



The Dynamics of Negotiated Protectionism

Author(s): Vinod K. Aggarwal, Robert O. Keohane and David B. Yoffie

Source: *The American Political Science Review*, Vol. 81, No. 2 (Jun., 1987), pp. 345-366

Published by: [American Political Science Association](#)

Stable URL: <http://www.jstor.org/stable/1961956>

Accessed: 28/10/2014 18:31

Your use of the JSTOR archive indicates your acceptance of the Terms & Conditions of Use, available at
<http://www.jstor.org/page/info/about/policies/terms.jsp>

JSTOR is a not-for-profit service that helps scholars, researchers, and students discover, use, and build upon a wide range of content in a trusted digital archive. We use information technology and tools to increase productivity and facilitate new forms of scholarship. For more information about JSTOR, please contact support@jstor.org.



American Political Science Association is collaborating with JSTOR to digitize, preserve and extend access to *The American Political Science Review*.

<http://www.jstor.org>

THE DYNAMICS OF NEGOTIATED PROTECTIONISM

VINOD K. AGGARWAL

*University of California
Berkeley*

ROBERT O. KEOHANE

DAVID B. YOFFIE
Harvard University

Recent protectionism by the United States has principally taken the form of negotiated barriers to trade, such as voluntary export restraints. These barriers tend to evolve over time and to display three patterns, which we label institutionalized, temporary, and sporadic protectionism. Cartel theory and studies of the politics of protection suggest that the dynamics of negotiated protectionism will depend on three variables: the barriers to entry into an industry, the size of the domestic industry, and the exit barriers for domestic firms. Low barriers to entry will lead to institutionalized protectionism when the domestic industry is large and exit difficult; temporary protectionism results when the domestic industry is small and exit easy; and sporadic protectionism is likely when barriers to entry are high. Brief studies of U.S. protectionism in textiles and apparel, steel, footwear, televisions, and automobiles illustrate the value of this framework.

Trade protectionism has often been thought of as a unilateral act by a sovereign state. Yet much protectionism during the 1970s and 1980s has been negotiated rather than unilaterally imposed. Voluntary export restraints (VERs) and similar arrangements have become the preferred means by which the United States has sought to cartelize industrial sectors threatened by imports. Such negotiated protectionism has been particularly evident in five industries in the United States during part or all of the last quarter century. In textiles and apparel, steel, footwear, television sets, and autos, the United States has negotiated trade restrictions with numerous foreign exporters. While the U.S. government has occasionally provided unilateral measures of protection for small indus-

tries, all U.S. administrations since World War II have been reluctant to countenance general schemes of protection for major industries. Yet, beginning with the Eisenhower administration's negotiations in textiles in 1956, virtually every U.S. president has actively sought VERs for economically and politically sensitive industrial sectors.

Most research on protectionism has sought to uncover why governments impose trade barriers and how those barriers affect the economy (Bauer, Pool, and Dexter 1972; Cline 1983; Destler 1980; Pastor 1980; Strange 1985). Some social scientists have focused on explaining the height and impact of trade barriers (Baldwin 1986; Lavergne 1983); others have looked at the ideological and political roots of protectionist policies (Goldstein

AMERICAN POLITICAL SCIENCE REVIEW
VOL. 81 NO. 2 JUNE 1987

1986a; Schattschneider 1935); and still others have looked at how restrictions such as VERs—quantitative measures negotiated with selective exporters—are different from other forms of protection, such as tariffs and global quotas (Bergsten 1975; Yoffie 1981). This article, by contrast, examines what happens to negotiated protectionism in the United States *after* agreements have been reached. Casual observers often assume that trade barriers persist automatically, that once a country begins down the slippery slope of protection, there is nothing to do but slide further. Yet this generalization is false for the United States over the last quarter century. Indeed, we have identified three quite different patterns of negotiated protectionism involving the United States during this period. Protectionism in some industries has been temporary, in others it has a long institutionalized history, and in still others it has been sporadic.

Under *temporary* protectionism, the United States negotiates agreements with one or several exporters, but it allows them to lapse after some initial period. The restrictiveness of the protection is generally not very high. Protectionist arrangements in the color television and footwear industries have reflected this temporary pattern. In the case of color televisions, the United States negotiated an Orderly Marketing Agreement (OMA) with Japan in 1977, which was followed by two OMAs with Korea and Taiwan in 1978.¹ The Japanese OMA was allowed to expire in 1980, while the Korean and Taiwanese agreements expired in 1982. Similarly, in footwear, the Carter administration negotiated OMAs with Taiwan and Korea in 1977, but in 1981 the Reagan administration allowed both OMAs to lapse. Despite substantial political controversy and import penetration rising above 75% of U.S. consumption, the footwear OMAs have not been renewed.

The second pattern is one of *institutionalized* protectionism, where protec-

tionist agreements expand over time, becoming more complex and gradually encompassing larger numbers of exporting countries and more and more categories of products. Such restrictions persist across administrations. This pattern of increasing institutionalization has characterized protectionism in textiles and apparel since the mid-1950s. Restrictions in textiles and apparel began with a simple bilateral agreement between the United States and Japan that limited Japanese exports in a few categories of cotton textiles in 1957. Four years later, a multilateral agreement was negotiated that provided a framework for the U.S. and Europe to restrict the cotton textile and apparel exports of about 30 countries. By the 1980s, the industrial countries were protecting hundreds of categories of cotton, wool, and synthetic fiber textiles and apparel from all producing countries in the world (Aggarwal 1985; Yoffie 1983a).

The third pattern of protectionism follows a more *sporadic* course. In this pattern, initial agreements lapse, but protectionism is subsequently renegotiated. This nonlinear pattern can be observed most clearly in the steel industry. In 1968 the United States negotiated a tripartite agreement with the European Community and Japan in basic steel. Although the initial three-year agreement was extended through 1974, the Ford administration allowed protection to lapse. In 1977, however, the steel industry again managed to convince the Carter administration to reimpose trade barriers. These restraints have persisted in a variety of different forms through the mid-1980s.

The existence of different dynamic patterns of protectionism in different industries provides us with our major puzzle. How do we account for the varying patterns exhibited by negotiated U.S. protectionism? Because we are interested in the evolution of negotiated protectionism rather than in its origins, we begin at the point when protection has first been

implemented on a sectoral basis. To account for patterns of change, we sketch an interpretive model that emphasizes the size of the industry and two additional variables not usually stressed in discussions of protectionism: (1) the height of economic barriers restricting entry of foreign producers into an industry and (2) the exit or adjustment strategies of the domestic firms. Having outlined an interpretive model of U.S. protectionism, we then discuss our five industry cases: textiles and apparel, steel, color televisions, footwear, and autos.²

Explaining the Dynamics of Negotiated Protectionism

Negotiated protectionism is fundamentally different from tariffs and auctioned quotas (Bergsten 1975). Unilateral forms of protectionism attempt to shift the burden of adjustment from an importer to an exporter, while VERs constitute cross-national cartel agreements that seek to allocate market shares between exporters and importers, thereby sharing the benefits and burdens of protectionism. Furthermore, VERs restrict exports from specific countries in specific product categories and are generally negotiated on a country-by-country basis. Even though these arrangements are designed to raise prices for consumers (who are excluded from the game), they are supposed to allow a domestic industry to generate profits as well as to allow an exporter to reap scarcity rents. The more stable the cartel arrangement, the greater the likelihood that the domestic industry will become more profitable.

In order to understand cartel stability, it is essential to look at an industry's structure. While the effectiveness of oligopolistic coordination can be affected by many variables, such as the number of sellers in a market and product heterogeneity, cartels cannot function for very

long without high barriers to entry (Chamberlin 1962; Itoh and Ono 1981; Kierzkowski 1984; Scherer 1980). If barriers to entry are low—for example, when there are few scale economies, low capital requirements, and little product differentiation—new firms (or countries) will quickly enter the market when they see abnormally high profits. In an industry such as apparel, where capital requirements are very low and technology is widely available, any effort to create a cartel would immediately draw new entrants and reduce the effectiveness of protection.³ When barriers to entry are high, however—for example, because of high capital requirements (e.g., steel), unavailable technology (e.g., semiconductors), or high levels of differentiation and expensive distribution channels (e.g., autos)—it may take substantial investments and long periods of time for new entrants to take advantage of output restrictions.

The implication of this argument is that the height of economic entry barriers will to a great extent determine a cartel's success. Recall that VERs restrain particular exporters. High barriers to entry are conducive to the success of such an arrangement because under these conditions new exporters, unrestrained by the VER, will be unable to enter the U.S. market. Therefore, high barriers to entry should produce a relatively stable cartel. Conversely, low barriers to entry should vitiate the effectiveness of a VER because unrestrained foreign producers will immediately begin exporting to the U.S. and bid away any economic rents. Instead of reducing import pressure, VERs in industries with low barriers to entry may speed up the diffusion of production to new foreign manufacturers in countries whose exports have not been restricted by negotiated agreements.

The success or failure of VERs helps to determine their evolution over time, because success and failure set in motion

different patterns of political action. To understand how this occurs, we need to make some assumptions about when firms demand trade barriers and under what conditions the United States government will be disposed towards supplying protection. The purpose of these assumptions is to allow us to predict how the initial success or failure of a VER is likely to affect the subsequent evolution of negotiated protectionism in a particular sector. Although we will not provide empirical support for these assumptions, we believe they are plausible and consistent with the existing literature on the politics of U.S. trade policy.

We start by assuming that the *demand* for protection generally intensifies when industries encounter economic distress due to growing import penetration (Baldwin 1986; Lavergne 1983). If firms are satisficers, they are most likely to demand trade barriers only when they confront declining production and profitability.⁴ Furthermore, we assume that large industries with high levels of resources in votes, campaign funds, political organization, and so on will be able to pay more for protection than less well-endowed industries.⁵ And finally, we assume that the more difficult it is for firms to leave the industry—that is, the higher the barriers to *exit*—the more the industry will be willing to invest resources in protection. As Hirschman has argued, the impossibility of exit stimulates voice (Hirschman 1971). Thus the demand for protection by an industry will tend to be a function of economic distress as indicated by profitability and employment trends and of the political resources available and the difficulty of exit.

On the *supply* side, we assume that U.S. governmental policy will not simply mirror industry demand: since the 1930s, many industries have pleaded unsuccessfully for protectionism (Lavergne 1983). This leads us to assert that the U.S. government is not merely a cipher, registering

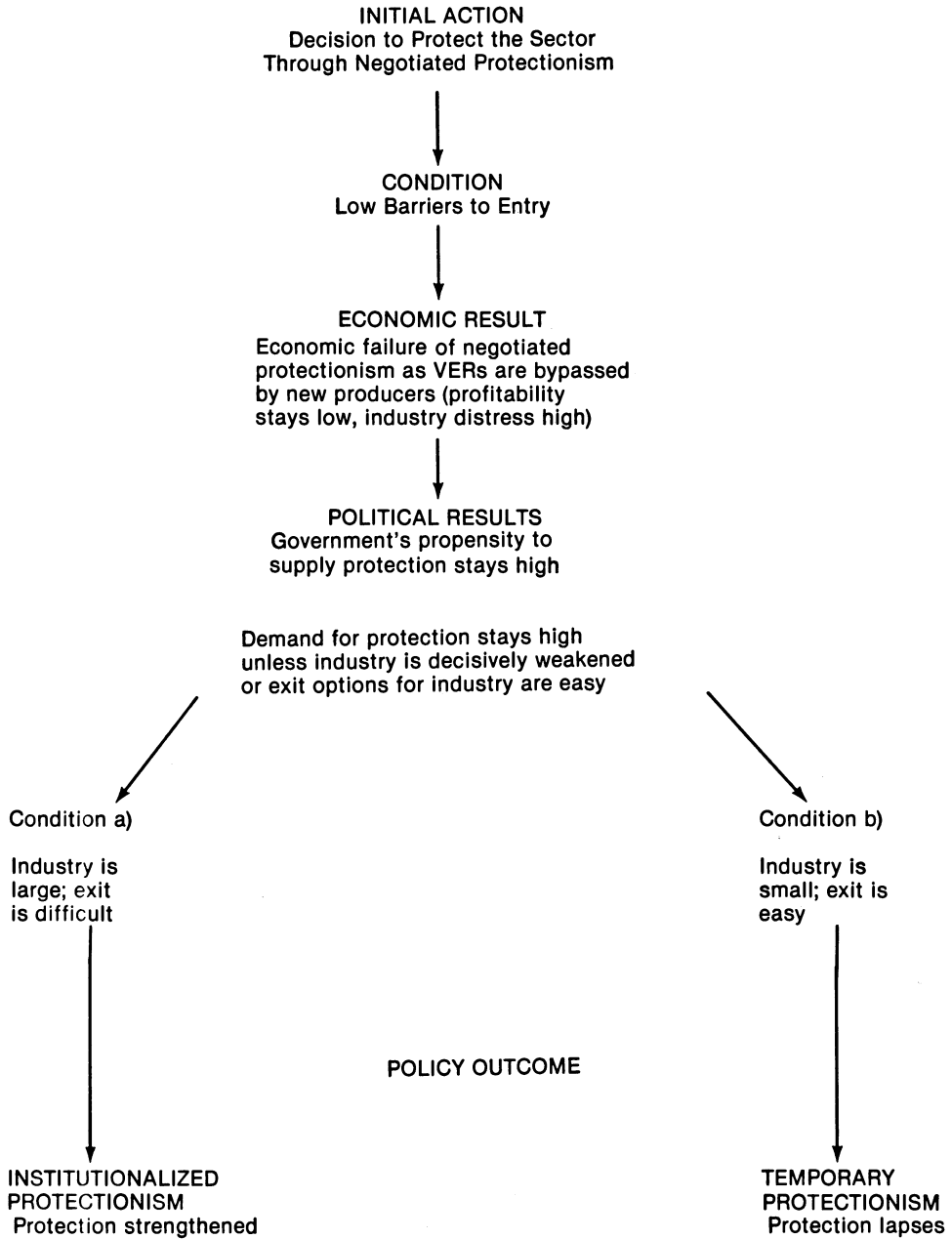
political pressures (Destler 1980). Instead, the willingness to supply protection will be a function of (1) the economic and foreign-policy costs of trade barriers and (2) the values of governmental officials who have their own policy preferences. With regard to costs, the U.S. government would be discouraged from imposing trade barriers if protection adversely affected politically influential domestic actors (e.g., by causing inflation for powerful downstream producers) or led to retaliation by trading partners. Indeed, if the U.S. employed tariffs and auctioned quotas instead of VERs, the inflationary consequences would be more transparent to domestic actors, and the U.S. would be obligated by the General Agreement on Tariffs and Trade (GATT) (Article 19) to provide compensation to its trading partners or allow retaliation.

Similarly, one can reasonably assume that governmental values, which in the case of the United States have been predominantly liberal in the postwar period, will also affect the supply of protection (Baldwin 1986; Goldstein 1986a, 1986b). For the purposes of our model, we assume that liberal values of the United States yield policy preferences that can be summarized in three injunctions:

1. Protection should be accorded only to firms and industries in distress, as manifested by low profitability and declines in employment that appear to result in large part from imports. The U.S. government offers protection to alleviate distress rather than to promote new or innovative industries that have the potential to be highly competitive.
2. Protection should be temporary, enabling industries to adjust, and should be quickly terminated for an industry that regains profitability.
3. If U.S. firms face "unfair" competition from abroad, it is legitimate for the government to provide sufficient protection to offset that unfair advantage.

1987 Negotiated Protectionism

Figure 1. Protectionist Patterns with Low Barriers to Entry



Using these assumptions about the supply of and demand for protection, we are now in a position to sketch our dynamic model. The logic underlying the model is relatively simple and straightforward. If protectionism fails to raise profits for a domestic industry, then, *ceteris paribus*, firms will increase the intensity of their demand for future trade barriers and the U.S. government will generally be sympathetic towards supplying additional protection.⁶ Because we assume that industries work harder for protection when profits are low and that the U.S. government will provide temporary protection for firms in distress, trade barriers that are ineffective are likely to be expanded. On the other hand, if trade barriers improve an industry's economic health, then firms in that industry will reduce the intensity of their lobbying efforts, and the U.S. government will be less receptive to those pleas. Thus, for producers, there is irony behind the success of protection: the more profits domestic firms generate as a result of trade barriers, the more difficult it becomes to justify those restrictions. Today's success in lobbying for protectionist arrangements contributes to tomorrow's failure.

Because the critical issue is the success or failure of negotiated protection, we distinguish at the beginning between industries with high and low barriers to entry. The flowchart in Figure 1 illustrates what happens when barriers to entry are low. Negotiated protectionism will fail to restrict imports because the VERs will be bypassed by new producers. The profitability of domestic firms will stay low, and in view of the values we have ascribed to U.S. officials, the government's propensity to supply protection will remain high. The industry's desire for protection will also remain strong and may even increase. Frustration over continued low profits could lead to a more effective industry organization and an even higher level of protectionist pressure.

If the industry is large and faces high barriers to exit, our model predicts increasing protection: lacking exit possibilities, the industry will intensify its demands by exercising voice, and the government will supply further protection due to continued industry distress. Over time, the government will have to extend the VERs to more and more countries to increase the effectiveness of the protection. As larger numbers of producers become covered by the measures, such protectionism is likely to become institutionalized and may even lead to a system of global quotas, as indicated by outcome *a* in Figure 1.

A strengthening of protectionist pressure, however, is not the only possible result of economically unsuccessful protection. When an industry's *barriers to exit* are also low (Caves and Porter 1976), that industry may contract as firms leave the industry, causing it to lose politically potent resources.⁷ Moreover, firms that anticipate continued competitive pressure from imports may shift from domestic manufacturing to importing, further reducing the demand for protection. If such an industry started off politically and economically weak, the exiting of firms may shrink the industry to such an extent that the remaining firms will no longer have sufficient resources to lobby effectively for added protectionism. Hence, our model predicts that a strikingly different pattern of protectionism will emerge when barriers to entry and exit are both low and the industry is small. Under these conditions, protectionist arrangements will be temporary as firms leave the industry and fewer resources are available for seeking protection (see outcome *b* of Figure 1).

Two other logical possibilities excluded from the chart for the sake of clarity, should also be mentioned. First, if an industry faces low barriers to entry and exit and also happens to be large, we would predict a pattern of institutional-

ized protection that would be unstable in the long run. As long as the costs of lobbying remain lower than the costs of exit, the demand for protection will remain high. Over time, however, this calculus may change. With VERs rather than global quotas, new entrants will continue penetrating the domestic market, industry distress will continue to be high, and domestic firms will increasingly exit. As a result, the industry will become weaker politically. The lobbying cost of protection for the remaining firms will increase, and exit will become even more attractive. In the long run, the industry will lose its critical mass, and the demand for protection will fall off.

A second possibility is that the barriers to exit might be high, and the industry small. Because barriers to entry are low, as in all the cases depicted in Figure 1, new entrants will continue to penetrate the domestic market. The ineffectiveness of protection will lead some firms to disappear or to exit despite the difficulties. This will weaken the industry, making it less and less likely to succeed in securing protection. Therefore, we expect protectionism under these conditions to be temporary, although its duration will be more extended than in the pure case of a small industry with low exit barriers.

In Figure 2, we display our expected sequence of events when barriers to entry are high. Because unrestricted foreign firms cannot immediately enter the U.S. market, protection will be economically successful, resulting in a slowing down of import penetration and higher profitability for domestic firms. In view of the values we have ascribed to the U.S. government, such success reduces the government's inclination to continue providing protection. At the same time, the demand for protection from the industry will also fall as its level of distress eases. In short, we expect protection for industries with high barriers to entry to be temporary in the initial round.

Suspension of protectionism will then lead to another round of import penetration, which under certain conditions may lead to a renewal of protectionism. Once again, our model regards the barriers to exit as an important factor. If firms can easily exit from domestic production, either by ceasing operations, moving production offshore, or becoming importers, the industry's demand for trade barriers will fall and protectionism will not be renewed (condition *a*).⁸

In industries with high barriers to exit that do not adjust during the period of protection, rising import penetration will lead to renewed industry distress (condition *b*) and renewed protectionism. Whether this sporadic protectionism continues depends on whether the barriers to entry fall over time. If the barriers remain high, the pattern of Figure 2 will repeat itself (condition *b1*)—the VERs will be effective, profitability will be restored, and the protectionism will lapse. However, if barriers to entry fall in the meantime—due, for example, to technological change or increased sophistication in developing countries—the subsequent sequence of events will follow the course identified in Figure 1.

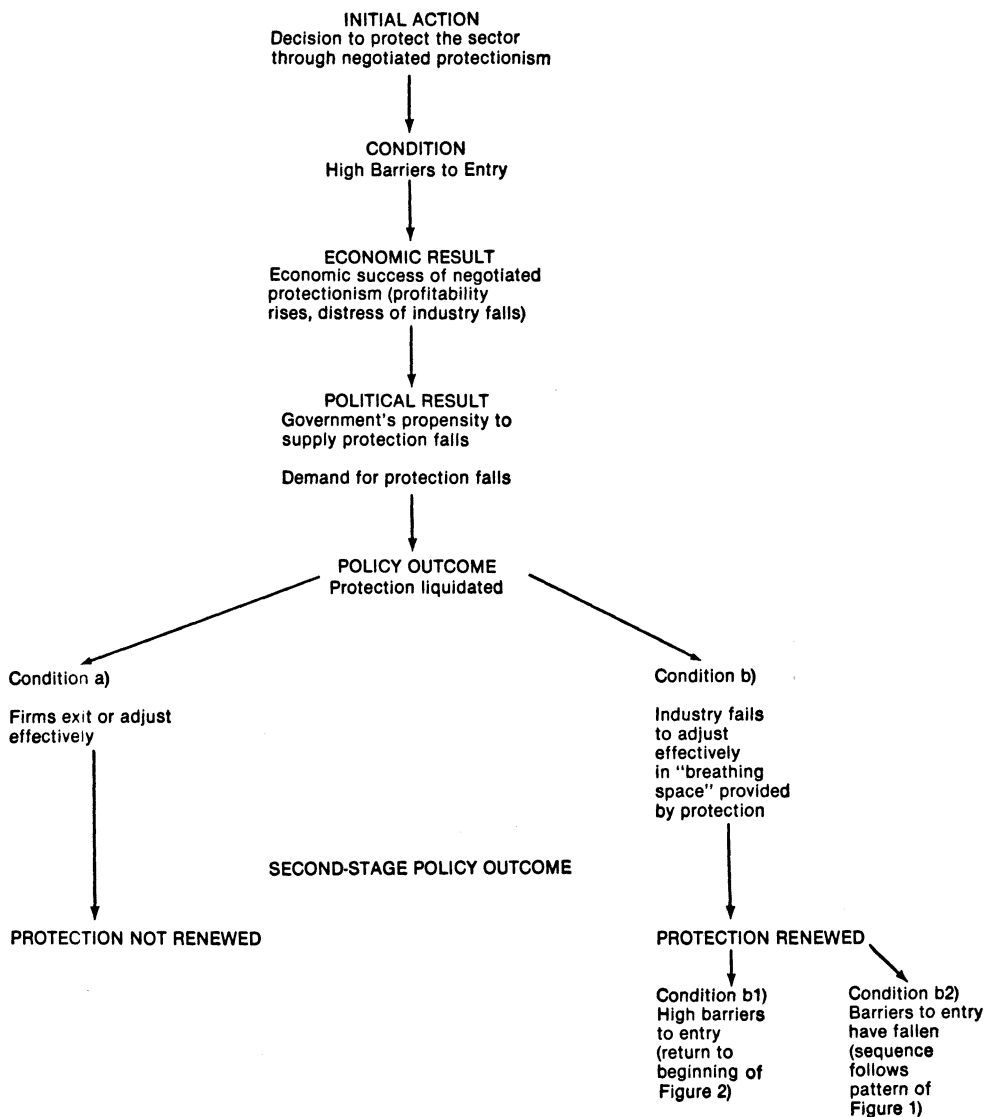
This long-run indeterminacy is a result of the fact that firms exercise choice. Our model provides us only with a first-cut structural explanation for different patterns of protection. We also have to take into account the survival strategies adopted by firms in the protected industries. Although the modal result of unsuccessful protection is renewed protectionist pressure, such pressure will fall if a small industry shrinks substantially as a result of cuts in employment and profitability, or if domestic firms become importers. Conversely, successful protection can lead not only to its own liquidation but to a renewal of protection in the future, depending on the adjustment and exit strategies followed by firms.

This interpretive model of the evolution

of negotiated protectionism is only valuable if it helps us to understand the complex patterns that we observe in industries in which the United States has used VERs and similar restraints to protect domestic

producers. We therefore turn to our empirical material. Does our model illuminate patterns of negotiated protectionism?

Figure 2. Protectionist Patterns with High Barriers to Entry



Illustrating the Model: Five Cases of Negotiated Protectionism

Our model of the dynamics of negotiated protectionism, which focuses on economic barriers to entry, size of the industry, and barriers to exit, should help us to understand the varying patterns of U.S. protection since World War II. To illustrate this model, we will briefly analyze the protectionist patterns in five major industries: textiles and apparel, color televisions, steel, footwear, and automobiles. A summary of these cases is provided in Table 1. Our analysis of the first three cases is interpretive because the model was largely derived from our knowledge of protectionism in these industries. The latter two cases, however, provide us with a partial test of the model's explanatory power. The Reagan administration's decisions to deny further protection to automobiles in the spring of 1985 and footwear the following fall, proved to be remarkably consistent with our expectations.

Institutionalized Protectionism: Textiles and Apparel

The textile and apparel industries, though strikingly different in their industrial characteristics, have followed a joint strategy in securing protection from imports since the late 1950s (Aggarwal 1983). The coalition strategy started to pay off in 1957, when the U.S. government reached an agreement with Japan that limited textiles and apparel exports for a period of five years. The Eisenhower administration opted for a VER largely because the domestic and foreign policy costs of any alternative in the mid-1950s seemed prohibitive. Tariffs or quotas on such a large industry would have been inconsistent with GATT and contrary to

U.S. concerns about the Cold War and U.S. efforts to liberalize international trade. Yet, after the U.S. negotiated this VER with one country, few would have guessed that protectionism in this sector would evolve into the most complex, institutionalized system of restrictions in the postwar period.

Our model of protectionism begins to analyze this problem by looking at the size and characteristics of these industries. With more than two million workers in the mid-1950s, textiles and apparel combined were the largest employers in the manufacturing sector in the United States. Although textiles was more capital-intensive than apparel, both industries could be classified as labor-intensive in the 1950s with relatively low barriers to entry. Capital requirements were low compared to industries like steel; and technology, raw materials, and equipment were readily available. Industry profitability was also low: textiles and apparel mills earned a meager 1.4% and 4.5% return on equity (ROE), respectively, in the mid-1950s, compared to a 9.9% return for all manufacturing (*Congressional Record* 1966, 20985).

Under these conditions, our model would predict that a single bilateral agreement between the United States and Japan would quickly attract new entrants. With low barriers to entry, non-Japanese manufacturers would seek to capture any scarcity rents that might be generated by the proposed cartel, making it difficult to protect the U.S. market effectively. Imports should increase, the profitability of U.S. firms should remain low, and the demand for protection should rise. In fact, the 1957 VER failed to protect U.S. producers (Aggarwal 1985; Yoffie 1983a). Asian exports of cotton manufactures bound for the U.S. boomed. Hong Kong alone increased its shipments from under \$1 million in 1956 to over \$60 million by 1960 (Hunsberger 1964). The combination of rising imports and profits well below

Table 1. Summary of Evidence

Industry	Protectionist Policies	Import Penetration ^a (%)	Pattern
Textiles & apparel	1956 (VER, Japan 1957)	2 ^b	Institutionalized
	1960 (STA/LTA, 1961-62)	6 ^b	
	1970 (VERs 1971)	9	
	1973 (MFA 1974)	9	
	1976 (MFA 2, 1977)	11	
	1980 (MFA 3, 1981)	12	
	1985 (MFA 4, 1986)	23	
Footwear	1976 (OMA, Taiwan & Korea 1977)	48	Temporary
	1981 OMAs dropped	50	
	1984 Protection rejected	70	
	1985 Protection rejected	76	
Televisions	1975	18	Temporary
	1976 (OMA, Japan 1977)	33	
	1978 (OMA, Korea & Taiwan 1979)	26	
	1980 OMA dropped (Japan)	12 ^c	
	1982 OMAs dropped (Korea & Taiwan)	19 ^c	
Steel	1968 (VER, Japan & EEC 1969)	17	Sporadic
	1970	14	
	1971 (VER, Japan & EEC 1972)	18	
	1974 VERs dropped	13	
	1977 (TPM in 1978)	18	
	1981 (VERs, Japan & EEC 1982)	19	
	1984 (VERs 1985)	26	
Autos	1980 (VER, Japan 1981)	27	Sporadic
	1985 VER dropped	32	

^aAll import penetration based on quantity (weight for textiles & apparel).

^bImport penetration for cotton products only.

^cThe drop in import penetration masks the movement offshore of U.S. firms and the direct investment in assembly by foreign producers. Total value-added of TVs manufactured in the U.S. was only 45%-47%.

^dAnnualized rates based on 11 months.

^eTo establish levels of import penetration prior to the conclusion of protectionist agreements, we have gathered data for the years immediately preceding the dates of such agreements. Parentheses are used to indicate that the years for which data are recorded and the years in which agreements were concluded are not identical.

Sources. Textiles. Unpublished chart 4 (Cotton textiles: U.S. Import Trends: Ratio of Imports to Apparent Domestic Markets), Office of Textiles, Market Analysis Division, Department of Commerce, February 1971; United States International Trade Commission (USITC), 1984, A-6. *Footwear.* USITC, 1985, A-15. *TVs.* USITC, 1980, D-6 for 1975-78; USITC, 1984, A-37 and A-105 for 1980-82. *Steel.* American Iron & Steel Institute, 1968-1980. *Autos.* *Ward's Automotive Report*, 1982, 1; "Imported Cars at 32.6% as Domestic Sales Fall," *New York Times*, 5 December 1985, D-1, City Edition. Data also received by telephone from the ITC and American Iron and Steel Institute.

the manufacturing average led both textile and apparel firms to step up their demand for protection (*Congressional Record* 1966, 20985).

Low profitability and rising import penetration gave legitimacy to the textile-apparel coalition's pleas for further protection. Hence, not only was the demand for protection higher, but the government became increasingly willing to supply it. With the foreign policy costs of non-negotiated protection still high, our model would suggest that the United States would expand the cartel to incorporate new players. The proposal by the Kennedy administration to extend textile restrictions in 1961 was therefore consistent with our expectations. The so-called short term arrangement, which was followed by a long term arrangement (LTA), sought to bring new players into the cartel.

Yet, given the industry's structure, even this cartel arrangement was not stable. New players continued to enter and import penetration continued to increase from 6% of the cotton market in 1960 to 12% in 1969 (United States International Trade Commission [USITC] 1978, C-3). More significantly, exporters shifted to unrestrained fabrics (wool, man-made fibers, and blends) to avoid the LTA. Imports rose rapidly—both in quantity and in value. From 213 million square-yard equivalents (SYE) in 1962, man-made-fiber-based imports rose to 1,453 million SYE in 1968. Imports of wool-based products rose from 141 to 210 million SYE in the same period. A similar rapid rise took place in apparel imports (USITC 1978, D-3).

Increased imports strengthened the unity of the textile-apparel coalition largely because the players had limited exit or adjustment options. Minorities and women dominated the work force, and more than two-thirds of the workers in textile and apparel factories were semi-skilled ("Textiles" 1982, 32c). This meant

that labor had little job mobility. For firms, the barriers to exit were growing in textiles because of the increasing capital intensiveness of production. Economic barriers to exit remained low in apparel, but emotional and strategic barriers to exit left firms with limited mobility. Retailers were very large and powerful, precluding forward integration; and the fragmentation of apparel producers into small, single-product companies, made it difficult to expand into overseas production (Porter 1980, chap. 12). The vast majority of apparel firms (28,384 of 31,181) had less than 100 employees, and the top 30 firms accounted for only 7.4% of the industry's value added. Because many apparel firms were family-owned, they would choose divestiture only as a last resort.

While demand for protection continued to increase, resistance to protection on the part of the government waned. Despite protectionism, the industry's return on sales and return on equity rarely climbed above 50% of the manufacturing average. Sympathy for the industry became so strong within the U.S. government that officials were even willing to sacrifice some broader foreign-policy interests. Until the mid-1960s, for instance, Hong Kong had avoided stringent controls on its exports by implicitly threatening to close down the U.S. listening post for China. By 1966, such threats fell on deaf ears (Yoffie 1983a, 111).

The consequence of greater government willingness to supply protection and the increasing demands for trade barriers was the Multifiber Arrangement (MFA) of 1974. Subsequent renewals of the MFA in 1977, 1981, and 1986 transformed the regime into one of the most protectionist instruments of the postwar era. Yet despite the increasing number of textile VERs and the growing restrictiveness of the arrangements, the industry's low barriers to entry have made it impossible to create a stable cartel, especially in ap-

parel. The restrictions simply failed to halt the decline in U.S. apparel employment or improve the competitive position of apparel producers. Japanese and East Asian producers have increasingly moved up-market into middle-range goods, while Association of South East Asian Nations (ASEAN) countries and other less-developed nations have taken over the lower end of the market. Some larger U.S. firms have adapted to import competition by engaging in outward processing while other apparel firms have become importers. Twenty percent of "American" apparel brands were imported in 1984.⁹ Smaller firms that have not found higher-fashion, higher-price-market niches, have been increasingly forced to exit. The result is that the U.S. apparel industry ran a trade deficit of over \$13 billion in 1984 (American Textile Manufacturers Institute [ATMI] 1985, 24).

The industrial characteristics of textiles have allowed manufacturers to become more competitive with imports. Textile employment has fallen by about 10% since the 1960s, but greater capital inputs have led to significant improvements in productivity. The textile industry, helped by cheap, regulated oil prices, even became a net exporter during the late 1970s. However, the deregulation of oil prices and the rise in the value of the dollar again squeezed the profitability and domestic-market share of textile manufacturers in the early 1980s.

In the aggregate, therefore, the industries comprising the textile-apparel coalition have experienced rising levels of import penetration and poor average profitability since the late 1950s, thus increasing the demand for protection. Barring large-scale exit from the textile and apparel industry or a new technology that would radically change industry structure, our model leads us to expect that institutionalized protectionism in this sector will become even more restrictive in the future.

Temporary Protectionism: Color Televisions and Footwear

Although faced with competitive problems similar to those of textiles and apparel, the television and footwear industries did not succeed in securing steadily expanding protection. Instead, the VERs of the 1970s in both industries were allowed to lapse. The demand for protection in these sectors was not as strong as in textiles and apparel. Not only were these industries relatively small, but lower barriers to exit weakened the merits of the industry's case for protectionism and reduced corporate demand for trade barriers over time.

Color Televisions. Imports of television sets into the United States started to grow when Japanese companies captured a large share of the monochrome market in the mid-1960s (Millstein 1983; Yoffie 1983a). By the early 1970s, Japan made inroads into the color market, accounting for 15% of U.S. consumption in 1975. One year later, imports had surged to 33% of the market, Japan alone taking a 30% share (USITC 1980, D-6).

Pressure for protection had been mounting since 1970, when Zenith Corporation first filed a countervailing duty suit. Over the next seven years, various legal suits were filed by Zenith and other industry and labor groups, but none yielded any immediate benefits. The government continually refused to supply protection to this relatively small industry (40 thousand workers in 1973 and only 26 thousand in 1976). The Carter administration altered this position, however, when the International Trade Commission (ITC) recommended tariffs in response to a Section 201 complaint (the U.S. counterpart to GATT Article 19) and several of the law suits filed by Zenith appeared to be bearing fruit in the courts. To undercut this growing protectionist sentiment and preserve important foreign policy

1987 Negotiated Protectionism

goals related to the Tokyo round of trade talks, the Carter administration negotiated a three-year OMA with Japan that began on 1 July 1977. The agreement limited Japanese exports to 1.56 million units per year and included a provision exempting sets in which 40% of the labor costs involved U.S. workers.

On the basis of our model, protectionism in this sector should be temporary, largely because the barriers to entry were moderate-to-low, the industry was small, and firms had viable adjustment options. By the mid-1970s, the color TV industry was relatively concentrated, with two firms—RCA and Zenith—accounting for 40% of the market. Other firms had liquidated their investments or sold their assets to the Japanese. Because all of the major producers of TVs except Zenith were diversified companies, divesting the unprofitable TV business did not mean life or death. Moreover, TV firms were large by textile and apparel standards and, in most instances, already multinationals. This made it relatively easy for firms to move offshore to reduce labor costs. In fact, RCA never joined in the battle for protection with Zenith precisely because it had already shifted much of its production offshore by 1977 and had licensed color television technology to the Japanese as early as 1962.

Barriers to entry in the industry were higher than in textiles and apparel, but surmountable. South Korea and Taiwan already had the necessary technology and were positioned to fill any gap in demand left by a reduction in Japanese exports. In 1978, Taiwan shipped 624 thousand sets (up from 235 thousand in 1976). Korean TV exports to the United States increased from 47 thousand in 1976 to 437 thousand in 1978 (USITC 1984, A-37). As a result, both profits and worker employment in the domestic industry continued to drop.¹⁰

The growth in imports led to only a temporary increase in protectionism.

Within four months of the OMA, Zenith decided to close its domestic plants, move offshore, and lay off one-quarter of its labor force. This action decisively weakened the protectionist coalition. The major remaining supporters of protection were labor, firms that supplied TV components and, ironically, two Japanese firms—Sony and Matsushita.

Under the terms of the OMA, the United States was obligated to restrict new entrants if Japanese manufacturers were placed at a disadvantage. This led the Japanese firms producing in the U.S. to pressure the U.S. government for equitable treatment by negotiating OMAs with South Korea and Taiwan. The U.S. government therefore proceeded to sign agreements with these two countries in December 1978, with the accords to run from February 1979 to June 1980. By the end of 1979, the U.S. dropped the OMA with Japan but extended the ones with South Korea and Taiwan for two years. Both of these agreements were then allowed to expire in 1982.

Korea and Taiwan each increased exports by almost 250% after the OMAs expired. But despite the increased imports and low industry profitability, demand for protection did not rise significantly. By 1984, 17 producers were assembling televisions in the United States, of which 12 were foreign-owned (USITC 1984, A-8). Zenith, formerly the major force for protection, increased its overseas activities and diversification efforts, becoming in the process a more profitable company involved in the production of computers and computer accessories. As expected, then, protectionism in color TVs remained temporary: the government had little incentive to supply protection, and the relocation of production weakened the demand for trade barriers.

Footwear. The footwear industry, like the color TV industry, had been petitioning the government for protection for almost 10 years before it achieved any substan-

tive results (Yoffie 1983b). When imports reached almost 50% of the market in 1977, the ITC recommended that tariffs be raised on nonrubber shoes. Faced with its first important trade case, the Carter administration decided to seek OMAs with Taiwan and Korea. It explicitly avoided the ITC recommendation for tariffs because it feared the transparent inflationary consequences. OMAs had the additional advantage of allowing the U.S. to avoid conflicts with important trade partners and allies, such as Italy and Spain.

The footwear industry, like textiles and apparel, has very low barriers to entry. Because the capital requirements were minimal and the technology has been stable, it would be a simple matter for other countries to increase their exports in response to the OMAs. Hence it was no surprise that imports increased by 60% from 1977 to 1978 and unrestrained countries such as Hong Kong and the Philippines increased their exports by 225% and 800%, respectively. If exit or adjustment options were constrained, as they were in textiles and apparel, we would predict that the industry's profitability would suffer, increasing the demand for protection. The government would also be sympathetic under these conditions, especially if it could minimize foreign policy costs by targeting the new, politically weak entrants, such as Hong Kong and the Philippines.

Yet this scenario did not occur. The critical difference between footwear and textiles lay in their industrial structures and the strategies available to major firms. The 20 largest footwear firms, representing about 50% of production, had viable exit strategies that allowed them to profit during the OMAs. Although profits of smaller firms suffered under the OMAs, large firms pursued strategies of forward integration into the highly fragmented retailing business and began importing footwear they could not make

competitively. While manufacturers of less than one-half million pairs of shoes earned only a 4% return on sales (ROS) during the late 1970s, profits of producers of more than two million pairs rose from about 6% ROS before the OMAs to 9.4% by 1980. These differentials in performance split the industry and reduced the aggregate demand for protection when the OMAs came up for renewal in 1981.

On the supply side, the belief that protection should be temporary and terminated—once profitability was restored—undermined the case for further protection. Thus it is no surprise that the Reagan administration allowed the OMAs to lapse. One of the most interesting developments was that Korea and Taiwan maintained their own VERs after the U.S. opted for free trade in 1981. Because both East Asian governments had found advantages in the cartel (it allowed them to raise prices and pushed their producers into higher-value products), they continued to limit exports in order to keep prices up and to force domestic producers into the high-end markets.

Once protection was terminated, our model would predict that small firms would continue to demand trade barriers but that large firms would have less and less incentive to seek protection. This led us to the prediction that as long as large firms continued to exit and pursue profitable retailing and importing strategies, the government would not grant a second round of protection for the footwear industry.

Twice in the last three years, this prediction has proven accurate. Between 1981 and 1985, imports grew from 50% of domestic consumption to almost 80%. Nonetheless, the industry has been unsuccessful in its efforts to regain protection. In 1984, the ITC refused to recommend trade barriers in response to a Section 201 petition because large footwear firms had become more profitable than the manufacturing average. A year later, however,

Congress changed the trade laws, partially in response to the footwear case. The new law dictated that the ITC could not reject a 201 case solely on the grounds of a single indicator, such as the level of industry profits. As a result, the ITC reversed its decision and recommended restrictions for the footwear industry in 1985. Yet the divisions within the footwear industry weakened the demand and the resources that the industry was able to mobilize. The president's eventual rejection of trade barriers was therefore understandable in light of our model.

Sporadic Protection

Thus far, we have only looked at industries with low barriers to entry, where it has been difficult for the U.S. government to create a stable cartel that would help U.S. manufacturers regain their profitability. The steel and automobile industries, however, were both characterized by high barriers to entry. In such cases, we would expect negotiated protection to allow firms to achieve higher profits—at least temporarily. If this is the case, then protection should be liquidated because the government will be reluctant to provide protection for an industry no longer in distress. Yet unless an industry makes fundamental adjustments in these cases, this favorable position will rapidly erode and the industry may again seek protection. The U.S. steel industry illustrates this pattern.

Steel. The U.S. steel industry first faced import competition in the late 1950s. Imports captured an increasing share of the U.S. market, rising from 4.7% in 1960 to 12.2% in 1967 and surging to 16.7% in 1968. Growing imports and declining profitability led the industry to seek protection. In 1969, the United States negotiated three-year VERs with the two major exporters: Japan and the EEC. The U.S. preferred a negotiated solution because

the costs of imposing a tariff or quota on such large exports of important allies were perceived as high. Although the negotiated agreements cut exports from Japan and the EEC by 25%, they provided enough flexibility to allow both importers and exporters to benefit.¹¹

Unlike textiles and apparel, footwear, and TVs, steel had comparatively high barriers to entry, especially in the late 1960s. Capital and technology requirements were high, making it difficult for new entrants to capture any significant scarcity rents generated by the VERs. Because Japan and the EEC were the only viable exporters to the U.S. in the late 1960s, our model would predict that the agreements should have produced higher profits for U.S. firms. In the short run, the VERs did produce a drop in import penetration from 16.7% of consumption in 1968 to 13.8% in 1970, but the industry continued to suffer financially. The 1970 recession cut the average return on equity in steel to 4.3%, less than half the average of manufacturing (Crandall 1981, 29). This poor performance combined with an increase in imports from a few unrestrained European countries in 1971 strengthened the demand for protection and led the administration to extend the VERs in 1972 for three more years.

This time the agreements were more specific, and the cartel more effective. Imports dropped from 17.9% of the market in 1972 to between 12% and 13% over the next two years. Equally important, the steel market boomed and the U.S. industry's profits rebounded. Return on equity jumped to 16.9% in 1974, two percentage points *above* the manufacturing average. U.S. steel workers were also rewarded during this period. Between 1969 and 1975, steel wages went from 4% above the manufacturing average to 67% above average. This rebound reduced the government's willingness to protect the industry, and protection was liquidated at the end of 1974.

Had U.S. steel firms used their six years of protection to adjust or exit the industry, the industry would not have renewed its demand for protection. But the industrial characteristics of this industry made exit or significant adjustment very costly. As Crandall (1981) has argued, it has been pointless for U.S. manufacturers to reinvest in greenfield facilities. There was so much excess world capacity in steel that the discounted returns from such an investment would have been negative (Borrus 1983). The option of going abroad was also unavailable to U.S. firms because most countries encourage the development of indigenous steel industries. The only option for large integrated producers was to use the profits resulting from restraints to buy assets in more promising industries—a strategy that would take a long time to implement, given the huge fixed-asset base of all large steel firms.

Because the industry had made no fundamental adjustment (and, in fact, was less competitive after the VERs owing to high wages), imports increased, especially as new entrants in foreign countries overcame the capital and technology barriers to entry. They reached almost 18% of the market in 1977 as countries other than Japan, the European Economic Community (EEC), and Canada increased their share of U.S. apparent consumption from 1.2% to 4.1% of the market (Crandall 1984). The addition of 67 thousand steel workers to the unemployment lines between mid-1976 and mid-1977 plus a drop in average return on equity to close to the lowest among U.S. manufacturers raised the demands for protection once again (U.S. Congress 1977, 323). Politically, the industry was in a strong position to secure some form of import restraints. Various firms filed antidumping suits, which would have had high foreign-policy costs if the treasury found they had merit. In addition, the steel industry had very strong congressional support.

To head off costly protectionist legislation introduced in Congress, the Carter administration sought a negotiated solution that would share the burden of adjustment between the United States and its trade partners. Under Secretary of Treasury Anthony Solomon devised a solution called a trigger price mechanism (TPM), which set a minimum price based on Japanese production costs, below which there would be an automatic presumption of dumping with a threat of countervailing duties. President Carter pushed the EEC and Japan to accept the imposition of this system in return for the manufacturers dropping their antidumping petitions (Crandall 1981). By basing the TPM on the lower Japanese costs, it forced some of the burden of adjustment on the U.S. firms. It also allowed producers in the U.S., Japan, and the EEC to raise prices, as if it were a legal cartel.

However, an effective cartel could not last. Barriers to entry had effectively fallen by the late 1970s, making it harder to create a stable cartel and thereby raising the demand for protection. Because most major exporting countries in the world had developed a capacity to manufacture steel by 1979, the system of targeting protection against one or two countries became obsolete. By the early 1980s, the TPM was dropped, only to be replaced by a new VER with Europe. Despite occasional tactical maneuvers by the U.S. government and U.S. firms that have produced a few months of free trade in steel, trade restrictions have been maintained nearly continuously. By 1985, negotiated protectionism in steel had been expanded to all major exporting countries, making it look more and more like the system of protection in textiles and apparel. Not only has the demand for protection continued to be strong, but because most foreign governments subsidize steel exports, the U.S. government has been willing to intervene on the basis of "fair play" in international trade.

According to our model, steel should

1987 Negotiated Protectionism

continue to follow the path of textiles and apparel. Because barriers to entry have dropped over the past 15 years, a stable cartel has become unlikely. The only possibility that steel might follow a different path would occur if steel companies adjust or exit the industry. Both possibilities exist (Gutfleish, n.d.). The steel industry has become increasingly differentiated. Some producers have reorganized, reduced wage costs, and a few have become profitable with a greatly reduced product line.¹² The U.S. minimills—with their specialized products, modern electric furnaces, and labor that have not joined the United Steel Workers—have been able to compete successfully with imports. In 1980, minimills achieved a 14% return on equity—twice that of integrated steel producers (Walter 1981). In addition, some U.S. steel producers have begun importing steel products, and a few foreign firms have bought U.S. firms in the hope of evading protection.¹³ Lastly, some U.S. steel companies have diversified out of steel production. Although steel firms have not been profitable, they have generated huge cash flow from the depreciation of their large fixed assets, which they have used to reduce their dependence on steel.

In sum, as more steel firms diversify and as minimills expand, the demand for protection could fall. As the industry splinters, its efforts to expand protectionism will be less and less likely to succeed. If, however, the diversification strategies falter, steel is likely to follow the path of textiles and apparel. The industry has the resources and the organizational strength to demand a high level of protection. Because the industry continues to be in distress and foreign countries subsidize their steel exports, the U.S. government is likely to regard protection as legitimate on grounds of fair trade.

Automobiles. The automobile industry provides a partial test to evaluate our model of the dynamics of negotiated pro-

tectionism. Because the barriers to entry have been high, VERs in autos should initially be successful in economic terms, leading to a reduction in protectionist pressure. Yet, as foreign producers outside of Japan overcome the barriers to entry, protectionist pressure is likely to reemerge. Unless auto firms exit the industry or make fundamental adjustments that improve their competitive positions, autos will follow a path similar to steel.

Historically, U.S. car manufacturers and U.S. auto workers supported free trade. Labor shifted its view toward the beginning of the 1970s, and the firms' position changed in 1979. In the wake of the second oil shock, U.S. citizens suddenly wanted small fuel-efficient cars, which Detroit was unable to provide. Japanese manufacturers filled the gap and Japan's market share jumped from 12% of consumption in 1978 to 20% in 1980. In 1979–80, the big three auto manufacturers closed 23 plants and sustained collective losses of four billion dollars. Auto unemployment increased to 26% in this period (U.S. Department of Transportation 1981).

By the end of 1980, the auto industry had formed a united front in favor of protection. The United Auto Workers (UAW), Ford Motor, and Chrysler led the charge, while General Motors, the firm best positioned to deal with the Japanese, reluctantly joined the coalition. Despite a rejection of a UAW-Ford Section 201 petition by the ITC, the industry used its considerable resources to pressure the administration to negotiate a VER with Japan in 1981. Like other cases of negotiated protection, the VER was designed to appease the domestic industry, avoid the transparent inflationary consequences of quotas, and avoid the high foreign-policy costs of directly violating GATT. The terms of the agreement represented significant give-and-take between Japan and the U.S.

Although the Japanese agreed to cut back their exports 8% from the previous year to 1.68 million cars, the agreement was extremely flexible and offered the Japanese opportunities to offset their potential volume losses.¹⁴

To understand the pattern of protectionism that would emerge in autos, we begin again with the barriers to entry, which in this case were extremely high. Not only were technology and capital requirements very large, but new firms require marketing and servicing capabilities to enter the U.S. Unless a foreign manufacturer enters into a joint venture with a U.S. or Japanese company to market its cars, it could take five or six years for a strong competitive threat to be mounted by new countries. Furthermore, other automobile manufacturers in unrestrained countries, such as Renault, Volkswagen, and Volvo, had a tiny share of the U.S. market, and they did not have the capacity to increase sales fast enough or in sufficient quantity to upset the stability of the cartel-like arrangement. Our model would therefore expect the cartel to be effective in raising the profitability of both the Japanese and the U.S. manufacturers, which in turn would reduce both the demand for protection and the government's willingness to supply it. As prices rose and profits increased, the legitimacy of protection for autos would weaken and firms would reduce their demand for trade barriers. The VER should have been allowed to lapse when the industry recovery took hold.

The VER had the predicted effects. Japanese manufacturers raised the prices on their cars, which allowed U.S. producers to increase their prices by an average of \$2,000 per vehicle. Profits for the big three auto manufacturers rose from a \$4-billion loss in 1980 to a \$7.7-billion profit in 1983, and a \$10-billion in 1984—their best year in history. Profit margins, including nonauto businesses,

also rose from 1.73% in 1980 to 11.78% in 1983. These margins allowed the U.S. companies to generate badly needed cash flow. Working capital for U.S. auto firms increased from \$0.9 billion in 1982 to \$8.1 billion in 1984 (Auto and Truck Industry 1986, 101). Most Japanese auto manufacturers also achieved record profits in the United States during this period. Japanese profit margins averaged \$2,000 per car under the VER in the U.S. market, which compared with \$85–\$125 per car profit in the Japanese market ("Profits" 1984, 68). The only unhappy Japanese producers were those with low exporting records before 1981: Mitsubishi, Fuji, Isuzu, and Suzuki would have preferred greater volume to the higher margins. Although Japanese car exports hovered between 1.7 and 1.9 million units from May 1981 to May 1985, the value of those exports rose from \$8.8 billion before the VER to an approximately \$12.4 billion in the year ending May 1985. This was especially impressive considering that the yen dropped in value by more than 10% during this period (Reagan 1985, 351).

Our model would lead us to expect that the record profits on both sides of the Pacific would reduce the demand for protection by U.S. manufacturers. When General Motors abandoned the protectionist coalition in 1985, it was only a matter of time before the VER would be dropped. Furthermore, the high level of profits and high costs of cars should have meant that the government would find little legitimacy in protecting highly profitable firms, especially with car prices rising. Thus, the decision by the Reagan administration to abandon the VER in May 1985 was consistent with our expectations. The decision by the Japanese government to maintain a VER, albeit at a higher level of exports, after President Reagan decided not to renew the agreement, was also not surprising. Because Japan prospered under the protectionist arrangement, the Japanese government

and the large Japanese firms would want to maintain the cartel.¹⁵

Whether the auto industry will follow the route of steel depends in large part on the barriers to exit and available adjustment strategies. As in steel, the barriers to entry are increasingly being overcome by new entrants attracted to the high potential profits in autos. Yugoslavia and Korea both began shipments to the U.S. market in late 1985 and early 1986. What could differentiate the pattern of automobile protection from that in steel is that there are more avenues of adjustment open to auto manufacturers. First, capital is more mobile in automobiles: as in color TVs, auto firms can move their production offshore to reduce wage rates and increase their cost competitiveness. Second, improved automation, lower wage rates, higher productivity, and a substantially lower value of the dollar could also reduce relative costs to make U.S. firms more viable. Finally, enhanced design, quality control, and marketing capabilities could make U.S. companies competitive with the Japanese, even if there are cost differentials. Any combination of these options by the major U.S. producers could keep the demand for protection from rising.

In sum, if U.S. firms internationalize more of their production, and continue increasing their productivity, they may be able to fend off a new onslaught of imports, especially if they are aided by a continued fall of the dollar against the yen. The result would be another case of temporary protection. If, however, U.S. firms fail to improve their competitiveness, then the demand for trade barriers will again intensify, profits will fall, and protection is likely to be renewed.

Conclusion

Our model helps us to understand the evolution of negotiated protectionism as

practiced by the United States over the last quarter century. After its initiation, protectionism displays various patterns, which can be characterized as *institutionalized*, *temporary*, and *sporadic*. These patterns are accounted for not by conventional variables, such as import penetration, but by less-noticed factors such as barriers to entry and costs of exit from domestic production, as well as the ability of firms to adjust.

U.S. protectionism has become institutionalized in textiles and apparel because these large industries face low barriers to entry and their firms do not have attractive exit options. On the whole, such protectionism has been economically unsuccessful. Imports have continued to rise and industry profits have remained low. Temporary protectionism in the United States has appeared in industries that are relatively small (color televisions, footwear) and that confront low barriers to entry. Yet the ability of major firms in these sectors to devise effective exit strategies has meant that the economic failure of protection has not been translated into political success for protectionist forces.

Sporadic protectionism characterized the early years of trade barriers in steel. The economic success of import restraints resulted from high barriers to entry into the industry and led in turn to a decline in political support for protection. In the absence of effective adjustment by domestic firms, the ensuing decline in protection led to increased imports and renewed trade restrictions. Recently, barriers to entry to the steel industry have fallen and, as our model anticipates, protection has been extended to more countries and products, becoming increasingly institutionalized and rigorous. The history of the first auto VER in the early 1980s followed a similar pattern to that in the early years of steel: the economic success of protection led to a dismantling of restraints. Whether auto protection will

turn out to be temporary or will recur depends in large measure on the effectiveness of the adjustment strategies pursued by domestic firms and the ability of non-Japanese foreign firms to overcome the barriers to entry.

Although our model does not allow us to make precise predictions of the trajectory of negotiated protectionism, it does provide some insight into this process. Negotiated protectionism as practiced by the United States has been neither linear nor cyclical but has followed more complex patterns. Economically ineffective protection often leads to political pressures for more extensive and highly institutionalized restraints on trade. By contrast, economically successful protection that increases profitability generates counterpressures that enhance the likelihood of protectionism's temporary demise. Protectionism's economic failures are often its political successes and vice versa. The dynamics of negotiated protectionism can only be understood by untangling the complex and dialectical relations between its political and economic components.

Notes

A version of this paper was presented at a conference on the political economy of trade in January 1986 sponsored by the National Bureau of Economic Research. We are grateful to the Bureau for its support and particularly to Robert E. Baldwin and Stephen P. Magee for helpful comments. Ronald Gutfleish, Elizabeth Norville, and Sigrid Bergenstein provided valuable research assistance. Excellent critiques of earlier drafts were offered at research colloquia at Berkeley and Stanford in 1985 and at Brandeis and Rochester in 1986.

1. Despite formal legal differences between OMAs, VERs, and other types of negotiated protectionism, we treat these restrictions as functionally identical and will usually use the term VERs.

2. We include textiles and apparel in a single category not because they exhibit similar industrial characteristics but because they have successfully identified themselves as a single industry in political bargaining. The adjustment strategies and survival potential of the two industries differ significantly, as

we indicate later in this paper; and it was not a foregone conclusion that they would get together in the first place (Aggarwal 1983).

3. Strictly economic judgments can also be complicated by political calculations. A strictly economic model incorporating rational expectations would hold that firms should not enter a market if they expect that future protectionism will make their investment unprofitable. Yet governments may decide to build textile or steel industries for reasons of security or national pride or because they expect positive externalities to ensue.

4. Maximizing firms, especially monopolists and infant industries, might anticipate future declines in profits and demand protection even in the absence of economic distress (McKeown 1984).

5. In our case studies, we use the industries' total revenues and employment as proxies for industry size. Since three of the industries are very large by these criteria and two are much smaller by an order of magnitude, our cases permit us simply to dichotomize this variable. A fully specified model would require more sophisticated measures. Revenue and employment data for our five industries at about the time of the first VER in the industry are as follows:

	Employment	Revenues (\$)
Textiles & Apparel (1958)	1,842,274	25.9b
Steel (1969)	436,400	22.3b
Color TVs (1976)	26,967	2.1b
Footwear (1977)	225,000	6.83b
Autos (1981)	1,205,000	118.3b

6. The *ceterus paribus* means no significant swings in the business cycle, no significant reduction in an industry's resources, and no significant exit by domestic firms. The latter two assumptions will be relaxed in the analysis.

7. Exit barriers are defined as "impediments to the removal of excess resources from an industry" (Caves and Porter 1976, 39). These impediments include not only fixed capital assets but also managerial and strategic impediments to leaving an industry. As Caves and Porter demonstrate, intangible factors, such as links to downstream and upstream operations (i.e., strategic barriers) and loyalty to a particular business or community (i.e., emotional barriers) may be just as significant as fixed investment in industry-specific assets.

8. It is conceivable that firms in an industry could use temporary protectionism as a "breathing space," to enable them to compete effectively with foreign industry, even without import barriers. This would also lead to a decline in pressures for protection.

9. Hank Gilman, "Clothing Shoppers Talk Domestic but Look First for Style, Savings," *Wall*

1987 Negotiated Protectionism

Street Journal, 15 October 1985, p. 35, Western edition. "Outward procening" refers to work performed abroad on materials exported from the United States that can be reimported with duty paid only on the value added, under section 8.07 of the U.S. Tariff Code.

10. The ratio of profits to sales in 1976 was 3.7%; by 1978 it had fallen to 1.5%. In the same period, employment in the industry fell from almost 27 thousand to under 24 thousand (USITC 1980, D-6).

11. The quantitative restraints pushed the EEC and Japan to produce higher-value steel and carve out market shares in higher-tech production. Although their import shares were cut from 8.4m and 7.3m tons respectively to 5.8m tons each, the value of their 1970 shipments was the same in 1970 as in 1968 (Adams and Dirham 1979, 98-99).

12. Daniel F. Cuff, "Forging a New Shape for Steel," *New York Times*, 26 May 1985, sec. F, pg. 4. Eastern edition.

13. Thomas F. O'Boyle and Doron Levin, "Wheeling-Pittsburgh Agrees on Venture in U.S. with Japan's Nishan Steel Company," *Wall Street Journal*, 8 February 1984, pg. 3, Eastern edition.

14. The United States accommodated the Japanese demands that trucks be excluded (which also meant the popular minivans that sold well in the United States in the early 1980s); that inventory estimated at four hundred thousand units be excluded from the quota; and, lastly, that Japanese producers would share in any growth in the U.S. car market after 1981 (Yoffie 1983a).

15. Japan was under severe pressure from the United States Congress, although not apparently from the executive, to maintain restraints. We attribute congressional pressure largely to concern about the huge overall U.S.-Japanese trade deficit, rather than to solicitude for the auto industry itself; this case therefore seems to provide support for our argument. If one viewed Japanese restraint as merely an informal continuation of the VER, in response to pressure from the U.S. automobile industry, this case could be regarded as an anomaly for our argument.

References

- Adams, Walter, and Joel Dirham. 1979. Unfair Competition in International Trade. In *Tariffs, Quotas, and Trade: The Politics of Protectionism*, ed. author. San Francisco: Institute of Contemporary Studies.
- Aggarwal, Vinod K. with Stephan Haggard. 1983. The Politics of Protection in the U.S. Textile and Apparel Industries. In *American Industry in International Competition: Government Policies and Corporate Strategies*, ed. John Zysman and Laura Tyson, 249-312. Ithaca: Cornell University Press.
- Aggarwal, Vinod K. 1985. *Liberal Protectionism: The International Politics of Organized Textile Trade*. Berkeley: University of California Press.
- American Iron and Steel Institute. 1968-80. *Annual Statistical Report*. Washington, DC: Author.
- American Textile Manufacturers Institute. 1985. *Textile Highlights*. March.
- Auto and Truck Industry. 1986. *The Value Line Investment Survey*. 28 March.
- Baldwin, Robert E. 1986. *The Political Economy of U.S. Import Policy*. Cambridge: MIT Press.
- Bauer, Raymond A., Ithiel de Sola Pool, and Lewis Anthony Dexter. 1972. *American Business and Public Policy: The Politics of Foreign Trade*, 2d ed. Chicago: Aldine-Atherton.
- Bergsten, Fred C. 1975. On the Non-Equivalence of Voluntary Export Restraints and Quotas. In *Toward a New World Trade Policy: The Maidenhead Papers*, ed. author, 239-271. Lexington, MA: D.C. Heath.
- Borror, Michael. 1983. The Politics of Competitive Erosion in the U.S. Steel Industry. In *American Industry in International Competition: Government Policies and Corporate Strategies*, ed. John Zysman and Laura Tyson, 60-105. Ithaca: Cornell University Press.
- Caves, Richard, and Michael Porter. 1976. Barriers to Exit. In *Essays on Industrial Organization in Honor of Joe S. Bain*, ed. Robert G. Masson, et al., 36-69. Cambridge, MA: Ballinger.
- Chamberlin, Edward H. 1962. *The Theory of Monopolistic Competition*, 8th ed. Cambridge: Harvard University Press.
- Cline, William R., ed. 1983. *Trade Policy in the 1980s*. Washington: Institute for International Economics.
- Congressional Record. 1966. 89th Cong., 2d sess. Vol. 112, pt. 16.
- Crandall, Robert. 1981. *The U.S. Steel Industry in Recurrent Crisis*. Washington: Brookings Institution.
- Crandall, Robert. 1984. The EEC-U.S. Steel Trade Crisis. Paper presented at the College of Europe Symposium on European-American Trade Relations and Global Economic Interdependence, Bruges.
- Destler, I. M. 1980. *Making Foreign Economic Policy*. Washington: Brookings Institution.
- Goldstein, Judith. 1986a. The Political Economy of Trade: Institutions of Protection. *American Political Science Review* 80:162-84.
- Goldstein, Judith. 1986b. Ideas, Institutions, and American Trade Policy. Paper presented at the National Bureau of Economic Research (NBER) Political Economy of Trade Conference, Dedham, MA.
- Gutfleish, Ronald. N.d. Why Protection? U.S. Corporate and State Response to a Changing World Economy. Ph.D. diss., University of California,

- Berkeley. Forthcoming.
- Hirschman, Albert O. 1971. *Exit, Voice, and Loyalty*. Cambridge: Harvard University Press.
- Hunsberger, Warren. 1964. *Japan and the United States in World Trade*. New York: Harper and Row.
- Itoh, Makoto, and Yoshihiko Ono. 1981. Tariffs, Quotas, and Market Structure. *Quarterly Journal of Economics* 96:295-305.
- Kierzkowski, Henry K., ed. 1984. *Monopolistic Competition in International Trade*. Oxford: Oxford University Press.
- Lavergne, Real P. 1983. *The Political Economy of U.S. Tariffs*. New York: Academic Press.
- McKeown, Timothy. 1984. Firms and Tariff Regime Change: Explaining the Demand for Protection. *World Politics* 36:215-33.
- Millstein, James. 1983. Decline in an Expanding Industry: Japanese Competition in Color Televisions. In *American Industry in International Competition: Government Policies and Corporate Strategies*, ed. John Zysman and Laura Tyson, 106-41. Ithaca: Cornell University Press.
- Pastor, Robert A. 1980. *Congress and the Politics of U.S. Foreign Economic Policy 1929-1976*. Berkeley: University of California Press.
- Porter, Michael E. 1980. *Competitive Strategy: Techniques for Analyzing Industries and Competitors*. New York: Free Press.
- The Profits Lie Abroad. 1984. *The Economist*, 14 July, 68-69.
- Reagan, Ronald. 1985. *Economic Report of the President*. Washington: GPO.
- Schattschneider, Elmer E. 1935. *Politics, Pressures, and the Tariff*. New York: Prentice-Hall.
- Scherer, Frederic M. 1980. *Industrial Market Structure and Economic Performance*. Chicago: Rand McNally.
- Strange, Susan. 1985. Protectionism and World Politics. *International Organization* 39:233-59.
- Textiles: An Essential Industry. 1982. *America's Textiles*, August, 32c-32v.
- U.S. Congress. House. Committee on Ways and Means. 1977. *World Steel Trade: Current Trends and Structural Problems*. 95th Cong., 1st sess., Vol. 33.
- U.S. Department of Transportation. 1981. *The U.S. Automobile Industry: 1980*. Washington: GPO.
- U.S. International Trade Commission. 1978. *The History and Current Status of the Multifiber Agreement*. Doc. no. 850. Washington: Author, January.
- U.S. International Trade Commission. 1980. *Color Television Receivers and Subassemblies Thereof*. Doc. no. 1068. Washington: Author, May.
- U.S. International Trade Commission. 1984. *Color TV Receivers from the Republic of Korea and Taiwan*. Doc. no. 1514. Washington: Author, April.
- U.S. International Trade Commission. 1984. *U.S. Imports of Textile and Apparel Products Under the Multifiber Arrangement, 1976-83*. Doc. no. 1539. Washington: Author, June.
- U.S. International Trade Commission. 1985. *Nonrubber Footwear*. Doc. no. 1717. Washington: Author, July.
- Walter, Ingo. 1981. Economics and Politics of Trade Policy in the Steel Industry. Paper presented at the National Science Foundation (NSF) Workshop on the Politics and Economics of Protectionism, Minneapolis.
- Ward's Automotive Report. 1982. Importers Feast on Record 27.3% Slice of U.S. Market in 1981. Vol. 57, no. 2. Detroit: Author.
- Yoffie, David B. 1981. Orderly Marketing Agreements as an Industrial Policy: The Case of the Footwear Industry. *Public Policy* 29:93-119.
- Yoffie, David B. 1983a. *Power and Protectionism: Strategies of the Newly Industrializing Countries*. New York: Columbia University Press.
- Yoffie, David B. 1983b. Adjustment in the Footwear Industry: The Consequences of Orderly Marketing Agreements. In *American Industry in International Competition: Government Policies and Corporate Strategies*, ed. John Zysman and Laura Tyson, 313-49. Ithaca: Cornell University Press.

Vinod K. Aggarwal is Assistant Professor of Political Science, University of California, Berkeley, CA 94720 and Harvard University, Cambridge, MA 02138.

Robert O. Keohane is Professor of Government, Harvard University, Cambridge, MA 02138 and David B. Yoffie is Associate Professor of Business Administration, Harvard University, Boston, MA 02163.