Japan: Engine of Asian Change

Watch Out for the New Boys!

by ARIYOSHI OKUMURA

Japan's economic and trading policies are bringing an era of mushrooming prosperity to the newly developed countries of Asia and the Pacific.

The development of the Asia-Pacific region will undeniably be affected in a major way by the future course of the US economy. Nevertheless, as in the past, an opportunity for further growth is presenting itself to the economies of the region - an opportunity created by advances in technological innovation and the industrial globalisation being promoted by Japanese industry on the basis of this advancing technology.

Technological innovation, particularly in micro-electronics and information processing, is changing corporate concepts of product development, production, and distribution - that is, ideas of what goods and services should be produced, and where and how their production and distribution should be conducted. Thus, Japanese industry is undergoing profound change - change that, coupled with the yen's appreciation, is rapidly accelerating the pace of industrial restructuring.

The direction of this structural change, brought about by technological innovation and the yen's appreciation, can be said to be toward the build-up of an efficient international industrial system. Internationally, this means the promotion of a horizontal division of labour, or industrial globalisation; domestically, it means the growing sophistication of industries along the lines of horizontal specialisation.

The evolution of industrial globalisation has gathered so much momentum that it will only keep moving forward. This current is building as Japanese corporations expand their direct overseas investments.

A look at the trend of direct Japanese overseas investment shows that it began to soar in the wake of the yen's sharp appreciation in September 1985, posting an 80 per cent gain over the previous year in fiscal 1986 and another 50 per cent rise in fiscal 1987.

Japan's fabrication and assembly industries have made considerable overseas advances, but the objectives of their moves have now changed substantially, as have the roles of their local production bases.

The first wave of Japanese overseas advances was seen in the 1950s, when electronics and electrical machinery manufacturers and auto makers began local production in South-East Asia and Latin-American countries. The purpose of these moves was to enter the markets in developing countries where imports of finished products were restricted. Production at that time was carried out by the knock-down method. The second wave started in the early 1970s, set in motion by trade frictions with industrialised countries.

In both of these waves, Japanese companies were compelled to move overseas, though to different parts of the world, and the products and parts they used were supplied mostly from Japan.

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The third wave, which was triggered by the yen’s sharp appreciation, is for more positive reasons. Japanese companies are now going overseas because the yen’s sharp appreciation has produced a significant difference between domestic and overseas production costs – a situation that has given rise to two questions: one, where in the world is it most efficient to assemble finished goods? and two, where should parts and materials be procured?

Relations between trading regions have now become complex, with the United States, European countries, South-East Asian countries and Japan supplying parts and products to each other. Japan’s fabrication and assembly industries can be said to have entered the ‘era of industrial globalisation,’ a stage in which overseas expansion is determined by cost factors rather than trade friction, the political factor that had determined them in the past.

This industrial globalisation will inevitably have a great impact on the economic development of the newly industrialising countries and the ASEAN countries. The rise in direct Japanese investment, the technology transfers that accompany it, and the expansion of exports to Japan that follows, and an increase in exports to third countries on the strength of the transferred technologies – these will become significant sources of future economic growth for those countries.

Further, the resulting enhancement of their export competitiveness will help maintain the trade balances of the NICs in a favourable state, while improving the trade balances of the ASEAN countries. In resource-exporting countries, in particular, progress in industrialisation will lead to a diversification of merchandise for export resulting in increased exports of manufactured products.

Direct Japanese investment in the Asian economic zone in the fiscal 1988-92 period is expected to reach a cumulative total of US$30.2 billion. During this period, the economics of the newly industrialising countries, ASEAN nations and Japan could be able to achieve an annual average growth rate of 4 per cent to 5 per cent – a robust growth rate that should bring brisk activity to the principal financial and capital markets in the region.

A look at statistics on the major offshore markets of the world shows that London is the largest market, worth $975 billion (as of June 1988), and that the New York market is worth $275.2 billion (July 1988). On the other hand, the offshore markets in Tokyo, Hong Kong and Singapore are $366.2 billion (July 1988), $349.1 billion (April 1988) and $241.7 billion (May 1988) respectively. The combined size of the three Asian offshore centres, together worth $957 billion, is comparable to that of the London market.

Massive funds will continue to flow into these financial and capital markets in Asia, enabling them to further strengthen their positions as financial and information centres on a par with New York and London.

In these Asian cities, industries will grow that perform required functions – such as financial services, information services, and urban-type industries. These industries will provide another driving force in the vitalisation of the Asia-Pacific region.

In the context of the economic and financial development of the Asia-Pacific region, the internationalisation of the yen presents itself as an important issue.

The debate started in the early 1980s with the liberalisation and internationalisation of the Tokyo financial markets, increasing the use of the yen as a currency of capital transactions. And it has now been spurred by the recent rapid development of the Asia-Pacific region.

But has the yen been internationalised in the true sense of the word? The answer is no. Even as a currency of settlement, its role is not yet impressive: while German mark-denominated transactions account for about 80 per cent of West German exports and 40-50 per cent of West German imports, yen-denominated transactions represent only about 36 per cent of Japanese exports and 10 per cent of Japanese imports.

With respect to the yen as a currency of capital transactions, the issue amount of yen-denominated bonds such as euroyen bonds and samurai bonds is increasing, but the bulk of euroyen bonds is purchased by Japanese institutional investors. Moreover, yen raised by foreign issuers is used after being converted into dollars or other currencies through swaps. Given these aspects of the yen’s present status, its internationalisation is not something that Japan can promote because it wishes, but something that should take place gradually as yen transactions make headway.

Even if Japan tries to push the internationalisation of the yen, it must do so taking care not to damage the credibility of the US dollar, aware that it is the world’s key currency. An internationalised yen would only be a secondary key currency.