



Divergent Paths: US-Japan Relations towards the Twenty-First Century

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Source: *International Affairs (Royal Institute of International Affairs 1944-)*, Vol. 72, No. 2, New Currents in Trade Policy Thinking (Apr., 1996), pp. 281-291

Published by: [Wiley](#) on behalf of the [Royal Institute of International Affairs](#)

Stable URL: <http://www.jstor.org/stable/2624356>

Accessed: 10-03-2015 01:40 UTC

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Divergent paths:

US–Japan relations towards the twenty-first century

BRUCE STOKES

This article examines the current state and future prospects of the bilateral relationship between the United States and Japan. Looking at the economic position of each state, the trade imbalance between the two and the security relationship grounded on the postwar security treaty, the author demonstrates that the interests of Japan and the United States may now be leading them in different, not to say conflicting, directions. He draws attention to shifts in public views of the relationship in each country as well as to domestic political pressures on leaders in Tokyo and Washington. As the relationship becomes detached from the fixed points on which it has hitherto been founded, he argues, it moves into uncharted areas in which neither side has a clear view ahead.

Mike Mansfield, when ambassador to Japan, was fond of saying that the US–Japan relationship was ‘the world’s most important bilateral relationship, bar none’. In fact, the former US Senator from Montana repeated this bromide so often that wags in Tokyo took to calling the American embassy in Japan the Bar None Ranch. Europeans, mindful of the historic significance of the Franco–German relationship, might take exception to Mansfield’s sweeping claim: but it is indisputable that in Asia, over the past two decades, economic ties helped to fuel first the Japanese and then the East Asian economic miracle. It is equally clear that the US–Japan security relationship helped to maintain the peace that made postwar Japanese and Asian economic prosperity possible.

If Mansfield had merely been stating the obvious, his observation might be judged a bit hyperbolic yet defensible. But the affable former majority leader of the US Senate was a politician, and his mantra-like repetition of this simplistic characterization of a complex international relationship had a purposeful, political aim: to remind both Tokyo and Washington just how much was at stake in the increasingly fractious US–Japan trade relationship and to spur the two capitals to resolve their differences.

In the early 1980s, when Mansfield first went to Tokyo as Ronald Reagan’s envoy, it was hard to fault his political and diplomatic goal. He hoped for a peaceful relationship of condominium between the world’s two economic superpowers. His objective was shared by diplomats, business leaders and

thoughtful commentators on both sides of the Pacific. Recent history, however, suggests that such ambition for the relationship was based on an unrealistic premise. Implicit in Mansfield's effort was the assumption that once reminded of how much both countries had to lose from a gradual fraying of their ties, both the United States and Japan would have the will and the wherewithal to deal with their mutual problems, reaffirming for the foreseeable future their symbiotic economic and strategic relationship. That assumption may have been justified once, but it rests on far from solid ground today.

On a range of issues, Japan and the United States now face disparate futures. At a macroeconomic level, the United States appears destined to remain the world's largest debtor, Japan the world's largest creditor. Debtors and creditors rarely see eye-to-eye. Tokyo's present inability adequately to recycle its current account surplus makes it a drain on the world economy; and even if Japan is successful in its efforts to resolve its current economic and financial troubles and re-emerges as banker to the world, the growing centrality of the yen to Asian commerce and finance will confront the dollar with an unprecedented challenge. On the other side of the Pacific, Washington's political paralysis in attempting to balance its budget reflects a broader unwillingness of the American people to stop living beyond their means, making the United States particularly vulnerable to disturbances in international capital markets.

On the microeconomic level, the picture is largely reversed. In recent years, the United States has dramatically restructured its domestic economy and once again has become one of the most competitive nations in the world marketplace. Japan, meanwhile, seems unwilling or unable to make the changes necessary to create a flexible, open domestic economy. Its resultant slow growth is a drag on the world economy and the impenetrable nature of its market is a source of recurrent friction.

On the trade front, the US-Japan trade imbalance, the source of so much travail over the last decade and a half, shows little sign of substantial improvement. While economists discount the theoretical significance of bilateral balances, the fact that three-fifths of Japan's surplus with the United States is in the auto sector, America's largest employer, ensures that the imbalance will remain a very practical political problem for some time to come. However, trade relations between the two countries reached what may have been a watershed in mid-1995, when Tokyo successfully resisted Washington's pressure to take explicit measures to open its auto and auto parts market. In the wake of that confrontation, Japan's trade relations with the United States promise to become increasingly like US trade relations with France: a mutually antagonistic relationship in which the two sides often agree to disagree and the resultant discord means that progress is slow in resolving even minor disputes.

On the security front, the venerable US-Japan security treaty may be on its last legs. In Japan, public support for the security relationship has dipped as the result of the recent rape of a teenage girl on Okinawa by three US servicemen. While the political mainstream in Japan remains divided over how to restruc-

ture military ties, there is a growing consensus that change is inevitable. In the United States, there is mounting concern about the threat to peace in Korea and the Taiwan Straits, alongside growing doubts about Tokyo's reliability in a time of crisis and a latent resentment of the one-sidedness of America's guarantee of Japan's security.

Among the American public, frustration is growing with Japanese import barriers and its perceived unfair trading practices. It is impossible to disentangle such sentiments from Americans' broader anxiety about the flux of modern economic life and their inclination to blame trade for their woes, and thus, indirectly, to hold Tokyo somehow accountable because Japan is America's principal international competitor. For their part, the Japanese, especially younger Japanese, are increasingly likely to see their nation's self-interest as distinct from that of the United States and to support those politicians willing to stand up to Washington.

Compounding the problem for both Washington and Tokyo is the fact that the evolution of the US-Japan relationship is not occurring in a political and economic vacuum. The rest of the world, especially the East Asian region, is also changing rapidly; and as both nations rush into that economic honey pot, friction over trade and security relations with China and South-East Asia is inevitable.

In 1996, the United States and Japan are on different courses economically and strategically. The two powers are not necessarily on a collision course, as many pundits once feared; but at best they are on parallel tracks towards an uncharted future, while at worst they are headed in divergent directions. As the two largest economies in the world, what each does will undoubtedly affect the fortunes of the other. But Mansfield's assumption that the US-Japan relationship was the world's most important because the two nations' destinies were irrevocably linked now rings hollow. Tokyo and Washington are fated to pursue their own separate paths. And the rest of the world will have to begin to plan for a future in which the United States and Japan are increasingly independent actors.

A watershed

Historians may one day date the turning point in US-Japan relations at 28 June 1995, when the United States and Japan stepped back from the brink of an unprecedented trade war over autos and auto parts. This sector has long been at the core of the US-Japan trade imbalance. In 1994, the United States had a \$66 billion trade deficit with Japan, 58 per cent of which was in autos and auto parts. That sum (\$38.3 billion) amounted to 23 per cent of the total US trade deficit with the world. Washington has long complained that Japan's auto market is effectively closed to foreign competition. While foreign auto-makers have 37 per cent of the US market, in 1994 foreigners had only 4.4 per cent of the Japanese market. To force open the Japanese market, the Clinton administration

had threatened to impose 100 per cent tariffs on Japanese luxury auto exports to the United States. For the first time ever, Tokyo refused to give in. The Japanese government rejected entreaties that it make a formal commitment to increase auto imports or to purchase more US-made auto parts. Ultimately, Washington was forced to accept Japanese regulatory reforms and Japanese auto-makers' business plans as signs of progress.

The initial returns on this market-based solution have been encouraging. US auto exports to Japan climbed nearly 30 per cent in 1995. Between August 1995 and January 1996, the Big Three—Chrysler, Ford and General Motors—signed up 23 new dealer outlets. Toyota has announced plans to build light trucks in Indiana; and both Honda and Toyota have ambitious plans to increase car exports from the United States. Even more significant are the deal's implications for trade policy. Never before had the United States threatened a trading partner with such punitive sanctions in such a high-profile case involving such an important industry. Never before had Japan so resolutely resisted such foreign trade pressure. Most important, the auto dispute marked the end of an era. No longer could the United States threaten sanctions and assume Japan would capitulate. Nevertheless, as conditions in the auto sector suggest, the US–Japan trade imbalance will remain a major irritant in the relationship for some time to come. But if bilateral trade was the main source of tension in the last decade, the tone of the relationship over the next decade is likely to be set by US–Japan relations in the East Asian region as a whole; and evidence is mounting that the United States and Japan face a growing potential for conflict in Asia.

Nowhere was this more apparent than at the 1995 Osaka summit of the Asia Pacific Economic Cooperation (APEC) forum. With Japan in the chair, APEC's momentum slowed appreciably. American trade officials had hoped to use the summit to set timetables for trade and investment liberalization in the region. But that effort has now been delayed by at least a year or two. This pause reflects a fundamental disagreement between the United States and Japan over the nature of economic liberalization in East Asia. Tokyo favours an 'Asian' approach that is based on consensus-building and allows each nation to liberalize at its own pace. Moreover, the Japanese favour granting the Europeans the benefits of Asian economic liberalization in a non-reciprocal fashion. Washington believes that nothing meaningful will be achieved without deadlines and that Europe should benefit from APEC liberalization only if it provides reciprocal benefits.

At the initial APEC summits in Seattle and Bogor the Japanese government had acquiesced in American leadership; in Tokyo, by contrast, the Japanese were unwilling to follow the American lead. The experience of the auto talks clearly emboldened Japan's trade bureaucracy. More fundamentally, Japan has a vested interest in the economic status quo in East Asia. Japanese firms have invested the time and the money necessary to exploit the existing maze of differing rules and regulations governing trade and investment in the region. They have begun to establish production networks that work behind or through existing

barriers. They have little immediate economic interest in changing conditions that work for them. Finally, their own history suggests to the Japanese that government intervention in the marketplace is beneficial and that American-style *laissez-faire* economics is not appropriate in a newly industrial Asian setting. East Asia has emerged as the new battleground, where US and Japanese business interests are locking horns; the two are vying for alliances with the most important new economic force in the region, the increasingly aggressive network of Chinese investors from Taiwan, Hong Kong and the People's Republic. While US direct investment in the region has grown both absolutely and as a share of its global total, Japanese investment has grown even more rapidly.

This confrontation is readily apparent in the auto sector. The East and South-East Asian vehicle market is small by global standards: fewer than 3 million cars and trucks are sold per year, compared with nearly five times that number in the United States. But recent rapid economic growth has sparked unprecedented demand. Already Thailand, with a population only a quarter the size of America's, has become the second largest market in the world for pickup trucks, trailing only the United States. Japanese auto analysts estimate the Asian vehicle market could grow by 25–30 per cent per year in the near future, making it the fastest growing in the world. Auto-makers participating in the rapidly growing East Asian car market in the years ahead will realize tremendous increases in sales volumes that will, in turn, allow them to slide down the cost curve faster than the competition. Companies which choose not to be active in Asia will not be able to learn from the rapidly changing consumer preferences and technological developments likely to occur there. As a result they will lack a competitive edge in other markets.

Until recently, Japanese auto-makers have had the Asian stage almost all to themselves, controlling 94 per cent of the Thai market, 68 per cent of sales in Indonesia and 40 per cent of the market in Malaysia. Detroit has belatedly become conscious of the need to broaden its Asian base. In the last year the Big Three supported the Clinton administration's efforts to crack open the Japan market, and they have announced plans for plants in China and elsewhere in East Asia.

The emergence of a yen bloc

As a result of Japan's growing involvement with trade and investment in East Asia, the region is emerging as a battleground for supremacy between the yen and the dollar. Asia is clearly still a dollar zone, but the tide may be slowly turning. Economic growth rates in Asia's newly industrialized economies now track the value of the yen more closely than they do the US economic growth rate, according to studies by Nomura Research. Over the last decade and a half, the yen holdings by Asian central banks have fluctuated, but have shown a steady increase over the period, as have the yen shares of the debts of Asia's newly industrialized countries. Yen-denominated debts now surpass dollar debts in

Indonesia, Thailand and Malaysia. Most important, Japan's growing dependence on trade with Asia and the recent appreciation of the yen have given Japanese manufacturers a powerful new interest in yen-denominated transactions as a means of protecting themselves against exchange rate risks. As Japanese investment and production in East Asia grow, more and more companies are now carrying out their intra-firm trade in yen.

Nevertheless, a yen bloc is not possible in the short run due to the weakness of Tokyo's financial market. If the yen is to become Asia's anchor currency, the current bank loan crisis in Japan must first be resolved. Then Japan's financial institutions and its financial regulatory system must become more competitive internationally, offering the transparency and range of financial products that are now available to international customers in New York and London. Such developments will take time, but the will to create a yen bloc should not be underestimated. Already powerful financial figures, such as Toyoo Gyohten, the head of the Bank of Tokyo, and a number of industrialists have begun to speak openly about the possible benefits of a greater role for the yen, sending up trial balloons in a subtle indication of growing pressure from the business community to alleviate exchange rate risks.

Washington can do little to resist this trend, but it has profound implications for the United States. In recent years the US Treasury has turned a deaf ear to Japanese proposals for yen-denominated 'Clinton' bonds as a means of raising money to fund the US deficit, regarding such a move with abhorrence, because it would expose the United States to the same exchange rate risks now faced by Asian borrowers in the Japanese financial market. However, as the yen gains prominence in international transactions, it may prove increasingly difficult for debtor Washington to continue to resist such proposals from its creditors.

The changing security relationship

The US-Japan security treaty has long been the linchpin of American strategy in Asia and the guarantor of peace in the region. But the basic rationale for the treaty has been called into question by the end of the Cold War. In the absence of a Soviet military threat, there may be an asymmetry between US and Japanese security goals; and there is growing concern in both Tokyo and Washington that these differences could lead to actions by either party that would result in termination of the treaty.

The Okinawa incident in the autumn of 1995 caused a furore in Japan over the American presence on the island, raising anew the question of the long-term practicability of stationing large numbers of US troops in Japan. Public support in Japan for the security treaty has tumbled from 52 per cent of those surveyed in April 1992 to 42 per cent in October 1995. Coming less than a year after publication of the Nye Report, representing an American effort to reassure the Japanese about the continuation of a US military presence in Asia, the Okinawa affair was a stark reminder of the fragility of the status quo and a

warning that security relations are, in part, hostage to events beyond the control of diplomats and strategic planners. Meanwhile, a new generation of Japanese political leaders has begun to emerge with a more independent vision of Japan's security role and responsibilities in the world. Moreover, the rapid emergence of China as a major player in the Asian security arena has altered the US-Japan security equation.

The central problem facing both Washington and Tokyo in managing the US-Japan security relationship is the unresolved confusion over the primary purpose of continuing to station American forces in Japan. With the Soviet Union no longer a threat, are the 47,000 US troops present to protect the Japanese and other Asians from the Chinese? Or are they there to protect Asia from a renewal of Japanese adventurism by effectively occupying Japan? No American or Japanese leader has been willing to tackle these questions head-on, because of the inherently explosive diplomatic and domestic political consequences of discussing them openly. But the tension created by the failure to resolve these core questions is rising closer and closer to the surface of the security debate.

In recent years, in lieu of that discussion, US military strategists have proffered various rationales for keeping the US-Japan treaty in place as part of a general policy of forward deployment of military forces in Asia. Their arguments include the need to defend US commercial interests in Asia, the need for the United States to play the role of balancer to prevent a regional power vacuum, the justification that it is cheaper to station forces in Japan than in the United States and the importance of Japan as a staging base for potential future operations in the Persian Gulf. The common thread that runs through each of these arguments is a desire to maintain military budgets and a natural conservatism on the part of military thinkers when dealing with the evolving security puzzle in Asia. But calls for change are now being heard from a range of responsible voices. Chalmers Johnson, the dean of American Japanologists, Mike Mochizuki, the Japan expert at the Brookings Institution in Washington, and Douglas Paal, the director of Asian affairs on George Bush's National Security Council, have all, in their own ways, proposed means of withdrawing US ground forces from Okinawa, to reduce the growing friction they cause there. The motivation for such proposals involves a judgement of priority: that it would be wise to sacrifice some US bases in Japan in order to avoid being asked to leave altogether, as happened to the United States in the Philippines, and so to preserve those US naval and air operations in Japan that are strategically more important. Such proposals have already found some resonance among high-ranking officers in the Pentagon, who have concluded from the experience of the Vietnam war that the United States should never again make security commitments that lack public support. While these colonels and generals do not make policy, their post-Vietnam approach undermines what had previously been an automatic response by the security fraternity to proposals for withdrawal from Japan.

To date, this debate has not broadened to encompass the general public. As recently as March 1995, three-quarters of Americans surveyed told pollsters for the *Wall Street Journal* that the United States would come to Japan's defence in a time of crisis. Only 16 per cent of those questioned said the United States would not come to Japan's assistance if it faced military aggression. (It is interesting to note that this is quadruple the proportion which said in 1991 that America should not defend Japan.) Reflecting the lack of public interest in substantially changing the security relationship, both Democrats and Republicans on Capitol Hill generally support the security treaty, albeit with some congressional grumbling about cost-sharing and questions about military support jobs being given to Japanese rather than to worthy American citizens. But in the context of a renewed American domestic focus, of a citizenry tired of the burdens of the Cold War and looking forward to an elusive 'peace dividend', and a growing suspicion of foreign entanglements and Japanese 'economic aggression', the treaty is likely to become the target of increasing criticism.

The Japanese perspective on the security relationship has evolved in a similar, if less articulate and less public fashion. In recent years three schools of thought on security matters have emerged in Japan. All of them support change. Leading politician Ichiro Ozawa has propounded the view of 'Japan as a normal country', rearmed with conventional weapons, active in UN peace-keeping activities, but still reliant on the US nuclear umbrella. A second school of thought takes a more distinctive nationalistic and Asian line, arguing that Japan should become more self-reliant in its own defence, with a limited nuclear capability. Proponents of this view do not look favourably on issues of 'collective security' or on Japanese participation in UN military activities. Finally, a number of Socialists favour limiting military expenditures, continuing to renounce the nuclear option, avoiding involvement in UN peacekeeping activities and maintaining the military alliance with the United States, albeit at arm's length. It is noteworthy that none of these perspectives supports maintenance of the security status quo. All would require some modifications in the security treaty, the Japanese constitution or Japan's international security obligations within the UN. Proponents of all three views agree that the security environment for Japan has changed since the end of the Cold War and that Japan must deal with this changed environment in a pragmatic way.

So far, this debate has largely been limited to a small elite within the intelligentsia, the bureaucracy and elements of the political leadership. There has been no serious public debate on security because the issue remains painful for most voters, a psychological legacy of the horrors of the Second World War and Japan's failure to come to grips with its culpability in that conflict. But this reluctance openly to re-examine the security relationship is waning. The Japanese defence establishment, long cowed by its humiliation in the Second World War, has begun slowly to emerge from its cocoon. The Self Defence Force has a sophisticated air force and navy and one of the world's largest mil-

itary budgets. In recent years, breaking with the past, Japanese forces have participated in the UN peacekeeping operation in Cambodia and are now taking part in policing the Golan Heights. Tokyo is actively pressing for a seat on the UN Security Council, which, if achieved, will expand Japan's international military responsibilities and involvement.

The US–Japan security relationship could be severely tested if problems were to arise in the near future either on the Korean peninsula or in the Taiwan straits. The security treaty is not reciprocal: the US is pledged to defend Japan, but not vice versa. Although the treaty was modified once in 1960 to insert the phrase ‘mutual’ in the title, the change of language did not reflect any change in real responsibilities. Japanese foreign ministry officials privately acknowledge that any crisis in Korea would paralyse decision-making in Tokyo, and few American experts on Japan expect that Tokyo would support Washington in a confrontation with China over Taiwan. In a crisis, any such foot-dragging in Tokyo or a refusal to support US military action would trigger an ugly public and congressional reaction in the United States, shattering all support for the security treaty and spilling over into the trade arena, spawning unprecedented trade retaliation.

Over the next few years, the mortar that helped cement the US–Japan security relationship in its Cold War configuration seems destined to erode. Americans' budget-driven concerns about US overseas security commitments, the Japanese public's revulsion over the Okinawa incident and the continuing US–Japan trade imbalance suggest that the security relationship will be increasingly subject to the influence of domestic political concerns, with the terms of the debate over alternative security scenarios framed by an ever-widening group of policy-makers far less committed to the old order.

The domestic political backdrop

In the end, the substantive policies at the core of future US–Japan economic and security relations will be shaped in part by public attitudes towards the relationship in both countries. On the whole, these remain good, although they are beginning to wear thin. In June 1995, 60 per cent of Americans described relations between Japan and the United States as ‘friendly’, according to a survey for CBS News, the *New York Times* and the Tokyo Broadcasting System. In eleven previous annual surveys, an average of 79 per cent of Americans questioned characterized the relationship as ‘friendly’. In Japan in 1995, only 39 per cent of those surveyed felt that relations with America were ‘friendly’, compared with an average of 57 per cent over the last eleven years. Nevertheless, when Japanese are asked to choose among countries they like and dislike, the United States is both their favourite foreign nation and their least disliked.

A more telling indicator of the potential for future problems in the US–Japan relationship may be public attitudes towards US–Japan trade. Two out of five Americans surveyed think Japanese companies compete unfairly. Only one out

of six Japanese think their firms are unfair. More broadly, Americans are increasingly doubtful about free trade. In 1994, 52 per cent of those surveyed by The Times Mirror Center for the People & the Press felt that free trade created jobs in the United States. In 1995, 55 per cent said free trade hurts job creation. Given these sentiments, it is hardly surprising that 69 per cent of voters approve of imposition of tariffs on products from countries such as Japan that run trade surpluses with the United States, according to a 1995 poll by EPIC/MRA/Mitchell. These tariffs were first proposed by the Republican presidential candidate Pat Buchanan, who made free trade the bogey in the early GOP primary debates. If trade remains a hot issue as the campaign proceeds, Japan is likely to prove an easy target for demagoguery. The 1995 confrontation with Japan over the auto trade earned Democratic President Bill Clinton points among his core Democratic constituency: union members, blacks and the poor. In fact, a late 1995 poll by EPIC/MRA in the anti-NAFTA, anti-GATT union stronghold state of Michigan showed that Clinton's trade policy, specifically his confrontation with Japan over automobiles, was considered one of his biggest accomplishments in his first three years in office. This lesson has not been lost on White House political operatives, who may push for more aggressive trade actions against Japan in the run-up to the November election.

They will not lack opportunities. The early, favourable results of the 1995 US-Japan auto agreement mask more complex and tenuous market conditions that could be a recipe for trouble. In 1995 Japanese auto-makers increased by 28 per cent their sales in Japan of cars manufactured at overseas plants, more than quadrupling the sales increase experienced in Japan by either Chrysler or GM. BMW, Mercedes and other German manufacturers have boosted sales even more rapidly than the Big Three and still hold a larger share of Japan's import market. And most of GM's increased sales were by Opel, its German subsidiary, a boon for GM stockholders and for German workers, but not necessarily a benefit for GM workers in the United States or for the US trade imbalance. Moreover, the favourable economic conditions that strengthened the US hand in the auto negotiations have already begun to erode. Profits are up among Japanese auto makers and they are replenishing their war chests for a counter-attack against the invaders. With the yen at 105 to the dollar, American cars and US-made auto parts are already 24 per cent more expensive than they were in August 1995. The cyclical slow-down in the US auto market will soon have Wall Street asking uncomfortable questions about when Detroit can expect to see a return on its expensive 'long-term' investments in new Japanese distribution networks and right-hand-drive vehicles for the Japanese market.

US-Japan trade relations face other tests, too, in the near future. The US-Japan semiconductor agreement, which led to a dramatic increase in US market share in Japan's previously closed chip market, expires in June 1996. President Clinton has promised the politically influential California-based semiconductor industry that the agreement will be extended. Japanese officials

vow they will not renew it. Meanwhile, a suit by Eastman Kodak against Fuji Photo Film threatens to force a confrontation with Tokyo over the application of Japan's own anti-trust laws. Japanese trade officials have refused to negotiate over this issue, hoping to use the confrontation to put an end to unilateral US trade actions under Section 301 of the 1974 Trade Act. While such a goal might be applauded by other governments, especially in Europe, the United States has too much at stake to acquiesce without a fight. If Japan insists on upgrading this disagreement to a matter of high principle, a relatively minor dispute over photographic film could become a major confrontation between Washington and Tokyo.

In dealing with these and future problems, Washington and Tokyo are heading into uncharted waters in their relations. And neither side has a map. For the time being, this may not pose a problem. Both Tokyo and Washington are now primarily focused on internal issues. Americans are preoccupied with the 1996 presidential election, which, despite recent campaign rhetoric, in the end traditionally turns on domestic issues. The Japanese are absorbed by their current political realignment and the Herculean task of cleaning up after their banking crisis; trade problems have largely been shifted to the back burner. And neither side has an immediate interest in a high-profile showdown on security issues. Nevertheless, the paradigm that long governed US-Japan relations is broken; and the danger is that without a script in which each actor knows his part, the dialogue between the two countries could become quite discordant over even the smallest matter. When the players start making it up as they go along, the drama could turn quite ugly quite quickly.