

Strategy for Trans-Pacific Integration: from Japanese Perspective

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Presentation

1. Introduction

2. East Asian economic integration from Japanese perspective

- ✓ Intense exchanges of intermediate goods (Fragmentation) and market-driven, *de facto* integration: platform of Japanese globalization

3. Latin American countries

- ✓ *de jure* integration and specialization in the export of primary products: low intensity of intra-regional trade

4. Future challenges for trans-Pacific integration

- ✓ How Japanese industries innovate global strategy?
- ✓ Trans-pacific integration (TPI) is useful for advancing Japanese strategy for globalization.

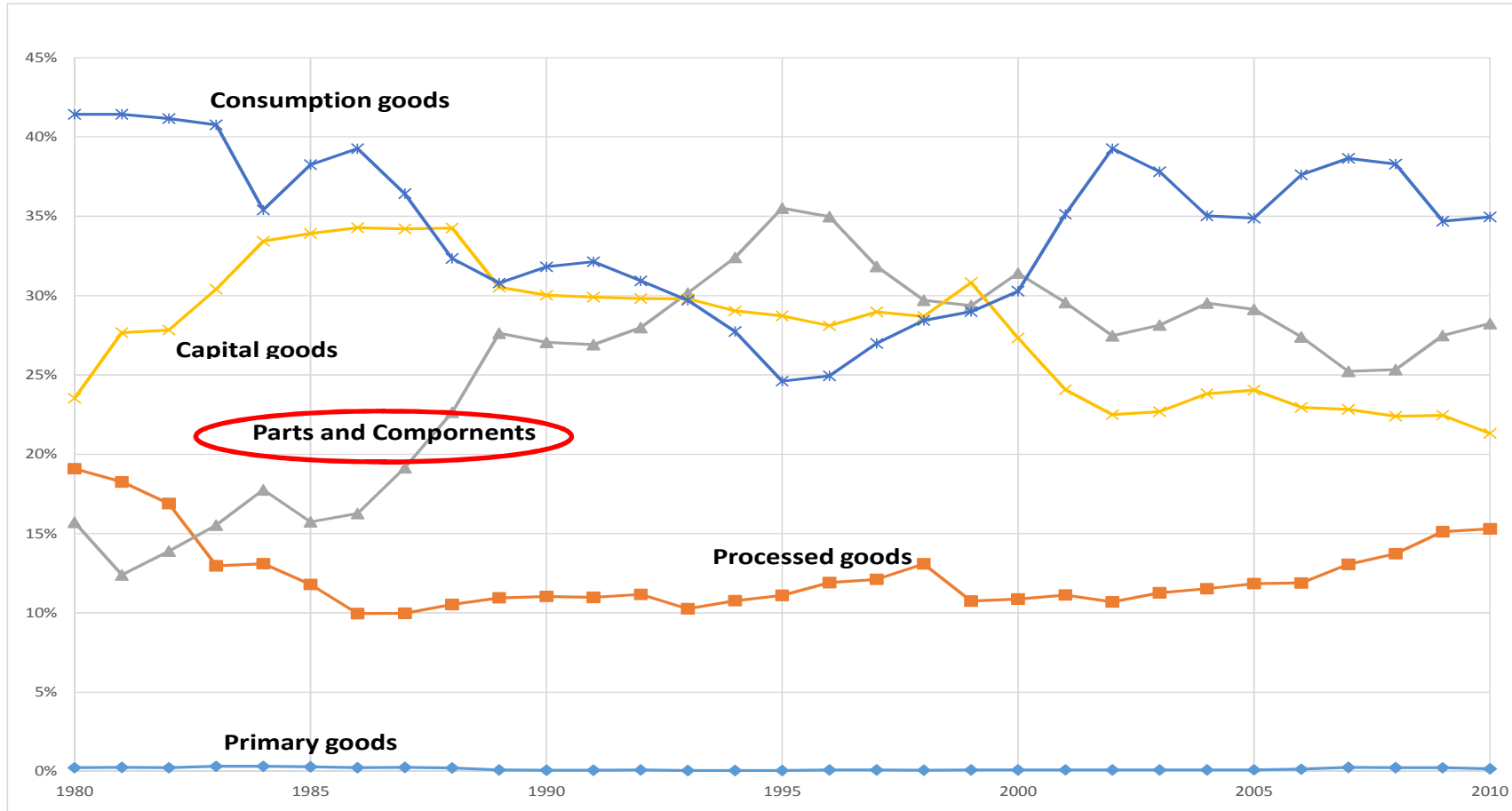
1. Introduction

- ✓ Japan has lost substantial weight in the global economy (stagnant economic growth, aging, etc.).
 - ✓ Emerging economies including Latin America are in the forefront of expanding consumers' demand.
 - ✓ However, Japanese industry has been too narrowly focused on East Asia.
- ➔ We discuss such strategy to make globalization of the Japanese industry one step forward taking advantage of new market opportunities based on its high level of technological capability

2. East Asian economic integration from Japanese perspective

- ✓ Japan exported capital-intensive final goods to the US market from the post-war high-economic growth period up to the mid-1980s. (increased labor costs, the sharp real appreciation of the yen after the Plaza Accord in 1985) →
- ✓ Japanese industries moved their production facilities and product development to other Asian countries (NIES4, ASEAN and, more recently, China) and Japan's FDIs overwhelmingly increased since the mid-1980: Catalyst role of Japanese firms.
- ✓ Japanese industries specialize in supplying intermediate goods for other firms or their own affiliates in East Asia (Fig.2). → creating industrial cores in East Asia

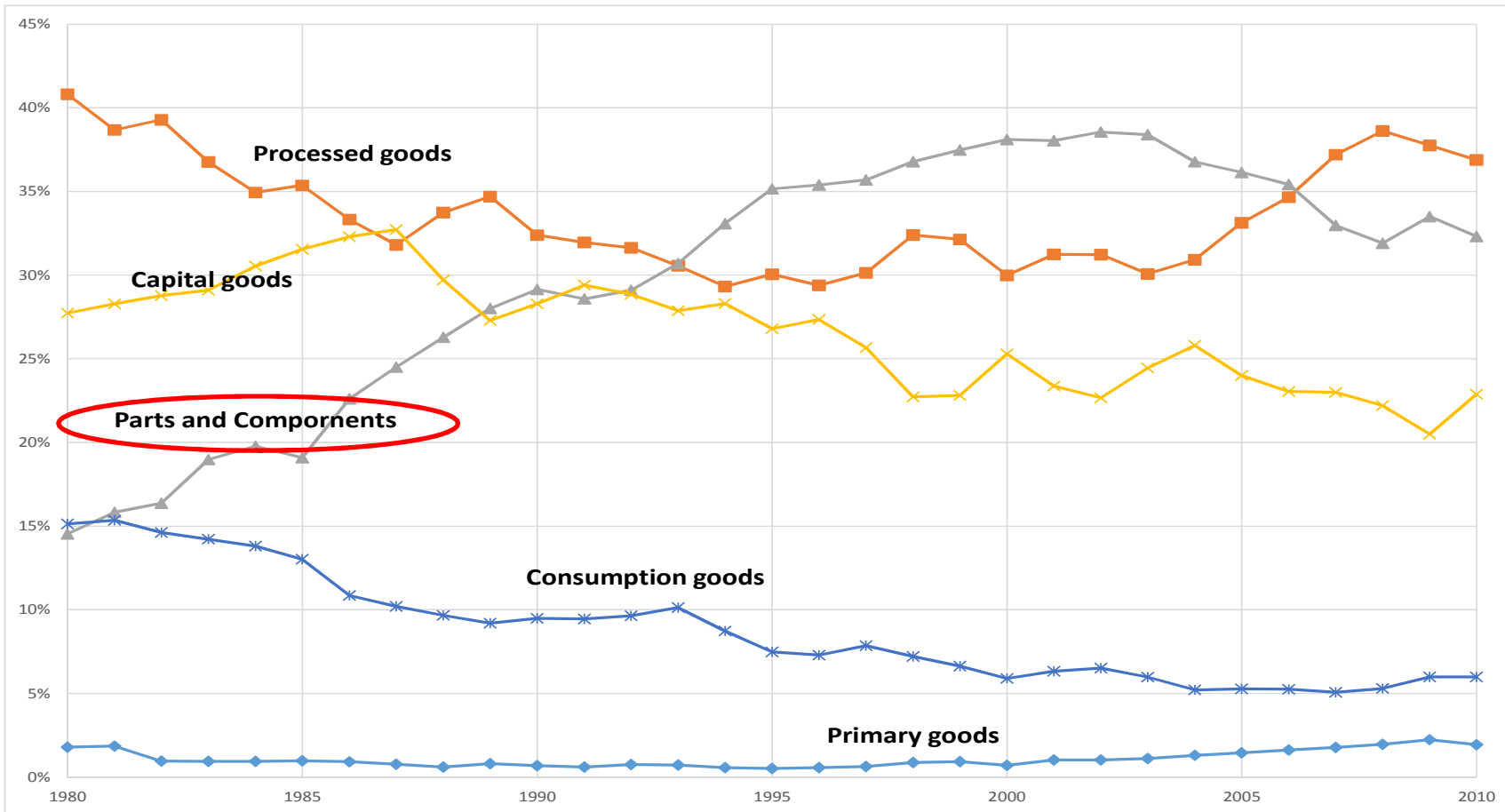
Figure 1. Evolution of Japanese exports to US by categories, 1980-2010



Japan- the US trade conflicts in the 1980s prompted Japan's local production in the US and parts and components exports. Recently, Japanese exports to the US concentrate more in luxury consumer goods such as cars.

Source: RIETI-TID 2012

Figure 2. Evolution of Japanese exports to East Asia by categories, 1980-2010



The share of intermediate goods from Japan to East Asia, especially parts and components, has increased since the mid-1980s.

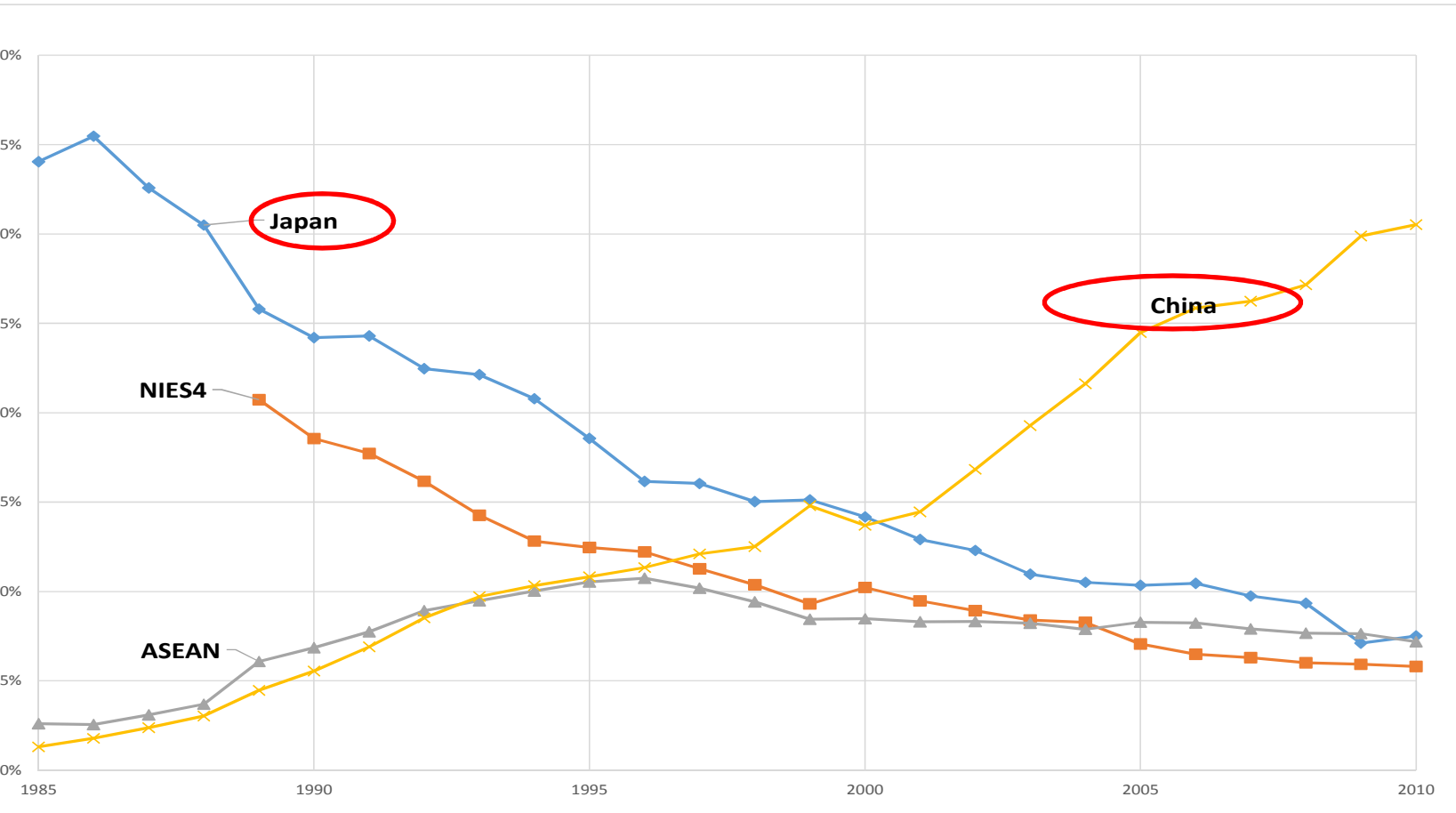
Note: some of machinery and transport equipment are included in intermediate goods.

Source: RIETI-TID 2012

Cont.

- ✓ The region as a whole has succeeded in exporting manufacturing final goods to the US market (Fig.3).
- ✓ East Asia succeeded in creating regional production network of intermediate goods and reducing dependence on extra-regional imports (Fig.4).
- East Asian integration is characterized by intense exchanges of intermediate goods ('fragmentation') and market-driven, de facto integration.
- ✓ Today's intra-regional intermediate goods trade is more competitive.
→ Intermediate goods producers need to seek a new market other than East Asia in order to maintain production in scale.

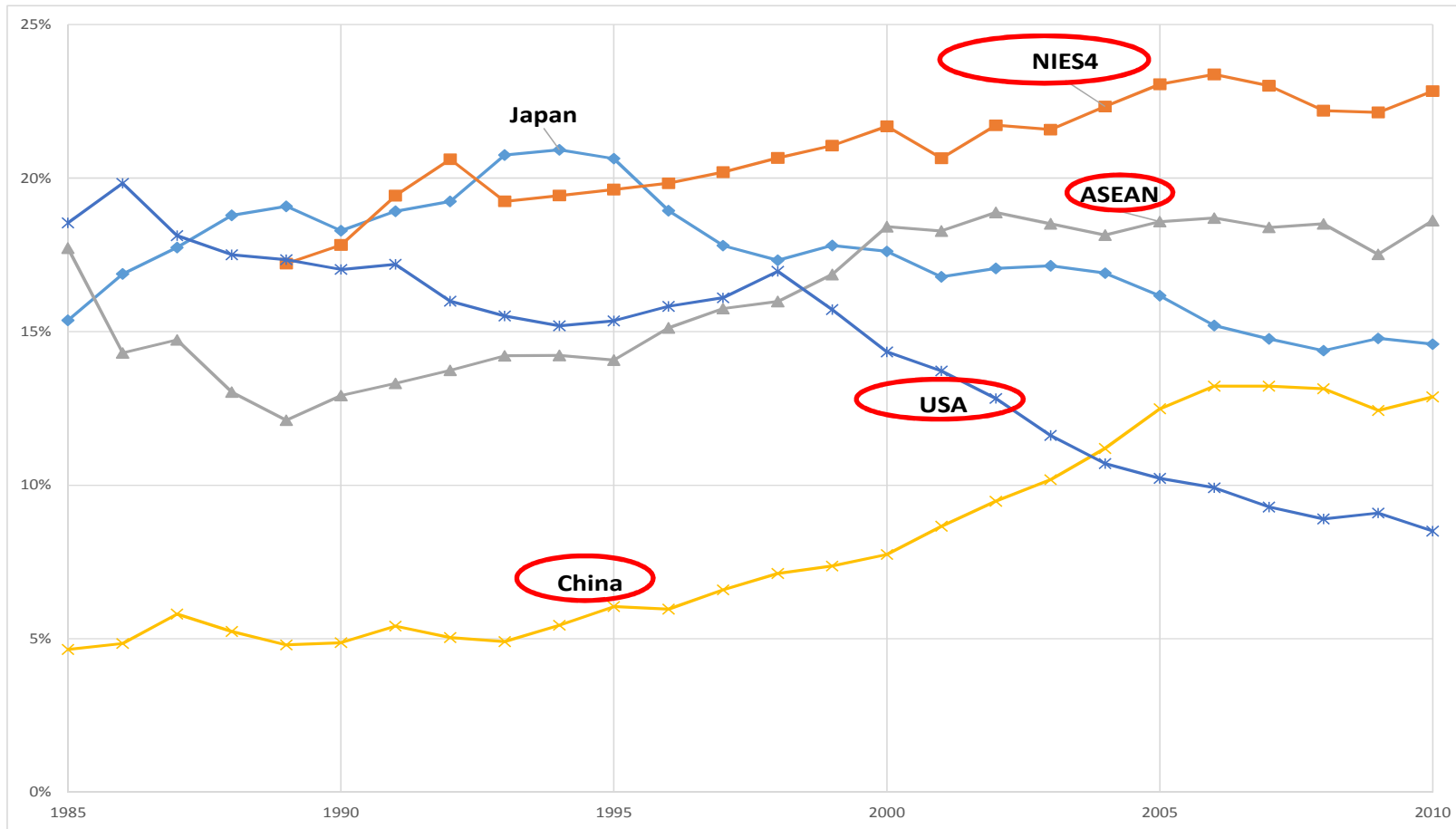
Figure 3. Evolution of East Asia's shares in the US final goods imports, 1985-2000



Japan has continued to decrease, while the expansion of China has been spectacular. The regional share in the US final goods imports maintained approximately 50% during 1985–2010. It is worth noting that Chinese products have so many Japanese parts and components inside.

Source: RIETI-TID 2012

Figure 4. Evolution of East Asia's intermediate goods import shares by origin, 1985-2000

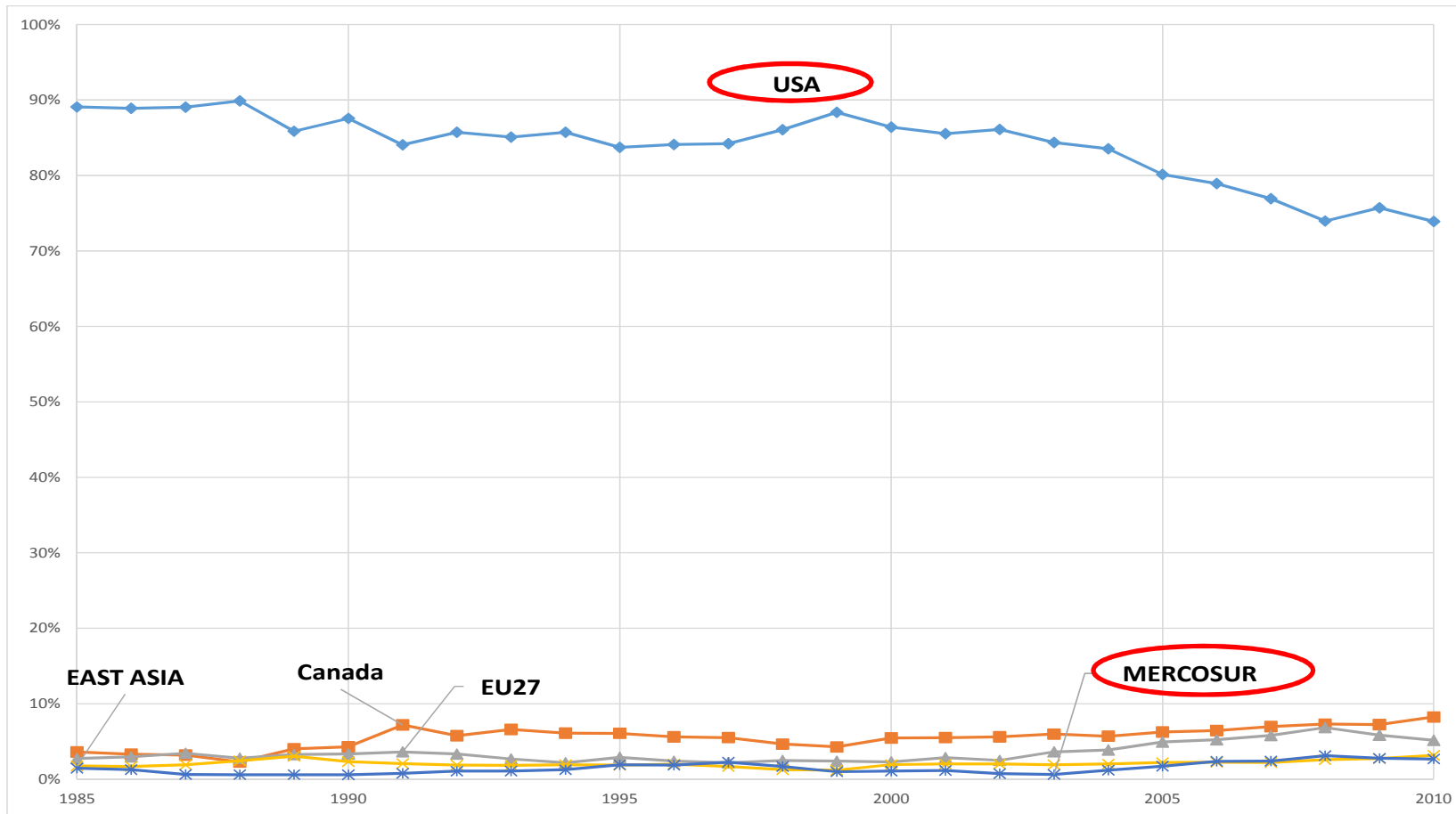


US (i.e., extra-region) decreased their presence of trade in intermediate goods imports in East Asia, while NIES4, ASEAN and China (i.e., inter-regions) overwhelmingly increased since the 1990s.

3. Latin American countries

- ✓ de jure regional integration are developed much further in LACs than in East Asia. However, LACs have not yet experienced the development of regional production networks.
- ✓ Current two basic trade patterns in LACs
 - Mexico (and several Central American countries) import intermediate goods from the US and East Asia and export final goods to the US (Fig.5). Mexico imports few intermediate goods from other LACs (Fig.6). → Mexico cannot create regional production network driven by trade in intermediate goods among LACs
 - Other LACs (mainly South American countries) export low value-added primary products (re-commoditization)
- ✓ The lack of TPI and regional integration in LACs makes it difficult for Japanese firms to draw a strategy for LACs.

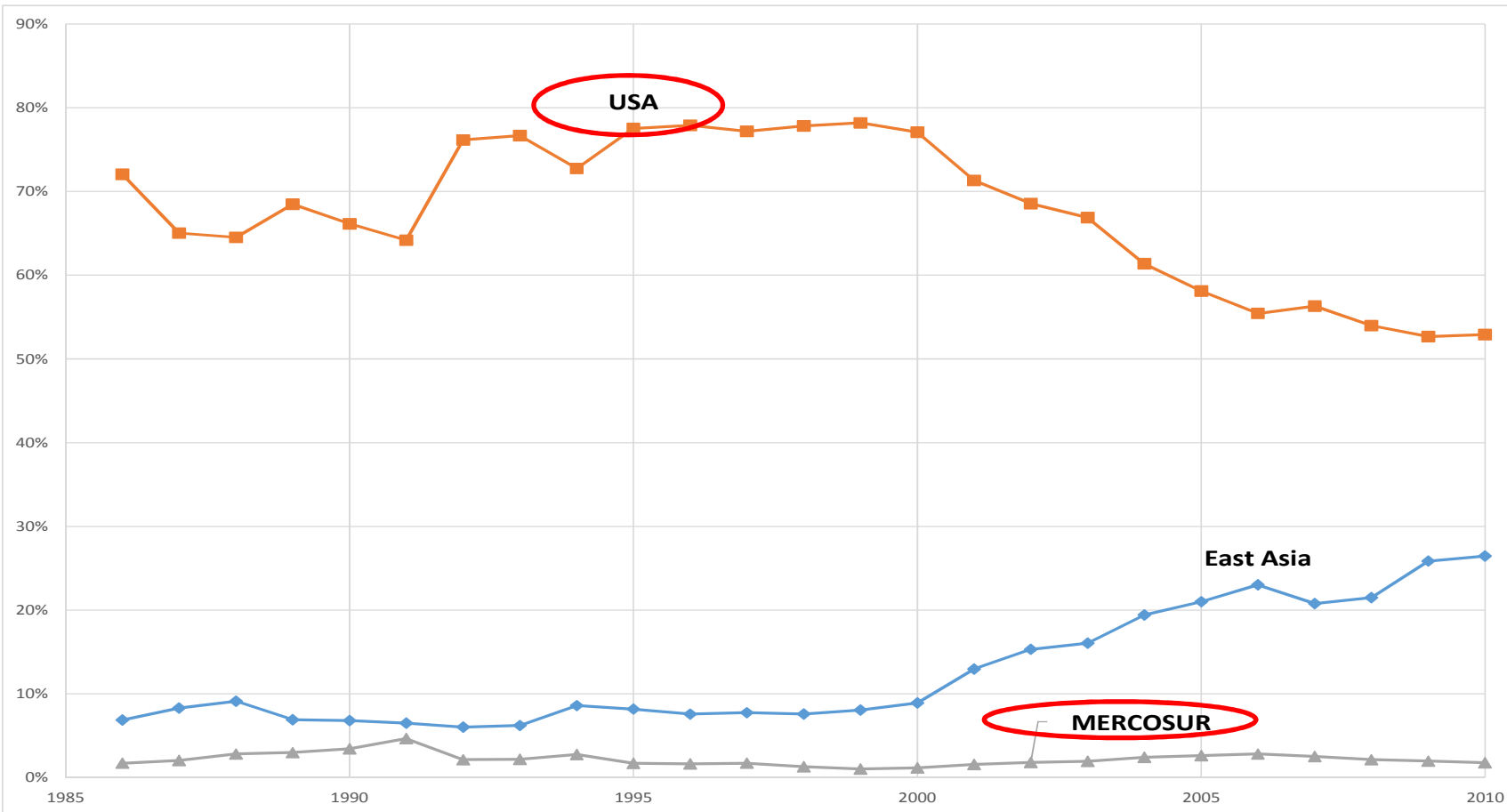
Figure 5. Evolution of Mexico's final goods export destinations, 1985-2010



Mexico is highly dependent on the US as the export destination (more than 80%) while other LACs absorb few final goods from Mexico (less than 3%).

Source: RIETI-TID 2012

Figure 6. Evolution of Mexico's intermediate goods import shares by origin, 1985-2010



Mexico is **highly dependent on the US** as the import origin of intermediate goods .

Source: RIETI-TID 2012

4. Future challenges for trans-Pacific integration

❑ Pending issues for Japanese firms in Latin American markets

✓ Japanese industry has not been able to establish a significant intermediate goods network in LACs (including Mexico) .

✓ The re-commoditization of exports in LACs has also been unfavorable for the Japanese industry.

✓ Slow progress in *de facto* economic integration of LACs also make less attractive for Japanese investment.

Cont.

□ Major challenges for the Japanese firms in Latin American markets as a foundation for more stable growth in both Latin America and Japan.

(1) More integration between East Asia and LACs (TPI) and within LACs → LACs should take advantage of connecting itself to the well-developed production network of East Asia to enhance productivity.

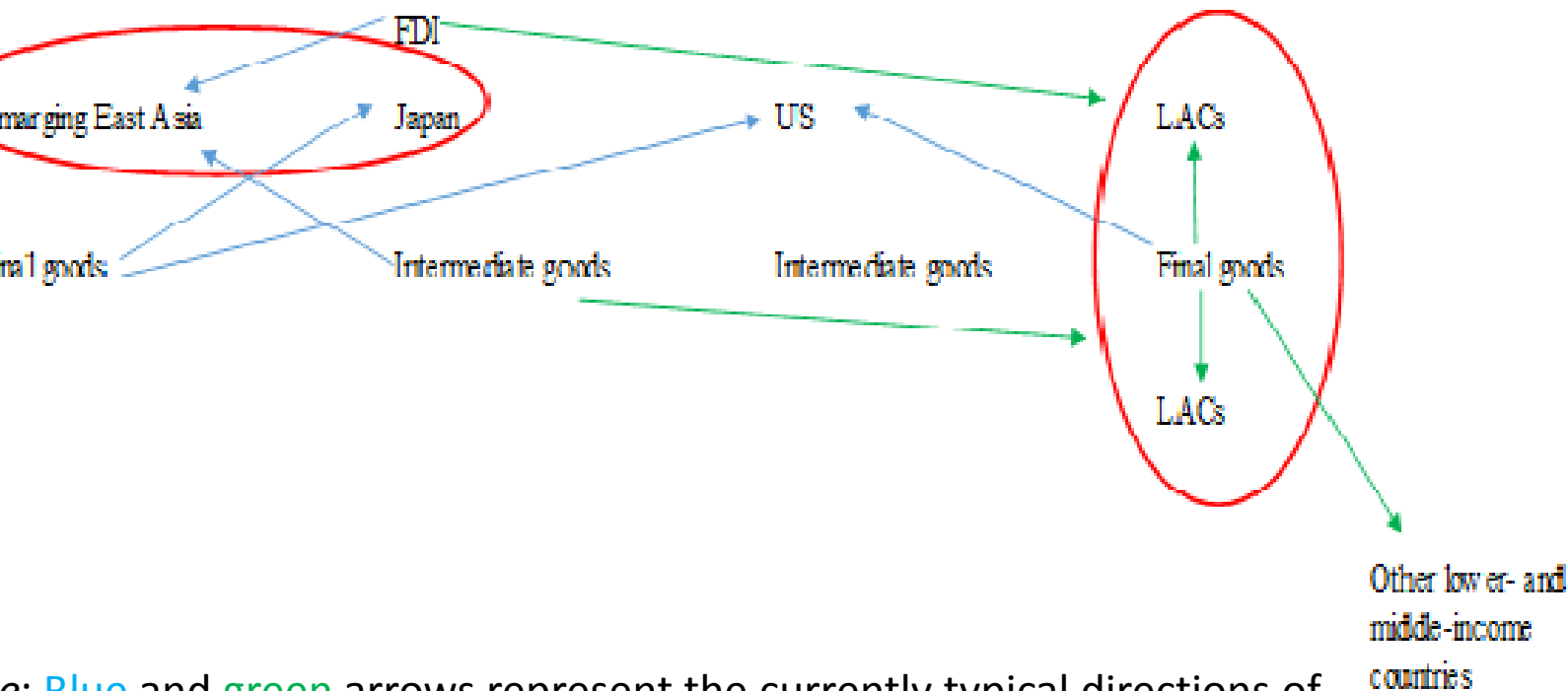
(2) Japanese firms have excellent business chances in natural-resource based industries in LACs → Investments in capital goods for: extraction and transportation of natural resource and processing to increase value-added.

(cf. Ishikawajima-Harima Industry (IHI) will construct drillship for deep sea oil field extraction in Brazil. IHI uses parts and components in a Japanese factory, which otherwise needs to cut job.)

(3) The emerging middle income classes in LACs have strong aspiration for high technology products → LACs can be regarded as a cradle of R&D of such products that can be also applied to other lower- and middle-income countries.

(cf. Recent adaptation of the Japanese digital TV system by most LACs based on Japan-Brazil technological cooperation is a good example)

Figure 8. Our proposed future trans-Pacific integration



- (1) LACs strengthen integration with East Asian countries (i.e., TP) so that Japanese firms can produce parts and components.
- (2) LACs could be more integrated so that production will be in scale to gain more competitiveness.
- (3) LACs will be a hub of R&D aiming at emerging consumers for both domestic and rest of LA markets.

Legend: Blue and green arrows represent the currently typical directions of exports and our proposed future directions of exports, respectively. Red ovals represent regional integration.

Remember: Historically, LACs have been always important partner of Japanese trade strategy (e.g., the revision of unequal treaties, immigration, and recently EPAs)