Strategic Alliances and Trade Dispute in Automobile Industry

From the Perspective of the Relationship between Government and Industries in Japan and Korea

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Abstract

Japan and Korea have experienced many trade disputes between the United States in various industries such as textiles, automobiles, steel, and semiconductors. However, the trade dispute in each industry differs presently. Although the trade dispute in the steel industry still continues, the trade dispute in the automobile industry has comparatively calmed down. This paper will focus on the present condition of the automobile trade dispute from the point of the relationship between the Japanese and Korean government and industries. It is suggested that the automobile industry, which has received much less government attention than the other basic industries like the steel industry, is more likely to ally with foreign firms to confront global competition. These alliances have a calming effect on the trade dispute in the automobile industry.

Keywords: *trade dispute, strategic alliance, automobile industry, Japan, Korea*

1. Introduction

After World War Ⅱ, the advancement of free trade was inhibited by trade disputes. Domestic industries, which lost competition and lost their market share due to the influence of goods imported from outside the country, requested their government for protection against imported goods.

Japan and Korea have also experienced many trade disputes between the United States in various industries such as textiles, automobiles, steel, and semiconductors. However, the trade dispute in each industry differs presently. Although the trade dispute in the steel industry still continues, the trade dispute in the automobile industry has comparatively calmed down. From 1995 to 2003, WTO recorded 19 disputes issued by the steel industry and only 7 disputes by the automobile industry. Moreover, according to the semi-annual reports of the WTO Members to the Committee on Anti-Dumping Practices, there were 712 dumping instances in the base metals and

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articles of base metal category, 19 instances in the vehicles, aircraft, vessels and associated transport equipment category from 1995 to 2003[1].

This paper will focus on the present condition of the automobile trade dispute from the point of the relationship between the Japanese and Korean government and industries. It is suggested that the automobile industry, which has received much less government attention than the other basic industries like the steel industry, is more likely to ally with foreign firms to confront global competition. These alliances have a calming effect on the trade dispute in the automobile industry.

Increased direct investments by Japanese automobile manufacturers in the U.S. which is caused by Voluntary restriction of car exports (VER) to the U.S. and the appreciation of the yen, is also said to be the reason why trade dispute decreased between Japan-U.S. automobile industries. However, such direct investment due to the trade dispute and the rise of yen is still considered possible with automobile industry's own judgment. Also, it can be interpreted that automobile trade dispute between Korea and the U.S. was settled under the fund raising process during the financial turmoil in 1997, the Korean automobile manufacturer who have conducted business with less government interference compared to other industries.

This paper is organized as follows: The first part describes the development of the automobile industry in Japan and the Japan-U.S. trade dispute focusing on the relationship between government and industry. In chapter 2, the focus will be on Korean automobile industry concerning on the same issue as the first part. The next part surveys the strategic alliances among automobile industries around the world. In the end, I present some tentative conclusions and recommendations for further study.

2. The Automobile Industry in Japan

2.1. The Automobile Industry in Japan

The Japanese automobile industry was a late developer compared to foreign automobile industries. Subsidiaries of foreign auto manufactures dominated the Japanese market prior to 1936 and for several years after World War Ⅱ. Japan Ford, founded in 1925, and Japan G.M. in 1927, and other foreign companies had accounted for more than 95% of new vehicle registrations between 1926 and 1935.

The watershed in the development of the Japanese automobile industry came with the military interest in the industry. After World War I the Japanese army became interested in trucks and sponsored a law in 1918 to provide subsidies to manufacturers and users of vehicles which military inspectors certified.

Although the three designated local firms were not able to produce any trucks except for a few

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1 http://www.wto.org

experimental vehicles, Isuzu was founded in 1933 from two of these local firms[2]. Following Isuzu, with the encouragement of the Japanese army Nissan and Toyota were founded in 1933 and 1936, respectively, and they had dominated the Japanese automobile market more than three quarters during the prewar peak period.

With the growing anti-foreign nationalism and the preparation of war, the Japanese army used this influence to introduce legislation in 1936 that openly restricted imports of complete vehicles and knockdown sets to be assembled by foreign subsidiaries. The law was effective in bringing the operations of foreign subsidiaries to stop in 1939, and in increasing the production share of Nissan, Toyota, and Isuzu up to 57% in 1938 and 100% in 1939 (Lee, 1989, p.110).

During the postwar Occupation period, American vehicles again dominated the Japanese market due to the low level of domestic production and the suspension of prewar import restrictions. The industry faced serious problems when the occupation's deflationary policy started in early 1949. Until the Korean War, which created the special procurement demand of automobiles, Nissan and Toyota were forced to cut back production and lay off thousands of employees during the crisis of 1949-50. Toyota was near collapse during this period, but the government's help was limited with only the Bank of Japan (BOJ) Nagoya branch mediating rescue loans by private banks to Toyota. Toyota executives were particularly virulent for the fact that the government did not help them during their crisis around 1950 (Lee, 1989, p.111). The postwar government was not keen on protecting and promoting the backward auto industry. Kaplan writes that powerful elements within government which favored liberal imports opposed the development programs for the industry at that time (Kaplan, 1972, pp.109-110).

The Ministry of International Trade and Industry (MITI) was starting to recognize the importance of the automobile industry after significant progress was made in the four basic postwar priority sectors of steel, coal, electrical power and shipping. However, BOJ argued to concentrate on limited resources in other sectors of comparative advantage. As the expectation of the continuing foreign exchange drain caused by imported cars strengthened the MITI's position, the policy debate was resolved in favor of developing domestic passenger car production, Even after the early 1950s when the MITI recognized the industry as a growth industry, the Japanese automobile industry was not given any significant aid from the government compared to the steel, shipping, shipbuilding, and computer industries. The Japan Development Bank's (JDP) loans financed roughly 9% of total investment in passenger car production facilities from 1951 to 1955. Direct subsidies to the automobile industry were not pervasive, either (Chung, 1995, p.171). As a result, auto industrialists in Japan thought that the MITI had done very little for the auto industry. The late development of a client relationship between the MITI and the industry made the MITI's later control in restructuring the industry rather difficult.

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[2] The three local firms which were authorized by the new law were Tokyo Gas and Electric established in 1910, Ishikawajima Shipbuilding established in 1889, and Kaishinsha an automobile repair shop and manufacturer established in 1911. Ishikawajima Shipbuilding separated its automobile division in 1929 and absorbed DAT Motors, the successor of Kaishinsha, in 1933. The new company, named Automobile Industries, began producing standard-size trucks, mainly diesels, under the "Isuzu"logo. The company changed its name to Isuzu in 1949 (Lee, 1989, p.110).

Facing a serious problem of technological inferiority and high production costs, the government began to protect the domestic market and promote the modernization of the industry. In June 1952, the MITI announced the Basic Policy for the Introduction of Foreign Investment into Japan's Passenger Car Industry with the clear intention to exclude foreign investment to the auto industry. The protection of the domestic market from imported cars was strengthened with quotas, tariffs, and commodity taxes.

The MITI launched another plan in 1955 in order to stimulate the development of a small "people's car" with an engine displacement of no more than 500cc, which could operate for a long time with little gasoline and without major repairs (Yakushiji, 1984, p.272). The MITI expected that one firm to produce 24,000 units of this model annually within three years. This was an ambitious plan considering the low production level of 20,000 cars in 1955. The plan quickly became controversial because the MITI's motivation was to concentrate the production of a passenger car in one company. It suggested that a performance contest be held and the winner of the contest would be granted government support for production and, in effect, a monopoly position in the domestic passenger car market and ultimately in the export market as well. However the idea was not realized, because no firm participated in the contest.

Throughout the 1960s, the MITI attempted to consolidate the automobile manufacturing firms into larger units to keep them competitive with foreign firms. In June 1961, at a meeting of the Industry Structure Investigation Council's (Sangyo Kozo Chosa Kai)[3] Subcommittee on Capital, the MITI released a proposal to reorganize passenger car producers into three groups based on the car's basic design type. The Three Group Concept was designed to limit the number of manufacturers of passenger cars in order to stimulate the mass production, which is critical to competitiveness. The producer's reaction, except those of Toyota and Nissan, was hostile. This was mainly because they thought that only Nissan and Toyota could survive as conventional passenger car manufacturers. Honda Motor Corporation was especially critical of the Three Group Concept. If the MITI's program had been implemented, Honda would have kept out of the market (Gender, 1990, p.141).

By early 1962, the MITI prepared legislation to implement the Three Group Concept which was titled the Passenger Car Industry Promotion Law (Joyosha Kogyo Shinki Ho). While this law was considered in a series of unsuccessful discussions, it was never submitted to the Diet and the main provisions of the Three Group Concept was subsumed into the Special Measures Law for the Promotion of Designated Industries. The Special Measures Law for the Promotion of Designated Industries was introduced to the Diet three times but was never considered. Gender argues, "Companies, wanting to maintain their own strength, rebelled against the MITI's reorganization programs. As with the People's Car Project, the industry fought to maintain its independence when the MITI attempted to control rather than work as a partner." (Gender, 1990, p.144)

[3] The Council was created on April 1, 1961 to prepare for Japan's overall liberalization.

In May of 1964, Japan entered the Organization for Economic Cooperation and Development (OECD) with a commitment to capital liberalization. Naturally, the primary concern of the Japanese government as well as the automobile industry was directed toward the advance of foreign capital on the soil of Japan. They felt that increased fragmentation of the passenger car market could lead to takeover of weak firms by foreign capital as capital liberalization approached. Having failed to obtain legal authority to enforce its views on industrial reorganization, MITI had no choice but resort to administrative guidance to induce voluntary mergers and tie ups between the automobile firms. Effectiveness of administrative guidance was severely limited because it was pretty much dependent on the individual companies' perception of their interests and competitiveness.

The MITI's major role in the merger movement was to search and arrange for a merger partner. However, the impetus for the merger was the competitive forces of the market place, not bureaucratic aims. As Kaplan argues, "financial necessity more than bureaucratic inducement was critical stimulus in the affiliations during this period." (Kaplan, 1972, p.128) Merger negotiations which occurred in the late 1960s clearly showed the relationship between the government and the industry in the merger movement.

In August of 1966, Nissan took over Prince. Since Prince was facing financial difficulties at the time, the merger was the result of financial necessity than a reflection of MITI policy. Besides the Nissan-Prince merger, six separate auto producer tie-up arrangements were negotiated in the late 1960s; Toyota-Hino (1966), Toyota-Daihatsu (1967), Fuji-Isuzu (1967), Mitsubishi-Fuji-Isuzu (1967), Mitsubishi-Isuzu (1968), and Nissan-Isuzu (1966).

Toyota-Hino and Toyota-Daihatsu mergers materialized. It is notable that the product lines of three companies were complementary; Toyota's passenger cars, Hino's trucks and Daihatsu's minicars. All three firms were profitable in their primary line of products. The stimulus for affiliations came from financial difficulties, not from bureaucratic guidance[4] (Kaplan, 1972, p.127). On the other hand、the four negotiations involving Mitsubishi, Isuzu, and Fuji failed because they could not overcome the various obstacles; product line overlapping, management independence, and antagonism between firms.

The cases of the merger movement indicate at least two notable facts. One is that the individual companies were keenly concerned with the maintenance of the separate identities. The other is that the MITI had only negligible impact on the progress of the mergers.

The MITI's next move was to attempt a consolidation of the automobile industry into the two dominant groups, Toyota and Nissan. It was closely tied to the progress of U.S.-Japan negotiations on capital liberalization from the fall of 1967 to October 1969. This policy initiated by the MITI was nothing new to Nissan and Toyota, which was envisioned under the Three Group Concept. Nevertheless, the Two Group Concept posed a potential threat to the smaller automobile manufacturers who regarded it as "a move to reinforce the oligopoly position of Toyota and Nissan, and eventually to shut out the other firms" (Duncan, 1973, p.91). As a measure of maintaining independence, the smaller manufacturers sought for limited tie-ups with American automobile

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[4] The arrangements seem to have been facilitated by the fact that the Mitsui Bank was the primary creditor for all three firms (Chung, 1995, p.232).

companies. Two Group Concept forced the smaller manufacturers to withdraw from the Hakone Declaration, which was unanimously agreed by major Japanese automobile manufacturers not to tie-up with foreign capital on July 20, 1968. During the time of the Two Group Concept controversy, on May 18, 1969, the President of Mitsubishi Heavy Industries Makita Yoichiro announced that Mitsubishi and Chrysler had reached an agreement to establish a joint venture in Japan. By the end of 1970, Isuzu announced a joint venture with General Motors. Toyo-Kogyo linked up with Ford.

The MITI's weak client relationship with the industry made not only MITI' intervention capacity limited but also the automobile industry's intention to survive even through alliance with foreign firms.

Following is the development of trade dispute between Japan and the U.S. focusing on the weak relationship of government and industries.

2.2. The Japan-U.S Automobile Trade Dispute

In the early 1960s, the American automobile industry settled down into a triad oligopoly of GM, Ford, and Chrysler, with little to fear from foreign competition. The sign of the vulnerability of the American automobile industry appeared when small-car imports took 11.2 percent of the market in 1967, up from only 1.6 percent in 1956. The American automobile industry reacted to this import surge by the introduction of "captive" small-car imports, while the foreign companies except Volkswagen failed to set up sales networks. Even though the American companies had tried to deter the small-car imports by importing captive small cars, they continued to produce large cars because of greater profitability.

The U.S. Big Three did make some attempt to compete with foreign cars during the 1970s, notably with the introduction of General motor's Chevette, Ford's Pinto and Bobcat, and Chrysler's Omni and Horizon. The share of small-size cars in the U.S. market in 1972 was approximately 37 percent; in the wake of first oil crisis, the share rose to 50.8 percent in 1975. After 1975, however, consumption of small cars fell down, but the second oil crisis in 1979 caused demand to increase sharply once again. Quite different from the effect of the first oil embargo, the second oil crisis in 1979 sharply accelerated the shift to small cars, and Detroit was wholly unprepared for this sudden change. The insulated American market came to be exposed to international competition, into which foreign companies, especially the Japanese, easily penetrated. The Japanese market share in the United States doubled from 11 percent in 1978 to 21 percent in 1980.Thanks to active sales in the United States, the Japanese production of motor vehicles actually surpassed U.S. production for the first time in 1980.

This was a symbolic indication of the end of the postwar American supremacy and leadership in the automobile industry. The year 1980 suddenly turned out to be the worst year for the U.S. automobile industry. Ford and General Motors suffered record losses, and government-loan guarantees were required to save Chrysler from imminent bankruptcy. The suddenness and magnitude of the downturn in the automobile industry in 1980 shocked Americans and led to certain manufacturers (mainly Ford) and the United Auto Workers (UAW) applying for strong pressure on the government to negotiate export restriction with Japan.

After several negotiations, an agreement was made between Japan and the United States on May 1, 1981. Under this agreement, Japan promised to voluntarily limit passenger car exports to the United States to 1.68 million vehicles in the first year and 1.68 million vehicles plus 16.5 percent of any growth in the United States market in the second year. In addition, a third year of restrictions would be considered if conditions warranted. However, as a result, VER continued until 1994. On June 24, the MITI announced the quota shares of the individual companies, to which auto manufacturers expressed dissatisfaction. The VER caused tension and adversity between the state and automobile industry due to disagreement on the way to solve the trade conflict.

Since, this paper is particularly interested in the relationship between government and industries in Japan, the negotiations between the government and industries dealing with direct investment of this period will be discussed next. As one of the feasible political solutions to the rising unemployment rate in 1980, the U.S., particularly UAW, demanded Japanese automobile producers to expand their manufacturing facilities in the United State. In the course of handling the issue, the Japanese government's reaction was supportive to the U.S. demand and argued that they did their best to persuade Toyota and Nissan to invest in the United States. High-ranking officials of MITI conducted a series of meetings with Toyota and Nissan representatives to persuade them to invest in the United States. They even threatened to impose export controls under the Export-Import Transaction Law and sometimes publicly reproached the automobile manufacturers for their lack of cooperation. However the expected outcomes were not achieved out of these meeting (Chung, 1995, p.299). Toyota maintained its cautious attitude toward U.S. investments and countered Sasaki's request by bringing up such specific problems as labor quality and overcapacity in the U.S. market[5].

There were also other reasons why Japanese companies have resisted investing in the United States. According to Nihon Keizai Shinbun (March 13, 1980), U.S. officials admitted that the Japanese would have problems not only in the areas of labor management but also in the spare-parts supply system. The United States even admitted that the legislative environment was not ready for the Japanese to apply the unique management styles of Japanese corporate executives in the United States.

However, it is very interesting to observe that the Japanese were beginning to reconsider the defunct alternative of direct investment in the United Sates, which they vehemently opposed, when it was first suggested by the United States. While they reduced their automobile shipments under the agreement of VER for two years, they carefully analyzed the merits and demerits of direct investment and began to realize that it was not a bad idea.

Most Japanese automobile manufacturers were beginning to be convinced that trade barrier in the form of voluntary export restraint was not of a 'temporary' but 'long-term' duration. Furthermore, the distribution of quota was solely under the discretion of the MITI. This environmental change forced the Japanese manufacturers to reevaluate the direct investment in the

[5] Yomiuri Shinbun, March 15, 1980.

United States as a viable alternative and they started to use it as a new tool for ‘tariff-jumping’. By 1986, every manufacturer in Japan except Daihatsu announced plans to invest either in the United States or Canada. This investment had given over 4.6 million passenger cars into the U.S. and Canadian market by 1989[6].

All in all, voluntary export restraints allowed Japanese automobile manufacturers to invest directly when they thought there was need to.

3. The Automobile Industry in Korea

3.1. The Automobile Industry in Korea

The Korean automobile industry began from scratch. Although there were small industries after 1945, their level of technological sophistication and capacity were pretty much similar to those of common repair shops or small garages. After Japan annexed Korea, Japan used Korea as a supply route to Manchuria and North China as well as a manufacturing and repairing station for machinery and automobiles produced mainly in Japan because of geographical distance from Japan to China.

After the liberation of Korea in 1945, the Korean automobile industry did not have any chance to develop its own automobiles largely because of political instability and the United States Army’s domination. Some workers who used to work for Japanese-owned parts manufacturing companies started manufacturing some automobile parts for the U.S. military. With the outbreak of the Korean War in 1950, the Korean automobile industry provided auto parts and repairs for the Korean and U.S. armed forces[7].

The Korean government launched the first Five-Year Development Plan in 1962. The Ministry of Commerce and Industry (MCI) enacted the Automobile Industry Protection Law in 1962. The law exempted the import of parts and components for assembly production from tariffs while prohibiting the import of complete cars, and parts and components, not for assembly production.

As Korea and Japan normalized their relationship, Japanese capital could flow into the Korean economy. The first modern assembly plant was established by Saenara Automobile Company with $35 million of loans and technical assistance from the Nissan Automobile Company in Japan.

Although the Korean government attempted to develop the automobile industry, the government was reluctantly in promoting the industry. The Korean economy in the 1960s was still underdeveloped and light export industry oriented. Since the automobile industry was not an export industry, the industry could not receive favorable tax breaks and preferential loan packages from the government (Han, 1998, p.217). The government policy was not consistent either. MCI was in

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6 Honda decided upon overseas investment in order to search for a new market, before voluntary export restraint was taken.

7 The founder of Hyundai Corporation, Chung Ju-Young, started a repair shop in February of 1940 in Seoul, Korea, and later he began using name “Hyundai” for his repair shop in 1946.

charge of the automobile industry, while the Economic Planning Board (EPB) was taking care of foreign investment. The Blue House also was much involved in the industry. The first semi-knock down (SKD) automobile company, the Saenara, was established by Kim Chong Pil, who was the founder of the Korean Intelligence Agency (KCIA) and the second most powerful person next to Park Chung Hee. The company imported SKD Nissan Bluebird parts and components for 130,000 won and sold an assembled car for 250,000 won. A Japanese-Korean investor, Park No Chong, accused Kim of embezzling the profit from the company. Along with other corruption by the new military rulers, the company was a part of a scheme to raise the fund for the newly created KCIA operation and new ruling party.

Because of the better quality of the imported Japanese cars and the government's policy of only one company in automobile industry, the corrupted Saenara caused bankruptcies within the existing small auto parts industries. That is to say, the government's policies bankrupted the existing small parts industry, favoring one company that was dependent on foreign technology and parts. After bankruptcy of small auto parts companies, Saenara itself went bankrupt in 1963. The CKD factory was taken over by a businessman who had a connection with Lee Hu Rak, a next KCIA chief after Kim Chong Pil. Since the government only allowed one automobile company, the Sinjin took over the bankrupted Saenara and started to have complete knock-down (CKD) assembly production of the Corona with Capital and technology imports from Toyota and Mitsubishi in 1966[8]. The company monopolized the domestic market until other companies, such as Hyundai, Kia, and Asia, entered into passenger car assembly production after MCI allowed three companies in December 1967.

After the palace coup of the so-called "Yusin" in 1972, the Korean Government announced the very nationalist Long-Term Automobile Promotion Plan in 1973 and confirmed it as a policy in 1974. It was aimed at the so called "people's cars" by three designated firms: Kia, Hyundai and GM-Korea. The size of engine (Kia:1,000cc; Hyundai:1,300cc; GMK:1,400cc), production volume (over 50,000 cars per year), number of models (one to each firm), local content (up to 95%), price (around $2,000), and production schedule of these firms (until 1975) were to be more tightly supervised by the government than ever.

The government promised that if a company was successful in manufacturing a prototype, the company would receive government backing. Manufacturing of the people's car had to begin in 1975. Unlike the Japan's contest-like announcement, the Korean government not only designated three major companies to produce the people's car but almost forced them to participate in the project. No participation meant no support from government (Han, 1998, p.226).

Kia first produced the Brisa in 1974 with technological cooperation with Mazda and immediately captured a passenger car market by 55.12 percent in 1975. Hyundai successfully manufactured the Pony in October 1975. As soon as the Pony entered the domestic market, Pony

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8 When Toyota withdrew from Korea because of Chou Enu-lai's Four conditions, Sinjin agreed upon a 50:50 joint venture with General Motors in 1972. The company later went bankrupt and was absorbed by Daewoo Motors because its GM models were too big, heavy and energy consuming.

immediately took 43.56 percent of passenger car market share. With Pony's domination in the domestic market, Brisa from Kia lost out. Failing to deliver a satisfactory model to receive government support, Shinjin and Asia went bankrupt and were later absorbed by Daewoo and Kia in 1981, respectively.

Because of the Korean government's big push to develop an automobile industry in a short period of time, the Korean manufacturers did not have time to think about indigenous research and development programs. Although two Korean manufacturers succeeded in producing the people's cars in a record breaking time, the project made the Korean manufacturers dependent on out-dated Japanese automobile technologies (Han, 1998, p.228). Nevertheless the Korean automobile industry grew remarkably at this time, the growth was not promoted in nurturing or protective way. The industry could vigorously compete in domestic and international market later with their own indigenous planning and technology.

In 1980, General Chun made a successful coup and his military junta promulgated the Order of Automobile Industry Unification that was aimed at economies of scale through the radical reorganization of the Korean automobile industry structure. In order to do so, the merger of the two largest terminal firms-Hyundai and Saehan (GM-Korea)—into one terminal firm-a new Hyundai -was necessary. The government designated two other terminal firms to specialize in commercial and special-purpose cars. However, it did not proceed the way the government planned to. First of all, Kia and Tong-a could not agree to a merger, so the production of specialty vehicles was open to all companies. Kia was prohibited producing passenger cars, and was allowed only to manufacture trucks and buses. Asia was designated to produce military vehicles. Tong-a was to produce specialty vehicles (fire engine, concrete mixer., etc.). Kohwa was to produce civilian jeeps. Secondly, Hyundai had to absorb the Daewoo's capital share in Saehan. A problem was that the Saehan Motors' foreign partner was General Motors[9]. According to the original merger plan by the Special Committee for National Security Measures (SCNSM), Hyundai could take over management control, owing 80 percent of the merged company's total equity share, and GM would hold only 20 percent of total equity share, so the multinational company would lose veto power in management. GM opposed it. As a part of the "World Car strategy[10]", GM wanted to control a subsidiary in Korea and to increase its share to 50 percent. Hyundai repeatedly argued that the company would not give up the control of management to GM[11]. On 28 February 1981, Daewoo was allowed to produce passenger cars. In doing so, Hyundai's independence from foreign capital was assured, while GM could remain as foreign partner with Daewoo.

The reorganization and rationalization policies were inconsistent with ambitions in the private sector. Consequently, the 1980 Order had to be replaced in 1981 with the Order of Automobile

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9 In contrast with the Japanese government, the Korean government promoted foreign investment, because the Korean government thought that the presence of foreign capital would safeguard the security of Korea (Han, 1998, p.220).

10 "World Car Strategy" is to find the right combination of manufacturing plants, markets and dealer-distribution networks worldwide that would produce the lowest costs and high profits.

11 The Hyundai Motors company, which had a 50:50 joint venture with Ford broke a tie with Ford in 1973, which regarded Hyundai as mere CKD assembly plant in third World country.

Industry Rationalization that allowed two major firms to produce passenger cars.

It is certain that the government policies in auto industry were effective. On the other hand, there is perhaps not such a strong casual relationship between the governmental policies and the pattern of automobile industrialization as some statists argue (Back, 1990, p.86) [12]. The Korean automobile industry, which received much less government attention at the beginning of the development, had a weak client relationship with the government. Therefore government policies, even though they are specific on issues, are hardly specific enough to the performance of each auto firm in Korea. In most cases, the real sources of competitiveness of each firms are its technological, managerial, and financial superiority over other firms[13].

3.2. The Korea-U.S. Automobile Trade Dispute

The Korea-U.S. automobile trade dispute began in June 1993 when American Automobile Manufacturers Association (AAMA) urged Bill Clinton, the president of the U.S. at that time, for Korean automobile market liberalization. In the beginning of September 1995, AAMA asked Kantor, U.S. Trade Representative, to put Korea on a priority list for action that could lead to U.S, sanction if no progress is made on opening its market to foreign car imports. Kantor had to decide whether to initiate action against Korea until the end of September 1995 or not.

Korea and the U.S. reached an agreement on detailed steps to increase market access for foreign autos in South Korea on September 28, 1995. With signing of the Korea-U.S. memorandum of understanding (MOU) on auto trade, Seoul avoided Washington's application of Super 301 provisions, which could impose 100 percent retaliatory tariffs on Korean exports to the United States. Washington will also refrain from bringing the automobile trade question to the WTO at least for the time being. Yet, this, of course, does not preclude another wave of U.S. trade pressure against Seoul, as the Clinton administration redesignated South Korea as an Area of Concern measuring that Washington will not turn off the pressure to fully open Korea's car market. Accordingly, Seoul will be closely monitored by Washington to ensure it is in full compliance with the agreement, while leaving open the possibility of bringing the case to the WTO in case U.S, car exports to Korea are not drastically increased.

In July 1997, because the United States strongly demanded the revision of the MOU, the negotiations between Korea and the U.S. opened in early August. The main points of contention were the Korean import duty and tax system. Washington demanded the 8 percent duty imposed on

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[12] For example, Stephan Haggard and Chung-in Moon assert, "Indeed, much of their economic success (Brazil, Mexico, Taiwan, and Singapore, as well as South Korea) appears attributable to such state strength." (Haggard and Moon, 1983, p.140)

[13] The rapid growth of production and export in the Korean automobile industry is largely due to the superior performance of Hyundai. While Korea's development strategy under Park's ruling coalition was export-oriented in general, the actual strategy of automobile industrialization in particular was import substitution until the late 1970s. Only in 1977, after the success of Pony in both the domestic and international markets, did the Korean government select automobile industry as a major strategic industry for export.

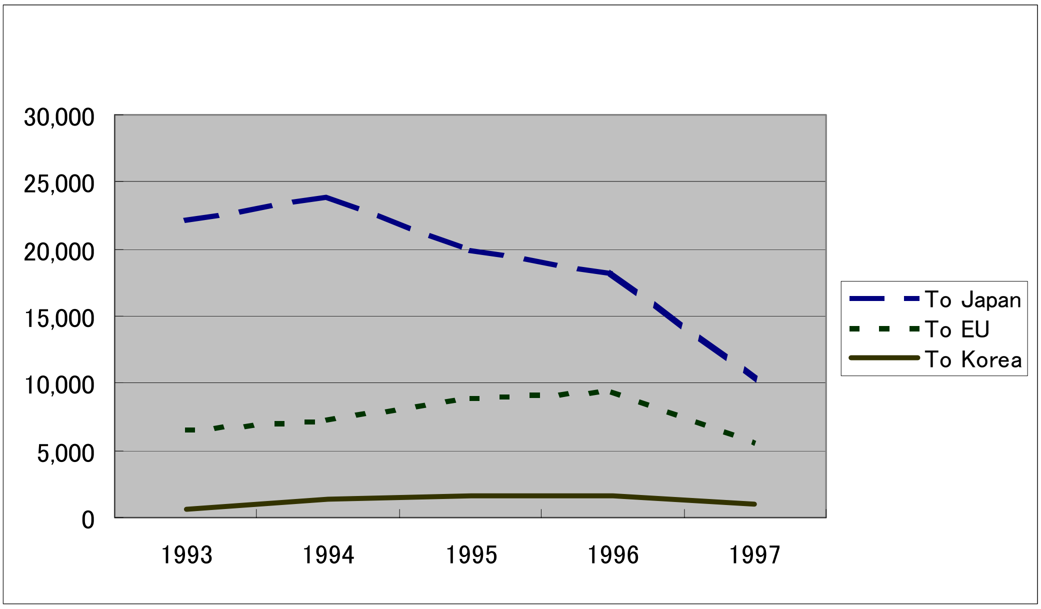
imported cars be lowered. But Seoul declined the demand, arguing that the rate is lower than the European Union's 10 percent. The two sides also disagreed on the automobile tax system. Washington insisted on reducing the taxes imposed on cars, but Seoul said it would take time to streamline the system.

In October 1997, the United States designated South Korea's auto market as Priority Foreign Country Practice (PFCP) under the Super 301 provision of U.S. trade law. With the Korean market designated PFCP, the U.S. administration is allowed under Super 301 to impose retaliatory import duties on Korean products unless Seoul and Washington settle the dispute by October 1998. Seoul officials said that they would take the case to the WTO's dispute panel if Washington takes retaliatory measures against Korean goods.

After several negotiations, Korea and the United States reached an agreement in Washington on October 20, 1998. Korea did not give in to the U.S. demand that import duties on foreign vehicles be cut from the current 8 percent to 2.5 percent, but Korean government did yield to requests to revise its complicated automobile tax system.

The year 1993, when the U.S. demanded the liberalization of Korean automobile market, was a year of lowest Korean automobile export rate to the U.S. Unlike the case of Japan, the U.S.'s demand of market liberalization was not due to the trade deficit between Korea and the U.S.

3.1 The U.S. trade deficit in automobile industry Unit: million dollars



Source: Kim, Gu Te, 1998, p.20.

Although the Korean automobile manufacturers were not major competitors for the U.S. automobile manufacturers, the reason why the U.S. big three (GM, Ford, Chrysler) demanded the U.S. government to take sanction against the Korean auto manufacturers, was due to global strategy of the Big Three. To overcome the depression of domestic market caused by stagnation of the U.S. market and the depression of market share due to the increase of Japanese and European cars in the

U.S. market, the Big Three had actively considered of going for foreign market. In case of GM, in order to raise their already gained 5% Asian market share up to 10%, they founded need for expansion of share in the Korean market. GM chairman John Smith also once noted that the company wants to advance into South Korea and one of the reasons for the move is that country's part industry has technical competitiveness with around a 20-30 percent price advantage over other competitors[14]. In other hand, since the financial turmoil in 1997, Korea automobile manufacturers also eager to attract foreign investment and strategic partnerships to survive the severe financial crunch following the collapse of the nation's economy[15]. From the beginning of 1998, while the negotiation was held between Korea and U.S. government, Daewoo and GM began to discuss the alliance. If the alliances between Daewoo and GM were formed, GM could take advantage of Daewoo Motor's spread of production strongholds in Asia, eastern Europe and India, while the Korean auto maker could acquire advanced technology and funds needed to push its marketing in the United States and to enhance its name value in Asia[16]. In the meantime, Ford was in the midst of talks with Kia over its capital increase. Ford at the same time had staged talks with Samsung for a possible partnership or a joint venture. As a result, alliances were made between French automaker Renault and Samsung Motors in 2002, and between GM and Daewoo in 2001

The Big Three's search for cooperation with the Korean auto manufacturers in the process of advanced embarkation into the Asian market, and Korean companies' effort to overcome financial depression through foreign alliances, led to the alleviation of trade dispute.

4. Strategic Alliances in the Automobile Industry

The automobile industry is one of the major globalized industries. One of the reasons the automobile industry allies with foreign firms is to survive global competition under a weak relationship between the government and the industry.

There are 8 types of alliances according to Fujimoto and Takeishi; Equity Investment, Joint venture, Provision of production technology, Supply of completed car, Supply of components, Joint R&D and Joint manufacturing (Fujimoto & Takeishi, 1994, p.295).

4.1 Alliances within the Automobile Industry

	Equity Investment	Joint venture	Provision of production technology	Supply of completed car	Supply of components	Joint R&D	Joint manufacturing	Joint marketing	Total
1985	9	10	5	4	6	0	0	2	36
1990	12	24	0	4	10	36	6	12	102
1994	8	27	2	17	16	26	11	14	121

Source: Fujimoto & Takeishi, 1994, p.295.

14 Korea Times, April 4, 2002
15 Korea times, February 2,1998
16 Korea Herald, February 2, 1998

4.2 Interrelationships among the Automakers in Japan and Korea (as of September 1988)

company	Equity Arrangement	Joint venture	Supplies or Buys Major Components	Marketing/ Distribution Arrangement	Technology Arrangement	Manufacturing/ Assembly Arrangement
Toyota	Daihatsu	Daihatsu Ford GM Nissan Renault	Daihatsu GM	Daihatsu GM Volkswagen	Daihatsu GM Nissan Volkswagen	CNAIC Daihatsu Volkswagen
Nissan	Fuji Heavy Siam Motors Yulon	Ford Fuji Heavy GM Toyota	Daewoo Ford Fuji Heavy GM Peugeot Second Auto Works Volkswagen Yulon	Fuji Heavy Mazda	Daewoo Fiat Ford Fuji Heavy Mazda Second Auto Works Toyota	Ford Fuji Heavy Siam Motors Yulon
Honda	Rover	Mitsubishi Rover	Daewoo GM Mitsubishi Rover	Chrysler Daewoo Rover	Daewoo GM Rover	Daewoo Isuzu Mercedes-Benz Mitsubishi Peugeot
Mazda	Ford Kia	Ford Isuzu	Ford Isuzu Kia Mitsubishi Suzuki	Cycle&Carriage Bintang Fiat Ford Isuzu Kia Nissan Peugeot	Ford Kia Mercedes-Benz Nissan Porshe	Cycle&Carriage Bintang Fiat Ford Kia Suzuki
Mitsubishi	China Motors Hyundai Proton	Chrysler Honda Mercedes-Benz Suzuki Volvo	Chrysler GM Honda Hyundai Mazda Mercedes-Benz Proton Renault Volvo	Hyundai Mercedes-Benz	Chrysler Hyundai Proton Volvo	China Motors Chrysler Honda Isuzu
Hyundai	Mitsubishi		Mitsubishi	Mitsubishi	Mitsubishi	
Suzuki	GM	GM Mitsubishi Peugeot	Daewoo GM Mazda	Ford	Daewoo GM	FirstAuto Works Ford GM Mazda
Fuji Heavy	Nissan	Isuzu Nissan Siam Motors	Fiat Ford GM Nissan Volvo	Nissan Volvo	Fiat Nissan	Nissan Volvo
Daihatsu	Toyota	Peugeot Toyota	BMW Kia Toyota	Toyota	Kia Peugeot Toyota	Betron Toyota
Isuzu	GM	Fuji Heavy GM Mazda	Daewoo GM Mazda	GM Mazda Volvo	Daewoo GM Volvo	GM Honda Mitsubishi Peugeot
Daewoo		GM	Honda Isuzu Nissan Suzuki	Honda Volvo	Betron Honda Isuzu Nissan Suzuki	GM Honda
Kia	Ford Mazda		Daihatsu Mazda	Ford Mazda	Daihatsu Ford Mazda	Ford Mazda
Ssangyong	Mercedes-Benz		Mercedes-Benz	Mercedes-Benz	Mercedes-Benz	Mercedes-Benz

Source: Yoshino&Rangan, 1995, pp.10-15.

In 1990, the alliances in the automobile industry increased about three times from 1985. Joint venture increased from 10 in 1985 to 27 in 1994, and supply of completed car and supply of components increased from 4 to 17, and from 6 to 16, respectively. Joint R&D and joint manufacturing was non-existent in 1985, but increased to 26 and 11 in 1994, respectively. This means that the strategic alliances presently are pursuing mutual benefits, not one-sided benefits. For example, Hyundai Motor, DaimlerChrysler and Mitsubishi Motors signed an agreement to set up a three-way joint venture manufacturer of passenger car engines, with Hyundai offering its self-developed mid-sized engine to the German and Japanese alliance partners on May 5, 2002. "Sharing of the new engine platforms will enable the three automakers to sharply cut engine development costs and thus enhance competitiveness," said Hyundai in a press release[17].

Figure4.2 shows the complexity of interfirm relationships in the auto industry in Japan and Korea. This illustrates that strategic alliances are formed between rival companies, both foreign and domestic.

The reigning theory is that as long as a production scale of four million or higher is not established, development costs cannot be funded and that such companies will be shaken out of the market (Oshima, 2002, p.13). Moreover, the development of low fuel consumption and environmentally friendly compact economy cars, is believed to contribute to strategies alliances, which will increase drastically from now on and it will contribute to the calming of the trade disputes in the automobile industry.

5. Conclusion

In recent years, we have witnessed a surge of alliances among major corporations all around the world. The primary driver of strategic alliance is the emergence of intense global competition. The growing integration of the global marketplace over the past decade has spawned new strategic approaches in many industries. The automobile industry is one of the major globalized industries.

The automobile industry in Japan and Korea is actively allying with the foreign automobile industry to confront global competition, because they have a weak client relationship with the government. This paper suggested that the active strategic alliances in the automobile industry contribute to calming of the trade dispute in the automobile industry.

Unlike the automobile industry, which was developed with less government attention, the steel industry was developed by government initiatives in many countries including the U.S. and EU. Even though it is not as apparent as the auto industry, it is notable that there are alliances between the steel industries. Usinor and Arbed combined to create Arcelor, which has in turn merged with Bethlehem of the U.S. Arbed was already the result of a merger of two European companies and the establishment of Arcelor is indicative of the need to achieve grater volume for enhancing competitiveness in the steel industry. In regard to these alliances in the steel industries, it is worthwhile to watch the trade disputes in the steel industry from now on.

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17 *The Korea Herald*, May 6, 2002.

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