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THE WHITE HOUSE
WASHINGTON

August 21, 1997

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INFORMATION

MEMORANDUM FOR THE PRESIDENT

From: Daniel K. Tarullo **DKT**
Subject: U.S. -- Japan Civilian Aviation Talks

Next week negotiations resume on a new civil aviation agreement between the United States and Japan. While a breakthrough is unlikely, this round of talks could set the stage for an agreement by the end of September. We have indicated to Japanese officials that long-standing disputes over U.S. cargo routes must be resolved by that time. We have intimated (and the Japanese understand) that sanctions will be forthcoming thereafter, a development which would likely disrupt passenger talks.

Over the summer there has been a noticeable shift in the Japanese attitude towards these negotiations. It would appear that they are genuinely interested in resolving some of our long-standing problems -- in cargo and passengers -- and are willing to accommodate to a number of our positions. However, they will not agree to an "open skies" regime (i.e. removal of essentially all constraints on all carriers), either immediately or as a goal after a transition period. Prime Minister Hashimoto has staked out this position publicly, as well as privately to you, on several occasions. While Japanese officials will not say so explicitly, they obviously fear that their carriers would be overwhelmed in a totally deregulated environment.

Short of "open skies," Japan may be willing to solve existing disputes and offer significant new passenger opportunities to our airlines that now have very limited rights. The result would be appreciably greater service between U.S. and Japanese cities and regions, and would likely be beneficial to our carriers in head-to-head competition with Japanese carriers. Most U.S. carriers, and many U.S. cities, would welcome such a deal.

The Japanese price for these concessions will probably be the designations of a second passenger carrier and a second all-cargo carrier as having unlimited rights under the treaty. Since 1952, the U.S. has had two passenger and two all-cargo carriers with at least theoretically unlimited rights, while the Japanese have had one each. This asymmetry has been at the core of Japan's conflict about the "unequal" nature of the treaty.

In commercial terms, the designation of second Japanese carriers will have only modest effects -- neither of the new designees is strong enough to take full advantage of open route rights. The

major problem we could have with this kind of deal is political. Northwest has been waging a very public campaign against anything but a complete "open skies" deal. The airline is suggesting in full-page ads that anything less would be a U.S. capitulation that is indefensible in light of our large bilateral trade deficit with Japan. Many industry observers believe Northwest is simply trying to protect its current privileged position in the market by arguing that the only acceptable liberalization is a sort it knows to be unattainable. However, by wrapping itself in the mantle of our overall trade problems with Japan, Northwest may find some political traction.

We will have to await the next round of negotiations to see whether a deal is possible that advances our overall aviation goals short of an "open skies" agreement. I have scheduled a Principals Meeting on U.S. - Japan economic issues for early September, at which time we will review the latest developments on the civil aviation negotiations and report back to you.

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cc: The Vice President
Chief of Staff