Section 3 History of Japan’s globalization

In the period from the end of World War II through the second half of the 20th century, the Japanese economy achieved rapid growth while enjoying the benefits of the advance of globalization and free trade amid the deepening of its connectedness with the global economy. In particular, the value of Japan’s GDP in dollar terms started growing at an accelerating pace in the 1980s because of economic growth and the rapid appreciation of the yen following the Plaza Accord in 1985. In 1993, Japan’s GDP accounted for around 18% of global GDP. The value of trade, which started growing rapidly in 1980, temporarily declined but has returned to an uptrend, supporting the Japanese economy (Figures II-2-3-1 and II-2-3-2).

Figure II-2-3-1 Changes in GDP in Japan

![GDP and Percentage of Global GDP](chart)


Figure II-2-3-2 Changes in trade values in Japan

![Trade Values](chart)

Source: DOTS (IMF).
Japan’s trading partners have also changed. In the past, the largest trading partner was the United States, but it has now been replaced by China. In addition, Japan’s trade with other countries/regions in Asia also increased (Tables II-2-3-3 and II-2-3-4).

Table II-2-3-3  Top 10 export partner countries of Japan

<table>
<thead>
<tr>
<th></th>
<th>1990</th>
<th>2000</th>
<th>2010</th>
<th>2019</th>
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<tbody>
<tr>
<td>1st</td>
<td>U.S.</td>
<td>U.S.</td>
<td>China</td>
<td>U.S.</td>
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<td>2nd</td>
<td>Germany</td>
<td>Taiwan</td>
<td>U.S.</td>
<td>China</td>
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<td>6th</td>
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<td>8th</td>
<td>Thailand</td>
<td>U.K.</td>
<td>Germany</td>
<td>Singapore</td>
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<td>9th</td>
<td>Australia</td>
<td>Malaysia</td>
<td>Malaysia</td>
<td>Viet Nam</td>
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<td>10th</td>
<td>Canada</td>
<td>Thailand</td>
<td>Netherlands</td>
<td>Australia</td>
</tr>
</tbody>
</table>

Source: Trade Statistics of Japan (Ministry of Finance (MOF)).

Table II-2-3-4  Top 10 import partner countries of Japan

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<thead>
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<th>1990</th>
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<th>2010</th>
<th>2019</th>
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<tbody>
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<td>1st</td>
<td>U.S.</td>
<td>U.S.</td>
<td>China</td>
<td>China</td>
</tr>
<tr>
<td>2nd</td>
<td>Indonesia</td>
<td>China</td>
<td>U.S.</td>
<td>U.S.</td>
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<tr>
<td>3rd</td>
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<td>ROK</td>
<td>Australia</td>
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<tr>
<td>4th</td>
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<td>Taiwan</td>
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<td>Taiwan</td>
<td>Thailand</td>
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<td>Taiwan</td>
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<td>Germany</td>
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<td>Germany</td>
<td>Qatar</td>
<td>Viet Nam</td>
</tr>
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</table>

Source: Trade Statistics of Japan (MOF).

By product item, in terms of trade, the share of general machinery and transportation equipment, including automobiles, is large, while the share of electrical equipment, such as TVs, indicates a downward trend (Figure II-2-3-5).
On the other hand, services trade is growing. In 2019, services exports recorded a surplus for the first time under the current standard. One factor behind this surplus is an increase in in-bound tourism. In 2019, the travel account recorded a surplus of more than 2 trillion yen (Figure II-2-3-6).

Source: Trade Statistics of Japan (MOF).

Source: Balance of Payments Statistics (Bank of Japan (BOJ)).
In the meantime, Japanese companies shifted their manufacturing bases to Asia and started production there, particularly in the 1990s and later. The wave of the second unbundling that was discussed in Section 1 was prominent in Asia, and production networks in Japan and various Asian countries expanded.

As outward foreign direct investments continued to increase, the balance of such investments expanded by more than two-fold over the past 10 years. Inward foreign direct investments are also on an upward trend, reflecting the increasing financial connectedness with the rest of the world (Figures II-2-3-7 and II-2-3-8).

Figure II-2-3-7  Balance of outward foreign direct investments by industry

Source: Balance of Payments Statistics (BOJ).

Figure II-2-3-8  Balance of inward foreign direct investments by industry

Source: Balance of Payments Statistics (BOJ).
In terms of the differences among regions, the balance of outward foreign direct investments in Europe, North America and Asia is large. In particular, outward foreign direct investments in Asia have increased in recent years, which suggests that Japan is incorporating Asia’s high growth into its economy (Figure II-2-3-9).

![Balance of outward foreign direct investments by region](chart)

**Figure II-2-3-9  Balance of outward foreign direct investments by region**

Source: *Japan’s Outward and Inward Foreign Direct Investment (Balance)* (JETRO).

Japan’s global value chain participation ratio has continued to rise in terms of both forward and backward participation since 1990. A country’s forward participation ratio represents the value of its goods and services exported for use as intermediate input into other countries’ production of goods and services for export as a proportion of its total export value. A country’s backward participation ratio represents the value of goods and services imported from other countries for use as intermediate input into its production of goods and services for export as a proportion of its total export value.

Japan’s forward participation ratio has remained high for many years because of its supply of intermediate goods and services to other countries. This means that Japan has taken advantage of the high levels of its technological prowess and service quality as its comparative advantage to promote business expansion globally. In addition, demand created by an invigorated global economy was captured by the Japanese economy through an increase in exports. On the other hand, in recent years, Japan’s backward participation has increased, indicating that Japanese companies are shifting to a business model that seeks to increase productivity at their domestic production bases through the international optimization of production processes.

Japanese direct investments in Asia have been steadily increasing since the 2010s, particularly in nonmanufacturing industries. The number of Japanese companies operating in China and ASEAN4 increased in both manufacturing and non-manufacturing industries (Figures II-2-3-10 to II-2-3-13).
Figure II-2-3-10  Changes in Japan’s global value chain (GVC) participation ratios

Source: OECD TIVA.

Notes: The GVC participation ratios represent those in exports on a value added basis. As the ratio becomes higher, the contribution to creation of global GVC becomes higher.

Figure II-2-3-11  Japanese direct investments in Asia by industry

Source: BOJ.
Figure II-2-3-12  Changes in the number of Japanese companies engaged in overseas operations (manufacturing)

Source: Survey of Overseas Business Activities (METI).
Notes: The values of China include those in Hong Kong.

Figure II-2-3-13  Changes in the number of Japanese companies engaged in overseas operations (non-manufacturing)

Source: Survey of Overseas Business Activities (METI).
Notes: The values of China include those in Hong Kong.
As a result of the advance of economic globalization, Japan also achieved a dramatic change in international finance. Under the postwar Bretton Woods regime, the fixed exchange rate system was adopted in order to maintain exchange rate stability, with the yen-dollar exchange rate fixed at 360 yen per dollar. After the Nixon Shock in 1971, Japan also shifted to the floating exchange rate system in 1973 (Figures II-2-3-14 and II-2-3-15). This move laid the foundation for realizing free movement of capital and implementation of independent monetary policy by the central bank under the floating exchange rate system. Indeed, it is known as a trilemma of international finance that a country cannot simultaneously have a fixed exchange rate, maintain an independent monetary policy, and permit free cross-border financial flows.

**Figure II-2-3-14  Changes in effective exchange rates**

(2010=100)

![Graph of effective exchange rates](image)

Source: Bank for International Settlements (BIS).

**Figure II-2-3-15  Changes in exchange rates of yen to dollar**

(Per dollar)

![Graph of yen to dollar exchange rates](image)

Source: Refinitiv.
As Japan increasing interconnectedness with the rest of the world, the way that Japan earns income in the international balance of payments has also changed. Figure II-2-3-16 shows Japan’s current account balance since the second half of the 1960s. From 1965 until recently, the trade balance has generally stayed in surplus. In addition, in the 1980s and later, Japan steadily continued to record a current account surplus. In the meantime, the composition of the current account surplus changed. The trade surplus shrank in the second half of the 2000s and later, with a trade deficit recorded in some years in the 2010s. On the other hand, in recent years, the primary income balance (e.g., securities investment income and dividends) has been recording a surplus equivalent to 4% of GDP, underpinning Japan’s current account surplus. This reflects the establishment of production networks and the expansion of direct investments, mainly in Asia, indicating that Japan has incorporated Asian’s continuing high growth into its economy and shifts from a trade-based current account surplus to an investment-based current account surplus. In short, Japan is transforming itself from a trading nation to an investment-oriented nation. During this process, complex supply chains have been formed, which is already explained in the analysis in Chapter 1.

**Figure II-2-3-16 Breakdown of current account balance**

(Trillion yen)

Notes: The primary income balance represents interest and dividends arising from foreign financial receivables and debts.

The secondary income balance represents the balance of payment involving the provision of assets without compensation between migrants and non-migrants. In the 1980s, the categories of balance of payment changed. Before this, there were three categories of trade balance, invisible trade balance and current transfer balance. The invisible trade balance is equivalent to services balance.
and primary income balance now, while current transfer balance is equivalent to the secondary income balance now.