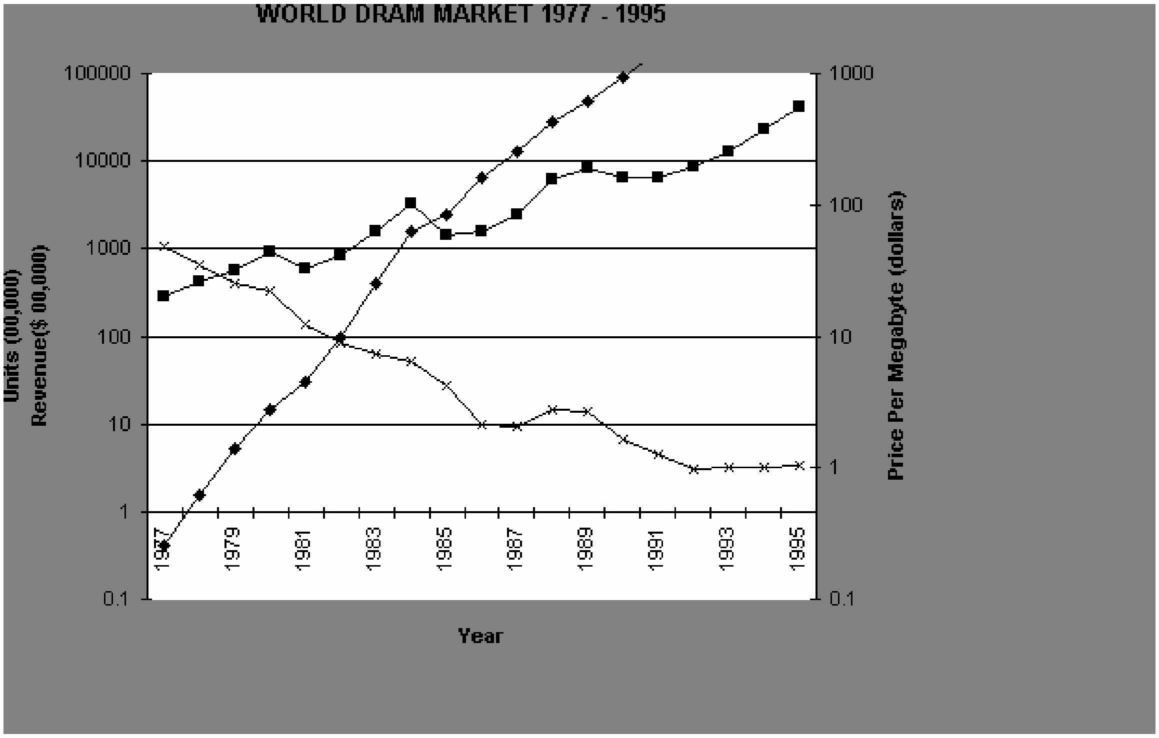

Exhibit C.4

U.S.-Japan Competition and Trade in the Global Semiconductor Industry

EPILOGUE 1996

I. THE FINAL ROUND?

In the days prior to the expiration of the second agreement, the trade associations of both countries put forth proposals showing their vision for how the agreement might continue. Not too surprisingly, these visions differed radically and met with strong opposition from their counterparts.

The EIAJ fired the first shot with a proposal submitted to the SIA for a three year industry-level agreement that focused purely on industry cooperation. It specifically rejected government involvement, instead suggesting the formation of a World Semiconductor Council to foster industry cooperation. The United States staunchly opposed this plan, and insisted that government involvement was necessary. Said one

U.S. industry official, “World councils don’t solve problems. They fashion grand statements once a year.”4[4]

The SIA fired back with a proposal of its own. It wanted to maintain a government role, ensure rapid response to unfair pricing allegations, and encourage more market openness in Japan. SIA also wanted to maintain provisions for measuring market share based on capital affiliation. Otherwise, the Japanese could include imports from its foreign subsidiaries when it measured semiconductor imports to Japan. As might be expected, the Japanese opposed the SIA proposal. Meanwhile, the European Union (EU) protested at not being part of the agreement and threatened to cease work on a separate global agreement to eliminate semiconductor, computer, and telecommunication equipment tariffs.

II. THE AGREEMENTS

The July 31, 1996 deadline set by U.S. president Clinton and Japanese prime minister Hashimoto to reach agreement passed without a deal being reached. But agreement was achieved at a meeting in Vancouver, Canada, on August 2, 1996.

The agreement consisted of two parts: a “governmental” part, or joint statement between the two governments, and an “industry trade association” part, which was a separate agreement between the SIA and the EIAJ.

The government agreement was called the “Joint Statement by the Government of Japan and the Government of the United States Concerning Semiconductors.” The statement contained no targets for market penetration. The two governments recognized Article VI of the GATT and reaffirmed that government measures should be consistent with WTO rules. But the statement contains no explicit provisions to guard against dumping or joint publication of market share categorized by capital affiliation, which SIA had sought. The United States got the extension of the agreement it had so badly wanted, but this time only for three years, not five as in previous pacts.

Another part of the governmental statement was the formation of the Global Government Forum (GGF) on semiconductors, whose purpose is to discuss the future of the semiconductor industry and ways to further liberalize trade and investment. The statement explicitly welcomed “the strong expression of interest by Europe” (Joint Statement by the Government of Japan and the Government of the United States Concerning Semiconductors) to join and invited Europe and countries elsewhere to attend the GGF annual forum. At a press conference, acting USTR representative Charlene Barshefsky suggested that China, Taiwan, and South Korea might be able to join.

The other part of the pact was the agreement between the two national trade associations called the “Agreement Between EIAJ and SIA on International Cooperation Regarding Semiconductors.” The main feature of this agreement was the formation of the Semiconductor Council, of which SIA and EIAJ were founding members. The council’s purpose was to “enhance mutual understanding, to address market access matters, to promote cooperative industry activities, and to expand international cooperation in the semiconductor sector in order to facilitate the healthy growth of the industry from a long-term, global perspective” (Agreement Between EIAJ an SIA on International Cooperation Regarding Semiconductors). The council was to make quarterly reports to governments and provide “analysis of semiconductor market and trade flow data.” This process replaced government publication of market share data, which the industry associations would now provide. The Japanese and U.S. governments would review these data once a year. Other governments were excluded from these consultations and were not allowed to submit data unless their associations joined the council. But only industry associations from countries where semiconductor tariffs had been eliminated completely would be allowed to join. In effect, this prohibited the European Union from joining the council, at least until it eliminated all tariffs. The council would also conduct cooperative activities in intellectual property, standardization, the environment, and worker health and safety. The industry agreement was subject to review in three years, and could be terminated by mutual agreement of the parties.

III. <u>THE END OF THE SAGA?</u>

So it seems, at least for now, that another chapter in the tempestuous history of U.S.-Japan trade relations in the semiconductor industry has closed. But is this the end of the story? Japan, seeing how the United States engineered a comeback in the 1980s, plans a comeback of its own. The *New York Times* describes this comeback as a series of consortiums and cooperative R&D programs not seen since the project two decades ago that catapulted Japan's semiconductor industry into the front ranks of the world chip makers. Will this become another source of conflict in the future? And will

Japan, after 15 years of struggle and major changes in the worldwide semiconductor industry, open its market enough to satisfy the Americans?