White Paper on International Economy and Trade 2014 [Outline]

June 2014

Ministry of Economy, Trade and Industry

Structure of the White Paper on International Economy and Trade 2014

- Non-statutory white paper published as an annual report concerning Japan's external economic policy
- This year's white paper is the 66th annual report since the first in 1949.

Part I Trends in the World Economy – Global Economic Conditions and International Trade and Investment Trends in Japan–

Chapter 1 World Economic Trends after the Global Economic Crisis
- ○ Changes since the Global Economic Crisis
- ○ Effects of the Tapering of the Quantitative Easing Program in the United States

Chapter 2 International Trade and Investment Trends in Japan

Part II Economic Fundamentals and Growth Strategy and Structural Reform Initiatives in Other Countries – Analysis of Growth Strategies, Structural Reforms and Changes in Economic Structure in Major Countries –

Chapter 1 Growth Strategy and Structural Reform Initiatives
- ○ Labor Reforms in Europe
- ○ Reappraisal of Manufacturing and Domestic Production and the Effect of the Shale Gas Revolution in the United States
- ○ China in Search for New Growth Models
- ○ ASEAN Efforts to Advance to the Next Growth Stage

Chapter 2 Economic Fundamentals and Growth Strategies in Emerging Countries
- ○ Economic Fundamentals (Risk Tolerance, Basis for Growth) of Emerging Countries
- ○ Structural Reform in South Korea after the Asian Financial Crisis
- ○ Growth Strategies Adopted in Mexico and Brazil
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Chapter 3 Expansion of Trade and Investment in East Asia and Japan's Contribution to Growth Model Changes in East Asian Countries

Part III Development of a Business Environment which Expands the Business Opportunities of Japanese Companies

Chapter 1 Worldwide Expansion of Economic Partnership Networks

Chapter 2 Strategies Targeting Emerging Countries

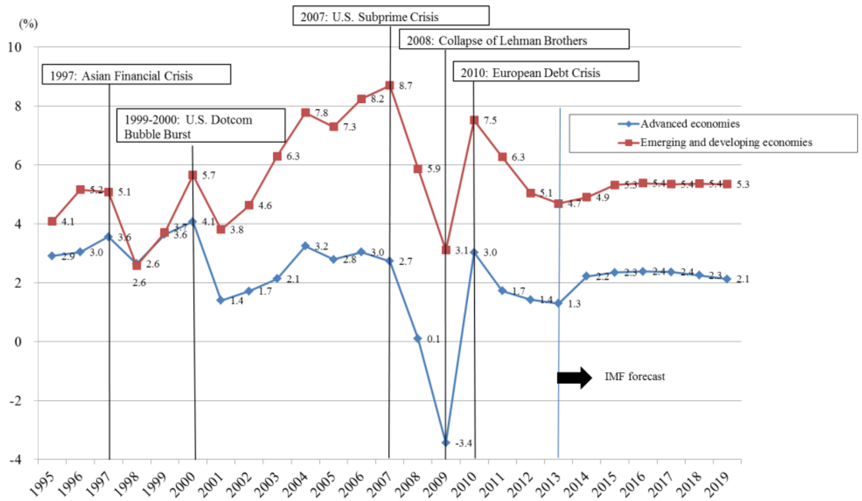
Chapter 3 Promotion of Inward Direct Investment

World Economic Trends after the Global Economic Crisis

- More than five years have passed since the 2008 collapse of Lehman Brothers, and the economies of the United States and other advanced economies are returning to growth tracks (Chart 1), but the momentum is not so strong compared with the previous economic recovery phases (Chart 2). Furthermore, emerging economies, which have been driving forces of the world economy following the collapse of Lehman Brothers, began to show some signs of vulnerability (Chart 3).

[Chart 1: Changes in GDP of Advanced and Emerging Economies]

– The world economy has been in a moderate recovery trend after the collapse of Lehman Brothers and European Debt Crisis –

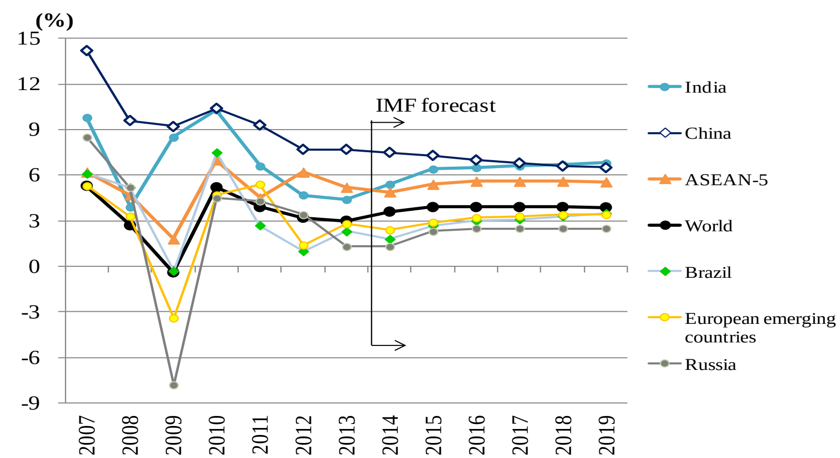


[Chart 2: GDP forecasts of Major Countries]

– Lower growth rates are projected in both the U.S. and China –

	Growth rate (actual results from Q2 of 1953 to Q4 of 2007)	Potential growth rate (forecast for Q3 of 2013 to Q4 of 2024)
U.S.	3.3%	2.3%
	Growth rate (actual results from 1980 to 2013)	Target growth rate (2014)
China	9.9%	7.5%

Source: Economic Report of the President (Mar. 2014), IMF World Economic Outlook, April 2014, Report on Government Activities Given at the National People's Congress (March 2014)



Notes: 1. ASEAN-5: Indonesia, Malaysia, the Philippines, Thailand and Vietnam
2. Figures for India are for the accounting year, based on market value.
Source: IMF World Economic Outlook, April 2014

[Chart 3: Changes in the Current Account Balances of Major Emerging Economies in the aftermath of the collapse of Lehman Brothers]

	2008	2013	Changes in current account balances (billion dollars)
China	420.6	188.7	231.9 (Surplus diminished)
Russia	103.9	33.0	70.9 (Surplus diminished)
Malaysia	39.4	11.8	27.6 (Surplus diminished)
Brazil	-28.2	-81.4	53.2 (Deficit expanded)
Indonesia	0.1	-28.5	28.6 (Deficit expanded)
Turkey	-40.4	-65.0	24.6 (Deficit expanded)
India	-27.9	-37.2	9.3 (Deficit expanded)

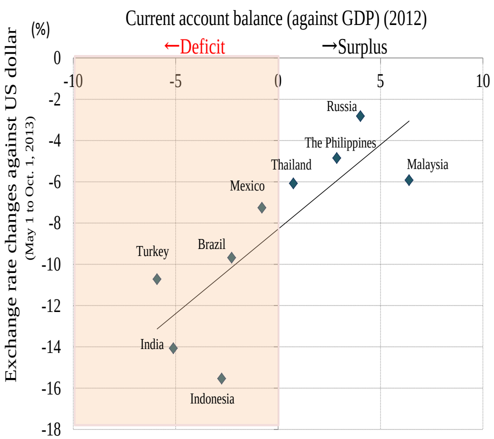
Source: IMF World Economic Outlook, April 2014

Necessity of Reform to Achieve Growth

- Since May 2013, the anticipated tapering quantitative easing program in the United States has triggered some market turmoil in emerging economies, resulting in capital outflows and currency depreciation (Chart 1).
  Through experience from past currency crises, emerging economies have increased resilience as a whole (Chart 2).
  However, in order to counter external shocks, there were movements to implement reforms in such countries as India and Indonesia, under the recognition that domestic reforms are necessary to strengthen growth potential, while financial measures to protect local currencies are taken as well. (Chart 3).

[Chart 1: Correlation between Current Account Balances and Currency Depreciation]

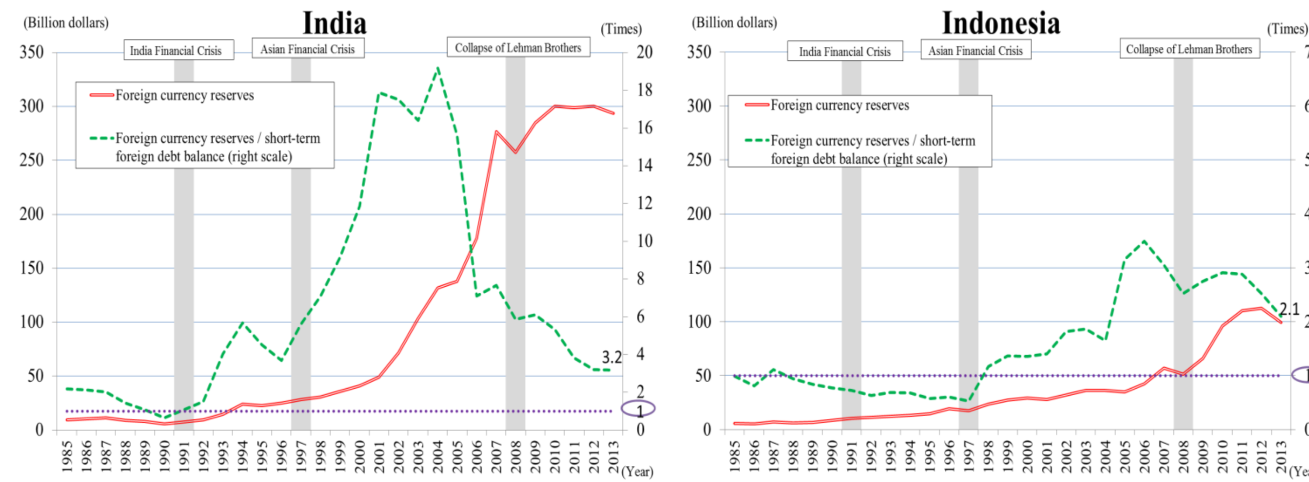
– Countries with larger current account deficits, suffered more serious currency depreciation and capital outflows –



Source: IMF World Economic Outlook, April 2013 (current account balances (against GDP) for India and Turkey are estimates) and data from Thomson Reuters EIKON

[Chart 2: Foreign Currency Reserves and Foreign Debt Stocks of India and Indonesia]

– Compared to previous currency crises, the countries have sufficient foreign currency reserves to repay short-term foreign debt, and have thus strengthened resilience to external shocks –



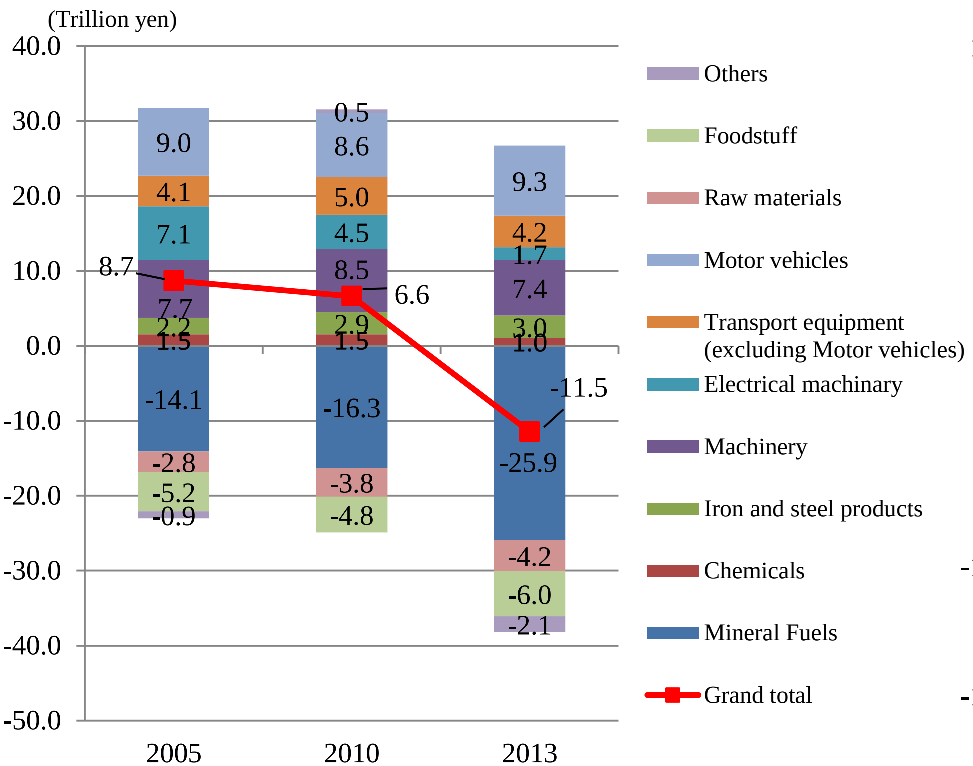
[Chart 3: Currency Protection Measures Taken in Response to Tapering Quantitative Easing Program in the United States and Reform Policies to Achieve Growth]

	Currency support	Reforms to achieve growth, etc.
India	Jul. 2013 –Central Bank of India announces rupee stabilization measures Sep. and Oct. 2013 and Jan. 2014 – Policy interest rate increases	Jul. and Aug. 2013 – Government announces additional easing of restrictions on foreign investment and measures to reduce current account deficits (such as restrictions on gold imports)
Indonesia	Jun., Jul., Aug., Sep., and Nov. 2013 – Policy interest rate increases	Jun. 2013 – Decision to reduce fuel subsidies, which have caused strain on the country's finance Aug. and Dec. 2013 – Compilation of an economic policy package aimed at improving the balance of payments

International Trade and Investment Trends in Japan (1) Outline

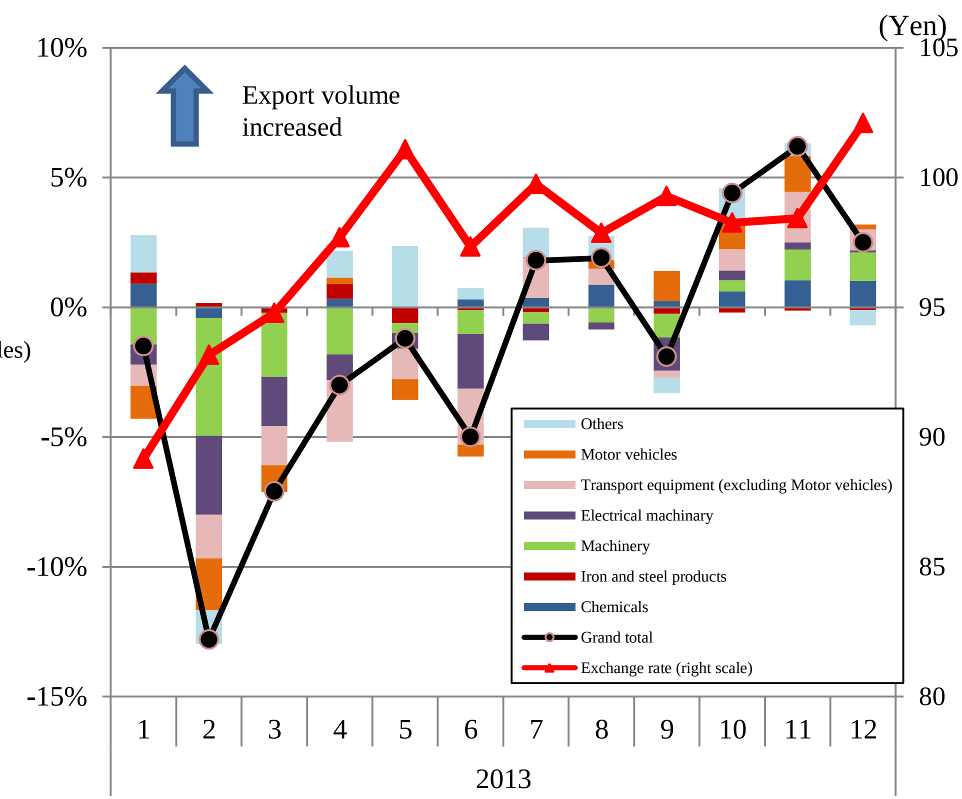
- Japan recorded its largest ever trade deficit in 2013. While the deficit increased significantly due to fossil fuel imports, the surplus from exports of general machinery, electrical equipment, etc. has been diminishing (Chart 1). Growth in export volume has remained sluggish, but has been on a moderate upward trend since the third quarter of 2013 (Chart 2).

[Chart 1: Trade Balance by Commodity]



Source: Trade Statistics of Japan (Ministry of Finance)

[Chart 2: Analysis of Export Volume Contribution Ratios (Y/Y Changes) (2013)]



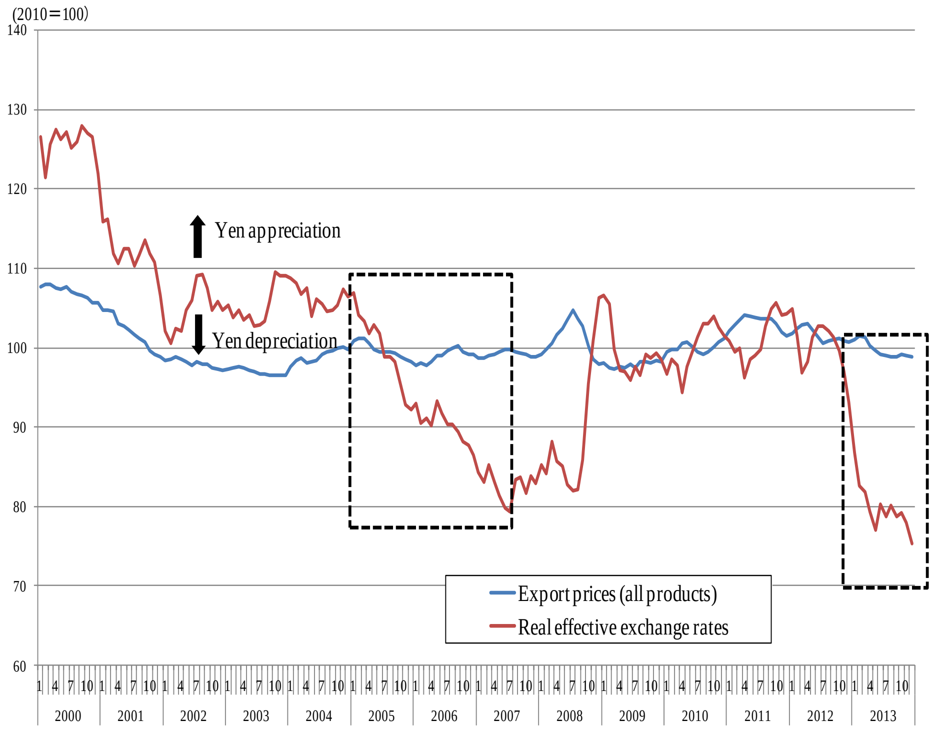
Source: Trade Statistics of Japan (Ministry of Finance)

International Trade and Investment Trends in Japan (2)

– Reasons for Current Weak Export Volume Growth –

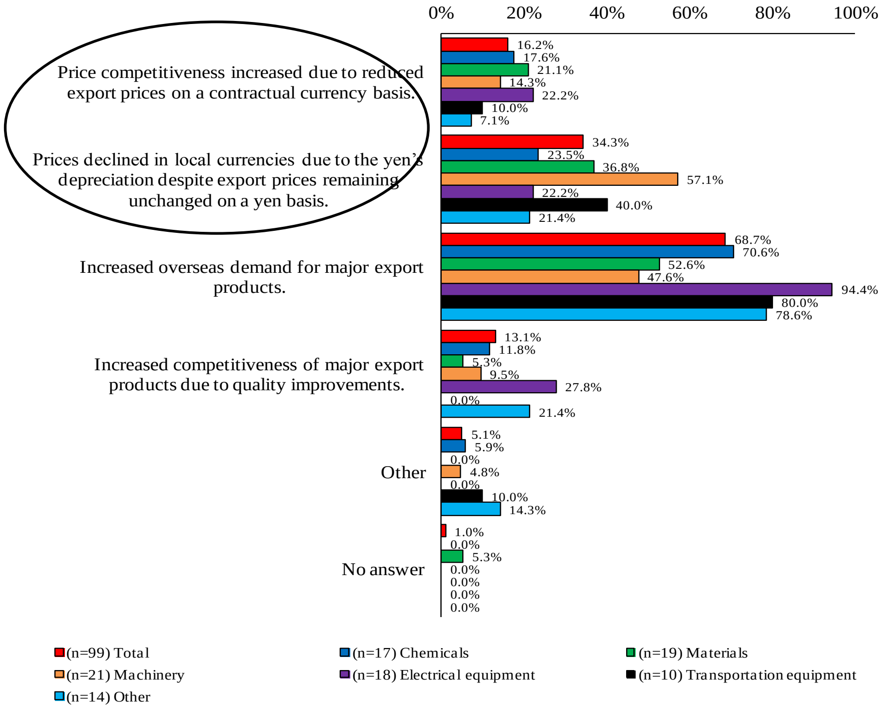
- Reasons for the current weak growth in export volume include decreased demand in emerging countries and the fact that companies - with some exceptions - have not significantly reduced prices despite the drop in the yen.
- Looking at trends in exchange rates and export prices, the total export prices of all products have not changed notably despite currency fluctuations throughout the 2000s, remaining almost the same irrespective of the yen's relative strength (Chart 1).
- The yen's weakening since November 2012 has enabled some companies to increase export volumes due to (i) lower commodity prices in local currencies while export prices remained unchanged on a yen basis, or (ii) price reductions on a contractual currency basis (Chart 2).

[Chart 1: Changes in Real Effective Exchange Rates and Export Prices (All Products; Contractual Currency Basis)]



Source: Real Effective Exchange Rates and Corporate Goods Price Index (2010 basis) (Bank of Japan)

[Chart 2: Reasons for the Increase in Export Volume (since November 2012, when the yen began to weaken)]



Source: Research on Companies' Pricing Practices Compared with Exchange Rate Fluctuations (Mitsubishi UFJ Research and Consulting)

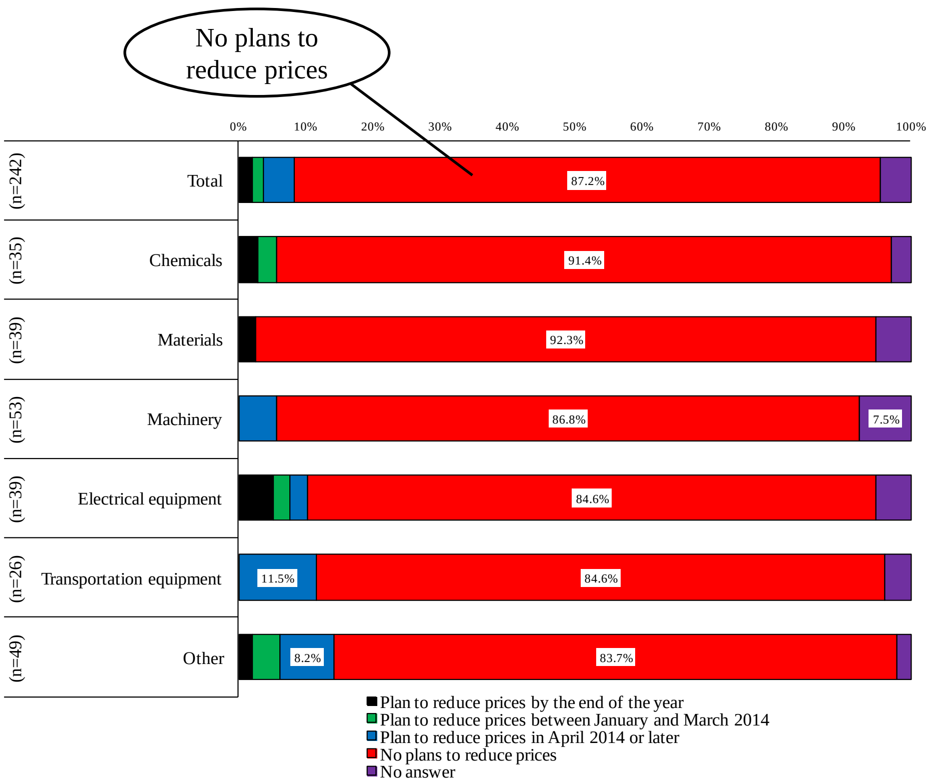
International Trade and Investment Trends in Japan (3)

– Reasons for Current Weak Export Volume Growth –

- Many companies that have not revised prices currently have no plans to do so (Chart 1).
- As reasons for their caution with regard to price revisions, many stated that sales cannot be expected to increase even if prices are reduced or that prices are revised when product models change but that there are no such plans at present (Chart 2). Export volume growth has remained weak partly due to this corporate behavior.

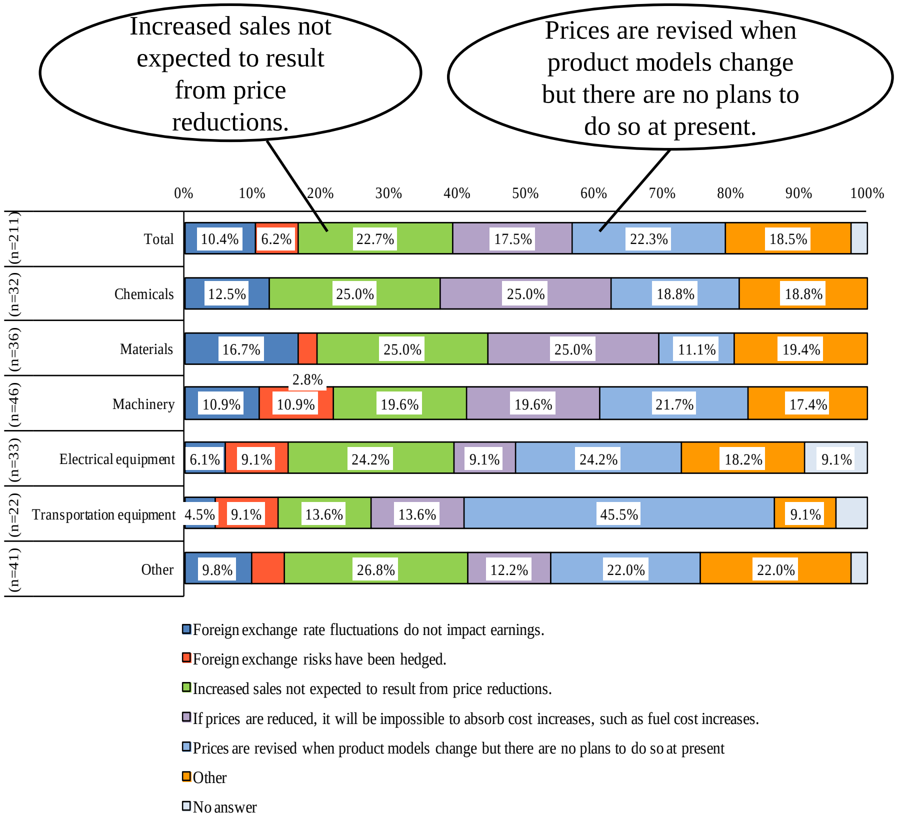
Notes: The survey was conducted in January 2014. It is possible that a larger number of companies may reduce prices depending on world economic trends and future stabilization in the exchange market.

[Chart 1:Future Price Revision Plans of Companies that Have Not Revised Export Prices]



Source: Research on Companies' Pricing Practices Compared with Exchange Rate Fluctuations (Mitsubishi UFJ Research and Consulting)

[Chart 2: Reasons Export Price Reductions Are Not Planned]

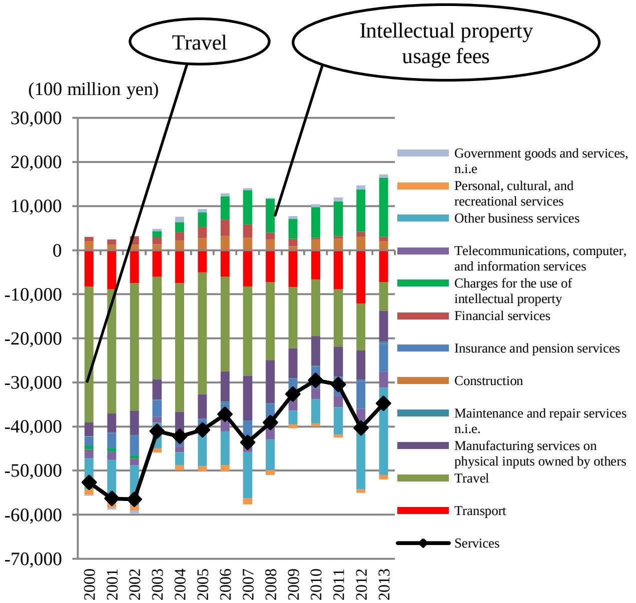


Source: Research on Companies' Pricing Practices Compared with Exchange Rate Fluctuations (Mitsubishi UFJ Research and Consulting)

International Trade and Investment Trends in Japan (4)

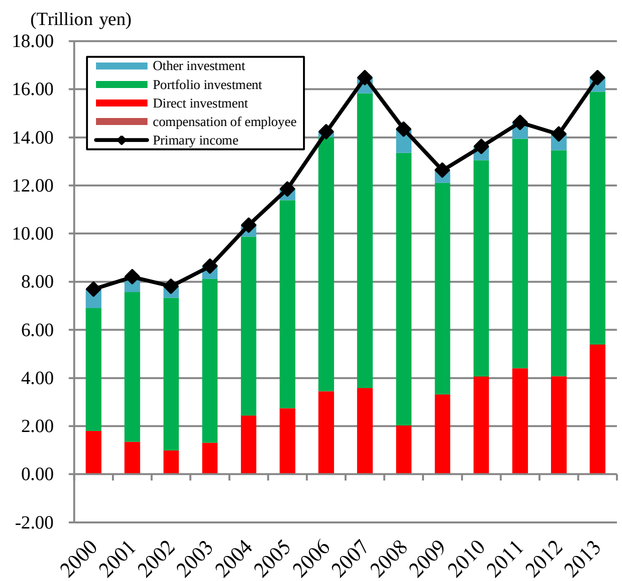
- The services account deficit decreased by around 1.5 trillion yen, from around 5 trillion yen in 2000 to around 3.5 trillion yen in 2013, due to improvements in the balance relating to travel and intellectual property usage fees (Chart 1). Due to increased overseas investment, coupled with yearly increases in direct investment and portfolio investment earnings, the primary income balance recorded a surplus of around 16.47 trillion yen in 2013 - the second largest following the approximately 16.48 trillion yen surplus in 2007, prior to the Global Economic Crisis (Chart 2). However, as a result of the expansion of the trade deficit, the current account balance for 2013 was a surplus of 3.2343 trillion yen. The surplus has narrowed in three consecutive years (Chart 3).
- In order to maintain the current account surplus, it is important to further decrease the services account deficit by, for example, inviting more tourists and increasing earnings from intellectual property usage fees. The income surplus must also be further increased by improving overseas investment returns while endeavoring to decrease the trade deficit by strengthening export competitiveness and ensuring stable, low-cost resource procurement.

[Chart 1: Changes in Services (2000 to 2013)]



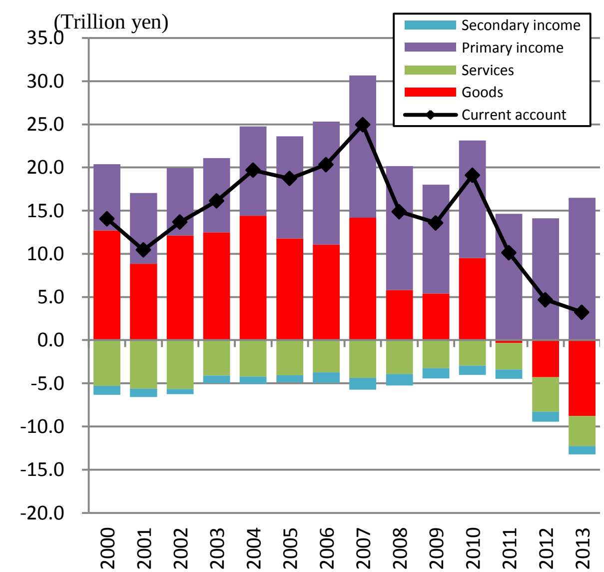
Source: Balance of Payments (Ministry of Finance)

[Chart 2: Changes in Primary Income (2000 to 2013)]



Source: Balance of Payments (Ministry of Finance)

[Chart 3: Changes in Current Account (2000 to 2013)]



Source: Balance of Payments (Ministry of Finance)

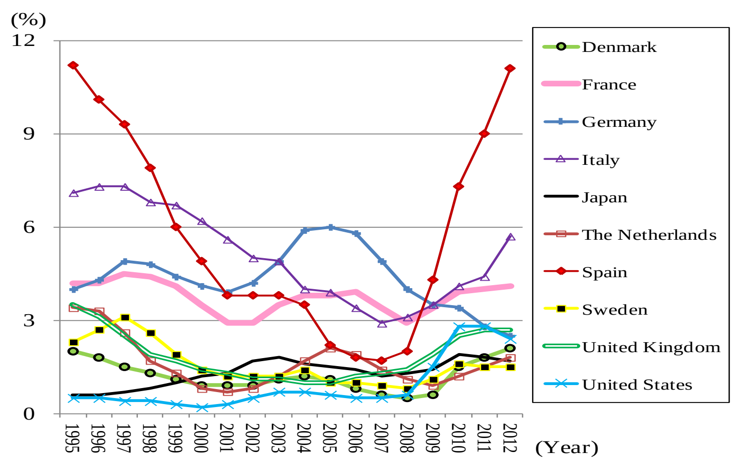
Labor Reforms in Europe

- In Europe, signs of economic recovery are finally appearing, but the unemployment rate remains high. To deal with this structural problem, labor market reform remains an urgent issue (Chart 2).
- While measures taken in southern European countries to increase labor market flexibility (easing of wage adjustment procedures, etc.) have attracted public attention, narrowing disparities (between regular and non-regular workers) and active labor market policies (support for unemployed people to find jobs, etc.) have also been emphasized (Chart 1 and Chart 3). This suggests the importance of the policy mix in making reforms.

[Chart 1: Recent Labor Market Reforms in Europe]

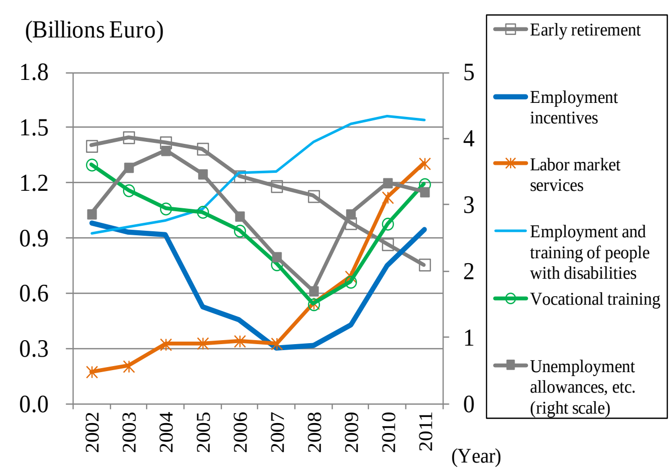
Objectives	Contents	Countries that took relevant measures
Stabilization of employment and strengthening of regulations on non-regular employment	Avoidance of prolonged temporary contracts (setting of a maximum period, automatic conversion to permanent contracts after a certain period of time elapses), improvement of working conditions for non-regular employment, increasing the cost of non-regular employment, etc.	Spain (2010), Italy (2012), France (2013), the Netherlands (2012 and 2014), Germany (2011) and the UK (2011)
	Protection of the rights of posted workers across borders	EU (2014)
	Introduction of a unified national minimum wage	Germany (agreed in April 2014; system planned to be introduced from 2015 until 2017) (All of the major countries, excluding Italy, Sweden and Denmark, have statutory minimum wages.)
Increasing labor market flexibility	Increasing of wage flexibility	Spain (2012) and France (2013)
	Easing of regulations on the dismissal of regular workers	Spain (2012) and Italy (2012)

[Chart 2: Comparison of Long-Term Unemployment Rates]



Notes: Long-term unemployed: people who have been out of work for 12 months or longer
Source: Data from Eurostat

[Chart 3: Changes in Expenditure Related to Labor Market Policy in Denmark]



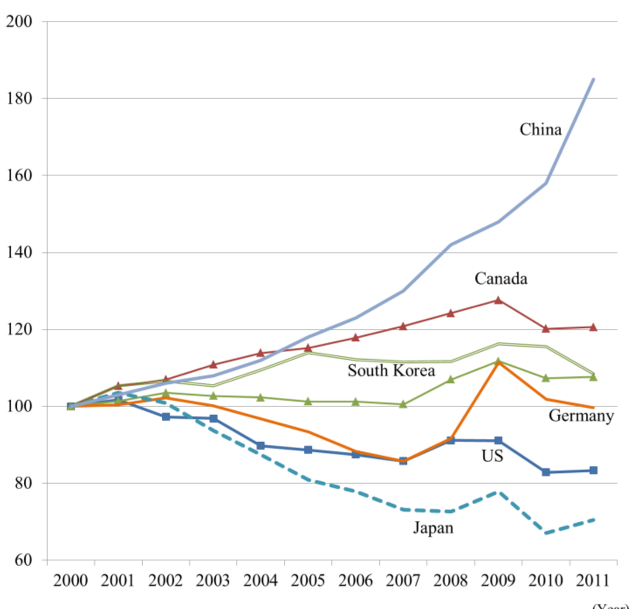
Source: Data from Eurostat

The Manufacturing Renaissance & Reshoring in the U.S., the Effect of the Shale Revolution (1)

Reshoring, the return to the U.S. of its manufacturing base, focused largely on domestic demand, is occurring because of an improved business environment due to a result of rising wages overseas (Chart 1) and the risk of technology leakage, against the background of the recent policy prioritizing manufacturing (Chart 2, Chart 3 and Chart 4).

[Chart 1: Comparison of Unit Labor Costs transitions in Manufacturing (2000=100)]

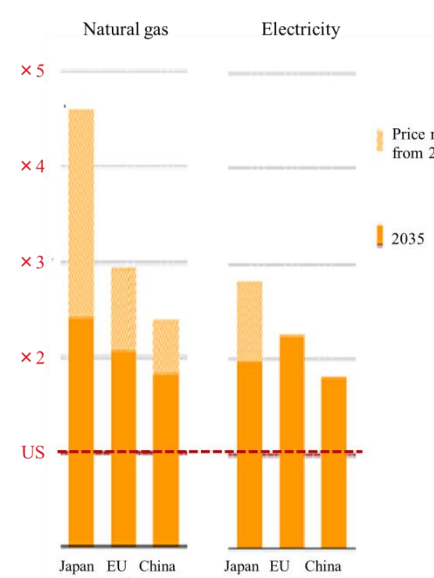
– Wage differences have slightly diminished –



Notes: The figures for China are economy-wide.
Source: Data from the US Department of Labor and the US Department of Commerce (ESA)

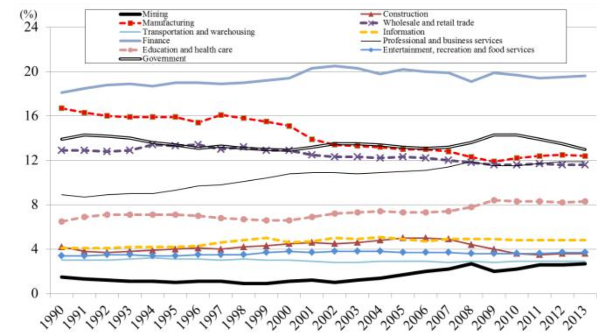
[Chart 2: Industrial Energy Prices in Comparison with the United States]

– Partly due to the shale gas revolution, industrial energy prices have declined in the United States –



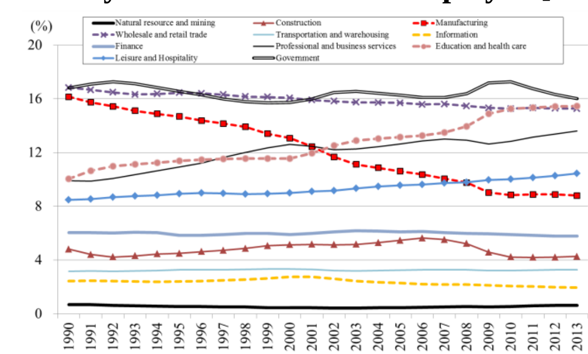
Source: Reprinted from the digest version of World Energy Outlook 2013 (IEA)

[Chart 3: Individual Industry Percentages of Total Nominal GDP]



Notes: The standard was revised in 1997 onward.
Source: Data from the US Department of Commerce

[Chart 4: Percentage Accounted for by Each Industry in Total Number of Employees]

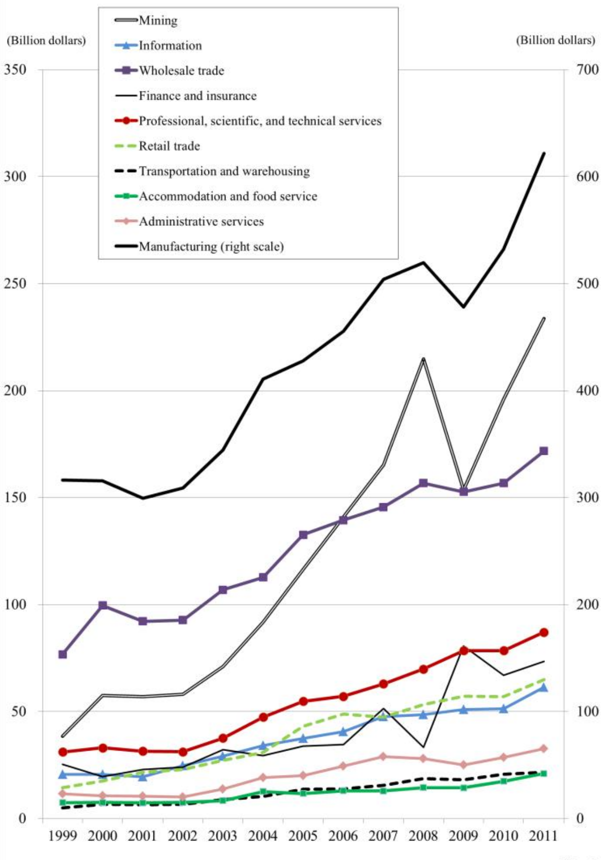


Notes: Annual average of the monthly number of employees in non-agricultural sectors
Source: Data from the US Department of Labor and the CEIC database

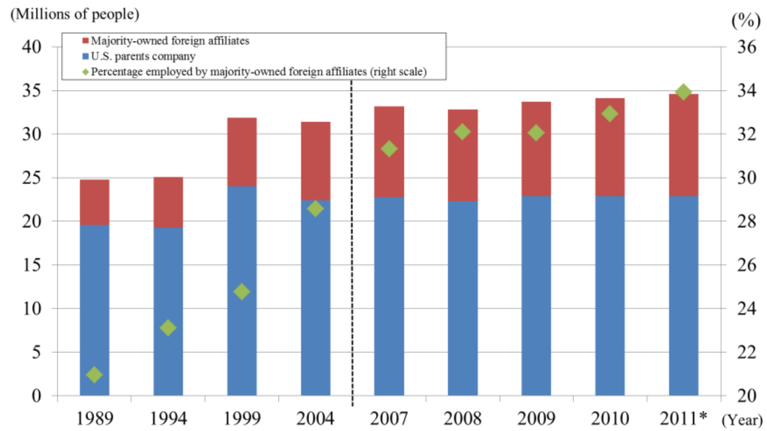
The Manufacturing Renaissance & Reshoring in the U.S., the Effect of the Shale Revolution (2)

The overseas deployment of U.S. businesses as a whole remains on a upward trend, as value-added(Chart 1), employment(Chart 2), fixed investment and other indexes of their overseas subsidiaries continue to rise(Chart 3).

[Chart 1: Changes in the Nominal Added Value of American Overseas Subsidiaries by Industry]

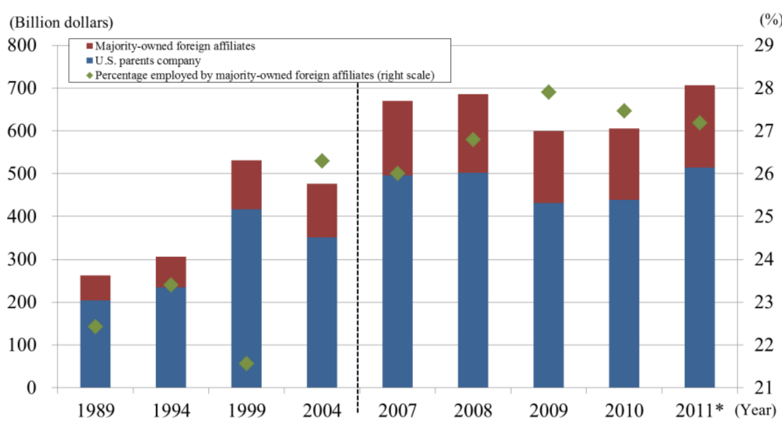


Notes: Banks are not included in the "finance and insurance" category from 1999 to 2008.
Source: Data from the US Department of Commerce (BEA)



Notes: Beginning with 1999, very small affiliates, and parents of very small affiliates, are included in the estimates. A "very small" affiliate is one whose assets, sales, and net income (positive or negative) were each not greater than $7 million. 2011 figures are preliminary.
Source: Data from the U.S. Bureau of Economic Analysis (BEA)

←[Chart 2: Changes in the Number of Persons Employed by Multinational U.S. Parent Companies and by their Majority-owned Foreign Affiliates]



Notes: Beginning with 1999, very small affiliates, and parents of very small affiliates, are included in the estimates. A "very small" affiliate is one whose assets, sales, and net income (positive or negative) were each not greater than $7 million. 2011 figures are preliminary. For the years before 2007, the capital expenditures for bank U.S. parents and foreign affiliates are estimated.
Source: Data from the U.S. Bureau of Economic Analysis (BEA)

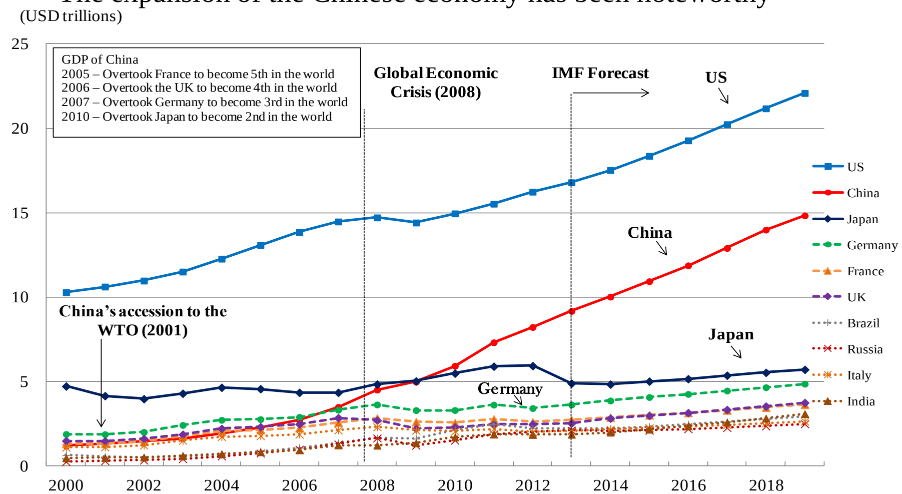
←[Chart 3: Changes in the Capital Expenditures of Multinational U.S. Parent Companies and Their Majority-owned Foreign Affiliates]

Search for New Growth Models (1) China

- China has achieved annual growth averaging nearly 10% for over 30 years through quantitative expansion of human and physical capital, and has strengthened its presence in the world economy (Chart 1). However, the growth rate recently dropped to approximately 7%. As seen in demographic movement, in particular (Chart 2), some changes have emerged among the conventional growth elements.
- There is an urgent need for China to change its growth model, which is excessively dependent on investment. China must also address the issue of excessive production capacity and problems concerning state enterprises (Chart 3 and Chart 4).

[Chart 1: Changes in the GDPs of Major Countries]

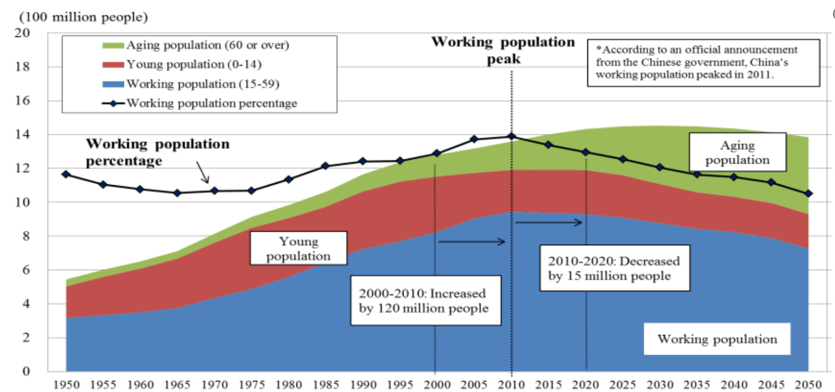
– The expansion of the Chinese economy has been noteworthy –



Notes: Countries whose GDPs were in the top ten in 2013 are indicated.
Source: IMF World Economic Outlook, April 2014

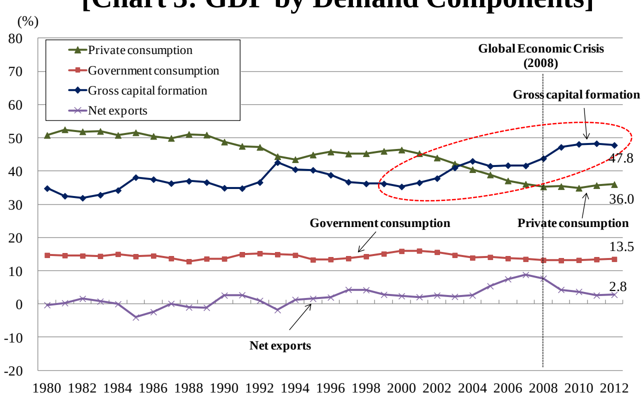
[Chart 2: Changes in Chinese Demographics]

– Working population hit a peak in 2010 and China will enter the population onus stage –



Notes: 1. There are three types of United Nations World Population Prospects (high variant, medium variant and low variant). Here, the medium variant prospects are indicated.
2. Working-age is defined to be between the ages of 16 and 59 in light of the press release dated January 20, 2014 issued by the National Bureau of Statistics of China.
3. According to an announcement by the National Bureau of Statistics of China, China's working population peaked in 2011 and decreased in 2012 and 2013.
Source: World Population Prospects: The 2012 Revision (United Nations)

[Chart 3: GDP by Demand Components]



Source: Data from the National Bureau of Statistics of China and the CEIC database

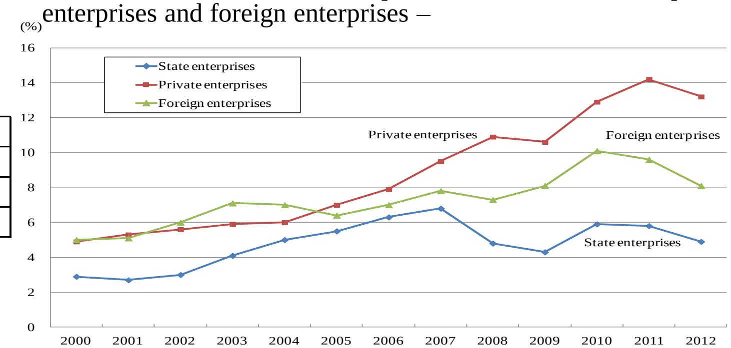
– High dependence on investment even in comparison with Japan during its high-growth period, Republic of Korea or Taiwan –

Capital formation percentage of GDP

	Maximum	Year
Japan	36.4%	1973
Republic of Korea	38.0%	1991
Taiwan	30.9%	1980

[Chart 4: Return on Corporate Assets in the Mining and Manufacturing Industries]

– Return on assets of state enterprises is lower than that of private enterprises and foreign enterprises –



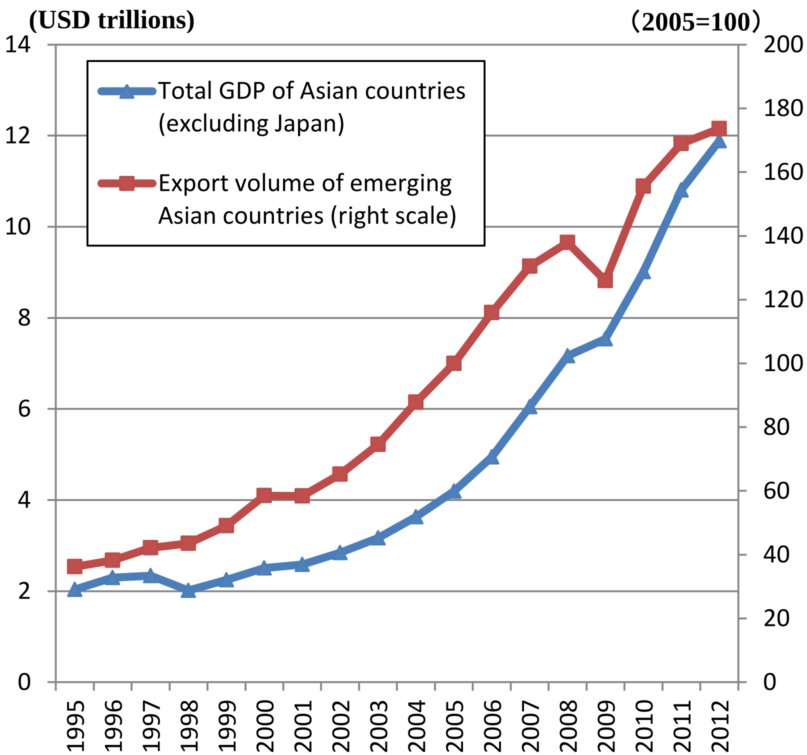
Notes: 1. The mining and manufacturing industries include the mining industry, the manufacturing industry and utilities.
2. Return on assets is obtained by dividing total profits from the respective enterprises by total assets.
Source: Data from the National Bureau of Statistics of China and the CEIC database

Search for New Growth Models (2) ASEAN

ASEAN has built supply chains covering the entirety of East Asia and has achieved export driven growth based on the competitive edge provided by low labor costs (Chart 1). In order to ensure sustainable growth through a virtuous cycle of expanding domestic demand and enhancing productivity, these countries need to further promote liberalization as well as fostering innovation, improving infrastructure and establishing economic systems that support further growth (Chart 2).

[Chart 1: Growth of Asia and Changes in Trade Volumes]

– Asia has achieved export driven growth –



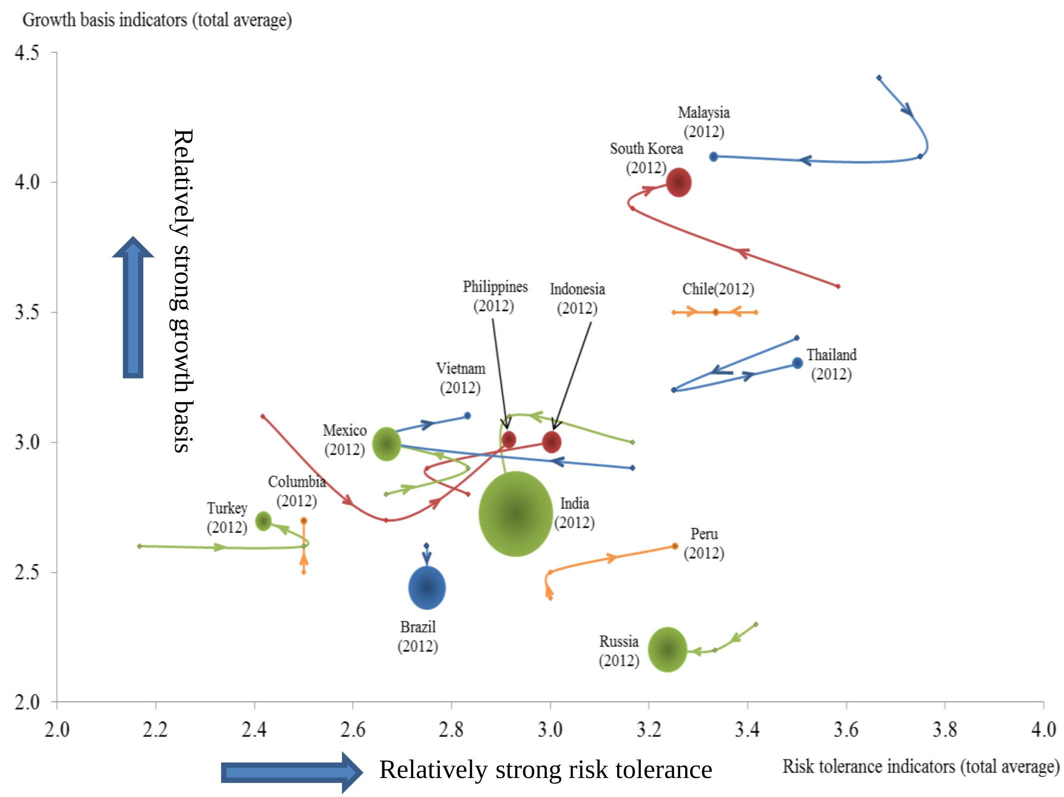
Source: IMF World Economic Outlook, April

	[Chart 2: Economic Characteristics and Initiatives for Achieving Growth]
Thailand	The government has adopted a dual track policy in an attempt to generate growth driven by both external and domestic demand while intensively investing in the formation of a cluster to foster certain designated industries such as the automotive industry. Thanks to the elimination of tariffs under AFTA and AFTA+1, accumulation of the automotive industry has accelerated. The government has been making efforts to foster high value-added industries and increase the sophistication of industries, and raised the minimum wage significantly to expand domestic demand and increase national income.
Malaysia	Since the 2000s, home appliance manufacturers have moved production to such countries as China, Thailand and Vietnam, and this has reduced the total nominal GDP percentages of the electrical equipment and electronics industries. The government intends to strengthen the services industry in the future.
Indonesia	Export share of raw materials increased and the trade structure has become vulnerable to resource price fluctuations. In the meantime, imports increased due to rising domestic demand and the country recorded a trade deficit in 2012. The government decided to redouble its efforts to promote structural reform of industries and exports, and the key issues are whether it can actually implement policies which create a favorable environment for exports, such as the development of infrastructure.
The Philippines	The economy is led by private consumption and the services industry thanks to significant outsourcing. Specifically, the country now serves as the world's largest call center hub. Outsourcing has expanded from call centers to such fields as software development and medical secretarial services. The government also considers it as a priority industry.

Analysis of Economic Fundamentals in Emerging Countries

- When quantifying emerging countries' economic fundamentals using various indicators in terms of risk tolerance and basis for growth, countries with high financial vulnerabilities tend to accompany a relatively weak growth basis. However, differences among countries shrunk as a whole from 2005 to 2012.

[Scatter Diagram of Risk Tolerance Indicators and Growth Basis Indicators (2005 to 2012)]



Notes: Points and lines show movements in the combinations of risk tolerance indicators and growth basis indicators (total averages) for each country from 2005 to 2012. The bubble charts indicate the 14 countries' GDP shares (based on purchasing-power-parity (PPP)) as of 2012.

[List of Risk Tolerance Indicators]

Group	Indicators
Macro economy	Real GDP growth rate; unemployment rate; inflation rate
Government sector	Governance; fiscal balance (% of GDP); government debt (% of GDP)
External economy	Current account balance (% of GDP); trade balance (% of GDP); short-term foreign debt / total reserves
Trade structure	Concentration of export destinations (countries and regions); dependence on resources or primary products in exports
Capital composition	Ratio of inward portfolio investment

[List of Growth Basis Indicators]

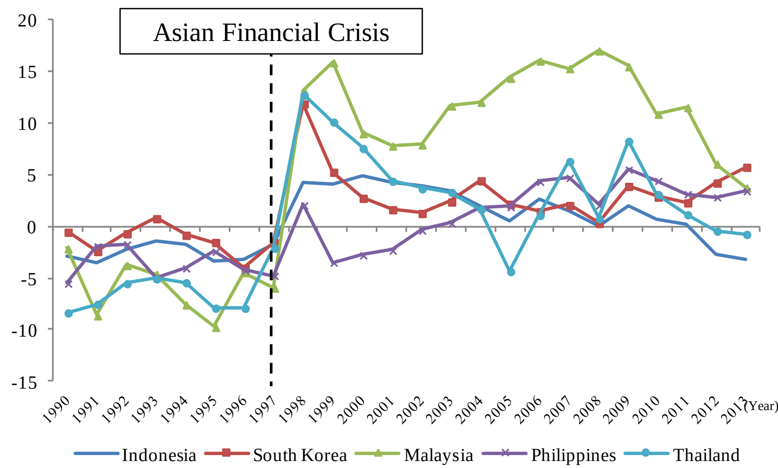
Group	Indicators
Macro economy	Investment ratio; trade openness
Human resources	Population dynamics and structure; human capital
Level of development	Quality of overall infrastructure; urbanization rate; value-added in manufacturing (% of GDP)
Economic and social systems	Intellectual property protection; governance
Financial deepening	Market capitalization of listed companies (% of GDP); domestic credit to private sector by banks (% of GDP)

Policies that Effected Structural Changes after Previous Economic Crises

- Efforts to proactively promote trade policies to liberalize the external economy have been made in addition to structural reforms to strengthen financial tolerance (Chart 1) triggered by financial crises or other economic shocks. These efforts have contributed to strengthening the longer term basis for growth (Chart 2).

[Chart 1: Changes in Current Account Balances (against GDP) after the Asian Financial Crisis]

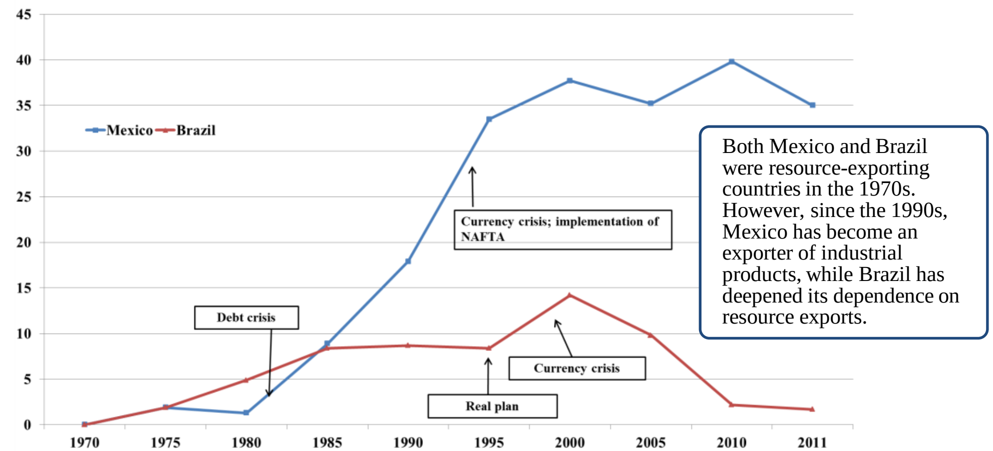
– After the Asian Financial Crisis, South Korea, Malaysia and Thailand have turned to record current account surpluses –

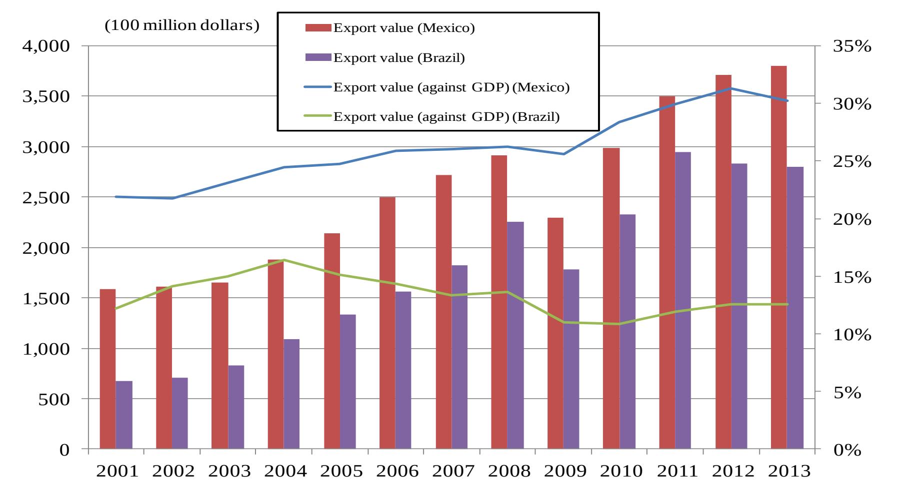


[Chart 2: Comparison of External Economic Policies after Currency Crises, etc.]

South Korea (after the 1998 financial crisis)	The government promoted liberalization of capital transactions and proactively promoted FTAs in addition to financial system, corporate and labor market reforms.
Mexico (after the crisis in the 1990s)	The weighted average tariff rates were reduced from 11.9% in 1990 to 7.3% in 1995, and then to 2.2% in 2010. The government is implementing an FTA hub strategy.
Brazil	The weighted average tariff rates were reduced from 19% in 1990 to 11.0% in 1995, and then to 7.7% in 2012. The government promotes FTAs in a limited manner.

[Mexico and Brazil: Ratio of Export Value of Industrial Products among Top 10 Exports]





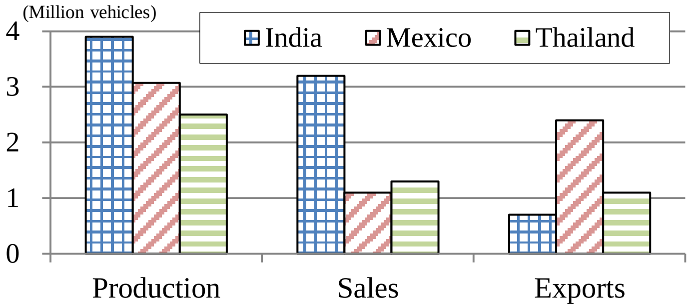
Notes: Because Mexican GDP is publicized industry by industry (not by demand item), export value, a demand item, is determined some time after the publication of GDP. Therefore, the 2013 export value for Mexico is not available.
Source: Data from the Brazilian Institute of Geography and Statistics (IBGE), the Mexican National Institute of Statistics and Geography (INEGI), and the CEIC database

Automotive Policies in Mexico, Thailand and India

- Mexico has strengthened its external economic relationships and has achieved export driven growth. Taking advantage of its geographic proximity to a huge U.S. market, Mexico is characterized as an assembly and export base for U.S.. Thailand is seeking to form industrial clusters, including the parts industry, focusing on both domestic and external demand, as well as enhancing external economic relations. India has achieved growth while developing its domestic market such as fostering its own automobile manufacturers.

[Number of Automobiles Production, Sales, and Exports in 2013]

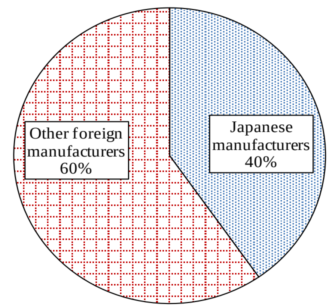
– The largest number of domestic automobiles production and sales in India –



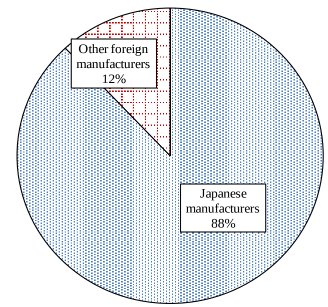
Notes: "Exports" figure for Mexico is the number of production for exports.
Source: Production and Sales: the Marklines database; Exports: data from the Society of Indian Automobile Manufacturers (SIAM), the Mexican Automotive Industry Association (AMIA), the Federation of Thai Industries (FTI), and the CEIC database

[Domestic Market Share in Mexico, Thailand and India by Nationality of Automobile Brand]

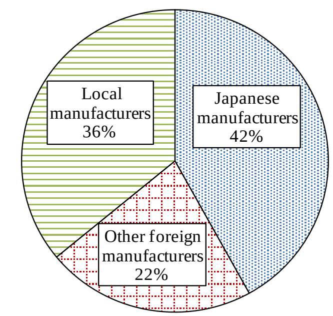
Mexico



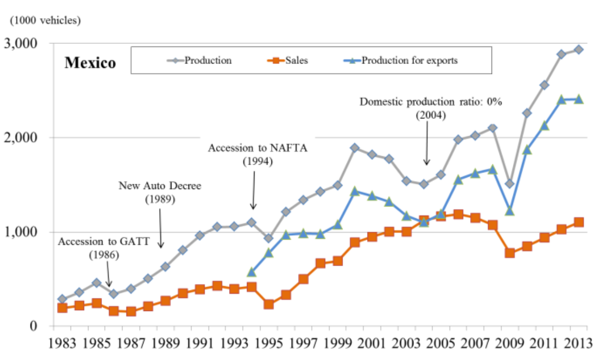
Thailand



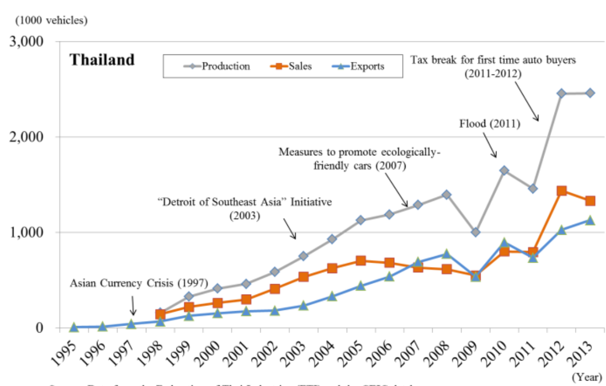
India



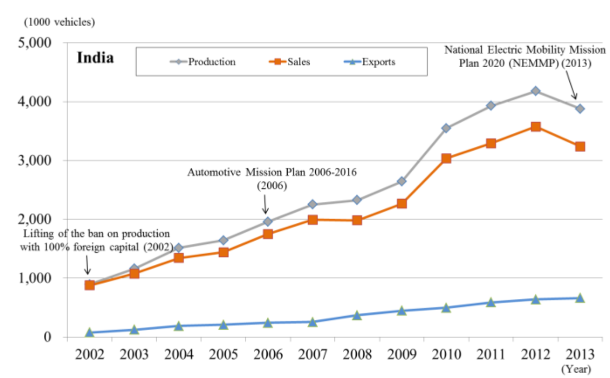
[Changes in the Number of Automobiles Production, Sales, and Exports in Mexico, Thailand and India]



Notes: 1. Excludes large buses and trucks
2. The number of automobiles production is based on INEGI data up to 1993 and on AMIA data for 1994 onward.
Source: Data from the Mexican Automotive Industry Association (AMIA), the National Institute of Statistics and Geography (INEGI), and the CEIC database



Source: Data from the Federation of Thai Industries (FTI) and the CEIC database



Source: Data from the Society of Indian Automobile Manufacturers (SIAM) and the CEIC database

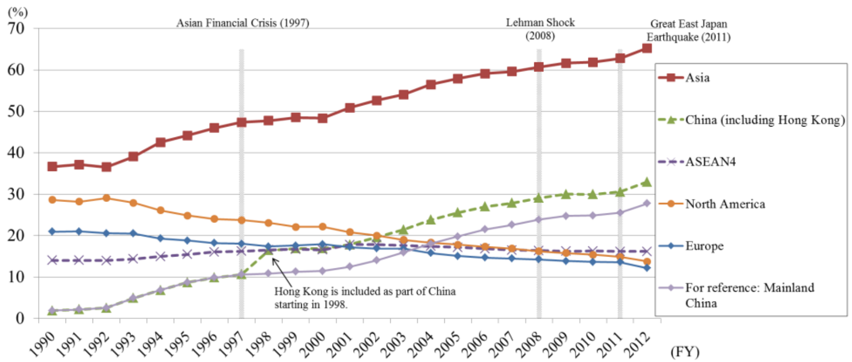
East Asia for Japanese Companies (1)

– Possibility of Contributing to Growth Model Changes in East Asian Countries –

- Asia, in which the largest number of Japanese overseas affiliates are located, is an important area for Japan (Chart 1 and Chart 2).
- Payments to Japanese investors (dividends and royalties) from Japanese overseas affiliates in Asian countries account for the largest percentage in the manufacturing industry (Chart 3).

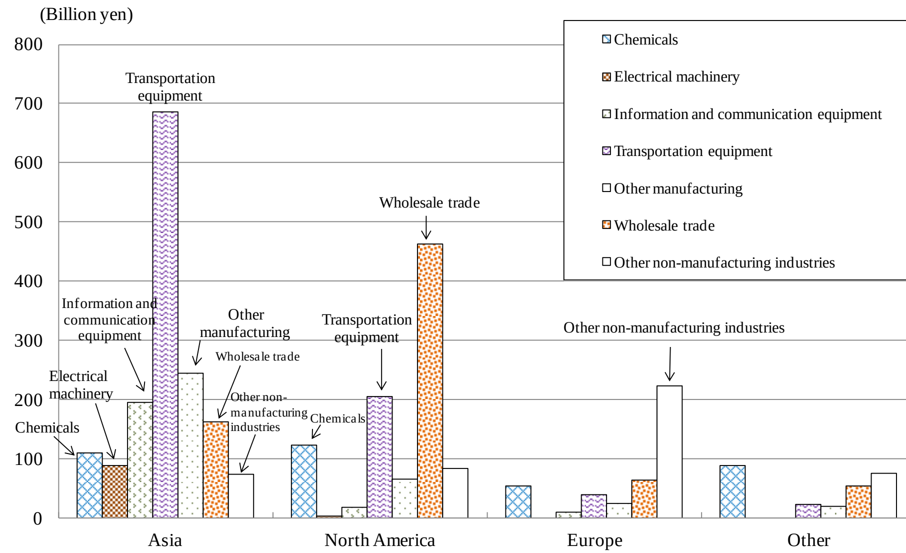
[Chart 1: Changes in Percentages of the Number of Japanese Overseas Affiliates in Respective Countries]

– The percentage of the number of Japanese overseas affiliates increased, particularly in China –



Notes: 1. North America: The United States and Canada; ASEAN4: Indonesia, Malaysia, the Philippines and Thailand; China includes Hong Kong from 1998 onward.
2. Figures for FY2012 are preliminary ones.

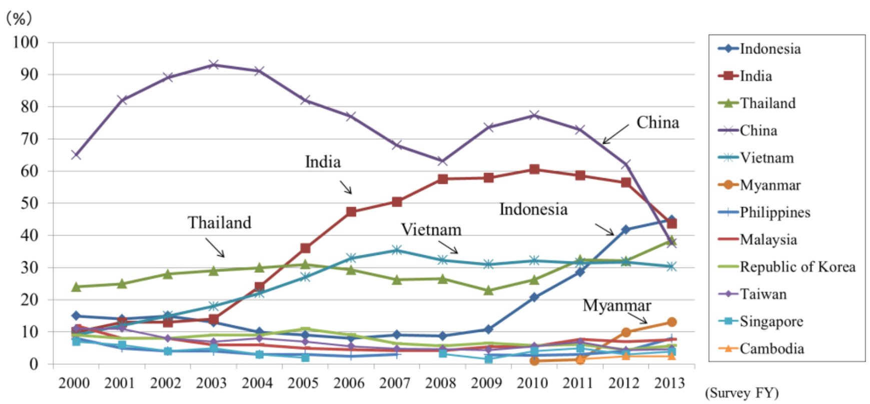
[Chart 3: Payments to Japanese Investors by Japanese Overseas Affiliates (2012)]



Notes: Payments to Japanese investors include both dividends and royalties.
Source: Basic Survey of Overseas Business Activities (Ministry of Economy, Trade and Industry)

←[Chart 2: Promising Countries/Regions for Overseas Business over the Medium Term]

– Until FY2012, China had been considered the most promising country for overseas business, but according to a survey conducted in FY2013, Indonesia has taken over first place, followed by India, Thailand and China –



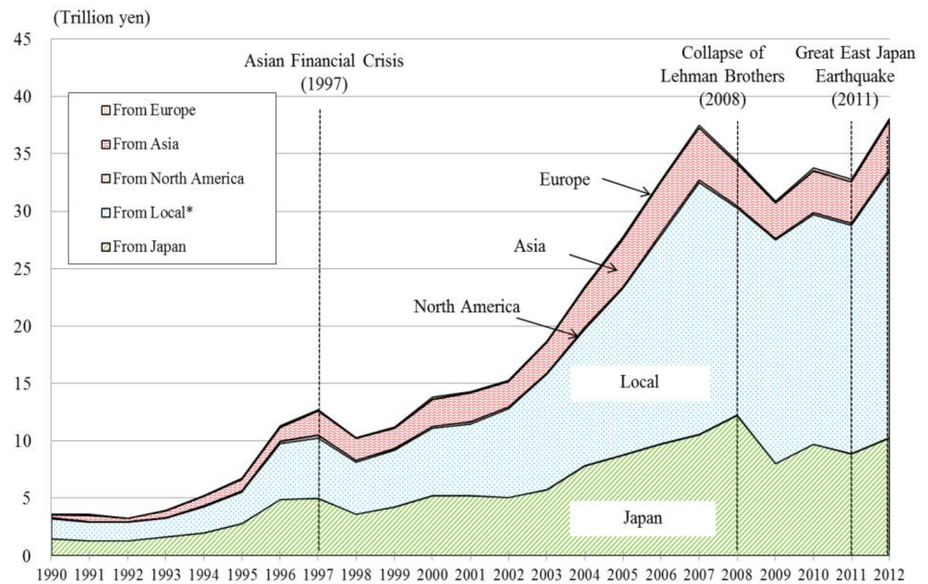
Notes: Promising countries/regions for overseas business over the medium term (next three years or so).
Source: Survey Report on Overseas Business Operations by Japanese Manufacturing Companies (FY2000-2013) (Japan Bank for International Cooperation)

East Asia for Japanese Companies (2)

– Possibility of Contributing to Growth Model Changes in East Asian Countries –

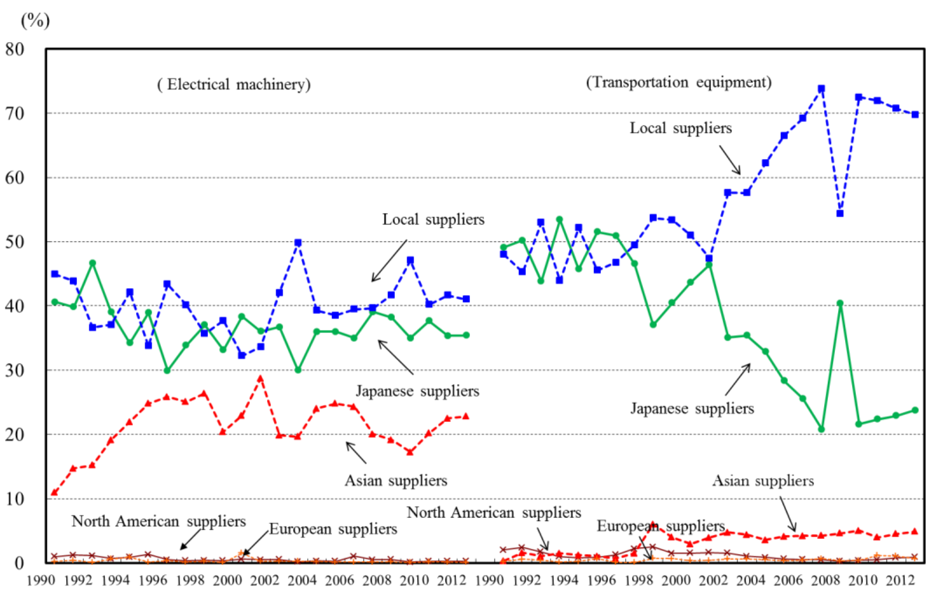
- Trade and investment relations have deepened between East Asian countries, and Japanese companies have also been active in promoting East Asia-wide development and production.
- As Japanese companies began engaging in production in East Asia, local content rates increased but the value of purchases from Japan did not decline (Chart 1).
- Looking at different sectors, certain percentages of supplies for the electrical machinery industry come from the countries where overseas affiliates of Japanese companies are located while some from Japan or other Asian counties. The percentage of local purchases has increased significantly in the transportation equipment industry (Chart 2).

[Chart 1: Purchases by Japanese Manufacturing Affiliates in Asia]



Source: Basic Survey of Overseas Business Activities (Ministry of Economy, Trade and Industry)
* Local: Country in which overseas affiliates of Japanese companies are located

[Chart 2: Purchases by Japanese Manufacturing Affiliates in Asia (by Sector)]



Notes: Industrial classifications were modified in 2001, but in the interest of statistical continuity, figures for the electrical equipment industry have been calculated to include the totals for both the electrical equipment and information and communication equipment industries under the new classifications.
Source: Basic Survey of Overseas Business Activities (Ministry of Economy, Trade and Industry)
* Local: Country in which overseas affiliates of Japanese companies are located

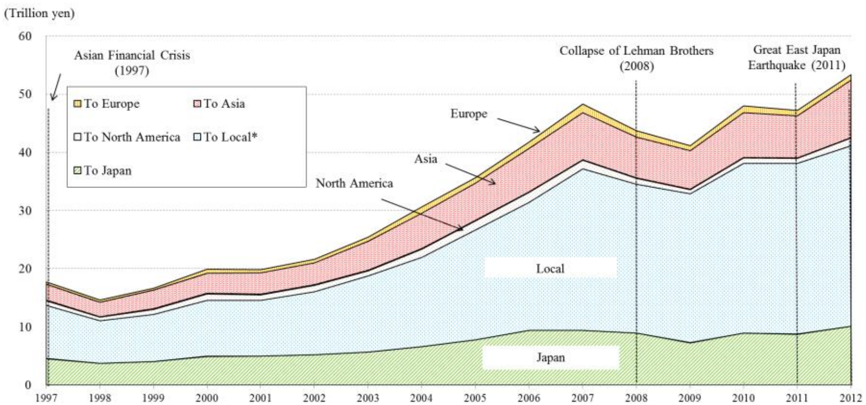
East Asia for Japanese Companies (3)

– Possibility of Contributing to Growth Model Changes in East Asian Countries –

- Japanese companies' shares of local sales are increasing (Chart 1) and they are also actively involved in R&D in Asia (Chart 2). Japanese companies have thus been further deepening their local business activities.
- Japan will be able to continue contributing to the long-term development of other Asian countries by offering assistance in the development of human resources in addition to transferring Japanese business models and know-how (Chart 3).

[Chart 1: Sales of Japanese Manufacturing Affiliates in Asia]

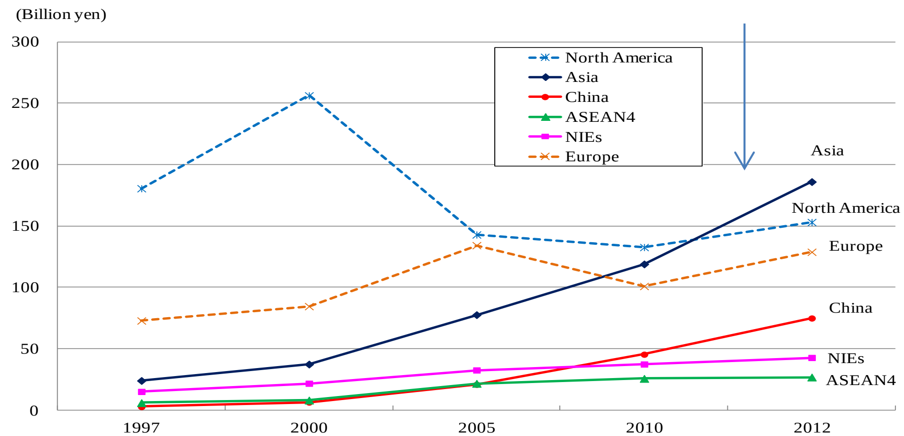
– Japanese manufacturing affiliates in Asia have become more dependent on local sales, with decreasing share of exports.



Source: Basic Survey of Overseas Business Activities (Ministry of Economy, Trade and Industry)
* Local: Country in which overseas affiliates of Japanese companies are located

[Chart 2: R&D Expenses of Japanese Manufacturing Affiliates]

– R&D expenses in Asia exceeded those in North America in 2012 –



Notes: Hong Kong is included in the NIEs for 1997 and in China from 2000 onward.
Source: Basic Survey of Overseas Business Activities (Ministry of Economy, Trade and Industry)

Chart 3: Examples of Japanese Contributions
Establishment of the University Thai-Nichi Institute of Technology (2007)
Establishment of the Malaysia-Japan International Institute of Technology (MJIIT) (2011)
Establishment of the Toyota Technical Training Institute (India) (2007)
Assistance in fostering human resources specialized in production management technology for the garment industry (Myanmar) (FY2008 – FY2013)
Establishment of the Economic Research Institute for ASEAN and East Asia (ERIA) (2008)

Global Outreach Strategy Based on Japanese Trade and Investment Trends

- Japan has recorded a trade deficit for three consecutive years and its current account surplus has been diminishing. Under these circumstances, it has become increasingly important to develop favorable business environments both within and outside Japan to further strengthen the competitiveness of Japanese industry.

- To strengthen competitiveness, the government has been making intensive efforts to jumpstart industrial vitality, by, for example, promoting private investment and venture capital investment as well as promoting innovation and the sustainable development of SMEs and small businesses.

- Japanese companies must rebuild their business models in response to a new pattern of value creation with the goal of balancing business speed with expanding business scale and diversification in order to succeed amid global competition.

- It is important to reinforce leading medium-sized enterprises and SMEs that support Japanese industry and local economies seeking to adapt themselves to global environmental changes by concentrating their management resources on limited specialized sectors with the goal of becoming highly profitable niche companies with large shares of the global market.

- The government is promoting the three-pillar Global Outreach Strategy, to promote the exports of top global niche companies and expand opportunities for Japanese people and companies doing business overseas to enjoy the fruits of the growing world economy.

Three Pillars of Global Outreach Strategy

I. Build Economic Partnership Networks around the World

Develop a business environment favorable to overseas expansion to promote the capturing of growth markets

⇒ **The government will multilaterally promote not only the Trans-Pacific Partnership (TPP), but also the Regional Comprehensive Economic Partnership (RCEP), the Japan-China-South Korea FTA, and the Japan-EU EPA to build economic partnership networks covering most of Japan's trade partners.**

II. Strategic Approaches to Emerging Countries

Make strategic and intensive efforts to (i) support Japanese companies' international expansion, (ii) export infrastructures and systems, and (iii) secure the supply of resources from emerging countries in accordance with the characteristics of each type and each country.

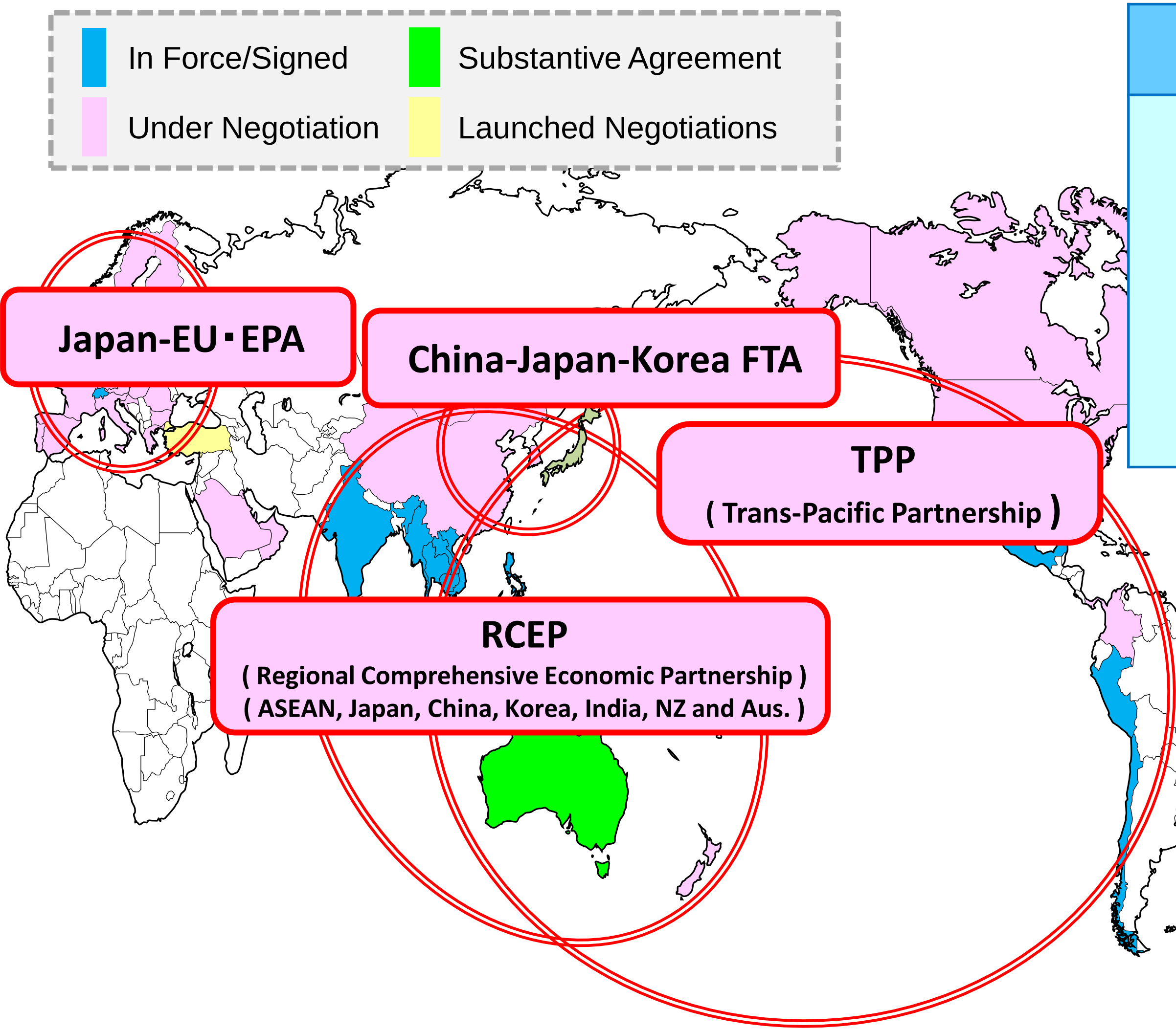
⇒ **Given the differing circumstances of each country and region with regard to such factors as levels of economic development, market participation by Japanese companies, and competition with local companies or other foreign companies, the government will promote a strategic approach specific to each emerging country while identifying priority sectors.**

III. Promotion of Foreign Direct Investment

Attract leading technologies and personnel and accelerate innovation and job creation in Japan

⇒ **The government will increase investment incentives and strengthen the systems for discovering, attracting and supporting technologies and personnel while listening to requests from the top management of global companies in order to produce concrete system improvements.**

I. Development of Japan's EPA/FTA Networks



In Force/Signed (12 countries and 1 region)			
Asia	Singapore	Asia	Viet Nam
	Malaysia		India
	Thailand	Latin America	Mexico
	Indonesia		Chile
	Brunei		Peru
	ASEAN	Europe	Switzerland
	Philippines		

Substantive Agreement (1 country)	
Pacific	Australia

Under Negotiation (4 countries and 5 regions)			
Asia	C-J-K	Europe	EU
	RCEP	North America	Canada
	Mongolia		
	Republic of Korea (Negotiation suspended)	Latin America	Colombia
Asia/ Pacific	TPP	Middle East	GCC* (Negotiation postponed)

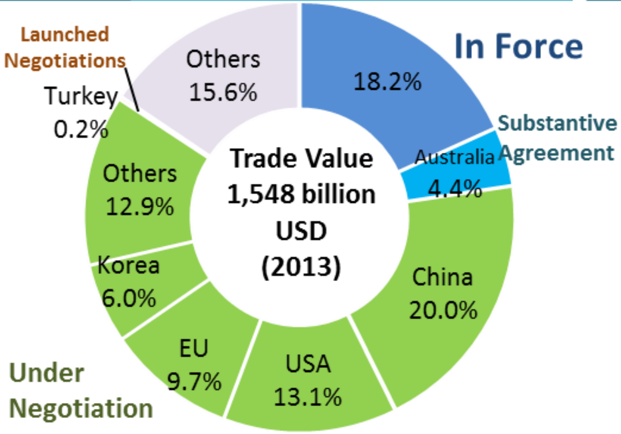
Launched Negotiations (1 country)	
Middle East	**Turkey**

* GCC: Gulf Cooperation Council (UAE, Bahrain, Kuwait, Oman, Qatar, Saudi Arabia)

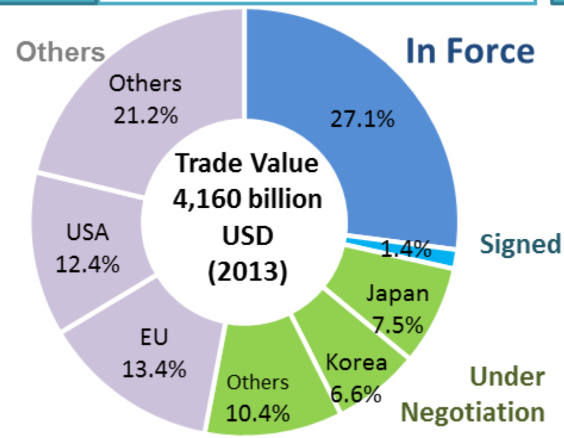
I. Coverage of EPA/FTA

Japan's Target: **FTA Ratio in Force 70% by 2018** (currently 18.2%). *Japan Revitalization Strategy, June 14, 2013, Cabinet decision*

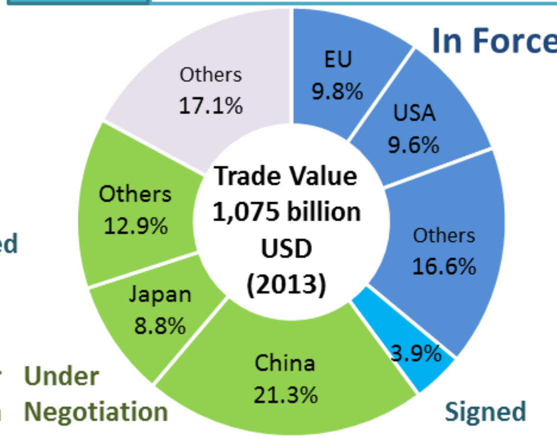
Japan
In Force: 18.2%
Including Substantive Agreement : 22.6%
Including under Negotiation: 84.2%



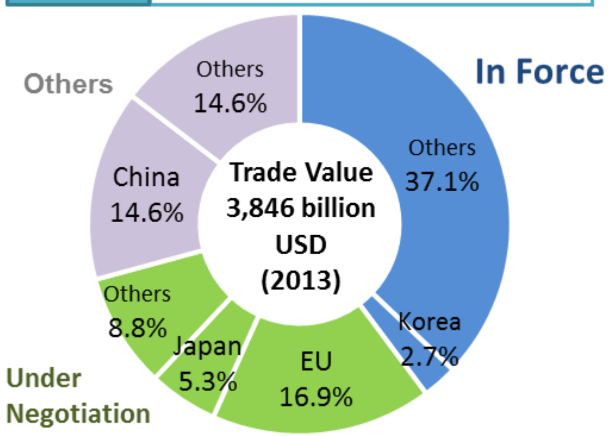
China
In Force: 27.1%
Including under Negotiation: 53.0%



Korea
In Force: 36.0%
Including under Negotiation: 82.9%

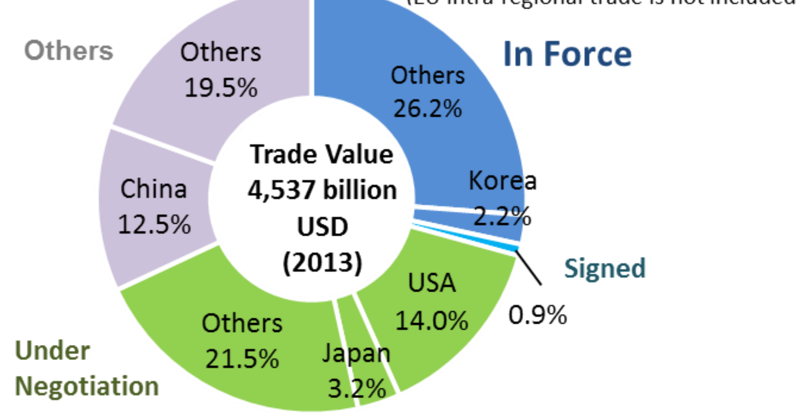


USA
In Force: 39.8%
Including under Negotiation: 70.8%



EU28
In Force: 28.4%
Including under Negotiation: 68.0%

(EU intra-regional trade is not included)

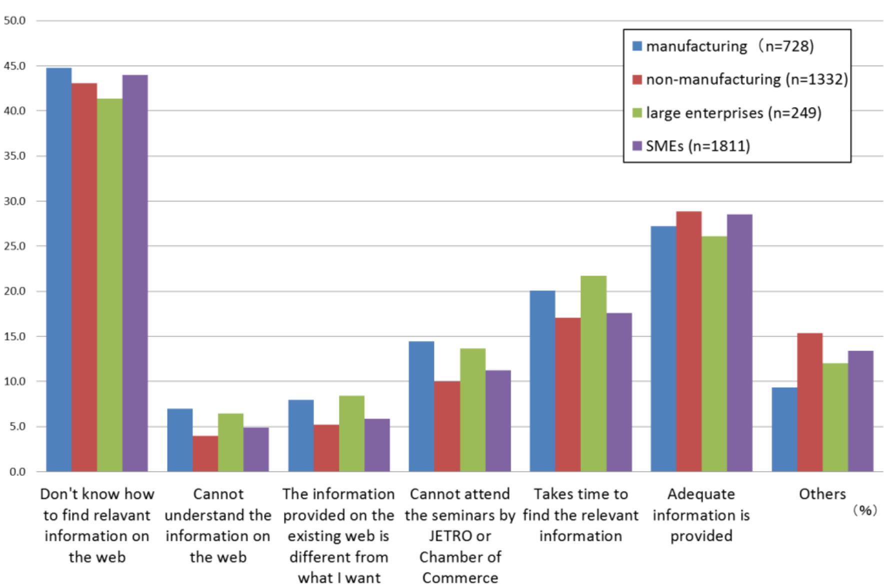


The items (Japan, China, Korea, USA, EU28) are arranged in descending order (clock-wise) of trade value per country within each progress status of negotiations. - When a country is in both bilateral FTA and plurilateral FTA negotiations with the same country at the same time. - Trade Values Reference: Global Trade Atlas (2013) . - The item is classified in more progressed status (in force → signed → under negotiation → others). - Percentages of items are calculated on rounded data, which may not necessarily add up to 100%.

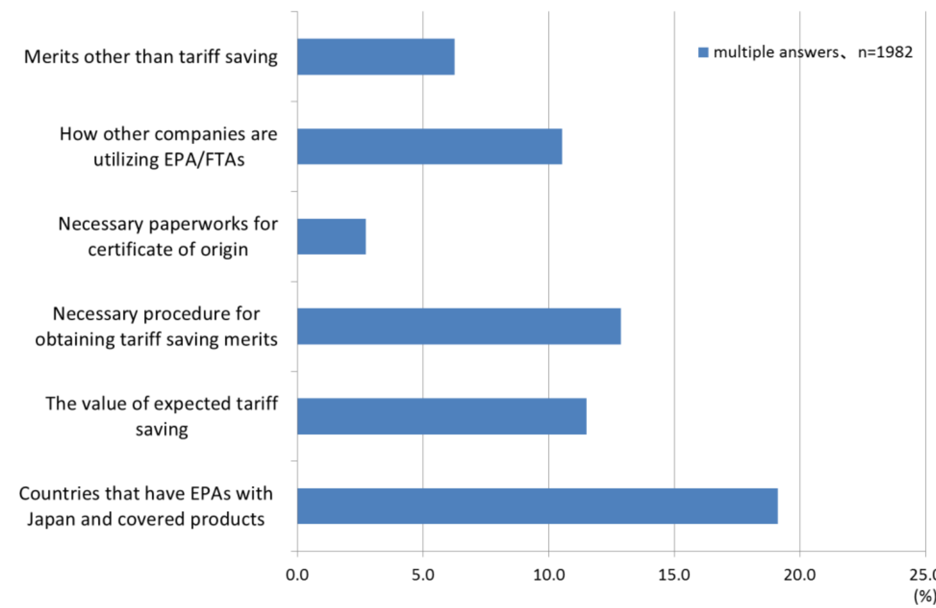
I. Economic Partnerships: How Japan's EPA/FTAs are used

- According to the questionnaire, Japanese companies answered "tariff reduction" most frequently as merits of EPA/FTAs. Other major merits listed are "easing of foreign investment restriction" and "improvement of business environment excluding the easing of foreign investment restriction" (Chart 1) .
- There are gaps in knowledge of EPA/FTAs among companies. Some companies want basic information such as the countries which conclude EPA/FTAs with Japan and which products are covered in tariff elimination/reduction schedules. Other companies want specific information such as how other companies are utilizing EPA/FTAs (Chart).
- Some companies answered that seminars conducted by public institutions such as JETRO or JCC led them to think about the merits of utilizing of EPA/FTAs. Other companies answered that their customers initially asked them to utilize EPA/FTAs.

[Chart 1: Opinions on the EPA/FTA related information provided by public institutions]



[Chart 2: Necessary information in order to assess the merit of EPA/FTA utilization]



I. WTO Initiatives

- The WTO, which is the basis of the world trade system, plays the most important role in promoting trade liberalization together with economic partnership agreements.
- In the Doha Round negotiations, Members agreed on the Bali Package, consisting of trade facilitation, some elements of agriculture and development, at the ninth Ministerial Conference of the WTO held in December 2013. Discussions on how to advance negotiations are underway.
- Plurilateral negotiations are an effective approach in promoting trade liberalization. Japan is actively engaging in Information Technology Agreement (ITA) expansion, Trade in Services Agreement (TiSA) and environmental goods negotiations.
- Regarding protectionist measures taken mainly by emerging countries, Japan has been actively utilizing the WTO dispute settlement procedures.

Details of the Trade Facilitation Agreement (TFA)

- The TFA specifies measures that WTO Member countries should take to simplify customs procedures and enhance the transparency of trade regulations.
- It is the first agreement to which all Member countries have agreed since the establishment of the WTO in 1995.
- According to an OECD estimate, the agreement will reduce trade costs of developing countries by a maximum of 15%.

Outline of Plurilateral Negotiations

[Information Technology Agreement (ITA) expansion]
- 55 countries and regions, including Japan, the United States, the EU, and China, are negotiating with the aim of expanding the coverage of the ITA (at present, 78 countries and regions are members of the ITA).

[Trade in Services Agreement (TiSA)]
- 23 countries and regions, including Japan, the United States, the EU, and Australia, are negotiating in order to further liberalize trade in services and strengthen related rules.

[Environmental goods]
- 14 countries and regions, including Japan, the United States, the EU, and China, have issued a joint statement aiming to commence plurilateral negotiations for the liberalization of trade in environmental goods at the WTO.

Effective use of the WTO Dispute Settlement Procedures

Cases that Japan recently referred to the WTO

[Against China]
- Measures Related to the Exportation of Rare Earths, Tungsten and Molybdenum
- Measures Imposing Anti-Dumping Duties on High-Performance Stainless Steel Seamless Tubes

[Against Argentina]
- Measures Affecting the Importation of Goods

[Against Russia]
- Recycling Fee on Motor Vehicles

[Against Ukraine]
- Definitive Safeguard Measures on Certain Passenger Cars

II. Strategic Approaches to Emerging Countries

- Make a strategic advance into new markets by classifying emerging countries into three types.
- Make strategic and intensive efforts to A) support Japanese companies' international expansion, B) export infrastructures and systems and C) secure the supply of resources from emerging countries in accordance with the characteristics of each type and each country.

(1) China and ASEAN

Number of Japanese companies: Approx. 30,000 companies

(i) Although Japanese manufacturers have formed industrial clusters and gained a substantial market presence, China and South Korea are catching up. It is necessary to build infrastructures in order to create more advanced supply chains.
(ii) The consumption market has expanded. It has become more significant to gain market shares.

Full-fledged advance

(i) Further strengthen competitiveness in sectors into which Japanese companies have already advanced.
(ii) Gain market shares in a broad range of industries, including non-manufacturing ones (e.g., the "Cool Japan" initiative).

(2) Southwest Asia, Middle East, Russia and CIS, and Latin America

Number of Japanese companies: Approx. 3,000 companies

(i) The wealthy and middle classes have grown, the market size is large and the growth rate is high, but Japanese companies have lagged in advancing into these regions.
(ii) There are many resource-rich countries, so it is necessary to establish and strengthen broad economic relationships from the perspective of securing resources as well.

Reaching critical mass

(i) Make full-fledged advances into promising sectors and gain some market share and presence
(ii) Strengthen relationships with resource-rich countries by increasing investment and promoting technical cooperation

(3) Africa

Number of Japanese companies: Approx. 500 companies

(i) There are high expectations of population growth and market expansion, making it necessary to advance into the region as soon as possible, but Japan is lagging so much that it is losing out before competing with other countries.
(ii) There are many resource-rich countries, and resource development and infrastructure building have proceeded.

Creating successful cases of advance into the region

(i) Create as many successful cases of advance into the region as possible
(ii) Win contracts for (carry out) specific projects relating to resources and infrastructure

A) Support Japanese companies' international expansion

B) Export infrastructures and systems

C) Secure the supply of resources from partner countries

III. Promotion of Foreign Direct Investment

- Foreign direct investment position against GDP is 54.3% for the United Kingdom, 16.9% for the United States, and 12.4% for South Korea, and only 3.8% for Japan. Japan's foreign direct investment is extremely low by international standards.
- Competition for the business of foreign companies has intensified worldwide, and it is important for Japan to promote foreign direct investment, in which it lags behind other countries. Promoting inward direct investment would stimulate open innovation and also energize local economies.
- The Conference on Promoting Foreign Direct Investment in Japan takes the initiative in reforming regulations and systems based on the opinions of foreign companies and promotes to attract foreign companies in collaboration with JETRO, foreign diplomatic missions and forward-thinking local governments to achieve as much success as possible.

Government's "Control Tower" Function (Establishment of a Ministerial Meeting)

Establishment of the Conference on Promoting Foreign Direct Investment in Japan(*)

- To directly sound the opinions of managers of foreign companies, the Conference discusses required regulations and system reforms in collaboration with relevant ministers and other committees.
- JETRO and foreign diplomatic missions find prospective investment projects, and the Conference determines policies for investment in Japan and manages the progress.

(*) The Prime Minister directed the establishment of the Conference at the second joint meeting of the Council on Economic and Fiscal Policy and the Industrial Competitiveness Council (April 4, 2014). The first meeting of the Conference was held on April 25, 2014.

Product Development (Promotion of Structural Reform, etc.)

Promotion of Regulation and System Reforms and Utilization of Special Zones

- The Conference on Promoting Foreign Direct Investment in Japan and related committees collaborate to accelerate discussions on regulation and system reforms to improve the investment environment.
- Strengthening and collaborating with special national strategic zones, etc.

Provision of Investment Incentives

- Financial assistance for the expenses of developing bases and easing tax burdens

Business Operations (Creation of Investment Projects)

Strengthening Invest in Japan Activities (Finding, approaching and supporting foreign companies)

- Invest in Japan Activities by JETRO and foreign diplomatic missions
- Top-level sales by the Prime Minister and cabinet members
- Strengthening of collaboration with local governments that actively attract foreign companies
- Deepening understanding concerning investment partnerships between foreign companies and medium-sized enterprises and SMEs and support for matching them