

Japan: Economic Trends and Outlook

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A. Major Trends and Outlook

Japan is America's largest overseas trading partner. It is also the world's second largest economy with a gross domestic product (GDP) of roughly \$5 trillion in 1995. That is 70 percent of the United States' GDP, while Japan has only half the population of our country.

Japan's economy is larger than that of Germany, the United Kingdom and France combined. It is ten times the size of China and 17 times the size of India. U.S. exports to Japan exceed our exports to China, Taiwan, Hong Kong and Singapore combined. Japan represents almost three-quarters of the entire Asian economy. And in 1996, the 3.6 percent growth rate in Japan's economy was the highest in the industrialized world.

Over-investment and over-hiring in the late 1980's has forced many Japanese companies to undertake cost-cutting efforts in the 1990's. Since the implied social contract in Japan still effectively prevents large Japanese companies from massive layoffs, many companies are reducing their payrolls through voluntary retirements, buy-outs, freezes on new hiring, or transfers of personnel. Yen appreciation has encouraged some Japanese companies to move production overseas in order to better service export markets, which has resulted in increased exports of parts and machinery from Japan. Faced with among the world's highest operating costs domestically, more and more firms have established new factories in countries with far lower labor and material costs such as China, Thailand and Indonesia. They also have begun to look for lower-cost sub-component supply sources to lower their bottom line....

In the early 1990's, Japan expressed its intent to reduce consumer prices to levels comparable to

other OECD countries. There has been little progress in reaching this goal. Prices in Japan reflect very high cost structures of land, distribution and labor, and government regulations protecting employment in inefficient sectors. We estimate that Japanese consumer prices are on average 40 percent higher, and prices of U.S. goods in Japan are typically 70 percent higher, than in the United States.

A societal trend taking place in Japan today will have profound impacts on Japan in the years to come. Japan's population is rapidly aging — a "greying" of the society. Because individual health care expenditures rise rapidly after age 60, this greying effect will force a rapid rise in the cost of providing health care over the next three decades. By the year 2025, the Ministry of Health and Welfare predicts that more than one of every four Japanese will be 65 or older (up from about one in every seven, today). In just one quarter, Japan will have gone from having the fewest elderly as a percentage of its population to having the highest percentage among all industrialized nations. As a result, because fewer workers will be forced to support more retirees, taxes on those employed will increase. Already expensive labor is likely to become increasingly more expensive, probably leading companies to increase their off-shore capacity. Manufacturers will design production to minimize labor inputs and ensure increased demand for capital-intensive, high value-added manufacturing....

Japan is the world's second largest market for information technologies equipment and services (telecommunications, computers, peripherals, software, and multimedia) and is forecasted to be valued at \$1.23 trillion by the year 2010. Fueling the current strong demand for telecommunications infrastructure is the Government of Japan's goal to connect all Japanese businesses, government offices, schools, and homes by 2010 through a "Fiber to the Home" project. Current investment in telecommunications infrastructure is \$33 billion annually and by 2007 is forecast to reach a cumulative \$500 billion. Japan's recent exponential growth in the market demand for networking, personal computers, Internet applications, wireless communications, and satellite communications is expected to continue through the turn of the century

Surveys have shown that Japanese houses are two to three times more expensive than equivalent American houses, and many Japanese people are not satisfied with either the quality or price of their current housing stock. In contrast, imported American-style homes are regarded as offering high quality, low cost and earthquake resistance. The Japanese Ministry of International Trade and Industry (MITI) and the MITI-affiliated Japan External Trade Organization (JETRO) are now actively promoting the import of high quality, affordable houses from North America and Europe....

Tokyo, Japan's sophisticated capital and the surrounding prefectures of Kanagawa, Saitama and Chiba, occupy the largest flat area in Japan called the Kanto Plain. Together, these four prefectures have a population of over 31 million, equivalent to the New York and Los Angeles metropolitan areas combined. Tokyo is the governmental, business, higher education, information, media, fashion and cultural center of Japan. Most major Japanese companies, trade associations and U.S. companies have their headquarters or major branches in Tokyo. Kanagawa, which includes the cities of Yokohama and Kawasaki, is by far the richest prefecture in Japan, with a per-capita income almost 50 percent above the Japanese average. A presence in Japan usually means a presence in Tokyo. Despite high rental costs, most U.S. companies locate in Tokyo because of the need to interface with their Japanese customers, to obtain market information and in many cases, to handle relations with Japanese Government ministries. Consumers in Tokyo are more likely to come into contact with foreign products, food and styles than elsewhere in Japan. Also, consumer styles and fashions emanate from Tokyo in avidly read magazines as well as the television networks. In addition to consumer goods, value-added food products, apparel, furniture and automobiles, good export prospects to the Tokyo area include medical products, computers, telecommunications hardware and software and business services....

Japanese agricultural production is steadily contracting on a year-by-year basis, with key sectors seeing decreasing production in most years. Cereals, rice, dairy, beef and pork, and fruits and vegetables are all sharing this decline to greater or lesser degrees. Efficiency is hampered by the small and scattered nature of farm lands and by inordinately high input costs. Farmers are limited by the government and the cooperative system in their ability to make decisions regarding production, pricing and marketing.

At the same time that local production is poised for a precipitous decline, access for imported agricultural products has never been better. Due to persistent negotiation by the United States and others throughout much of the 1980's and 1990's, Japan has eliminated many of the agricultural market access barriers for which it was once famous. Where earlier quotas and outright bans restricted the market for U.S. beef, citrus, fruit juice, cherries, apples and ice cream, all of these markets have now been opened. Market access remains limited in a few key commodities, such as rice, tariffs remain high on high value added processed food products, and some problems remain in technical issues concerning food additives and phyto-sanitary barriers on fruits and vegetables. However, these exceptions aside, the Japanese market is, contrary to popular belief, substantially open to U.S. food and agricultural products.

The combination of this radically improved market access and declining domestic production has resulted in phenomenal export growth for American agriculture. Already the largest importer of U.S. agricultural products, Japan may increase its agricultural imports from the U.S. by \$1 billion per year each year until the turn of the century. 1996 imports of U.S. agricultural/forestry and fisheries products reached \$16.6 billion, up from \$16.3 in 1995. Export stars include beef, pork, ice cream, broccoli, asparagus, frozen vegetables, cherries and processed snack foods. ...

C. Government Role in the Economy

... Business in Japan traditionally has maintained very close relations with the bureaucracy and politicians. Japanese politicians have depended on contributions by big business. Big business also provides lucrative employment for high-level bureaucrats who leave government service. Bureaucratic paternalism blocks new companies from entering the market and pushes up prices. Members of the Japanese National Diet have small staffs and traditionally rely on ministry officials for policy initiatives and the drafting of legislation....

D. Balance of Payments Situation

Japan's trade and current account surpluses, the largest in the world, continued to decline in 1996 after several years of steady increases. The trade surplus fell from \$132 billion in 1995 to \$83 billion in 1996, based on U.S. Embassy calculations based on official yen data, as rapid import growth out-paced strong growth in merchandise exports. The current account surplus fell even more sharply, from USD 111.4 billion in 1995 to USD 65.9 billion in 1996, as a widening services and "invisibles" deficit complemented the decline in the trade deficit. Japan's bilateral trade surplus with the United States also declined last year, from USD 45.5 billion to USD 32.5 billion.

Source: Excerpted from "Japan: Economic Trends and Outlook," U. S. Department of Commerce - National Trade Data Bank, September 1997; TradePort (an authorized distributor of STAT-USA data).

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