

Annual Review 2024

Policy Recommendations & Roundtables with the Experts



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Introduction

We have been searching for solutions to the challenges facing the global economy and Japanese economy.

Against intensifying geopolitical risks such as the US-China rivalry, the international political and economic order is in crisis. Meanwhile, the Japanese economy has been in prolonged stagnancy, with depopulation and lowered productivity. How to restore a rules-based global political and economic order to mitigate uncertainties and how to revitalize the Japanese economy for strengthened national security – these two challenges will be examined for solutions.

With the help of a number of distinguished experts in Japan as well as overseas, we published the following policy recommendations, and for each we organized a roundtable with the experts to discuss the issues, which you can see below. We will continue to pursue the paths to solutions.

I Research on solutions for the rule of law and rule-based international political and economic order

1. Policy Recommendations for Rebuilding the International Order

(November/December 2024 issue_Cover_Story_2)

2. Roundtable on How to Rebuild an International Order in Chaos

(July/August 2024 issue_Cover_Story_1)

3. Policy Recommendations for a Rule-Based International Trading System

– Roundtable on Trump 2.0 – How Can We Tackle Trade Policy Issues?

(January/February 2025 issue_Cover_Story_1)

(https://www.jef.or.jp/en/research/research_group/international_trading_system/)

II Research on solutions for revitalization of the Japanese economy

4. In our solutions, keys to revitalization are service sectors and AI

– Policy Recommendation: Strategy for Japan’s Service Industry – Making the Service Industry a Source of Prosperous Growth (March/April 2025 issue_Cover_Story_1)

5. Roundtable on Making the Service Industry a Source of Japan ‘s Soft Power

(March/April 2025 issue_Cover_Story_2)

6. Roundtable on Is AI a Friend or Foe of Humans? (May/June 2025 issue_Cover_Story_1)

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Policy Recommendations for Rebuilding the International Order

By the Working Group on the Future International Political Order

July 2024

This was to have been published in the *Japan SPOTLIGHT* Sept./Oct. 2024 Issue, but the translation was delayed, and so it is included now in this issue.

1. Current Situation & Background: How Did the Current State of Confusion Arise?

(1) Current situation

The invasion of Ukraine by Russia that began in February 2022 has drastically changed the course of history, transforming an “era of peace” into an “era of war”. What is particularly noteworthy is that it shook the foundations of an international order based on the “rule of law” and transformed it into one in which military power, especially nuclear power, occupies a central part. The pursuit of security that relies on strong deterrence, rather than rules-based discussion, is becoming the centripetal force in the formation of the international order.

For example, the ongoing war in Ukraine has created an urgent need in Europe to strengthen the defense capabilities of NATO based on a more robust deterrence. The Ukraine crisis has led to a global division between the West and authoritarian states such as Russia and China, and this division has been further complicated by the destabilization of the Middle East triggered by clashes between Israel and Hamas in Gaza since October 2023.

Israeli Prime Minister Benjamin Netanyahu launched a counterattack against Hamas, which has committed terrorist acts that have killed 1,200 innocent people, but international public opinion seems opposed to Israel's attempts to eradicate Hamas, even at the cost of civilian casualties in an urban war in the narrow Gaza Strip. The United States also abstained from an anti-Israel resolution at the UN Security Council for the first time, straining relations between President Joe Biden and Netanyahu.

(2) Background

① Retreat of Advanced Countries and G7

The Ukraine crisis occurred in the context of the ongoing diminution of developed countries. While the G7's share of the world economy has fallen below 50%, Chinese nationalism has increased as the Chinese economy continues its high growth, and China and Russia's aggressive diplomatic stances were already evident in the 2010s, notably the former's military strategy in the South China Sea and the latter's occupation of Crimea in 2014.

② America's Inward-Looking Trend in Foreign Policy

The influence of the US as a world leader continues to recede. In particular, the administration of former President Donald Trump retreated from its approach to solving global health and other global problems and regional conflicts through cooperation among major powers. The question of how much cost and risk the US will bear in the future to support the international order is a fundamental issue for the US, and foreign policy arguments with unilateralist overtones have become dominant, especially with presidential candidate Trump. With the presidential election coming up in November 2024, US politics remains even more divided, creating great uncertainty internationally.

③ China's Threat

It was around 2010 that China overtook Japan in terms of GDP and became the world's second-largest economy. In less than 15 years, China's GDP has grown to nearly four times that of Japan, and it is now two-thirds the size of US GDP. This has created an awareness in the US of the failure of its engagement policy and the arrival of an era of great power competition, and the US-China confrontation has become more serious.

④ The Global South Holding the Casting Vote

The Global South has emerged in response to the retreat of the developed countries led by the US. The term Global South (emerging and developing countries) spread when India hosted the Voice of the Global South Summit in January 2023 to rally non-aligned countries. Some of these countries have developed, become powerful, and have a voice by opening up to the outside world and adopting capitalist policies, even though their domestic regimes remain authoritarian.

Among the emerging nations of the Global South that have gained strength are Saudi Arabia, Malaysia, Thailand, Brazil, Mexico, Colombia, Peru, Kazakhstan, Turkey, Iran, Algeria, South Africa, Indonesia, the Philippines, Bangladesh, India, Pakistan, Vietnam, Egypt, and Nigeria, to name a few. Of these countries, India, for its part, has been pursuing multipolarity in the international community as a result of its emphasis on “strategic independence” that excludes interference by major powers, adheres to non-aligned principles, and expands its own sphere of action. This is one of the reasons why

India has behaved as a representative of the Global South. However, India is also a multi-ethnic country that has difficulty promoting national integration and needs to improve its economic strength, and its capacity for self-reliance is not yet sufficient.

In March 2022, immediately after Russia's invasion of Ukraine, the resolution condemning Russia in the UN General Assembly was passed by a margin of approximately 140 to 50, but the resolution on sanctions against Russia was met with almost 90 in favor and 90 against, abstaining, or not voting. Considering that among those in favor of sanctions there are 50 of the developed Western countries, only 40 of the 140 developing nations support sanctions. It seems that the obvious criticism of the "rule of law" being violated by the invasion of Ukraine is not accepted by the Global South. Possible reasons for this include:

- Deep-rooted distrust of former colonial suzerain states such as Britain and France
- Long-standing dependence on arms supplies from Russia (India, Vietnam)
- Skepticism about double standards in developed countries
- Economic losses resulting from conflicts between Russia and developed countries, such as higher fuel and food prices.

In addition, economic growth fueled by the population explosion has made African countries more assertive, and they have more opportunities to challenge the postwar international order that has been formed under the leadership of the West.

⑤ The Escalation of the US-China Confrontation & Economic Security

In response to the Global South nations, China is promoting their international inclusion with the formation of a "Global Partnership Network". With such an approach, the possibility that the international order will be restructured from a deeper level, around values and perceptions, is not small.

What is distinctive about China's foreign economic policy is its coercive trade policy toward its trading partners, weaponizing the interdependence of economies deepened by globalization. This is to coerce them into submission by using the supply of goods on which they have no choice but to depend. Furthermore, with "military-civilian fusion" it aims to promote "self-strengthening and self-reliance" by integrating and promoting the upgrading of military power and industrial power in an integrated manner, and by domestically producing strategic industries such as semiconductors from upstream to downstream in the supply chain. By doing so, it seeks to increase its economic "counterattack and striking power" by making foreign countries dependent on it. It is also pursuing a strategy of attracting foreign companies with cutting-edge technologies to China in order to gain access to such technologies.

In response, the US has passed the Inflation Reduction Act to support manufacturing facilities for EVs, solar panels, and other products, and with China in mind, aims to break away from

dependence on certain countries. These threats to economic security are growing rapidly as geopolitical risks increase. When discussing security issues, cybersecurity has also been a major issue in recent years. Cyberattacks target not only government and military organizations, but also companies, universities, and hospitals with critical infrastructure. Even if a cyberattack by itself does not cause much damage, when combined with other physical means it can cause significant harm.

⑥ Formalization of the Rule of Law

In the crisis of the international order described above, the rule of law is often forgotten because we have moved into the age of power games. The UN is dysfunctional in the sense that the Security Council continues to be ineffective and unable to stop the invasion of Ukraine, a violation of the UN Charter. Security Council reform has not progressed in over 20 years and has yet to generate negotiating momentum.

On the economic and trade fronts as well, the dispute settlement function of the WTO, which consists of a two-trial system, has not been functioning due to the lack of nominated members of the Appellate Body. Furthermore, as economic and security issues have emerged rapidly, discussions have not been able to be started without resolving the conflict between the US view that security exceptions are to be determined solely by the parties concerned and the WTO panel's view that the WTO panel can make the determination.

As for energy security, a number of issues have also become salient in light of the US-China confrontation, the rise of the Global South, the realization of US energy independence through the shale revolution, and the abandonment of the US role as "world policeman".

The exclusion of SWIFT (Society for Worldwide Interbank Financial Telecommunication) from the dollar settlement function, which took place immediately after Russia's invasion of Ukraine, had a large political impact, but the overall effect of the economic sanctions, together with Europe's suspension of Russian oil and gas exports, was limited. The reason is that the complete exclusion of Russian oil and gas, which respectively account for 30% of the world oil and gas export market, from the international energy market would lead to a sharp rise in energy prices. China, India, Turkey, and other countries have been allowed to import Russian oil at low prices even after the sanctions. Russia, which depends on energy exports, has rather benefited from the soaring oil prices. Trade between China and Russia has increased, and because it is settled in Chinese yuan, the ratio of yuan use as an international currency has increased. In addition, Russia's domestic military industry is in full operation, and Russia's economic growth rate has reached 3%.

Against this background, the world is becoming increasingly chaotic. Even the US, which remains the most powerful country in the world and which has always placed the propagation of universal values such as freedom, democracy, and the rule of law in its national interest, now accounts for only a quarter of the world's GDP,

and the GDP of the West as a whole (Japan, the US, and Europe) is less than half. With the increasing weight of the Global South, which is not aligned with either the US-centered Western world or with China and Russia seeking its own spheres of influence, the UN and the WTO have become dysfunctional, and we are now adrift on the brink of a security crisis and an international economic crisis unprecedented in history.

2. Response: What Would a Desirable International Order Look Like?

(1) Restructuring the Rule of Law

① United Nations Reform

No universal organization can replace the UN. On the other hand, the UN originally had no military forces, no economic power, and is powerless without the support of its member states. Reaffirm the following principles in order to realize the purposes of the UN: “to maintain international peace and security”, “to respect the principle of equal rights and self-determination of peoples”, and “to promote respect for human rights and fundamental freedoms”.

- (a) Equality of sovereignty of all member states
- (b) Faithful fulfillment of the obligations owed in accordance with the Charter
- (c) The settlement of international disputes by peaceful means
- (d) Refrain from the threat of arms or use of military forces against any nation.

However, the current situation is far from ideal, and it is necessary to secure a consensus among many countries in order to realize this goal.

② WTO Reform

- (a) to restore the dispute settlement function of the WTO by achieving the appointment of members of the Appellate Body
- (b) to increase the number of Plurilateral Agreements, while at the same time revising unanimous rule and restoring the WTO's legislative function.

(2) Promote Free Trade & Establish Economic Security

Promote free trade as much as possible through free trade agreements and regional agreements without waiting for a functional restoration of the WTO. In this case, it is important to support the losers in free trade through human resource development and other measures to assist them on the path to development and growth. On the other hand, minimal exceptions should be made for threats to economic security arising from differences in values and economic systems from the perspective of “Small Yard, High Fence”.

With regard to the extermination of companies of certain countries by other countries through low-priced exports backed by overproduction in strategic advanced technology fields such as electric vehicles, if this is recognized as an obstacle to fair competition due to unfair subsidies, retaliatory measures authorized

under the WTO Agreement shall be considered and implemented. This will further clarify our stance to uphold a rules-oriented international order.

(3) Avoiding a Taiwan Contingency

In addition to the crisis in Ukraine and the conflict in Gaza, another concern in Asia is the enforced reunification of Taiwan by China. In light of the UN Charter, Japan must deter any change to the status quo by military force, which is unacceptable. To this end, Japan should strengthen its own defense capability, promote defense cooperation with the US, Australia, the Philippines, and other countries, and promote dialogue with China. In addition, China is increasing its pressure on Taiwan, both militarily and economically, and the question is how the international community should respond.

(4) Wait for China to Mature & Continue Dialogue with it

Until China comes to understand that liberalism and democracy are what will bring happiness to its people and development to its country, continue dialogue with it and prevent unnecessary friction while avoiding war through deterrence.

(5) Support & Cooperation with the Global South

Continue to provide support and technical assistance to the countries of the Global South to help them achieve sound development. Support and coordinate efforts to combat climate change, not by imposing Western values but by achieving decarbonization as quickly as possible, administratively, economically, and technologically.

3. Role of Japan: What Role Can Japan Play?

Japan, as the country that has most benefited from the system of world peace and prosperity that nations have so tirelessly built over the past 80 years since the end of World War II, is expected to make a significant contribution to its restoration. And, importantly, it is necessary for Japan to use its own creativity to produce measures to address the current situation in which the US is becoming increasingly reluctant to play the role of leader.

(1) Contribution to the Restructuring of the Rule of Law

The following reforms are important for observing Japan's national interest, preventing global fragmentation and restoring economic prosperity and stability.

① United Nations Reform

Japan's mission is to continue to seek reform and improvement of the UN and to make it an organization that will exist for another 100 years. The first step should be to achieve reform by creating a quasi-permanent member or a long-term member, rather than focusing on Japan becoming a permanent member of the UN Security Council. The reform of the more fundamental permanent members of the

Council (expansion, contraction, and phasing out) should be achieved by 2045, the UN's centennial year.

② WTO Reform

In order to restore the dispute settlement function of the WTO and prevent “appeals into the void”, it is necessary to resolve the Appellate Body issue as soon as possible. In light of the rapid increase in the number of such appeals on security exceptions and other issues, it is worth considering the introduction of a one-trial system instead of a two-trial one, even if only temporarily.

In a world of growing economic interdependence, economic security must be realized, and efforts to supplement the current international trade regime are indispensable in this regard. In this context, it is important to strengthen the monitoring function for security matters.

③ Training of Japanese Personnel to Become Heads of International Organizations

It is not desirable for the heads of international organizations to be monopolized by a particular country. It is an old saying, but there is an urgent need to strategically develop human resources in Japan who not only have language skills, but also the creativity for new large-scale ideas to interact with the international community.

(2) Contribution as a Flag-Bearer of Free Trade & Economic Security

① Demonstrating Japan's presence by promoting regional free trade agreements, such as by expanding membership in the CPTPP, a comprehensive and progressive agreement on the Trans-Pacific Partnership, will also be an important deterrent.

② On the other hand, strengthening economic security is also important to promote free trade. Advanced technology is now both for industrial and military use. The artificial distinction between security-related technology and civilian technology is a phenomenon unique to Japan and should be stopped. Japan should have an industrial policy comparable with that of other advanced nations, in which advanced industry itself is the foundation of national security. Academia and industry should work together to implement industrial policies that strengthen the competitiveness of industries, especially advanced industries, while taking into consideration relations with China. Foster industries with strategic indispensability that make the country more dependent on Japan. Efforts will also be made to reduce dependence on specific countries in critical goods that cause economic coercion.

③ Review the state of export controls to minimize the risk of technology leakage to China. In solidarity with the US and other Western countries, consider strengthening export controls for emerging technologies such as semiconductors, quantum, and biotechnology.

(3) Strengthen Deterrence to Avoid Taiwan Contingencies

① Strive to strengthen defense capabilities to deter the use of military force by states seeking to change the status quo, and maintain close relations with the US, including the Japan-US Security Treaty, as well as with EU countries, India, Australia, South Korea, Indonesia, the Philippines, Vietnam, and others.

② In order to strengthen Japan's cyber security capability, it is important to introduce active cyber defense to eliminate the threat of serious cyberattacks on critical infrastructure in advance. For this purpose, it is necessary not only to drastically increase the number of cyber defense units of the Self-Defense Forces, but also to establish a data center to monitor the cyberspace situation, create a Cabinet Cyber Security Bureau in charge of cyber security for the entire nation, establish a government cloud, and review the legal system concerning the confidentiality of telecommunications.

③ The decline in the international presence of the Japanese economy due to population decline is the greatest security risk, and it is important to strengthen the economy. In addition to security needs, if government spending is essential for measures to prevent declining birthrates and an aging population, it is essential to strengthen smart fiscal and tax revenue bases, including spending cuts. As in major Western countries, consideration should also be given to accepting foreign workers. In doing so, in order to prevent social friction, it is essential to give priority to those who are needed by Japanese society and to deepen the Japanese side's understanding of the history, civilization, culture, and language of the country or region from which the foreign workers come, and to create an environment in which the foreign workers can feel comfortable.

(4) Strengthen Dialogue with China

① It is important to make diplomatic efforts to build Japan's allies, and at the same time, it is important not to cease dialogue with China. There is much room for cooperation between Japan and China, not only on sensitive issues such as politics and security, but also in addressing global environmental problems, fostering venture capital, tourism, and aging societies with a declining birthrate, and there is much room for building cooperative relations by the promotion of dialogue.

② It is important to maintain a stable relationship by maintaining a dialogue channel that functions as a proxy for the leaders of Japan and China, which since 2014 has been the coordination mechanism between the director general of the National Security Bureau of Japan and the director of the Office of the Central Committee for Foreign Affairs of the Communist Party of China (CCPCC). To complement this, it is also necessary to build a multilayered network among government, local government, legislators, the private sector, and academia, all of which are currently thin.

(5) Support and Collaboration for the Global South

We will make it a clear policy that strengthening relations with emerging and developing countries while maintaining close ties with the US and Europe is the basis of Japanese diplomacy. Such diplomacy is the first step to ensure Japan's security at a time when it is clear that Japan's national power is declining and US leadership is declining. We must abandon the illusion of being a great power and work with the Global South as a representative of the global middle powers. This is important in the sense that it will save the world from fragmentation, but it will also contribute to Japan's security.

① To emerging and developing countries concerned that developed nations' argument that the "rule of law" based on freedom and democracy is important is simply designed in their favor, we need to explain convincingly to them that Japan's post-WWII economic development achievements are the result of its digestion of freedom and democracy and that they are the foundation of development. Japan can make a persuasive argument because of its own experience. Japan should recognize that it is the only country that can serve as a bridge between developed countries and the Global South.

② It is especially important to persuade them that the loss of the "rule of law" will allow the regional powers to dominate and the interests of developing countries will be harmed.

③ Japan is easily accepted not only because of its experience in economic development as mentioned above, but also because it apologized for its colonial rule relatively early after its defeat and has almost no negative legacy of colonial rule outside of East Asia, compared to Britain, France, and other countries. In aid to developing countries, there is flexibility to modify universal principles to those that are more acceptable to developing countries. For example, in Pakistan, many girls could not go to school because women were not allowed to go far away. Japan has been praised for solving this problem by providing small schools near their homes, rather than criticizing this from the universal principle of gender equality, as in the West. Backed by this long-term, indirect approach, Japan has maintained relatively good relations with developing and emerging countries. Now is the time to put that experience to good use.

④ Such flexibility is important to promote stronger and more effective assistance to developing countries that cannot hope for much due to their declining national strength and weak financial base.

If Japan can fully demonstrate its uniqueness in the future, it will be able to build more friendly relations with the Global South, and this is where Japan can play a major role in saving the world from division.

(6) Policies to Make Partners

① Among the Global South, relations with Southeast Asian countries have a long history and are extremely important. Faced with food and fertilizer supply crises as a result of Russia's invasion of Ukraine, these countries have been oriented toward a diplomatic strategy of "not choosing to be on any side of the group of nations" in the great power, but in the face of its limitations they have come to reaffirm the importance of multilateral diplomacy and a regional cooperation framework that includes mini-lateral ones.

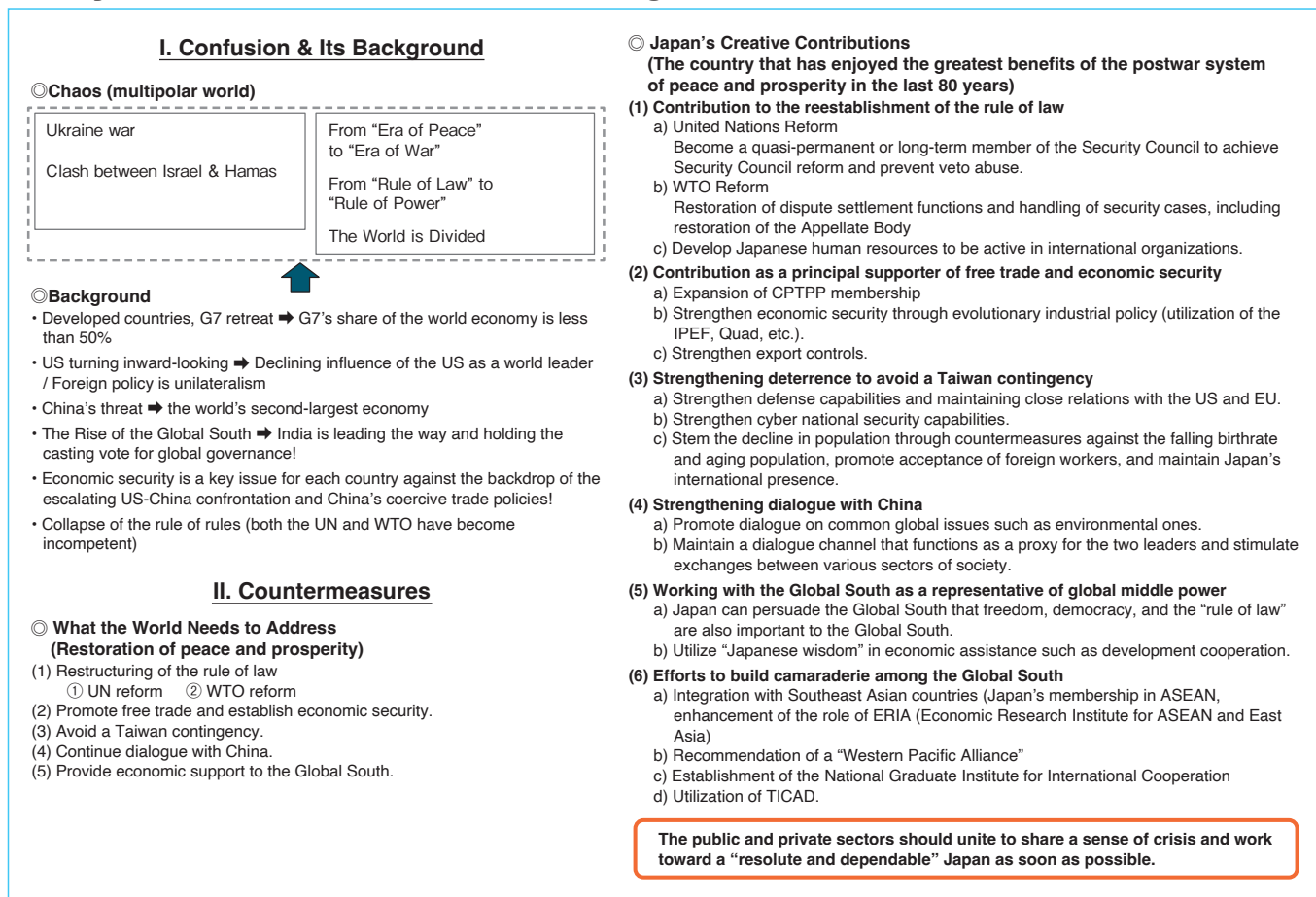
Building a close alliance with the Southeast Asian region is a top priority for Japan in its efforts to incorporate the Global South. It is important for Japan to form a new social contract with them and unite with them, including considering Japan's own membership in ASEAN. The time left for this is not long: ASEAN's economic power is expected to overtake Japan's within a decade. The generation of Southeast Asians who recognize Japan as an economic superpower and welcome an alliance with Japan are now in their 40s or older, and the younger generation is not particularly aware of the importance of Japan. Thus, Japan should deepen its alliance with ASEAN while the people in their 40s are still leaders of ASEAN society; the time left for us is about only 10 years from now.

Regular meetings of public intellectuals are needed to deepen intellectual exchanges and mutual understanding with ASEAN. In addition, scholarships for accepting foreign students from developing countries should be dramatically increased, and a National Graduate Institute for International Cooperation should be established to accept them, with particular emphasis on students from ASEAN.

② While it is important to aim for supply chain stability through the IPEF and the Quad, the roles of APEC (Asia-Pacific Economic Cooperation) and ERIA (Economic Research Institute for ASEAN and East Asia) are also important in building a close relationship with Southeast Asia over the long term. In particular, ERIA's contribution to establishment of closer and constructive relations between ASEAN and Japan is very important. In terms of energy security, the Zero Emission Center established at ERIA is expected to play a complementary role to the IEA, but the expected role of ERIA goes beyond that. By reorganizing close exchanges with Southeast Asia, such as the promotion of intellectual exchanges and the formation of high-level networks to promote understanding among the younger generation who will be responsible for the future of Southeast Asia, on the study of Asia-wide regional governance models and economic policy, and the importance of Japan as their partner in the region, ERIA could prevent political, economic, and social fragmentation and strengthen Japan's security.

③ In addition to the ASEAN countries, the concept of a "Western Pacific Alliance" to build a relationship with Australia and Pacific island countries to help each other in disaster prevention and maritime security is also extremely important from the viewpoint of building a network of friends with Japan.

Policy recommendations for rebuilding the international order



Source: Working Group on the Future International Political Order

④ We will also strive to strengthen relations with Africa by utilizing the 30-year history of the Tokyo International Conference on African Development (TICAD), which was held in 1993 as the world's first conference of its kind.

4. Japan's Preparedness

It is not an easy task to launch such a wide range of policies in such a short period of time. To achieve this, the public and private sectors must come together and share a sense of crisis. Even the task of increasing the number of Southeast Asian friends, which seems relatively easy, will not be easy in 10 years. The entire nation must urgently confront the challenges of diplomacy, economics, and security. We live in an era in which conceptual ability and originality are constantly put to the test. We must actively speak out to the international community based on this original conceptual ability. This is an era in which Japan must demonstrate its leadership by acting as a mediator in global crises such as the war in Ukraine and the wars in the Middle East.

The time has come for Japan to consciously make a major change in its leadership, moving away from simply following the US while maintaining the Japan-US alliance as the cornerstone.

Article translated from the original Japanese by Naoyuki Haraoka, editor-in-chief of Japan SPOTLIGHT & executive managing director of the Japan Economic Foundation (JEF)

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The Japan Economic Foundation (JEF) initiated the Working Group on the Future International Political Order with Japanese experts in February 2022 and will conclude its role by publishing recommendations later in 2024.

Roundtable with Prof. Shinichi Kitaoka, Prof. Nobukatsu Kanehara, Prof. Chisako T. Masuo, Prof. Nobuhiro Aizawa & Masakazu Toyoda (May 31, 2024)

How to Rebuild an International Order in Chaos

By Japan SPOTLIGHT

Participants: Prof. Shinichi Kitaoka, Special Advisor to the President, Japan International Cooperation Agency (JICA)

Prof. Nobukatsu Kanehara, Professor, Doshisha University

Prof. Chisako T. Masuo, Professor, Kyushu University

Prof. Nobuhiro Aizawa, Professor, Kyushu University

Moderator: Masakazu Toyoda, Chairman & CEO, Japan Economic Foundation (JEF)

Participants



Prof. Shinichi Kitaoka



Prof. Nobukatsu Kanehara



Prof. Chisako T. Masuo



Prof. Nobuhiro Aizawa



Masakazu Toyoda

Introduction

Toyoda: Russia's invasion of Ukraine has created a menace to the existing international order. But it seems also to have unintentionally exposed the major limitations of the post-World War II international order. On the international political front, the United Nations seems dysfunctional, in the sense that the Security Council itself is divided and unable to stop violations of the UN Charter. The United States, while supporting Ukraine, is restricting the capability of the weapons it provides to Ukraine to prevent excessive confrontation, including a nuclear war with Russia. The G7 is acting together on economic sanctions against Russia, but it has not gained enough support from China and the global South. So I think it must be said that these measures are not very effective.

To this situation was added the conflict between Israel and Hamas in Gaza. The G7 was basically pro-Israel, but now there are voices of support for Palestine within their respective countries, and I think it is fair to say that Israel is becoming isolated. The International Court of Justice has ordered an immediate halt to military operations in

Rafah, but Israel has not stopped its attacks.

The same is true on the trade and financial fronts: the dispute settlement function of the WTO, which consists of a two-tier system, is not functioning, as members of the WTO's Appellate Body have not been appointed; as for the WTO's legislative function, the unanimous consensus approach has set the Doha round adrift and it is no longer expected to be concluded except for a few pluri-agreements. On the international financial front, the regulation to exclude Russia from the Society for Worldwide Interbank Financial Telecommunications (SWIFT), an international network for money transfers and settlements by US dollars among banks, which was introduced soon after the Ukraine crisis, has not been fully effective. In fact, there has even been an emerging alternative network by competing currencies.

As described above, unfortunately, it appears that "the rule of law" has been forgotten in an age of multipolarity, both in international politics and in trade and finance, and that we have moved into the age of power games. We are joined today by four experts in international politics, and we would like to discuss the following

three points. First, why has the international order entered this period of turmoil? Second, what kind of international order should the world seek? Third, what role is expected of Japan, which has no power, and can it even play a role?

I would like to introduce Prof. Emeritus Shinichi Kitaoka of the University of Tokyo, who chairs the Future International Order Study Group organized by our foundation and who has served as ambassador and deputy permanent representative of Japan to the United Nations and special advisor to the president of the Japan International Cooperation Agency (JICA). Then Prof. Nobukatsu Kanehara of Doshisha University, who was originally at the Ministry of Foreign Affairs and he for many years as deputy chief of the National Security Secretariat in the Cabinet Secretariat. And then Prof. Chisako T. Masuo of Kyushu University who specializes in Chinese political diplomacy, and Prof. Nobuhiro Aizawa of Kyushu University, who studies trends in the Global South, including Southeast Asia.

Factors in the Disruption of the International Order

Toyoda: I would like to begin our discussion by asking why the disruption of the international order has occurred. First, I would like to ask Prof. Kitaoka. The US, which until now has prided itself on being the world's policeman, has become extremely inward-looking. Moreover, even within the US, the Republican Party and the Democratic Party differ to a considerable extent in their opinions. Some even call it a split in national opinion. There is a theory that the main cause is the change within the US itself, but what do you think about this?

Kitaoka: The Cold War was over, but the Cold War was, in a sense, an international order. The US and the Soviet Union had a tight control on their respective camps, the capitalist camp and socialist camp. Although there were minor conflicts, they managed to avoid major clashes. This order was over.

There were two consequences from the end of the Cold War. One was that the world became dominated by the US, and the US no longer needs to control its own camp carefully in the exercise of its leadership. At the same time, though the US used to pay much attention to the UN because it was in conflict with the Soviet Union there, this approach has disappeared now and disrespect for the UN has been increasing. Meanwhile, there has been the spread of Islamic extremism, including 9/11. This is not coming from a nation state, but from extremist terrorism. There is no easy way to deal with this. In war, all that is needed is for the other side to surrender, but terrorists do not surrender. The US, having insisted on saying that this must be the war against terrorists, has tried to fight against

them too much. And I think that has caused their failure to build trust with the Muslim nations.

Meanwhile, in the 1990s, globalization made significant changes to the economy. The end of the Cold War, along with the development of technology, having encouraged globalization, has created many gigantic billionaires in the US. But the lives of those who are not so rich are not getting better, and even their average life expectancy is not increasing. It is often said that the lower-middle class, especially those who are not highly educated, thus tend to believe that their standard of living is getting worse and that what threatens it comes from the excessive US involvement in international affairs and the increased numbers of immigrants from overseas. Thus, there emerges a significant divide between the rich and the poor, or elites and non-elites, which has been a vital cause of domestic political disruption in the US.

Toyoda: Prof. Kanehara, having been involved in foreign policy for a long time, from a bird's eye view, what do you think has changed?

Kanehara: For the first time, the relative size of the G7 economies is beginning to shrink. Leading the G7 has been the US. The US alone used to account for half of the world's GDP, but it is now at 25%, and the G7 economies accounted for roughly 70% to 80% in their heyday, but now account for less than 50%. Unfortunately, the newly emerging nations do not yet have much sense of responsibility to support this liberal international order together.

Then there are two countries that have turned their backs on this liberal international order. One is Russia, which has left the G8 and turned its back on it completely. President Vladimir Putin's "anti-West" stance has become a value in itself for him, and he wants to return to 19th century-style power politics and once again have Russia take on the status of a major power on the Eurasian continent. But I believe the war in Ukraine will now take a dark turn for Russia. US Secretary of State Antony Blinken has started to say that he will allow Ukraine to use US weapons to attack Russian territory, and the course of war will change again.

The other is China. Since the normalization of diplomatic relations with Japan and the US in 1972, China has come into the West and has grown larger by absorbing the capital and technology that the West has. The Chinese economy, which was the same size as the Japanese economy at the beginning of the administration of late Prime Minister Shinzo Abe in 2012, is now four times that size.

China has begun to turn its back on the liberal international order. I think the Chinese realize that they grew up thanks to the open Western economy, but President Xi Jinping is beginning to think that liberalism is an ideology that will kill the communist dictatorship. I think Xi is completely wrong in thinking in that way, but he has established an absolute personal dictatorship, and that will last

another 10 years and more.

Respect for freedom and democracy was an Enlightenment idea born in Europe, but since the American Revolution, the US has embodied it as an actual nation and has vigorously promoted its ideals on a global scale. Until the first half of the 20th century, however, because of racism and colonialism, Western liberalism and democracy were not universal at all, but local ideas with limited application only in Europe and the North American continent. It was Mahatma Gandhi, Dr. Martin Luther King, Jr. and President Nelson Mandela who greatly expanded the universal values of today – freedom, democracy and the rule of law – to all human society in the latter half of the 20th century.

When Europeans and Americans hastily insist on respect for human rights, freedom, and democracy, newly emerging countries that have now gained power will respond by saying, “You are the ones who did terrible things to the colonies.” In response to their views, Japan would stand up and need to say, “In World War II, we took up arms and raged against the injustice of the international order such as racism and European domination of Asia, but nothing good came out of it. Humans grow ethically and justice prevails in the end. You can rise in this liberal international order as much as you want if you work hard and honestly in it. Postwar Japan succeeded in doing so.” We need to get a message out from Japan that the liberal international order is a fair system with universal values, so let’s support this system globally together.

By the way, emerging developing countries are more interested in economic development than in issues of values, as they want to make money and prosper first. I believe that Japan has an important role to play here as well. That is the promotion of free trade. It is necessary to properly say that it is in the free trade system that developing countries can find a way to succeed. Since the beginning of this century, Japan has helped to create huge free trade zones and mega trade zones, such as the RCEP, CPTPP, and the EU-Japan EPA. Japan is the only country that has done this in this century. Under the free trade system, capital and technology are transferred to emerging countries in the form of direct investment. While developed countries will suffer from declining birthrates, aging populations, and industrial hollowing out, emerging countries will grow, and the world economy as a whole will grow even more. I believe that Japan must become a leader of free trade and tell emerging and developing countries that we will work together within this free trade system.

Toyoda: I would like to ask Prof. Masuo what she thinks about the view that the change in the international order has been brought about by China’s remarkable high growth or by China’s transformation?

Masuo: Xi often says, “What is going on in the world today is a transformation that has never happened in the past 100 years.” I believe he mentions this with the international system since the Industrial Revolution in mind. It is often asked whether China’s transformation has brought about changes in the international order. But perhaps the international order is not so rigid in nature. From a realist point of view, the international order gets universally transformed when the old power structure that supports it from the ground is changed.

Xi thinks that we are now experiencing the deepest level of transformation since the Industrial Revolution. I myself believe this may be true to some extent. In short, I believe we are now facing an international regime change at a point in history where the Western ruling regime that has continued for several hundred years may collapse due to the impact caused by China, a non-Western rising power. My understanding is that the current change in the international order has certainly been triggered by China, but this would have happened at some point eventually and cannot all be attributed to China.

However, when we consider how it is actually occurring, it is still closely connected with the situations on the Chinese side. If we cast our eyes at China, I must say that the Xi generation is very special even in China. They were the very people who, during the Cultural Revolution, worked as Red Guards and engaged in revolutionary activities to destroy the existing system. Xi, for example, did not even graduate from middle school because he stopped studying at the second grade when the Cultural Revolution broke out. In Confucian Chinese society that generally favors and respects higher education, this is a generation with unusually low level of education.

China usually has a strong tradition of elite-leading politics. But since they spent their youth as Red Guards, they are nationalistic and inclined to populism. They tend to move collectively and go extremes. They also had a strong antipathy to the existing system. It is this special generation that are now in charge of China.

Thus, the global power shifts and Chinese internal power shifts are joining together to form a new international current at this moment. China is a socialist country founded on Marxism, which is basically a materialist ideology. The idea is that politics is built on economic foundations. Therefore, the Chinese naturally expect changes in political structures will occur on the basis of global tectonic change, caused by China’s economic rise. In other words, they believe that China’s economic rise may finally overturn the Western dominance of the world, and that it must be the mission of the Chinese Communist Party (CCP) to make this happen. In order to realize the “common destiny for mankind” – a political slogan of the CCP – China must overturn the rule of the West at all costs and come to hold power over the international order, or else there will be no beautiful future for mankind. The Xi administration has been creating

this narrative domestically and spreading it to the world. It also seems that not a few countries actually agree with it. This is because many people have been dissatisfied with the West's centuries-long grip on the mainstream of international relations.

Toyoda: Prof. Aizawa, from the perspective of the Global South, such as Southeast Asia, how do you see the Ukraine crisis or the conflict in Gaza? Why doesn't the Global South join in sanctions against Russia? I would like to know more about this issue.

Aizawa: The term "Global South" is basically a term for a political movement, and while I think it is relevant to say "We in the Global South" as a political statement, it is still misleading to talk about the Global South as a unit of analysis, especially in our strategic conversation. This is because the strategic locations and socio-economic realities among the countries categorized in the terminology are too different from each other. It is not just misleading, but we will lose our strategic edge if we avoid articulation. In this roundtable talk, therefore, on the question of the Global South, I would like to limit my answer to Southeast Asia, in which the strategic diversity in itself is already wide enough to risk irrelevancy.

I think that the war in Ukraine and the war in Gaza, from the perspective of Southeast Asia, raise primarily the issues of justice. The main reason for most Southeast Asian countries not joining in sanctions against Russia is to object to the international trend in justifying economic sanctions. Without question, they are with the international rules and principles, adhering to the inviolability of territory. But on the other hand, there is a strong objection to the justification for collective economic sanctions in terms of enforcement. Southeast Asian countries have been subjected to economic sanctions in the past, so they know the harsh reality of being on the receiving end of them. In addition, if they are part of the collective economic sanctions this time, it will be difficult for them to defend themselves when they are faced with a similar situation that may eventually happen to them. So, in addition to the principle of justice, I think there is also a strategic rationale behind the decision.

There is another justice issue regarding the war in Gaza as well. It is the issue of colonialism. Many countries in Southeast Asia have experienced colonial rule, and the issue of Gaza is connected to the issue of international norms regarding self-determination. Israel's expansion of its settlements is recognized as a colonial act, and the US and other countries that fall short in stopping Israel's expansion and remain silent have been seen as not upholding the international norms of self-determination. Thus, while condemning the attack by Hamas as violating international principles, countries that have experienced colonial rule will be firm in rejecting Israel's position.

With regard to the Ukraine crisis, there is an economic issue

besides justice. For Southeast Asian countries that need to grow their economies in a speedy manner, the war will cause a crisis in food and energy supplies and a rise in international prices, which will indirectly deprive them of opportunities for economic growth. In order to minimize the negative impact of the war on their own economies, Southeast Asia is clearly expressing its position that an immediate ceasefire is a priority over a long-term war for the complete withdrawal of Russian troops from Ukraine.

What Kind of International Order Should We Seek?

Toyoda: The next major theme is also one that I would like to ask you to discuss: what kind of international order should the world seek? I would like to hear from Prof. Kanehara. Next year will mark 80 years since the end of World War II. The long era of peace seems to be coming to an end. Has the era of rules ended and the era of power arrived? Japan is also moving forward to double its defense spending. Does this mean that Japan is preparing for an era of power? In addition, in the midst of rising geopolitical risks, the discussion of economic security has come up, but how should we think about this in the overall context?

Kanehara: The international community is a decentralized one. Since there are no fools who will kill each other forever, in the end people instinctively seek stability and peace by managing power relations. It is just like the balance of factions in a company. If the major actors in international politics change and the power relations change, it is only natural that the balance will change, so we must think about how to create a new stable balance.

Japan unfortunately became ideologically and politically divided within the country during the Cold War, with the Socialist Party supporting Beijing, the Communist Party supporting Moscow, and the members of the Diet who thus became part of the East holding more than one-third of the seats. There is no such country in the West. In the West, both the ruling party and the major opposition parties were members of the West. As Dr. Henry Kissinger astutely pointed out in his book *The World Order*, in reality Japan was not part of the Cold War. Since it has been 30 years since the end of the Cold War, the Japanese people have completely forgotten the harsh domestic and ideological divisions of that era.

That does not mean that the Japan-US alliance was ineffective. In particular, the military bases that Japan offered to the US were vitally important. Without the Japan-US alliance, the defense of South Korea would not have been possible in the Korean War. Without the US-Japan alliance, the defense of the Philippines and Taiwan would collapse in any future Taiwan contingency. Without Japan, the US military cannot protect these countries and regions.

The peace and prosperity of East Asia as a whole rests on the regional stability supported by the Japan-US alliance. Today, China's rise is remarkable, and the situation over the Taiwan Strait is becoming increasingly tense. In order to maintain the deterrence of the Japan-US alliance, I believe that Japan's conventional forces must be drastically increased and enhanced. The efforts should be extended to new fields such as outer-space, cyber-space and cognitive warfare.

The other issue is free trade. China's economic power is attractive to emerging and developing countries. However, as long as free trade spreads the wealth of the West to the South, everyone will follow the West. The economic power of the West as a whole is still twice that of China, so as long as we are not only strong and prosperous but also united, we should be able to continue to take the leadership.

What is worrisome is that the US is beginning to reverse the course from free trade. The US seems to be returning to protectionism and isolationism. I think it will get worse if Donald Trump becomes president again. This is where I believe Japan needs to support free trade. Japan was maligned as a "bastion of protectionism" in the last century and only in this century is it being recognized as a "leader of free trade".

A recent argument to complement free trade is economic security, aimed at regulating free trade from the national security perspective. The US is not saying "regulate all trade with China", but it is saying that it will not allow the export of cutting-edge technology to China, because it can be used in a war that results in the deaths of US soldiers. In particular, they are asking that the export of cutting-edge semiconductors and their manufacturing equipment to China be stopped at all costs. They are going to build a high wall around the export of cutting-edge semiconductors, and those semiconductors only. I think this is the right approach.

In the world of naval law, there is a rule that allows belligerents to regulate the cargoes of neutral countries. This is a system known as "contraband", and I think it can be said that this argument is now seeping out a bit into peacetime with regard to cutting-edge semiconductors, but this is only a correction of free trade, not a distortion of the free trade system itself.

There is one more thing that must be done in Japan's particular situation. In other countries, the government puts huge amounts of money into companies and universities for the development of national security-related technologies. There is a common understanding that if a technology is state-of-the-art in any areas of basic research, applied research, and R&D, it is national security-related technology, and the national security-related technologies are not understood as just narrow military technologies. In Japan, however, both academia and industry remain strongly anti-military and pacifist in ideology, and have long shunned anything related to

national security. This is why Japanese industry has lost out in the world. The Pentagon has a science and technology budget equivalent to 10 trillion yen for research institutes in industry, government, and academia. In the Japanese private sector, the military sector is small, and even in the defense industry, the civilian sector accounts for about 95%. Academia has completely turned its back on defense cooperation with the government. Industry leaders are also largely reluctant to be engaged in business related to national security. There is no other country in the world like this.

If we can properly utilize the talents of Japan's excellent civilian engineers for national security, Japan can be included in the AUKUS and cooperate in defense technology as a real part of the West. From now on, I believe that Japan must bring national security into the core of its industrial policy-making process.

Finally, there is the question of values and leadership. As I mentioned earlier, there is still a dark anger of anti-colonialism burning in the guts of the nations of the Global South. Japan did not become a colony and has only been subjected to racism, so I don't think we really know what their anger is about. After hundreds of years of being discriminated against because of the color of their skin and forced to work as slave labor in colonial farms and mines, their anger is not easily released. It is up to Japan to unleash that anger and nurture the emerging nations as leaders of the international liberal order.

Medium-sized countries like South Korea and Australia should be allowed to join the G7 in the future. It may be still too soon for South Korea to join the G7, because if the opposition Democratic Party of Korea (DPK) comes back to power, it will turn ideologically anti-American, anti-Japan, pro-China, and pro-North Korea again. I hear that Canada is being mean to Australia and saying it will not let her in, but I think this is a typical example of sisters quarreling when they grow up.

The main contenders in East Asia are India and Indonesia, and they will grow very rapidly. ASEAN as a whole and India will overtake Japan's economy in 10 years, so it is important to capture them. But India and Indonesia, as well as Brazil, are large, have strong egos, and will not always listen to the US. How to build up the new leadership of a multipolar international liberal order in this century is a big problem. The US probably would not like to include India and Brazil in the G7.

Although we are talking about the Global South, what we actually mean by it is the second wave of the industrial revolution worldwide. The countries that are riding this huge wave are becoming emerging powers. How to incorporate these new powers into the liberal international order is a major issue, and Japan must take the lead in bringing them together. Especially in the Asia-Pacific region, there is no single powerful leader, so I think we have to bring the leading Asia-Pacific nations together. At the same time, we must seriously

consider how to restrain China and Russia from using force unilaterally, how to enable Ukraine to win, and how to keep China from going to war over Taiwan.

Toyoda: I would like to ask Prof. Masuo the next question. The Xi era has been seen as challenging to the extent that it has been called “wolf-warrior diplomacy”. Amid the escalation of the US-China confrontation, there was the recent China-Japan-Korea summit. While there are concerns about armed reunification with Taiwan by China, the summit agreed on “commitment to the international order through the rule of law”. But what does China really think of a rules-based order?

Masuo: You have indicated an important point. I myself believe that “wolf-warrior diplomacy” was made because Chinese diplomats were ordered to protect Xi’s domestic authority, which had been damaged by the pandemic. On the other hand, how China thinks about the rule of law is an important issue. Simply saying, China is hostile to the “rules-based order” advocated often by the West gets us nowhere. In Chinese, it is always written in brackets. In other words, the Chinese authority judges it to be “a fake without substance”. In the Sino-Russian joint statements of March 2023 and May 2024, the two countries even argued that the countries implementing hegemony were advocating it.

The portion of the Joint Statement of the recent Trilateral Summit mentions, “We reaffirmed our commitment to the purposes and principles of the Charter of the United Nations and to an international order based on the rule of law and international law.” Perhaps this wording itself was the outcome of the negotiations between the diplomats of the three countries. Here, for China, it is important that it was able to place the UN Charter before the “rule of law”, which Japan emphasizes. China, at least on the surface, is UN-oriented. It considers itself an authentic permanent member of the Security Council, having been part of the UN since its formation (actually, the People’s Republic of China participated in the UN Security Council only in 1971; prior to that, the Republic of China was its member representing all China). After World War II, Japan replaced the Japanese word for the UN from *ren-go-koku* to *kokuren* to conceal its hostility toward itself, but in truth they are the same group of countries with the Allied Powers. In other words, for China, advocacy of the UN Charter coincides with its insistence that its own vested interests as a founder be defended. If the UN Charter is implemented “correctly” according to China’s wishes, China is happy. Nor is China totally opposed to the “rule of law”, though China’s interpretation of it actually differs greatly from that of the West. But I don’t think China understands this.

The Sino-Russian Joint Statement issued the week before this Trilateral Summit is a very interesting document. Here the two

countries state that “countries that espouse hegemony and power politics seek to replace and subvert the universally accepted international order based on international law with a ‘rules-based order’.” It presents a distorted worldview in which the Western powers are showing nothing but menace to the world order.

Another very interesting point in the statement, which is related to Japan, is the very end of the first section. Here it states that “Both sides remain resolutely committed to upholding the outcome of the victory in World War II and the postwar world order as enshrined in the Charter of the United Nations, and oppose the denial, distortion, and falsification of the history of World War II.” It goes on to specifically pledge that both countries will “educate people to a correct view of history” and even states that “both sides plan to solemnly celebrate the 80th anniversary in 2025 of the Chinese people’s anti-Japanese war against Japanese aggression and the Soviet Union’s victory in the Fatherland Defense War, and jointly promote a correct view of World War II history.”

What is of concern here is that since 2023 there has been a fairly active discourse in China that the San Francisco Peace Treaty should be revised. At the “Future of Asia” conference held by *Nihon Keizai Shimbun* in May 2023, Yang Bojiang, director of the Institute of Japanese Studies at the Chinese Academy of Social Sciences, who was appointed by the Chinese Embassy in Japan to attend the conference, made such a bold statement unapologetically. The San Francisco Peace Treaty was, of course, concluded by Japan with the Allied Powers. But due to international circumstances at the time, China and the Soviet Union did not sign it. Recently, there has been a growing perception in China that the Chinese were the victors in World War II, having defeated Nazism, Fascism, and Japanese militarism, and should therefore have a better position in the UN. In the latest Sino-Russian Joint Declaration, China invites Russia to call for the same. And in order to promote such new claims, it is activating a new historical issue of World War II and the UN.

To put this abstract argument into a more realistic perspective, China is very concerned about reinforcement of the US-centered alliance network in the Indo-Pacific region, especially the actions taken by Japan and the US to strengthen the defense alignment in Japan’s southwest islands and integrated operations to keep an eye on Chinese military activities throughout the Pacific region, not just around Taiwan. Living in Fukuoka, I can clearly see that China has been rapidly strengthening its approach toward dissidents in Okinawa recently, mainly through the Chinese Consulate General in Fukuoka. China does not have a consulate in Okinawa, so the Consulate General in Fukuoka is in charge of Okinawa issues within the Chinese bureaucracy. China sends its agents, sometimes masquerading as academics, to Fukuoka and Okinawa under the cover of academic exchange. And it is the Consulate General that is orchestrating them.

In short, to bolster its security against the strengthened US-centered alliance network in the Indo-Pacific, China is pumping up a new history issue and infiltrating other country's domestic politics to offset its weak points. Under the cover of spreading a correct historical view of World War II around the world, it wants to reassert its position in the UN as a permanent member and create a system that will not allow others to challenge it. And in doing so, China will try to bring developing countries onto its side.

For Japan, this means that the Chinese have been trying to overthrow the existing international order that we have enjoyed since the end of the World War II. We have also learned that its new target for operating this strategy is summer 2025. We should increase our vigilance over it.

So, to sum up the whole thing, from China's point of view, the "rules-based order" is nothing but a deception, and it is even against the idea of adhering to it. That is how difficult it is to achieve the "rule of law" with China.

Toyoda: Prof. Aizawa, what kind of international order is Southeast Asia seeking?

Aizawa: I think there is at least a very charged sense of danger and crisis about the current international order. Perhaps, considering history since 1945, we may represent it as a peaceful period in the sense that there were no world wars, but from the perspective of the Global South or Southeast Asia, wars have been going on for a long time. The period known as the "Cold War" was a time of war in Southeast Asia, starting with the Vietnam War. When the US became the sole superpower, the war on terror was fought in the Global South all over the world, and now we have the problems in Ukraine and Gaza. It is the arrogant historical view of the G7 that the international order that has been created has been a peaceful era so far, and from the perspective of the rest of the world, excluding the developed countries, the previous international order did not guarantee peace.

This has been reaffirmed by the Syrian crisis in particular, and I believe that a major characteristic of the current situation is that it is filled with frustration over the dysfunctional nature of global governance and the deceptiveness of managing conflicts between major powers at the expense of peace in specific regions and small and medium-sized countries.

The question, then, is what kind of international order can be created to seek peace and stability for such countries. What we can do, at least as a group of nations inferior in military and economic power, is to raise our voices and try to make the international community more decentralized so that political legitimacy in the international community is not formed exclusively by the major powers. Specifically, we should try to foster political legitimacy

through regional institutions, and the best approach is to be involved as much as possible in setting the stage whenever there are negotiations on rulemaking or power coordination that may result in a transformation of the regional order.

If Southeast Asia seeks a new international order, the biggest problem it will face is disparities in various aspects. In particular, I think of disparities in access to science and technology. This is because science and technology will play an increasingly important role as a factor in shaping the new order. If advances in science and technology are accessible to people all over the world, they may reduce global disparities, but today science and technology have come to define national interests in great power competition. If more science and technology is viewed as a strategic resource and its fruits are monopolized by a few countries that have the funds available to develop it, the difficulties that countries had in accessing vaccines during the recent pandemic disaster are likely to occur more frequently in the future. Southeast Asia, and other countries in the Global South, are concerned that access to science and technology will become a lever in the formation of the security order and that they will be shut out of the tools.

Therefore, how do we manage science and technology? I believe that the core of a stable international order will be to create a mechanism to make science and technology not a tool for national security but a global commons, an international public good.

Toyoda: Prof. Kitaoka, you were ambassador and deputy permanent representative of Japan to the UN, so you know it well. There is a sense of powerlessness in the air about the UN, but in this age of rules the UN really needs to function. Japan has long sought to be a permanent member of the UN Security Council, but what do you think the UN should be, including that point?

Kitaoka: The UN is by nature, powerless, because it has no military power and no economic power of its own. It cannot even run a peacekeeping operation without cooperation with the member countries. In fact, to run any military force, you need something like a general staff headquarter, which operates 24/7. But the UN has no such thing.

Though the UN was designed to maintain the world order, five permanent members were appointed to take special responsibility for peace and security in the world. However, these five were soon in conflict with each other, which brought about the Cold War, and although there had been tension during the Cold War, the UN had been able to serve as a kind of balancer in the conflict between the two camps. As such, in the independence of many Asian and African countries, the UN played a relevant role.

So, what can the UN do now? It is still important as a venue to provide a forum to mobilize international public opinion because

there is no organization of this kind in the world other than the UN. In this regard, I think Japan should stay on the Security Council as a non-permanent member as long as possible. So far, Japan has been on the council longer than any other country, but when Japan's term ends at the end of this year, Japan will take the next nine years off, as announced by the government. This would be the longest break Japan has ever had. I think this is truly to be avoided. Because now that Japan is on the Security Council, when there is an incident in Palestine, for example, Japan can make a statement like the other members of the Security Council, and the global media may carry this message. The world will know about it, and it will be carried in Japan. If Japan were not a member of the Security Council, it could happen that no one would know what Japan thinks about what happens in Gaza. I think we should work more on educating the Japanese public and communicating to the world Japanese views on international affairs, and we should seek a way of staying longer in the Security Council for that purpose.

To this end, there were two proposals in 2005, Model A and Model B. Model A is, in essence, for Japan to become a permanent member. Model B is to get a semi-permanent position, for example for a term of about four years, with the possibility of re-election. In other words, if elected, Japan would serve for four years, and if re-elected, Japan would serve for eight years. So, I think we should seek a direction to stay longer by introducing Model B after taking a break for four years. Model A is not possible because even in 2005, when Japan's financial contribution to the UN was much larger and opposition from Russia and China was not so strong, it was not possible. We should change our strategy to Model B as soon as possible.

There is very strong public antipathy against the permanent members of the Security Council having veto power. If a resolution were to be proposed to limit the veto power at the Security Council, I believe that almost all the member countries except for the US, China, and Russia, might agree to it. One way to do this would be to abolish the veto completely, but even if that is impossible, it could be logically possible, though extremely difficult, to change the veto system so that any veto would have to be supported not by one country alone but by around two countries together. Also, the secretary general's capacity and authority are seriously declining now, and in order to deal with this, I think it is possible to add a more powerful staff around the secretary general.

In addition, Japan has no friends in the UN. Unless a country has its friends, its presence in the UN is limited. Europe has about 30 members, so it has a certain voice. Even the small countries of Singapore, Switzerland, Liechtenstein, Jordan, and Costa Rica have formed a group called the S5, and when they speak as the S5, people listen to them a little. I think Japan should make a little more effort to communicate as a big mass by establishing a group with Southeast

Asian countries and Pacific Island countries.

Next Steps for Japan

Toyoda: I would now like to ask you to talk about what Japan should do in these times. Many people are concerned about China trying to reunify with Taiwan by military force. I think this must not happen, but is it possible to avoid a Taiwan conflict? Prof. Masuo, what should Japan do to prevent this?

Masuo: I believe that the situation surrounding Taiwan is still uncertain and that we cannot confirm an emergency will definitely happen. There should be a way to prevent it. If China could invade Taiwan, when and under what conditions would this occur? One possibility is if China views itself to be capable of doing so. This includes both military and economic capacity. This condition would be met if the invasion is expected to succeed at a relatively small cost, or if the countermeasures taken by the Western powers, particularly by the US and Japan, would not impact China that much.

I believe that Japanese experts have discussed a lot about our national defense capability in relation to China. To strengthen deterrence, Japan has been boosting integrated military operations together with the US and facilitating other ways of cooperation. Perhaps a little more consideration will be given to its economic strength.

China itself is no doubt concerned about its own economic problems. It appears to have been preparing for war-time economic control over the past several years, putting so much emphasis on food security. If such preparations progress and a situation arises in which China sees its own economic development as continuing even if its supply chains are cut off from those of the West, while Japan's economic strength is considered insignificant by them, it will be an incentive for them to initiate an invasion over Taiwan. Reestablishing Japan's robust economy is very important for increasing Japan's attractiveness to China. I believe that more can be done in this effort.

Another important factor that impacts China's invasion is the desire of the regime. The Xi administration has not yet firmly decided to "liberate" Taiwan. China does not actively want to reunify Taiwan by force. Many pundits have said that this is a last resort, and I believe the administration is of the same view. China is more likely to invade if the Taiwanese independence movement accelerates and its friction with the West becomes so extreme that Beijing believes it no longer needs to fear a breakdown of relations with the West. The likelihood of an invasion also increases when internal political conditions become so desperate and the Xi regime believes it needs to bolster domestic nationalism at any cost. These are all fairly extreme cases.

On the other side, I am concerned about the recent sharp decline

in exchanges between China and the rest of the world, especially with the West. In Hong Kong, the National Security Ordinance was passed in March, and we have already seen the first arrests based on this. Perhaps it has already become dangerous for us to go to Hong Kong and Macau. I often exchange views with Western researchers, but discussions between them and China are also rapidly decreasing. So there has been almost no real discussion among the experts of the true feeling that “No, we don’t really want this to happen, but we can’t help it because your country is doing this to us.” Chinese researchers have no choice but to write reports based on information they can get on the controlled Internet that asserts “Western countries are trying to encircle China to continue their domination.” Their judgment of the situation has become biased unfortunately.

The recent Sino-Russian Joint Statement does not logically explain why Xi would support the Russians to that extent. Unlike Russia, China is not at war, has deep economic exchanges with the free world, and is a beneficiary of the existing international order. It is not in China’s interest to depart from the current international order by being on the side of Russia. I guess the number of people within China, who have a proper understanding of the situation overseas, who can write fair reports and make rational policy recommendations to the top, has been decreasing.

I think Japan could make a little more effort on these issues in relation to information flows. Recently, the government has been very negative about joint research with China, and bilateral exchange programs have almost disappeared. However, this is precisely the right moment that we should make the effort to invite Chinese researchers to discuss things over drinks in Japan. It is much cheaper and easier than purchasing defense equipment. I believe that such a steady exchange is now desperately needed.

Toyoda: I believe that Japan has a long history of cooperation with Southeast Asia. Prof. Aizawa, is it possible for Japan to walk with the people of the Global South in Southeast Asia?

Aizawa: It is essential that we walk together, and not only walk together, but build a deeper relationship. Rather than a de facto alliance or a security alliance, we must work together with the intention of forming a social alliance with Southeast Asia. Furthermore, I would even propose that Japan should seek to join ASEAN. If we are to leverage the trust between ASEAN countries and Japan, that has been fostered by the long-standing cooperative relationships cultivated by our predecessors, this ambitious proposal could show and prove the political will in building up a new relationship, a relationship no longer relying heavily on economic cooperation and direct investment, as has been the case in the past. Frankly speaking, we should seek a relationship in which Southeast Asia can help Japan with its economic and social challenges, and we

should be prepared to change Japan’s domestic legal and customary settings to demonstrate our earnestness and seriousness in this regard.

One bold idea to showcase this point is to reform foreign language selection in university entrance examinations. Currently, the Standard university entrance exam includes German and French, as well as Chinese and Korean. I think it would send a strong message if we could make language choices such as Vietnamese and Indonesian as well. If Japan is serious about seeking human resources from Southeast Asia, this would be a very significant positive signal giving strong social legitimacy to the linguistic background of such human resources. I believe that such a decision would demonstrate Japan’s seriousness and willingness to form a social alliance, and would be the foundation for building a new relationship of trust in the coming years.

Remember, it is not only Japan that is trying to attract Southeast Asia. The same is true everywhere else in any region, including the US, which is looking for talents in Southeast Asia. Therefore, if Japan remains idle, it will soon lose out in this competition in attracting Southeast Asian talent. At the moment, Japan has a relationship of trust with Southeast Asia. That is why Japan must now take full advantage of its existing relationships with Southeast Asia and change.

The last thing I must say is that there is not much time left for Japan to further tighten relations with Southeast Asia. If anyone in Southeast Asia can think positively about forming a social alliance with Japan there, it is probably people in their 40s today, the group of people who were born in the 1980s and grew up in the 1990s, who at least knew Japan when it still had power, are just now in their 40s and now becoming political and economic leaders. If this group is taken over by the younger generation, and Japan’s perspective on Southeast Asia does not change, I believe Japan’s credibility and attractiveness will continue to decline. I think there are only 3-10 years left for Japan to send a signal that it wants to build a stronger relationship with Southeast Asia, and for this signal to be socially and politically effective.

Toyoda: I would like to ask Prof. Kitaoka if, looking at the current situation which could turn into a clash of powers, it is possible for Japan to uphold the rule of law? Also, with reference to your book published a few years ago titled “A Western-Pacific Union: Japan’s New Geopolitical Strategy”, what kind of role could this Western-Pacific Union play in the new international order?

Kitaoka: As far as the rule of law is concerned, the international community is an anarchical society because there are no police or courts. Meanwhile, it is the developed countries that are leading the rule of law today; the rule of law that the EU and other countries are

advocating for is too far advanced from the point of view of developing countries. Take, for example, the issue of gender. Gender equality is one of the fundamental principles, but such equality will not be immediately accepted in the Muslim world.

For example, people believe that women must be protected and are not allowed to go afar. As a result, they cannot go to school, leaving the literacy rate very low for woman. What do we, the Japan International Cooperation Agency (JICA) do in Pakistan? Rather than criticizing this belief straightforwardly, we build small schools in the neighborhoods of villages to encourage women's education. Instead of simply advocating for law and criticizing the developing nations for their lack of law, we should take a more long-term, indirect and conciliatory approach to compromise with the developing nations' culture, and I think it should be the responsibility of developed countries not to provoke antipathy from the developing countries by simply advocating for the rule of law while being reluctant to improve their social, political and economic system. I believe that Japan is the only developed country that has not done such a thing.

Another thing I find very regrettable in relations with developing nations is the actual lack of academic and scholarly exchanges with China. Everyone thinks that if you go to China and speak too frankly about any international political issue, which could be interpreted as criticism against the Chinese government, you may be arrested by the Chinese authorities and not be able to come back home. So, we have to discuss it outside of China. We should be able to openly and vigorously discuss about what China is doing in the world. For example, in the UN Charter, it says "national self-determination". This means that Taiwan should not be threatened by force. And there is the Uyghur issue on alleged violations of human rights, and China also has many areas where it could be severely criticized. These things should be discussed with Chinese scholars. I often say that the mainland Chinese political authorities did not actually rule Taiwan for that long. The longest period was from the beginning of the 17th century, and it was only for two decades or so that they effectively controlled the mountainous areas and even the west coast of Taiwan. These facts should be discussed properly with Chinese scholars.

Now, the Western-Pacific Union you are asking about is a concept I came up with six or seven years ago. To have a big voice in the international community, you must have a group. Japan is part of the JUSCANZ group (Japan, US, Canada, Australia, and New Zealand), but this is a group that listens to what the US says. If we have a conflict with the US, the US will leave the group, so in the end JUSCANZ will not be the right venue to express our voice. It is with Southeast Asian countries that we can express our opinions most frankly. I used to think that Japan should join ASEAN. I think it would be better for Japan to work together with each of the ASEAN countries to the point where we are on equal relations.

Basically, we have common interests. After all, Southeast Asia is

also afraid of China, but does not want to become a subordinate of China. To some extent, Southeast Asia know that the US military presence in this region is necessary in this regard. But Southeast Asia would not trust either China or the US. They believe that Japan is the one they can trust. Therefore, it is important for Japan to create special relationships with Southeast Asia in various places. We should build the social alliance that Prof. Aizawa mentioned with Southeast Asia. For example, Japan is supporting the creation of coast guard agencies in various countries in Southeast Asia. Since the Japan Coast Guard is not a military force, JICA can cooperate with them. This can serve as a kind of deterrence to China and improve information sharing among us.

Also, several years ago, when Indonesia experienced a major earthquake and people from all over the world rushed to help. During the second phase of reconstruction assistance, the Indonesian side decided, "We can't get together with various leaders to think about reconstruction, so we're going to ask Japan to do this; we're going to ask JICA to do this." I hope we can somehow create such a relationship. What is important to deepen our relationship with these Southeast Asian countries is closer interaction. I would like to see a special study abroad program, for example, the creation of a graduate university with Southeast Asian students as its core, and more frequent dialogues among young researchers.

I myself have participated in various dialogues with Japan and China, Japan and the US, Japan and the United Kingdom, Japan and Germany, Japan and France, but very few with Southeast Asia. It is the Ministry of Economy, Trade and Industry that is interacting with Southeast Asia. We need to expand and deepen this to the academic level. Southeast Asia has several countries that are now among the prime, emerging economies. Indonesia, of course, but also Thailand, Malaysia, Vietnam, and the Philippines are among them. We must try to attract these to the democratic side, the internationalist side, as much as possible. It is important not to let them go to the Chinese side, and there is a tug of war here. I think it is important to guide them in the direction of joining the OECD, not the BRICS.

Toyoda: In closing on this matter, I would like to ask Prof. Kanehara how Japan should approach the restructuring of the international order, especially with regard to the Global South.

Kanehara: For the first time in 200 years, the advanced industrial democracies are shrinking in proportion. The countries of the first wave of the industrial revolution are beginning to shrink, and a huge second wave is emerging like a tsunami. We call those emerging countries growing on this second wave the Global South. How to incorporate new countries in our liberal international order to maintain the balance of power relations to our advantage is extremely important. For Japan there is no alternative to the Japan-

US alliance. However, the Japan-US alliance alone is no longer sufficient to cope with the rise of China, so the question is what to do now. South Asia, starting with India, which is gaining strength, and Southeast Asia are important partners for Japanese diplomacy in the immediate future.

Since the Meiji Era, Japan has only looked up to the developed countries of the West. Finally, now our eyes are beginning to look down toward the South, but then we know nothing about those countries, neither about the history of Indonesia nor about the history of Vietnam, for example.

Today, a large number of Southeast Asians are entering Japan as foreign workers. For Japan, which is experiencing a population decline of several hundred thousand every year, it is inevitable to bring them into the labor market. There are 2.5 million foreign residents in Japan today, and this number will probably increase to about 10 million, or 10% of the population.

From now on, we must engage in earnest and serious diplomacy with Southeast Asia. The Japanese Ministry of Foreign Affairs is also sending its most talented ambassadors to Southeast Asia and West Asia. I think we have to deal with Southeast Asia and Western Asia with the same weight as we once did with Europe and the US.

Let me say a few words about the rule of law. The term “rule of law” involves values. The countries of the Global South now think that what the West says about the rule of law, democracy, and liberalism is a double standard. The countries of the Global South think, “Don’t lecture us now about the ‘rule of law’ as if you were always behaving respectfully. You were discriminating against us in the past.” It is true that in the 19th century, the liberal international order was centered on the West and was a local and partial order with clear regional and racial limits, but in the latter half of the 20th century, thanks to the efforts of people such as Gandhi, who helped lead India to independence, King, who spearheaded the civil rights movement, and Mandela, who overthrew apartheid, the liberal order has spread and become universal on a global scale.

There is no order that can replace the liberal international order. The core principle is that we are all equal and free, have a right to life and to pursue happiness and realize ourselves, and that we establish a government for that purpose and its legitimacy is based upon peoples’ free will and consent. This principle can very well go along with Asian political tradition. Nobody is against this except dictators. Therefore, I think we need to tell the emerging countries that we must support this together.

Europe and the US are radical, and when it comes to human rights and democracy, they are quick to impose sanctions, which is counterproductive. As in the case of corporal punishment in schools, students who are beaten resent it more than they feel remorse. Japan must be responsible for persuading Asian and African nations of the value of liberalism, democracy, and the rule of law, as these

are ideas that are commonly associated with the traditional values of Asians; they are universal, not just European. Only the Japanese, as Asians, can say that these ideas have been held by Asians for centuries. I think we need to continue to issue such a message.

Finally, I would like to mention the actual generational divisions within Japan, since it is because of these divisions that Japanese diplomacy has not been as effective as it could have been. People of the older generation beyond their 90s who knew about the Japanese Empire believe that the racial attitudes and colonial histories of the white democracies embodied a double standard. Then came the leftist generation in their 70s and 80s steeped in radical socialist and communist ideology. A liberal generation like ours, in our 50s and 60s, followed and we are the generation now responsible for Japan. We need to look squarely at our values and say out loud that Japan has practiced modern democracy, liberalism, and the rule of law for a long time now and has helped the liberal international order to spread on a global scale. In order to do so, I think we must quickly overcome the generational divisions within our country.

One last thing about Taiwan, if you look at international power relations as a whole, especially in terms of the size of the economy, it is two to one between the West as a whole and China, and the West is still strong right now. If we stay united, I do not think China will start an adventurous war. It is vital that the West does not become divided. I don’t think China is yet strong enough to start a Taiwan war and win in the end, but it can anyway start one. Once a war breaks out, there is no other way but to push back with military force. The human and material damage that would result from a Taiwan contingency is beyond imagination, so it is very important not to let it start.

The Taiwanese, who had lived in Taiwan before the end of WWII, are known as “native Taiwanese”. They are people who lived a very different history from that of mainland China for 150 years. They are brave people. After the Sino-Japanese War ended and Taiwan was ceded to Japan, the native Taiwanese fought bravely against the Japanese, though the Qing soldiers swiftly returned home. After Chiang Kai-shek tried to move to Taiwan, they again rioted. Each time, tens of thousands of people died. For the indigenous Taiwanese people, Chiang Kai-shek was after all a tyrannical intruder. Their feelings of national self-determination came to the fore in the constitutional amendments and free elections of 1994 and 1996. The native Taiwanese people still have a complicated fractured identity, but the growth of the “Free Taiwan” identity has not stopped.

The freed Taiwanese people aspire to national self-determination. On the other hand, a situation is being set up where China can invade Taiwan with its massive military power. In this context, the status quo must be maintained. Japan must say to Taiwan, “We must avoid a war,” and clearly say to China, “We support the status quo.” The tension over the Taiwan Strait will continue until China becomes a

democracy one day. And I think we have no choice but to resolve to hang on for maybe 100 years.

Conclusion

Toyoda: Finally, I would like to ask each of you to briefly state what you value most.

Kitaoka: Since power is necessary to maintain order, I believe we should enhance our deterrence capability and be careful not to provoke China, while at the same time strengthening our power so that if something happens, we will not remain silent. It would take a long time. When the US came to Japan in 1945, its first goal was to make Japan a country that would never again be able to produce the Zero fighter. That still lingers today.

Many products are today dual-use, military and civilian. To be or not to be a weapon is an almost impossible boundary. The strengthening of Japan's industrial capacity by collaboration among universities, the private sector and the government will lead to the strengthening of its military and deterrence. I believe we should strengthen our military power while making it clear that we will not use it first.

Kanehara: I believe that the cornerstone is to maintain a military balance with China by building up Japan's conventional forces more and more, based on the Japan-US alliance.

In terms of the economy, we need to stop thinking in terms of a national economy, but instead think first and foremost about the wealth of rising Asia as a whole in the context of free trade. We need to change our thinking so that Japan can absorb the growing wealth of Asia. We also need to correct the 80-year postwar mistake of not utilizing the technological capabilities of academia and the business community for national security at all. Our military, industry, and academia are too much divided. This is not good. We need to take it to the next level, such as producing all semiconductors for making cutting-edge weapons domestically. I think there are still big barriers in the way of industry-academia-government cooperation for security technology, such as the Science Council of Japan.

Finally, back to values again, I think we need to explain freedom and democracy in Japan's own words. John Locke and Jean-Jacques Rousseau are important, but what is it that the Japanese have been seeking for 150 years after the Meiji Era? Wasn't it freedom and democracy? If we cannot explain in our own words what we have struggled to achieve since the Meiji Era, no one in the Global South will come closer to us. If Japan cannot talk about freedom, democracy, and the rule of law in its own words, it will be difficult for Japan to become an international leader in the enhancement of universal values.

Masuo: There are many things that can be done, but I think the most important thing is to develop human resources that can work well in contributing to the international community as a whole. The next 10 years will probably be the most difficult period for the international community. But after that, a new generation will be reproduced. Japan has a good number of human resources who can engage with Western society, but this is not enough in times of change. It is crucial for us to develop a large number of people who understand the various positions of developing countries, and who can discuss and negotiate issues on equal terms with Russia and China that have completely different worldviews.

Aizawa: I still think that Japan must design and articulate our new model of the social contract: in other words, a social contract that pursues prosperity, security, and freedom, all three at the same time. Also, this social contract is not only for the Japanese but also for those who come to and live in Japan. I agree with Prof. Kanehara that it is very important to explain freedom in Japan's own language and terms.

We are now in a time when the relationship between state and society is being transformed by digital technology. This is not only a time of change in the international order, but a time of change in social order and both are intertwined. Each country, therefore, is looking at others to see what kind of society and state relationship each will create. I believe Japan must create a model that other countries can subscribe to – a new type of social contract that is suitable for this era. I think that this approach, dealing with social order as an international order, will have a great geopolitical effect.

Toyoda: Thank you very much for your views in this discussion. **JS**

R oundtable on Trump 2.0 – How Can We Tackle Trade Policy Issues? (Nov. 25, 2024)

By Japan SPOTLIGHT

Participants: Ambassador Alan Wolff, former deputy director-general of the WTO
Professor Joost Pauwelyn, the Geneva Graduate Institute and the law firm of Cassedy, Levy, Kent
Dr. Henry Gao, Singapore Management University
Dr. Akihiko Tamura, senior advisor of RIETI

Moderator: Masakazu Toyoda, chairman & CEO, Japan Economic Foundation (JEF)

Participants



Ambassador Alan Wolff



Prof. Joost Pauwelyn



Dr. Henry Gao



Dr. Akihiko Tamura



Masakazu Toyoda

Introduction

Toyoda: Thank you all very much for joining us. The postwar international order is now in chaos. The war in Ukraine and the conflict in Gaza are becoming more serious. Major countries invoked their veto power in the Security Council of the United Nations, so nothing was decided, unfortunately. The dysfunction of the UN has become apparent. On the international trade front, the World Trade Organization is similarly dysfunctional. On the legislative front, the Doha Round has stalled during negotiations and is not expected to conclude anytime soon. Meanwhile, on the judicial front, the two-tier dispute settlement system is not working. The members of the appellate body, which serves the superior tribunal, have not been appointed, due to opposition from a particular country. And so the dispute settlement mechanism is virtually non-functional. The international order, which has been steadily moving forward for more than 70 years since the end of World War II, has become stagnant and confused. Today I have five questions to discuss.

First, why is the international trading system in such disarray? What is the background? Second, on the legislative side of the WTO,

instead of the agreement of the Doha Round, many agreements such as pluri-agreements, FTAs and RTAs have been established. How should this be evaluated? Third, on the judicial side, will it be possible to rebuild the dispute resolution mechanism under the second Donald Trump administration? Should we expect the MPIA, the Multi-Party Interim Appeal Arbitration Arrangement, to replace the WTO dispute settlement for the time being? Fourth, the CPTPP is said to be the highest level of RTA. Is it possible to expand the number of participating countries of the CPTPP, link it with the European Union and eventually invite the United States, and finally to transplant its high-level rules to the WTO by consensus? Fifth, with the confrontation between the US and China, the concept of economic security has emerged. There is a growing consensus among developed countries that this scheme, at least with China, is necessary.

Will the era of free trade ever come again? We have asked four experts, from the US, Europe, Asia, and Japan to join us at a roundtable discussion on the international trading system. First, from the US, Ambassador Alan Wolff, former deputy director-general of the WTO. Prof. Joost Pauwelyn of the Geneva Graduate Institute

and the law firm of Cassidy, Levy, Kent is joining us from Europe, and Dr. Akihiko Tamura, director of the JETRO Paris office (who is from Japan), is also here. The fourth participant, from Asia, is Prof. Henry Gao from Singapore Management University.

Why Has Chaos Occurred in International Trade?

Toyoda: First, why has there been such confusion in the international trading system? Is it because of the relative decline in the power of the US, which had overwhelming military and economic power after the war? Is not enough being done in the US to address the losers in free trade? Do more and more people have a victim mentality toward free trade? Ambassador Wolff, I'd like to ask you for your opinion.

Wolff: Thank you very much. I'm very pleased to join this distinguished group to discuss these important subjects. You're right, the international trading order *is* in disarray. I do not see this as in any way a sign of US weakness. It has the strongest military by far, and an economy that is the envy of most others. Nevertheless, the US is becoming isolationist. It is no longer supporting the system that it was instrumental in building.

There is good evidence that the high point of the multilateral trading system occurred in 1998 when world leaders, including President Bill Clinton and Nelson Mandela, gathered in Geneva to celebrate the 50th anniversary of GATT and to express their hopes for the success of the new World Trade Organization. Nothing approaching that far-reaching nature of the Uruguay Round agreements that had just been concluded in 1994 on agriculture, services, intellectual property, and product standards, was ever negotiated again. Domestic US support for open trade eroded when technology, container ships, and communications brought stiffer competition from emerging economies. From the US viewpoint, the WTO failed to maintain a balance between open trade policies and the availability of trade remedies where harm was caused by trade. The WTO's problems lie partly in the deficiencies of the WTO structure itself. The creation of a world trade organization was not the original purpose of the Uruguay Round. So there was not a thoughtful and balanced system of governance devised, no effective legislative branch as there was insufficient common ground, no executive as is found in the World Bank, the IMF, or the OECD. Without adequate rules, dispute settlement could not address growing problems of subsidies and state intervention, and it was relied upon to too great an extent. Energy was drained from the WTO as members turned to bilateral and regional agreements. Later, nationalism and populism grew. Trade liberalization clearly had run its course. Substantial trade imbalances over an extended period of time were not politically sustainable. There were many causes of

dysfunction, which we see in the trading system. That's a quick overview of my answer.

Toyoda: Thank you very much. So it's not because of the weakness of the US, it's a problem of the WTO itself. Dr. Gao, please share your view.

Gao: Thank you. It's a pleasure to join this distinguished group and old friends, Aki and Alan. I fully agree with Ambassador Wolff that indeed, in absolute terms, US power has not really declined. I think that one major reason for this is the rise of China. So even though China is a rising national power as well as other nations in what we call Global South, if you look at the military power and GDP of these states, they still cannot match that of the US. But there is the perception from the Chinese leadership that the East is rising and the West is in decline. They think that its time has come, just like what Japan perceived before World War II, that it has risen to such a position that it could challenge the US. This is reflected in two major events in 2008.

The first was the financial crisis sweeping the US and Europe. China was not really affected by the financial crisis because its financial system, ironically, had not been fully opened up for many years after its accession to the WTO and therefore it was insulated from the global shocks brought about by the financial crisis. The second major event in 2008 was the Olympic Games, held in China. That was praised as marking China's coming of age as a major power on the international stage, because it hosted the Olympic Games, which some claimed as the best the world had ever seen. Because of that, China then decided to challenge US dominance. That is one reason behind the disarray in the international system.

Another reason is perception, not the reality, because there's always a difference between perception and reality. In both cases, I would argue that the Chinese perceptions are wrong. They do not reflect reality. But these perceptions drove the Chinese actions. The second perception is that actually exports are not so important in China's economic development. When Barack Obama was campaigning for the presidency, he criticized China for having a large trade surplus. China responded by saying that, although it exports a lot of goods to the US, the US exports a lot of services to China, so the two cancel each other out. But that didn't really work. So China then decided to look for other means. Around that time, 2009, the WTO started the "Made in the World Initiative". I think Ambassador Wolff was still the DDG at the WTO then, so maybe he can share the inside story. The Made in the World Initiative looks at the value added of each country in global trade rather than the pure numbers. Looking at the export of an iPhone that costs \$1,000, for example, it will be recorded as China exporting \$1,000 to the US. But actually most of the value added is not from China, but from the US. The IP is

from Japan, the chips and memory from Europe. The famous iPhone study done by JETRO concluded that China's contribution to the value added of an iPhone is actually less than 10%. It was originally around 7%, but then it rose to about 10%. The Chinese government was really interested in that study. The Chinese Ministry of Commerce (MOFCOM) encourages researchers to look deeper into the so-called trading value added.

They did a report around 2012 or 2013 that broke down the value added of different components of China's exports. One conclusion is really interesting, I discussed this in a [paper](#) I wrote two years ago on the shift from trading in value to trading in values. One of the MOFCOM conclusions was that the role of exports in China's economic development has been exaggerated. They say that, because our value added is so little for these exports, we should not rely on exports, but more on domestic consumption as a main driver of economic growth. That led to the later dual circulation strategy and China's reduction of its reliance on exports. But all that was wrong because where would the money for consumption come from? It came from all these exports Chinese firms did for all these world markets. So I think that is a wrong conclusion. But that was the conclusion that MOFCOM believed and they reported this to the senior leadership, who decided that they didn't need to rely on exports so much, but could challenge the US and rely on domestic consumption.

But 10 years has passed and domestic consumption is not really happening. That is the second reason why China is changing its position. That explains a lot about all these aggressive positions by China, all these trade wars with the US and mini-trade wars with Canada, Australia, Europe, etc. It also explains why China was a threat in other countries with its value chains during the Ukraine war, that highlighted the vulnerability of relying on China in the value chains. That led the world to start to delink or derisk from China. That also explains partly why the US is less interested in the WTO, because the US thinks it is quite risky to rely on partners like China, and therefore it should rely on its own capacity. That's my two cents worth, from the Chinese perspective.

Toyoda: Thank you very much. A very interesting view. Dr. Tamura, could you tell us your views, reflecting both the Japanese and the European perspectives?

Tamura: Thank you very much. I'm honored to be part of this interesting session, meeting some old friends. I'd like to add something to the eloquent statements by Ambassador Wolff and Professor Gao.

I share the view of all the panelists and moderators that the international trading system has been in trouble – not just since yesterday, but for a number of years. Therefore, the reasons for this

trouble must be multifaceted and diverse. I fully agree with Ambassador Wolff that one primary reason for the trouble derives from the systemic defect of this system, including the WTO Secretariat and the WTO system as a whole. Chairman Toyoda hypothesizes that it could be because of the relative decline in the power of the US. I'm not sure whether this is correct. Setting aside whether it is true that the power of the US is declining, the premise of this hypothesis may be the "hegemonic stability theory" advocated by Prof. Charles Kindleberger. But given the fact that this theory is now considered to be an inadequate explanation of what's going on in global society, such as the establishment of the WTO and the prosperity of many international regimes, it's fair to say that having hegemonic countries is unnecessary for stable orders. I would rather point out the importance of ideology for the stability of an international system. The ideology promoted by the UNCTAD in the 1960s, that is, the Prebisch-Singer hypothesis – an import-substitute policy – was not helpful to the prosperity of the developing countries concerned, and thus this UNCTAD campaign aimed at reforming the GATT system got into trouble and eventually failed. My point is that the recipe for a stable order is not the existence of superpowers, but the existence of a sound ideology and philosophy to give practical functionality and sustainability to the "regime" or global society. Therefore, we could argue that one reason why the international trade regime is in the current state may be at least partly because of the confusion of ideology.

The WTO has been in principle based upon the ideology of neo-classical economics, which is to assure us that more liberal more prosperous. However, another idea has emerged, which is that resilience is also important. We have to balance efficiency and resilience. The ideology which used to be placed at the center of the WTO system is now in question. So, to understand and fix the current problem of the WTO, we must go through some ideological switching. But there is no new consensus reached yet among the WTO members. Therefore, some people are starting to look for alternatives. Some people may want to put new ideology into the WTO as a new underpinning. However, that conclusion has not been reached yet. This is one reason why there is confusion in the current WTO system.

Toyoda: Thank you very much for this philosophical stance. It's probably because of a confusion of ideology. Prof. Pauwelyn, could you tell us your view?

Pauwelyn: Thank you. It's a pleasure to contribute to this fascinating debate. I would mention three factors that explain the long-standing trouble the global trading system is in. Firstly, the rise of China as "the factory of the world" and a leading tech power, largely as a result of a state-driven economic system that is radically different

from the market-driven economic system that countries were supposed to have in place as implied by WTO rules. As WTO membership and, especially, the diversity between WTO members grew, it became more and more difficult to adapt WTO rules to new realities, given that the WTO works with consensus. This meant that WTO disciplines, dating from 1994, before the Internet was commercialized, became increasingly less relevant. When a system cannot adapt, it fades. Where the WTO did evolve, by means of dispute settlement, it happened without the support of key WTO members, making things worse. Secondly, as emerging countries captured a larger share of world trade and became more competitive, often driven by state intervention, the US felt not only the gains of trade but increasingly also the pains and dislocations linked to trade. Combined with more inward-looking political trends, this has reduced US willingness to lead the cause of trade liberalization and the WTO, not because of an alleged reduction in US power, but rather from the perception that the US was no longer benefitting from the system. Thirdly, and this is a factor that goes beyond the US and China, in many other countries including Europe, the tables have turned against globalization and openness, with more protectionist and inward-looking politicians in positions of power, such as in the United Kingdom and also in Italy and France. This is a broader societal trend going beyond trade, but deeply affecting the popular support for trade deals. One core reason for this trend is that the system focused too much on liberalization and not enough on how to deal with the negative social, environmental and security spillovers of this liberalization.

FTAs & RTAs – Are They Strengthening International Trade?

Toyoda: Thank you very much for your view. Now to the second question. On the legislative side of the WTO, instead of the Doha Round Agreement, pre-agreements, FTAs, and RTAs have been established many times. How should this be evaluated from the perspective of strengthening the international trading system? Some call it an undesirable spaghetti bowl situation. Prof. Gao, Singapore is a member of ASEAN and has concluded around 30 FTAs. How do you evaluate the current situation with so many FTAs and RTAs?

Gao: Going back to Singapore's first FTA, which was concluded in 1992 with ASEAN neighbors, due to the rise of other trading blocs such as NAFTA and the EU, which were both largely concluded by 1992, Singapore felt it also needed to promote regional economic integration at the ASEAN level. At the ministerial conference held in Singapore in 1992, Singapore proposed building an ASEAN-wide FTA. That changed the nature of ASEAN. The main reason for its initial establishment in 1967 was to deal with the spread of

Communism from China. It was mainly established as a political organization, but in 1992 it was transferred into an economic organization promoting economic integration. Singapore's FTA strategy is composed of three components. The first is to promote regional integration and regional economic development, as Singapore is part of ASEAN, because Singapore realized that it is the only rich developed country in the region and it cannot survive on its own if its neighbors are poor. That is why it has always tried to promote regional economic integration since 1992. By doing that, Singapore is trying to ensure that all countries in ASEAN reach similar levels of economic development. There would be no great disparity and therefore the boat would be lifted for everyone and the other countries would not be envious of Singapore.

The second component of the strategy is to build friendships with the major powers. Until recently, Singapore was the only country in the world that had a bilateral FTA with each of the big four countries/groups, the US, the European Union, China, and Japan. But this changed with the conclusion of the RCEP. South Korea also now has all these FTAs. By doing that, Singapore tried to maintain the balance of the great powers in the region. The US is our traditional ally. Singapore recognized that the US is the benign hegemon. As some Singapore officials say, it is much easier to work with the devil you know than with the devil you don't. But China is emerging. Singapore recognized that it has to build a good relationship with China. So it has been courting China by signing both the bilateral FTA and also the ASEAN-wide FTA, and now the RCEP. The EU and Japan are also very important, so Singapore has signed FTAs with them.

The third strategic component is to build path-finding agreements or model agreements with like-minded countries. This is most evident in the TPP. The TPP started out as the agreement Singapore signed in 2005 with three likeminded friends – New Zealand, Chile and Brunei – in order to build this high-standard agreement. Hopefully, the US will join and this would make it a global agreement. The original name of the P4 agreement was the Trans-Pacific Strategic Economic Partnership (TPSEP); this evolved into the TPP and now the CPTPP. The other example is the Digital Economy Partnership Agreement (DEPA), which is basically the TPP for digital trade. Singapore again is trying to use the DEPA by teaming up with New Zealand and Chile as a way to design some new rules for digital trade and to then multilateralize this at the WTO level. This already happened to some extent with the conclusion of the substantive negotiations of the JSI on e-commerce. These three components comprise Singapore's strategy and that tells us how a small country like Singapore, a country with the highest trade to GDP ratio in the world, as high as 400%, achieves balance in the face of all this great power competition, and the emergence of rising economic blocs. I think this provides very interesting lessons to other smaller economies.

Toyoda: Thank you very much. Prof. Pauwelyn, could you share your views?

Pauwelyn: The EU has been the absolute champion of Preferential Trade Agreements (PTAs). It now has preferential trading arrangements with most of its trading partners either because of PTAs in place (37 at the last count, covering close to 70 countries) or Generalized System Preferences (GSP) with many developing countries. However, given the high trade volumes of countries like the US and China with whom the EU does not have a PTA (it also stopped granting GSP to China), a large chunk of EU trade still happens under WTO (MFN) rules. Given the diversity in WTO membership and the consensus rule to conclude new agreements at the WTO, it is unsurprising that PTAs have thrived since the late 1990s. However, since 2015, the increase in new PTAs concluded has peaked. With the election of Trump in 2016 and his immediate withdrawal from the TPP, it is unlikely that the US is going to conclude new PTAs anytime soon. The EU has just reached a political agreement with Mercosur countries on a PTA, but the big question is whether EU member states will ratify it. Also, in Europe the appetite for traditional PTAs is dwindling. If anything, the trade agreements in vogue today are not so much about trade liberalization but about how to deal with trade spillovers, be they environmental or labor-related. They are not across-the-board PTAs but sector-specific or even product-specific.

Toyoda: Thank you. Dr. Tamura, Japan has also concluded more than 20 FTAs and has four under negotiation. What is your assessment of Japan's FTAs? Is it time to clean up the spaghetti bowl situation?

Tamura: Japan's FTA policy began relatively late, compared with other more active and aggressive players in the field. The first Japanese FTAs, or EPAs, were enacted with Singapore and Mexico, early in the 21st century. Japan's FTA policy has been based upon real business activity that had already unfolded mainly in Southeast Asia. We already had the de facto integration situation of our industry with ASEAN counterparts, including Singapore, Taiwan, Indonesia, and others. Our FTA policy has been built upon that real industry movement.

My view of the Japanese FTA with ASEAN and Asian counterparts is not necessarily negatively affected by this slightly complicated situation. Indeed, many people argue that the complexity of FTA webs are like a spaghetti bowl, as you mentioned. However, the positive side of our web of FTAs with ASEAN is much larger than the technical complexity of FTAs with ASEAN counterparts. One of the sources of complexity of many FTAs is the diversified style of rules of origin (ROO). Some FTAs adopt certain types of ROO, and others

adopt different types.

However, our FTAs with ASEAN counterparts have been more or less standardized. Therefore, the downside of the complexity of the multiple styles of ROO has been reasonably addressed. Moreover, while the complexity of ROO has particularly a negative impact on manufactured products, which have to go through multiple manufacturing processes, at least as far as simpler products are concerned, including agriculture, there is much less of a downside to the spaghetti bowl. I think the spaghetti bowl effect has been exaggerated as far as FTAs in Asia are concerned. Rather, we should look at the positive side of FTAs particularly in the context of economic security. As I stated before, we are going through some shift of ideology or philosophy as the underpinning for the global trading order. I feel that we have to go through some supply chain adjustment process, or we may have to address our overdependence of trade or the economy on certain specific players. In order for us to address that, we may have to go for a certain level of friend-shoring. You may feel this pathway is a bit paradoxical, but I am of the view that a certain level of friend-shoring would rather help us regain confidence in the global trade order. FTAs may be considered as a rather effective way to form friend-shoring. Of course, it depends on the degree. However, the FTAs should not be considered as a negative standing block to move on to a more international order. Instead it should be considered an effective way to address ideological confusion currently incurred by the global trade order.

Toyoda: Thank you very much. Ambassador Wolff, the US has also concluded 14 FTAs with 20 countries. I understand that Congress has rejected the idea of entering into the TPP. The US-China conflict appears to be a constant background factor.

Wolff: I have learned a lot from the comments of my colleagues. The US did not have a coherent position with respect to FTAs. If you look at the FTAs of the US, they're random, there's no strategy. The US started with Canada, which made a lot of sense. The two countries are at a similar level of development and share a long common border. Their auto industries were deeply integrated already under the 1965 auto agreement, with an enormous amount of trade going back and forth across the border. Mexico was added in, without a lot of thought, other than it helped to stabilize a neighbor to our south. But each of the following FTAs do not have a particular theme. An FTA with Australia is not the same or motivated by the same issues as an FTA with Central America. The latter was to stabilize the region, so it had a foreign policy objective. Looking at the structure of the WTO, no one assumed back in the 1940s when GATT was drafted that Article 24, which gives permission to have discriminatory arrangements, was going to take as major a role as it ultimately did. That largely grew out of the colonial relationships that the EU, France

and the UK in particular, had with emerging countries. The US insisted that they become free trade agreements rather than preferential arrangements that worked in one direction only, in favor of the former colonial master. The system grew up. Now we're in an era when there's been little multilateral trade liberalization at all during the WTO timeframe, other than the agreement on information technology products. So FTAs became a default. Countries could not make progress going forward on a multilateral basis, so they tried to make progress otherwise. Into this came the US competition with China. The TPP was designed to put the US very much back in the Asia-Pacific region in order to offset China. And then the US lost interest in liberalization, became very sensitive to trade liberalization, and did not join the TPP when Trump came into office in 2017. The first thing he did was to get the US out of the TPP.

So we, in the US, are left without a strategy for the use of free trade agreements. I think they perform a very useful role in the current international trading system. They allow for additional liberalization, but are also laboratories for going further with respect to rules, like the Digital Economy Partnership Agreement (though not strictly an FTA), which allows rule-making to proceed among a subset of those who are interested, and that trend is growing. The US salutes and has been supportive of ASEAN and regional integration in Africa, the African Continental Free Trade Agreement. It does not object to the RCEP and was supportive of Japan and others going ahead with the CPTPP. The US is absent from all of these arrangements and, in a move against trade liberalization, it plans to join none of them. I don't see that changing in the next four years, and we'll see who gets elected in the 2028 election. For most countries and the EU, RTAs and FTAs are a default arrangement as long as the WTO is unable to reach agreements or get past the consensus rule. But there are issues that have to be addressed with a multilateral approach to be effective. Climate change is not a regional problem. The digital economy is not a regional but a global issue. Pandemic preparedness is not a regional but a global question. So there's a role for the WTO to come back in if it can cure its institutional deficiencies. One really hopes that this will occur.

Now, will the WTO rules be able to play any role whatsoever in the US-China competition? Potentially. I think that eventually there will be a new equilibrium reached in the US-China competition. It's possible that the template partially exists within the WTO's rules. Further work can be done to give guardrails to that competition. This will have to be addressed separately, I believe.

As far as the dispute settlement system is concerned, without an overhaul from the ground up, a complete change, I don't see that as playing a role in the US-China competition. There's a failure of transparency and in the rules. Moreover, WTO dispute settlement only works when there's a rule to apply that has clearly been agreed. We don't have sufficient rules on state involvement in the economy,

or governing subsidies. So I don't see WTO dispute settlement at this stage playing a role in normalizing US-China trade relations.

The Multi-Party Interim Appeal Arbitration Arrangement (MPIA)

Toyoda: Thank you very much. That's very interesting. We can go back to this judicial issue later. On question three, on the MPIA, will it be possible to review the dispute settlement mechanism of WTO under the Trump administration? It seems Ambassador Wolff is saying that it won't. But should we then expect the MPIA, the Multi-Party Interim Appeal Arbitration Arrangement, to replace WTO dispute settlement for a while? Prof. Gao, I understand you are not necessarily positive about the MPIA. Why is that? Do you expect that, under the Trump administration, there will be any appointments of members of the appellate body?

Gao: I am not in favor of the MPIA. Apologies to Prof. Pauwelyn who is now serving on the MPIA. We are friends but we differ in our view on this. The MPIA has two problems. The first is a constitutional problem, because it denies the members the right to appeal, which is guaranteed by the DSU of the WTO. The second is more practical, because I expect that there could be practical difficulties if some MPIA members decide not to honor the agreement, not to appeal into the void, notwithstanding the existence of the MPIA agreement. That could be really messy. I agree with Ambassador Wolff that under the Trump administration it seems highly unlikely that we are going to get the appellate body back, at least for the next four years. My preferred solution would have been for the WTO members to have a vote on the appellate body appointment process, so that they can appoint WTO appellate body members through majority voting, because that is already provided for in the Marrakesh Agreement establishing the WTO, which does not have any special rules for the appointment of the appellate body, unlike some other issues such as amendment or interpretation, which might require unanimity or a two-thirds or three-fourths majority. So I think voting would be the best solution, because with voting, we also deter other WTO members from trying in the future to abuse their power to block a consensus or block decisions on important issues. Having voting might anger Trump and make it more difficult for the members to work together with the US. I think this all depends on how Trump deals with the WTO this time around. If he's willing to work with WTO members, then let's hold off on voting and try to work with the US. But if he's not at all interested in the WTO, I do not see the value of trying to engage the US in the WTO. Maybe it's time to invoke the voting clause in the Marrakesh Agreement, because Trump doesn't like the WTO. Why should we stay out of the voting option just to placate the US, when the US is not interested in the WTO? We'll have

to wait and see.

Toyoda: Thank you very much. It's an interesting idea. Do you think majority voting can be accepted by other members, including the US?

Gao: It's not just the US. European nations and most developed countries also have reservations regarding voting because there are only about 30 developed countries in the WTO, a minority; they are afraid that if you start this precedent of voting, you might open the floodgates. But if you balance the risk of opening the floodgates and the risk of not having a functional dispute settlement system, the value of a functional dispute settlement system greatly outweighs the risk of voting. Also, I don't think voting would be abused in the future because even if some members try to get a vote, without the support of major members, it would not be able to get through in the WTO. On this appellate body issue, it is every WTO member against one single member, the US, the only one blocking it. If the US teamed up with China or the EU blocking, that would be different. It's just the US sabotaging the WTO, because it's unhappy with certain decisions. That's why I think we should try voting, to warn the US that if you try this again in the future, it's not going to work. You cannot hold the WTO hostage forever.

Toyoda: Thank you very much. Dr. Tamura, I understand you are in favor of the MPIA, which Japan joined last year. How do you evaluate the role of the MPIA?

Tamura: Japan is a member of the MPIA. I'm not saying that the MPIA is going to provide a solution to the successful revival of the appellate body or the conclusion of the discussion on dispute settlement reform. I don't have any clear answer. The MPIA could be considered an effective pathway to resolve concrete disputes among certain WTO members. The MPIA will be utilized only amongst the WTO members which participate in this MPIA system. The US is not a member of the MPIA. Therefore, the MPIA will not provide an effective solution to disputes between the US and China. Nevertheless, we also have to recognize that in certain cases involving economic coercion by China, the MPIA has been successfully solving these specific cases. Therefore, the MPIA should be considered an effective means to provide solutions to some disputes. But it does not mean that it will provide us with a decisive pathway to addressing the dispute settlement reform.

Toyoda: Thank you very much. That's very practical. Prof. Pauwelyn?

Pauwelyn: I am a member of the MPIA pool of appeal arbitrators,

but I speak in my personal capacity. I do not see a re-start of the appellate body as we knew it happening, neither in the short nor the long term. We can only expect a fully functioning dispute settlement system (DSM) once key substantive WTO rules have been reformed or added. In addition, the DSM itself needs updating and we must learn lessons from what went wrong. I am thinking specifically about making the system more efficient, faster and more responsive to members' needs, with a better balance between adjudicator independence and WTO members' input and oversight. Until these substantive and DSM reforms materialize, I expect a menu of options and variable geometry as to how WTO members can settle their disputes, from trade concerns before WTO committees, political negotiations, consultations and mediation, to WTO panels, with or without the possibility to block or appeal, and dispute settlement under PTAs. In this more complex setting, the MPIA has a role to play, and for those WTO members wanting dispute settlement at the WTO which cannot be blocked, it will most likely be the only option in the medium term. Another possible function of the MPIA is as a shadow, with the option to appeal (and the inability to appeal into the void) providing an incentive to settle cases, find compromises, or allow WTO panels to be adopted. We have already seen this since the creation of the MPIA: only one actual MPIA appeal proceeding was held. Yet the shadow of the MPIA meant that disputes between MPIA participants saw a much greater settlement rate (including by means of adoption of the panel's report) than other WTO disputes, where the new normal has become appeal into the void, thereby blocking the process. A final role the MPIA can play is as a testing ground for new ideas and possible reforms: an MPIA case needs a prior bilateral agreement at the start of each panel. In such bilateral agreements, disputing parties can include certain reforms or invite/allow the arbitrators to take certain steps to enhance the efficiency of the process and possibly correct certain "mistakes" from the past.

Toyoda: Thank you very much. Ambassador Wolff, as a former deputy director-general of the WTO, what is your evaluation? I understand the US does not support the MPIA. But, under the Trump administration, will it be possible to restructure the dispute resolution mechanism? We understand that the US criticizes the appellate body because it interprets the GATT Article on its own, and does not adhere to time limits. Why did the US oppose the MPIA when the WTO dispute settlement is not functioning?

Wolff: I found the comments of my colleagues on the panel very helpful in addressing this question. There is some history to US rejection of the MPIA. Why did the US find the MPIA was not very helpful? It was not designed to help the US by answering its primary objections. The real objections of the US were originally that it could not use trade remedies, anti-dumping, countervail, that these trade

remedies often didn't make it through the dispute settlement process. The US had not gotten what it bargained for in the Uruguay Round, in the anti-dumping agreement and as it affected countervail as well. So there was an imbalance in the system from the US point of view, due to the inability to employ trade remedies in a manner the US thought it had negotiated for, while trade liberalization had taken place.

Other problems emerged, such as the question of national security. No other WTO member agrees with the US that it was appropriate to use Article 21 as a justification for placing import restrictions on steel and aluminum. Meanwhile, it is bizarre that Russia could be justified in using a national security exception when it attacked a neighbor. So Article 21 is problematic as it's currently drafted. Part of the solution is that a country cannot use Article 21, the national essential security exception, as an excuse to apply protectionist measures. However, when a country does invoke Article 21 with good reason, it cannot be cost-free. This has to be solved.

Part of the problem is that the rules as they exist at present are insufficient to deal with issues that the US finds itself in litigation on before the WTO panels with respect to China, such as finding a subsidy in the Chinese system. The rather technical problem of the Appellate Body – the definition of what is a “public body” – was an issue of deep concern to the US.

Then the US itself began using subsidies for industrial policy purposes. The rules on subsidies are inadequate. Returning to binding dispute settlement for the US is not just a Trump issue, it's just not going to happen, absent far-reaching reforms. The MPIA, which I thought was deeply deficient, is not bad as a patch to the existing system if we want to keep it, with some reforms. I think some argue in the first case that came through that the MPIA could be an effective means of coming to agreed resolution to settle disputes. Prof. Gao's idea of having a vote, however, might just force the US out of the WTO entirely. The US is not going to agree to be bound by the MPIA. It will resist losing its ability to address fraudulent claims that it is appealing when there is no appeal available, or to be bound by an appellate body process by vote, in which it would naturally vote against the MPIA. We have to find a pragmatic way forward. The MPIA was one. Those who want to join it, do, and it seems to be working. Pragmatism is very important to the world trading system. The members of the WTO have found a partial way towards a solution. I hope they can go further.

Could an Expanded CPTPP Replace the WTO?

Toyoda: Thank you very much. A very pragmatic view. Now, question number four. Of the RTAs, the CPTPP is said to be the highest level. Some believe that the CPTPP should be expanded with

more participating countries, with the EU, and eventually with the US. What do you all think? Dr. Tamura, I understand that this is exactly what you are suggesting. What are your thoughts on China's application to join the CPTPP? If China can meet the requirements and join the CPTPP, then many others will join, which is equivalent to transplanting the CPTPP into the WTO by consensus. What is your view on this CPTPP as a basis to promote more integration, first with the EU, then the US, and finally China?

Tamura: As far as the CPTPP is concerned, I see it as the crown jewel for Japanese trade policy. As you correctly pointed out, the CPTPP is one of the highest-level FTAs in global trade policy. So we have to be quite prudent and smart in how to utilize the FTA in order for us to carry out global trade policy. In that respect, qualified potential members can apply to join the CPTPP. Applications are welcome.

You refer to the EU, an economic unit with the highest-level and reform-minded regime. So we can consider how to make a connection between the CPTPP and the EU. As Ambassador Wolff correctly pointed out, one benefit of an FTA is its use as an experimental field for new ideas on rules. One possible experiment in collaboration between the EU and the CPTPP could be to find a new subsidy rule. No doubt the EU has its own ideas on how to set up rules on subsidy, and particularly the rules to distinguish between good subsidies or bad subsidies. The CPTPP may want to discuss those rules with the EU. This discussion could be built upon the Japan-EU-US trilateral proposal on industrial subsidies, which was submitted to the WTO in 2020. So there are many ways of utilizing the CPTPP to move on to the eventual goal of prosperous global trade and order. Regarding the application by China to the CPTPP, there must have been lots of discussion amongst members on whether China is qualified and whether China has the will and capability to continue to satisfy the conditions. Maybe I'm a little biased because I'm physically in Europe, but I currently feel that there is a consensus that we must reduce dependence on China and diversify the supply chain for the sake of economic security. So I personally don't see any rationale for having the addition of an FTA with China on top of the RCEP. However, there must have been some discussion amongst members of the CPTPP about that.

Toyoda: Thank you very much. Ambassador Wolff, you worked for the WTO as a deputy director-general. May I ask you whether there is any possibility that the US will join the CPTPP under the Trump administration, or even after that? Why has the US, which was originally enthusiastic about the TPP, changed so much? You have already explained this to some extent, but could you please elaborate on the reasons why the US did not join the CPTPP?

Wolff: The US has shown no interest whatsoever in joining the CPTPP during either of the last two administrations, either the Trump administration, once it came out of the TPP, or the Biden administration, which had an opportunity, if it wished, to rejoin the CPTPP. There's a reaction against trade liberalization, against free trade agreements, by both political parties in the US. Now, I hope that view will change after January 2029; it is not impossible that it will. Presidential leadership just has not been provided in the US to emphasize the value of trade. It's a little like the EU and the UK on the benefits of the EU, that led to the Brexit vote. They did not sell the British people the importance of openness to trade, to the economy of the UK, and that risked losing other members as well. There are strong headwinds of populism or retrenchment. I understand it's a very challenging environment. That does not mean that change cannot take place. The Congress was very protectionist in 1930. Just four years later, in 1934, Franklin Roosevelt came along and said, let's have reciprocal trade agreements to open up markets home and abroad, and was successful in putting the US on this path. In 1970, there was major quota legislation, worse than tariffs, that was favorably considered by the congressional committees. And again, just four years later, in 1974, beginning with the leadership in 1973 of Richard Nixon, again, major authority was given to the executive to enter into trade liberalizing agreements. So presidential leadership makes an enormous difference. The US is going to experiment with high tariffs, obviously. That's quite apparent from Trump's statements. And there'll be a reaction. The American people will decide whether it was a good thing to have high tariffs on all products from all countries and much higher tariffs on products from China, and we'll see whether that experiment will change their view. The future is not told yet, but we can see possibilities from past history where protectionism gives way eventually to international cooperation and further interchange with trade. I look forward to that taking place.

Toyoda: Thank you very much. That is very optimistic thinking. I'd welcome that. Prof. Gao, Singapore is keen on FTAs. From Singapore's or Asia's perspective, what do you think of this idea? Can the CPTPP be expanded and somehow include the EU agreement and then invite the US to join?

Gao: As I said, Singapore was one of the initial founders of the TPP agreement. The original idea was to have this high-standard agreement, including all the key issues the US is interested in, like digital trade, competition, SOE rules, etc., and then attract the US to come in. Actually when the TPP was negotiated 20 years ago, the US did become interested and did indicate that it would like to join. But because of domestic political reasons, mainly problems with financial services and liberalization, the US didn't join then, and it

was only after Obama became president that it was announced in 2010 that the US would join the TPP agreement. So Singapore, and most of the countries in Asia, actually welcome the US to come back to the TPP. Because, to them, the US is like a friend, right? But China, which is in the neighborhood, is like a relative. You can choose your friends, but you cannot choose your relatives. You have to live with your relatives forever. So that is the reality here. That's why, even though Singapore always welcomed the US to come back to the region, it also stated on numerous occasions that Singapore doesn't want to choose between the US and China. It would welcome both because it realizes that, even though it would like to be friends with the US, China is not going away. China is going to be the relative in this region forever and it has to live with China.

That is why Singapore has always promoted this idea of open regionalism as championed by APEC and signed not only the TPP, but also the RCEP. When China applied to join the CPTPP a few years ago, many commentators were skeptical, but in an [op-ed](#) I wrote for the *Nikkei* at that time I argued that actually China's TPP application is more serious than most people think, because right after the TPP negotiations concluded about 10 years ago, China started translating all the chapters of the TPP and MOFCOM studied all these provisions carefully to see what reforms were needed for China to comply with the obligations under the TPP, and where the gaps were. It was only after this careful evaluation that MOFCOM decided that China should apply to the TPP. So I think China is ready, because if you look at some of the problematic chapters where people might say that China will never be able to meet the high standards of the TPP, I have a different view.

For example, regarding SOE, I discussed this in my [book](#) *Between Market Economy and State Capitalism*, where I look at the provisions in the TPP SOE chapter and China's accession protocol commitments on SOEs. I argue in the book that actually the obligations on SOEs in the TPP are not significantly higher than the ones already contained in China's accession protocol. So they are possible for China to meet. Similarly, on digital trade, many people were saying that China would never be able to accept provisions on the free flow of data and prohibition on data localization requirements but actually for China the main concern is cyber-security. As long as concerns with cyber-security can be addressed, China would be ready to accept these two provisions, and that was later confirmed by China's accession. China's has joined the RCEP, which does include provisions on free flow of data and data localization requirements, but also includes this security exception, presumably at China's request. So I don't think the TPP standards are that high for China to meet. I think the main reason why it has taken so long is because everyone was waiting for the US to come back to the TPP. Everybody was hoping that, even though in a first Biden administration, it was not possible for the US to join the TPP

for political reasons, in a second Biden term the US would be able to join. But now that Trump is coming back, that is not going to happen. So everybody realized they had to look at the Chinese accession more seriously. Maybe in the next four years they will realize that, rather than waiting for the US indefinitely, they should welcome China back to the TPP. That's why I remain optimistic on China's application to join the TPP over the next four years.

Toyoda: Thank you very much for your very interesting view. What is your opinion, Prof. Pauwelyn?

Pauwelyn: The CPTPP is not really on the radar screen of the EU. That said, and to the surprise of many, the UK did join the CPTPP. PTAs are politically impossible in the US, it seems. In the EU they are increasingly difficult. Even the EU-Canada Comprehensive Economic and Trade Agreement (CETA), has still not been ratified and it is hard to think of a country closer to the EU than Canada. In this context, the political conclusion of the EU-Mercosur FTA is a daring move by EU Commission President Ursula Von der Leyen. It remains unclear whether EU members like France, Italy, Poland, and The Netherlands will ever ratify this deal. My sense is that the future is not PTAs, let alone mega-deals like the CPTPP, but rather mini-deals, on specific topics, in specific sectors, even for specific products, and often bilaterally concluded or between a variable group of like-minded countries, depending on scope and topic. A good example in this respect is the Agreement on Climate Change, Trade and Sustainability (ACCTS) recently concluded by Costa Rica, Iceland, New Zealand, and Switzerland.

Will Economic Security Dominate International Trade Rules?

Toyoda: Thank you very much for your thought-provoking view. Finally, question number five. This is about derisking with China. Developed countries currently believe that derisking with China is essential and the Trump administration seems to be willing to decouple. What are your thoughts on the idea that there will no longer be free trade from the standpoint of economic security in the true sense of the word under the US-China conflict? First, Ambassador Wolff.

Wolff: Both sides, China and the US, are moving towards what has been euphemistically called derisking but in reality moving further in the direction of decoupling. It may be impossible at the extreme but is being attempted, and it has economic costs. It is proceeding, but it will face increasing difficulties. There's a current likelihood that China will face a separate higher tariff schedule in the US. That has nothing to do with the WTO rules – it's completely contrary to them – but

we're already in that zone of lack of application of the trade rules between the US and China, at least with respect to tariffs. A new equilibrium has to be reached ultimately in US-China economic relations. How quickly that will occur is hard to say, but it could come relatively quickly. Trade historians remember that the US and Japan had great difficulties in the 1980s. Japan evolved, it changed. US policies did as well, in reaction. Here with China there's a national security issue, a geostrategic aspect that did not exist with Japan. So, even if there's a new equilibrium, there's likely to be an uneasy relationship for some time to come. An unknown is the degree to which China will move away from state direction of its economy that other countries worry a lot about and also move towards greater consumption at home, and not export-led growth. A lot of the future relationship will depend a great deal on whether China moves in the direction of more accommodating macroeconomic policies that will determine trade flows. I am not optimistic in the near term for there to be a further degree of great openness between the US and China, but I do see some possibilities of a less contentious economic relationship at some point.

Toyoda: Thank you very much. Dr. Gao, what is your view about the relationship between economic security and free trade?

Gao: Overall I agree with Ambassador Wolff that there is a possibility that the situation will improve, but it has to get worse before it gets better, since a lot of people are worried about the Trump presidency because they fear it may be disruptive of the world trade order and he's going to have a trade war with China and possibly with other countries. But I think at least with regard to China, over the past 23 years since China's succession to the WTO, people expected China to become more fully integrated and to move up the value chain, from labor-intensive industries to technology-intensive and maybe even capital-intensive industries. So then people would have more income and more money to spend, and China would become a rich country just like Japan and the other Asian Tigers. Then China would change its economic model.

But that has not happened because the political system in China is such that the people do not have a say in the process, in the redistribution of wealth. So that is why you see, even after 40-plus years of economic development, the shift has not really happened. You still have an economic model that largely depends on investment rather than consumption as a main driver of growth. That explains why, despite all these years of economic development, you still have such a large deficit between the US and China, though the expectation was that, as Chinese people get richer, they will be able to buy more goods from the US and then the trade balance would improve. But that didn't happen. So if Trump does put in place the 60% tariff or even 100% against China, as he threatened, hopefully

this would force China to negotiate with the US and the negotiation would result in agreement on deeper structural issues that should have been tackled in the phase two agreement of the US and China, which never happened. So, hopefully, the phase two negotiation would happen and this would address the deeper structural issues in China. Then China would have to change its economic model so that the fruits of economic development would be shared more with the people, rather than going back to the state or going back to the firm as reinvestment. Then, when the people have more money, they would be able to consume more and import more, and that would improve China's trade balance with the rest of the world, including the US. And then we would have a rebalance in the world economy. That is the best-case scenario, which I really hope will play out in the next few years.

Toyoda: Thank you very much. Dr. Tamura, what do you think about the idea that there will no longer be free trade from the standpoint of economic security?

Tamura: Everybody has been discussing the possible protectionism that may be implemented by Trump. It's difficult to get a clear picture of what kind of policy is going to be taken by the new US administration. Nevertheless, at least amongst developed countries, there seems to be consensus that we have to diversify our supply chain, so-called derisking. Therefore, our trade policy is going to move in that direction. If that derisking process is to take place dramatically, it's going to incur tremendous cost as well. So the process of derisking is going to unfold gradually, over the mid to long term. It depends on the nature of the product concerned. If a product is considered strategically crucial, the derisking process will advance quickly. But, generally speaking, the derisking process is going to move gradually. So we are moving in the direction based upon the idea of economic security, a process where we pursue a new equilibrium between efficiency and resilience. That new pursuit of the new ideology will be carried out for the time being. Maybe after this process, eventually we will be able to find a new equilibrium where we may have greater confidence in the revival of the global trading order. But until then, our uneasiness about the global trading order will continue.

Toyoda: Thank you very much. Prof. Pauwelyn, what's the European view?

Pauwelyn: Economic security is increasingly prominent also in EU circles. In the recently installed European Commission, the very title of Trade Commissioner has been changed to Trade and Economic Security Commissioner. That says a lot. The EU is taking sanctions and export controls more seriously. It is also expanding and

diversifying access to critical raw materials, and reducing dependency on China. But a genuine decoupling with China is not on the books, a different picture from the US. The EU view seems to be rather one of derisking, but not decoupling. We may restrict trade with China when it comes to a small portion of trade, where economic and other security concerns arise. Yet, other trade flows with China will likely continue even though they are under stricter scrutiny under EU trade defense instruments. Given the cost for business of high energy prices in Europe as well as a series of EU green deal measures, the competitiveness of EU industry is going to be one of the key concerns of the new European Commission. In the coming years, the future of the EU steel industry, for example, as well as many other energy-intensive industries such as ceramics, paper or plastics, is at stake. Voices are raised that these industries are strategic and must be saved so we keep a minimum production in Europe for purposes of economic security. Also, climate change is increasingly linked to security concerns. What the permissible outer-limits of trade restrictions in the name of economic security are or will become, remains uncertain. WTO panels have interpreted the GATT Article 21 exception for essential security measures rather narrowly. But the US has appealed these panels into the void. It remains unclear whether WTO rules offer a genuine check on such measures. Checks-and-balances may also come from scrutiny under domestic rules and procedures as well as the fear of emulation: if one country defines security excessively broadly, the risk is that others will follow suit, and this can backfire.

Toyoda: Thank you for your views. We have had a wonderful discussion among four people with different regional perspectives. Thank you all very much for this insightful and stimulating discussion.

JS

Written with the cooperation of Jillian Yorke who is a translator, writer and editor who lived in Japan for many years and is now based in New Zealand, where she is the curator of the Japan Library: Pukapuka.

Policy Recommendation: Strategies for Japan's Service Industry – Making the Service Industry a Source of Prosperous Growth (November 2024)

By the Study Group on the Service Industry in Japan

Overall Outlook for the Service Industry

(1) Current condition

a) Value-added/employer share

Both the value-added and worker shares of the service industry in Japan have steadily increased over the past 50 years (from 52% to 73% for the value-added share and from 45% to 74% for the worker share), and it is indisputable that revitalization of the service industry is the key to Japan's economic recovery (*Chart 1 & 2*).

b) Labor productivity

As a measure of industrial vitality, we take labor productivity (value-added per hour). Comparing labor productivity by various industries in major countries between 1997 and 2017, we find that while Japan's ranking is the same in manufacturing, especially in transportation machinery, the service industry has fallen in ranking across the board, except for professional and business support (lawyers, accountants, R&D, etc.) In 2017, in the service industry as a whole, Japan's ranking was about 50% of that of the United States. On the other hand, the low labor productivity of Japan's service industries stands out in comparison to the labor productivity of its manufacturing industry, which is about 70% of that of the US. This may be due in part to the

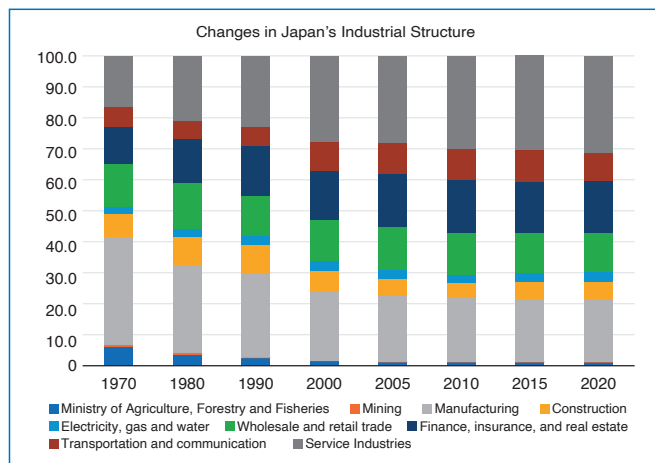
fact that the quality of services is not accurately measured. In Japan, it is said that the quality of services provided to customers in restaurants and hotels is more attentive and better than in other countries. Of course, there is an urgent need to improve efficiency through the use of artificial intelligence (AI) and other technologies. With labor shortages and an aging population, it is essential for Japan to develop technologies that will enable even the elderly to continue working in the service industry, and it is necessary to aim to improve labor productivity in the service industry. In addition, we believe that visualizing the efficiency of service provision (e.g., sales per employee and satisfaction with services by users) to show the direction of efficiency that the service industry is aiming for will also clarify the path that the service industry will take in the future.

c) Service balance

On the other hand, looking at the balance of services, another important indicator for measuring industrial vitality, the travel balance remains in the black on the back of strong inbound travel, but the deficit is widening in advanced fields such as digital and R&D-related fields (*Chart 3*). Much of the statistical analysis data and analytical tool programs used by research institutes are purchased from abroad, and many development costs are also flowing overseas.

CHART 1

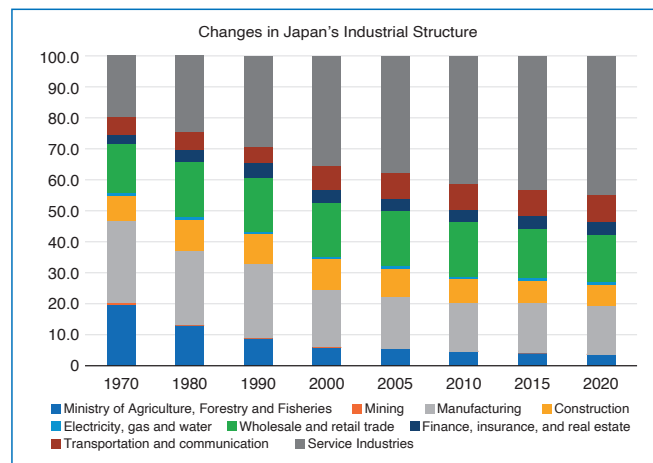
Value-added share



Source: Excerpts from the Cabinet Office's "National Accounts" 1990-2002 standard (1968 SNA) for the years 1970-1990, and 2015 (Heisei 27) standard (2008 SNA) for the years 2000 and later

CHART 2

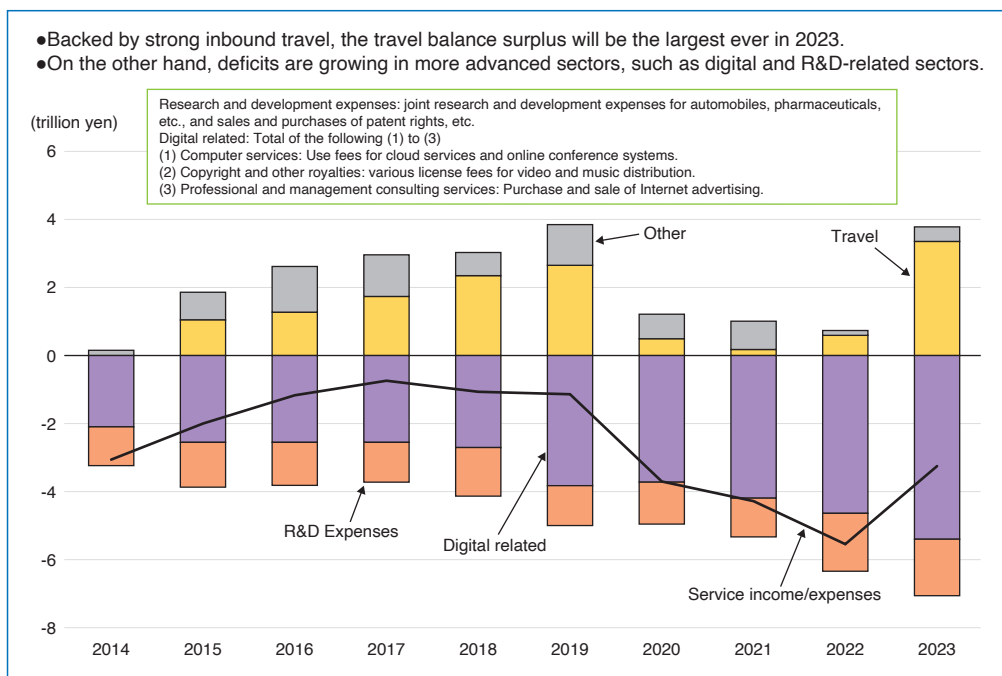
Share of workers



Source: Excerpts from the Cabinet Office's "National Accounts" 1990-2002 standard (1968 SNA) for the years 1970-1990, and 2015 (Heisei 27) standard (2008 SNA) for the years 2000 and later

CHART 3

Service balance



Remarks: P represents the preliminary figures.

Source: Bank of Japan, Balance of Payments Statistics (Time series statistics search site)

Source: Ministry of Finance, First Roundtable Meeting on Balance of Payments Appendix 1, p. 7

(2) Issues

While it is of utmost importance to sort out the issues in each service sector and consider countermeasures, we will first address issues common to the service industry as a whole and their countermeasures.

a) Low prices not reflecting quality

The quality of services provided by the Japanese service industry is highly regarded internationally, as exemplified by the hospitality provided by restaurants and inns. For example, a survey shows that, on average, Japanese service is rated 20% higher than the quality of services in the US (Chart 4). The problem in Japan is that such high quality is not fully reflected in the prices. In other countries, there is a custom of tipping, where prices reflect the quality of the service, such as an increase in the tip for higher quality service. In contrast, in Japan, the quality of services at all times has traditionally been *Omotenashi* service, which is not reflected in the price, in an effort to provide services that better satisfy customers.

b) Low labor productivity

While it is important to fully reflect the high quality in the prices, even taking into account this difference in quality, the gap in labor productivity between Japan and the US shown earlier is still remarkable (i.e., the difference of 50% is only reduced to 30%). The manufacturing industry is in an environment where efficiency can be pursued by improving waste in the production process if it is found. In contrast, the service industry provides invisible goods, and it is

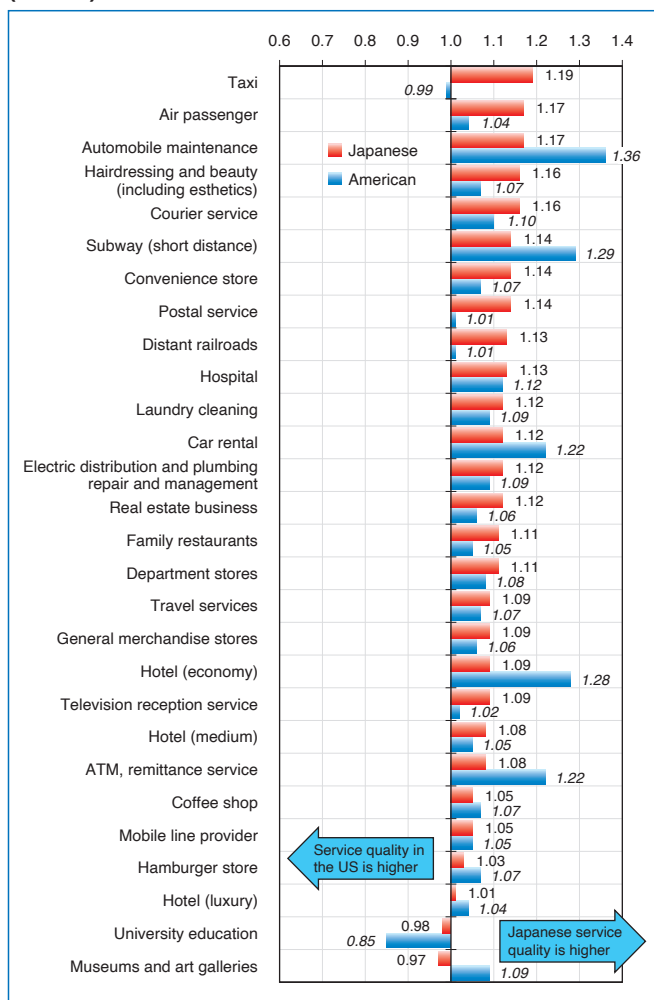
difficult to see waste as in the manufacturing industry. Many service providers are small, medium, and micro businesses, making it difficult to utilize AI and improve efficiency. For small, medium, and micro enterprises, it would be one idea for the government to provide AI and digital technologies that can be used commonly everywhere as public goods, and to encourage them to improve labor productivity in the service industry.

c) Sluggish domestic investment opportunities

The aging of the population and other factors have made the domestic market less attractive, and more direct investment abroad than domestic investment has resulted in the offshore transfer of production. As a result, demand in the domestic economy has declined (deflation) and wages have not risen, even if labor productivity were to rise. Efforts should be made to increase domestic investment opportunities amid an aging population. As the number of foreign tourists increases, the need for services for short-term visitors is expanding. It is important to identify investment needs to meet new service demands and provide them as new investment opportunities. The needs of the elderly in their daily lives are also very different from those of working people. Investments to meet the needs of services for the aging population are also expanding, and it is essential to identify investment needs from a different perspective and promote new investments that can meet those needs. For example, in depopulated areas, there have been attempts to provide a variety of services, such as medical services, financial services, and food provision services, on a single traveling bus. For aging or depopulated areas, it may be

CHART 4

Japan-US service quality difference (US = 1)



Source: Fukao et al. (2018)

necessary to establish a system that can provide such services at as low a cost as possible. In addition, it is important to make efforts to attract foreign investment into Japan for services such as software and accommodation facilities. In the area of medical services, it will be necessary to find new investment needs and increase domestic investment in such areas as the development of facilities that can meet the demand from overseas for advanced medical services.

d) Improvement of service balance deficit

(3) Measures

The following measures could be taken to overcome the challenges in the service industry.

A. “Aggressive” measures to improve productivity

a) Innovation promotion

Flattening the organization to link the promotion of AI utilization and

information and communication technology (ICT) investment to productivity improvement; fostering startups, especially AI companies; and promoting the development of new businesses.

(Note) In Japan, ICT utilization, etc. is often conducted on the premise of existing organizations, and is unlikely to lead to significant improvements in efficiency and the development of new services.

b) Digitization promotion

Promote AI utilization, ICT investment, and cloud computing

c) Improve human resource development and human capital investment

Investment in corporate education and training (whether formal or informal), and the provision of free online education for everyone by public vocational training facilities. Establish scholarship programs to support individual study abroad.

(Note) In many cases, the dispatch of young employees from companies to study abroad, which used to be common, has been discontinued because it is not beneficial to the company as it leads to their quitting the company after returning from studying abroad in disappointment that their study experience is not well matched with their company's working environment. As a company, it is essential to create an “attractive business environment” to prevent them from quitting.

B. Business environment improvement measures that should be taken by the government to increase productivity

a) Regulatory reform

Revisit labor regulations that impose high costs related to business compliance, such as regulations on dismissal of employees, environmental regulations and policies for protecting SMEs by differentiating them from large enterprises in order to prevent SMEs from merging with large companies or the other SMEs and becoming large companies.

b) Exit facilitation

Prevent prolonged benefits and subsidy support for low-productivity firms. Clearly define the purpose of subsidies, etc., and limit public support to the helping stage only. A system that allows firms to become self-supporting after that phase is completed and improvements in production efficiency are achieved is desirable.

c) Maintaining population agglomeration

Creation of compact cities, mergers of municipalities and prefectures in underpopulated areas, as well as continued remote work to promote residents' relocation from large cities to surrounding areas.

d) Ensure employment mobility

Revision of the lifetime employment and seniority system. Expand mid-career employment opportunities. Full-scale introduction of specified employment and abolition of the distinction between permanent and non-permanent employees (ensuring “equal pay for

equal work”).

(Note) It is important that the government be involved in the implementation of such measures as providing compensation for absence from work and opportunities for human resource development when employees leave the company, rather than simply abolishing restrictions on dismissal.

e) Development of digital infrastructure

The Ministry of Economy, Trade and Industry (METI) will develop “Digital Skill Standards”, which are guidelines for acquiring basic knowledge, skills and mindsets related to Digital Transformation (DX), and create a certification system that can certify the ability to follow these standards. Development of digital functions that can be used by the elderly should be done as well.

Outlook for Each Service Area

IT-related services

(1) Current condition

a) In the 1950s and 1960s, mainframes, a system in which hardware and software are integrated, were dominant, and Japan had a large global market share of 1/3 to 1/2 of the mainframe market. However, in 1969, IBM was sued for violation of the Antimonopoly Law due to its blanket rental system that provided hardware and software at unclear prices, which forced the company to provide hardware and software separately, creating a single software industry. The legal recognition of software copyrights in the 1980s created a very favorable situation for the software industry, and software companies in the US enjoyed high growth. The era of software that is not tied to any hardware, but is provided by various vendors and connected by networks, has arrived, and businesses that respond quickly to the needs of their customers have become mainstream. In the case of Japan, however, user companies have been forced to adapt their systems to their business operations without changing their own business processes. In other words, they did not invest in digital technology themselves, but chose to entrust system design to vendor companies, and those vendor companies chose a low-risk, long-term, stable business. As a result, innovative so-called platform companies were not nurtured. It would have been important to nurture startups that actively take risks.

b) Lagging behind the latest software development

Currently, however, the efficiency and reliability of such traditional software development is declining. In recent years, software development has become “as a service” and is provided over the network. As a result, users only need to create programs that can be added to the software, which speeds up the entire development process. Despite the labor productivity gains that can be realized by using such cloud services, 30% of Japanese companies still do not use them. Vendor companies develop new technologies and stabilize their offerings through a trial-and-error “ecosystem”, but there is a big gap between the per-employee revenue of listed SaaS (Software as a Service) companies in the US, which is over 30 million yen, and Japan,

which is 19 million yen. There is a large gap between the US and Japan. Technical assistance that can be used by small, medium, and micro enterprises in Japan is needed, and a system of remote training that can be taken by anyone with a smartphone for free should be established to promote skill improvement education. Such public support for digital skills should expand opportunities for the majority of the population to acquire skills, and encourage increased labor productivity.

(2) Issues

This difference between Japan and the US is caused by the following circumstances.

a) Low talent mobility – low productivity of IT firms

As mentioned above, once a vendor company first invests in a new technology and gains a certain (de facto) position, the rest is stabilized by the ecosystem. Vendor companies in the US invest there at once to scale up their business, standardize, increase productivity, secure first-mover advantage, and achieve stable earnings. In the case of the US, human resources are highly mobile, so it is easy for them to gather at the first investment location at a moment's notice. And once that is over, human resources are likely to go elsewhere. In the case of Japanese firms, the mobility of human resources is low and they are unable to keep up with the speed of the software industry.

In Japan, it is difficult to raise wages because it is not easy to fire employees and it is difficult to lower salaries. To overcome this problem by securing labor through outsourcing and temporary staffing, it is difficult for IT companies to increase their productivity. In order to raise productivity, it is important to raise salaries in line with the skills and abilities of the right people at the right places by promoting the mobility of human resources. To this end, along with the promotion of specified employment, reskilling (relearning) through enhanced training programs in both the private and public sectors is required.

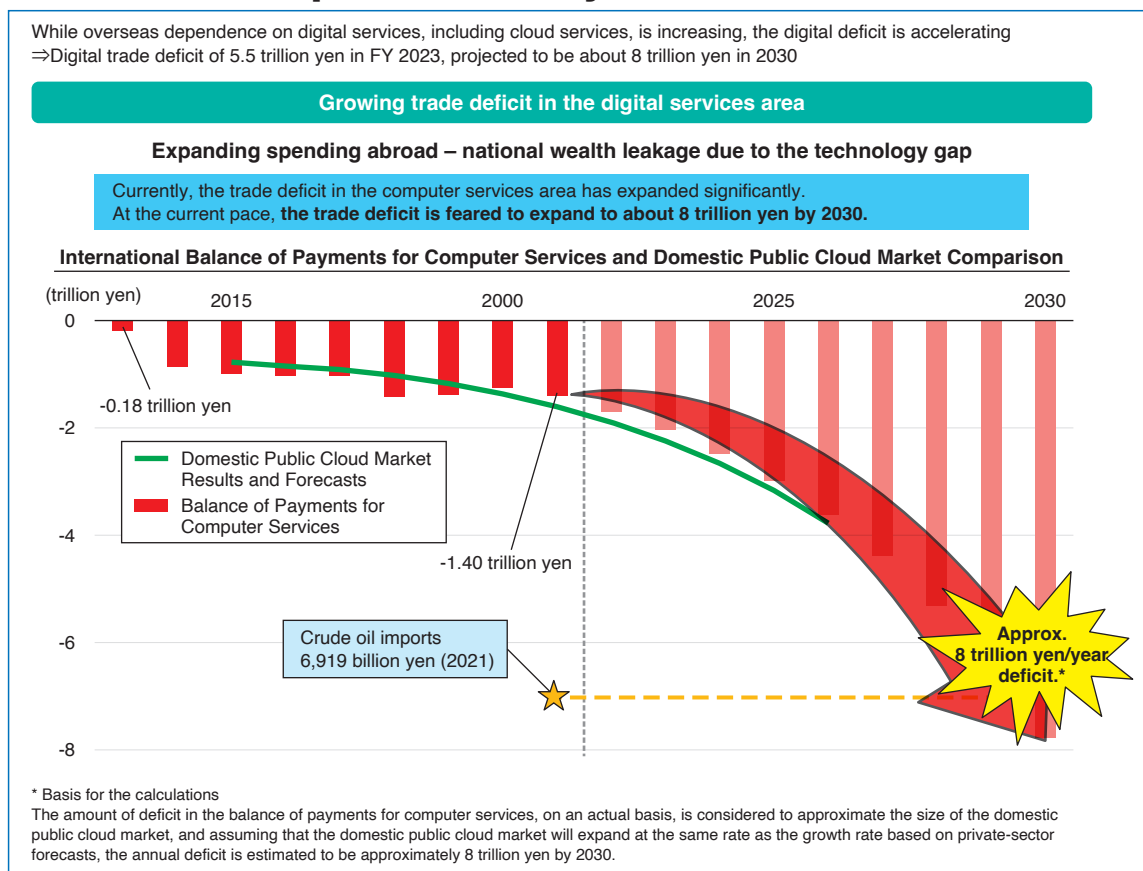
b) Entrenchment of a low-level stable multiple subcontractor structure without organizational reform

Japanese user companies basically use digital technology only to improve the efficiency of their existing operations, so they outsource digital investments to vendor companies instead of making them by themselves. The outsourced vendor firms enjoy low-risk and stable business over the long term. Since users try to adapt systems to their business without changing their own business processes, vendor companies' services are customized to individual companies, and standardized services are not created. As a result, productivity and profit margins are low. This is called a “multiple subcontracting structure of low stability without organizational reform” (legacy system). In addition, in the case of Japan, because systems must be built for the Japanese language, companies are limited in their overseas expansion, and inevitably services are often provided only domestically, resulting in high costs because it is difficult for the benefits of scale to work. Such “Galapagosization” leads to Japan's isolation and is totally inappropriate for the trend of globalization.

CHART 5

Problems with Japan's IT industry structure

While overseas dependence on digital services, including cloud services, is increasing, the digital deficit is accelerating
 ⇒ Digital trade deficit of 5.5 trillion yen in FY 2023, projected to be about 8 trillion yen in 2030



Source: Compiled by METI based on trade statistics (Ministry of Finance), balance of payments statistics (Bank of Japan), and domestic public cloud services market revenue forecast (IDC Japan)

Source: Ministry of Economy, Trade and Industry, "Toward the Realization of a Digital Society". https://www.meti.go.jp/shingikai/sankoshin/shin_kijiku/pdf/019_03_00.pdf

Policy support is needed to encourage overseas expansion by Japanese vendor companies and to increase the number of foreign countries that use Japanese vendors.

c) Widening digital trade deficit

In this context, the widening digital trade deficit is noteworthy. Many cloud service providers in Japan buy and provide software from the US, and the deficit is widening, partly due to the weak yen (Chart 5). Looking at universities and other research institutions, they also purchase software for quantitative analysis and international comparison data from overseas, paying many costs overseas.

(3) Measures

a) Innovation

- Standardization and componentization in competitive areas (areas where common platforms can be built for each industry and issue), and productivity improvement based on in-house production by securing and training human resources in competitive areas must be needed. In non-competitive areas, user companies should promote standardization and componentization using commodity technologies, while in competitive areas, they should promote

organizational reform, in-house production, and self-development.

• Leveraging the Flow of the AI Revolution

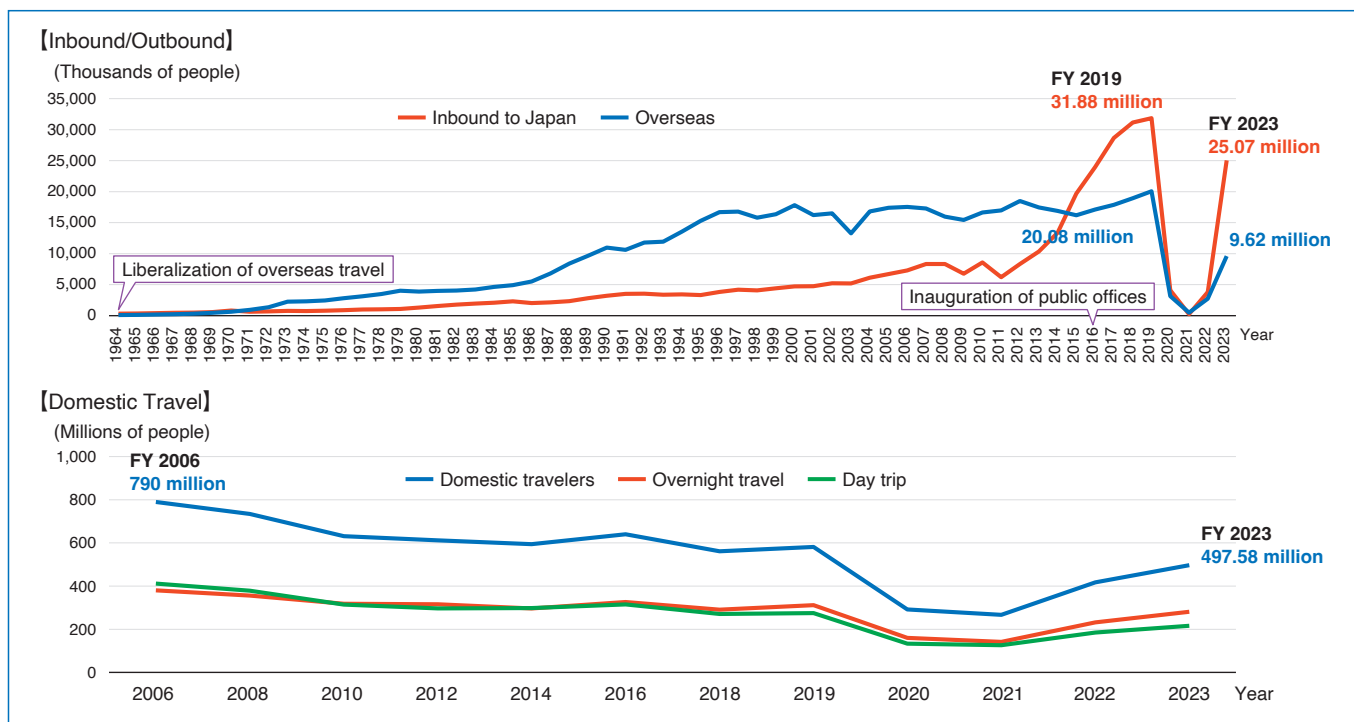
The AI revolution is an opportunity for Japan's software to change, as it functionally creates the ability to transform information from large amounts of data through correlation. However, the adoption of AI is not increasing in Japan and stood at around 50% between 2022 and 2023, while in the US it has increased from 55% to 72%. In addition, the use of generative AI has reached more than 90% in the US, compared to 54% in Japan, and as a mechanism for agile incorporation of AI, a large amount of data collected from IoT (Internet of Things) devices and various sensors is stored in the cloud, where it is learned and reasoned about. Such cloud AI will enable low-cost, short-time processing of large amounts of data, which will greatly help improve productivity.

b) Digitalization

- AI utilization, accompanied by ICT investment, and cloud computing to be promoted.
- Cultivate AI startup companies to replace platform companies such as GAFA (the four major US companies Google, Apple, Meta

CHART 6

Trends in travelers



Source: Japan Tourism Agency, "Travel and Tourism Consumption Trends Survey"

(formerly Facebook), and Amazon).

c) Human capital investment

- In order to prepare for the massive shortage of engineers that will arrive in 2030, it is necessary to establish a system that allows anyone to easily and cost-effectively improve their skills by providing training and free public remote technical assistance programs to improve the skills of engineers.
- In order not to miss out on the AI revolution, it will be important to direct the high-quality engineers with improved capabilities toward higher productivity through human resource mobility, in other words, the influx of human resources from outside the company. This will make it easier for AI to technically enter the organization. In addition, policy support is needed to increase the number of human resources capable of overseas expansion. Without capturing overseas markets, economies of scale will not work, and the high-cost structure will continue.

Further Promotion of Earning Power of the Tourism Service Industry

(1) Current condition

a) Steady recovery of inbound sales after the pandemic

Inbound growth was high until before the pandemic, reaching a record high of 31.88 million in FY 2019. Despite the damage caused by the corona disaster, the number of visitors was back up to around 25 million in FY 2023 (Chart 6). According to forecasts by travel

agency JTB, the number of visitors is expected to reach a record high of 33.1 million in 2024. In addition, the United Nations World Tourism Organization (UNWTO) forecasts that the number of international tourist travelers moving around the world is increasing, with growth particularly noticeable in the Asia-Pacific region (Chart 7).

b) The amount of travel spending by inbound travelers in Japan has increased more than 2.5 times over the past 10 years (Table 1).

(2) Issues

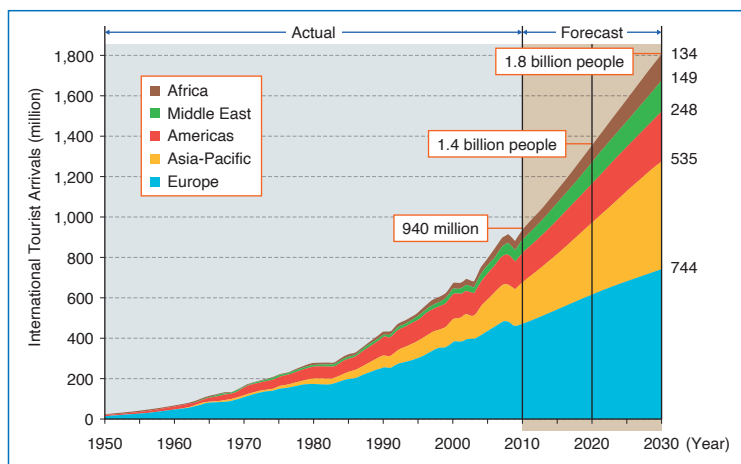
a) High value-added

Inbound consumption is expected to play a major role in compensating for the shrinking domestic market due to the serious aging of Japan's population and declining birthrate. In this sense, along with quantitative targets such as "achieving 60 million inbound tourists per year by 2030", the current challenge is to "add value to tourism" by having each foreign visitor to Japan spend a large amount of money. In Japan, where wealthy people from all over the world are not sufficiently attracted to Japan as tourists, the tourism industry is required to further realize its potential. (Incidentally, per capita spending by foreign tourists in 2014 was approximately 1.08 million yen, while it will remain flat at approximately 1.12 million yen in 2023.)

In addition, the creation of new investment opportunities to uncover new needs of foreign visitors to Japan that have gone unnoticed and to provide services to meet those needs will promote domestic investment. Among foreign visitors to Japan, there are two types of travelers: those who want to spend as little as possible and those who

CHART 7

International tourist forecast



Source: UNWTO, "Tourism Highlights, 2016 Edition"

are willing to pay even higher prices as long as they are satisfied, and it is necessary to establish a system to provide services that meet the needs of each type of traveler.

b) Attracting tourists to rural areas

Attracting tourists to rural areas is another important issue for revitalizing Japan's regional economies. The Ministry of Land, Infrastructure, Transport and Tourism's "Tourism Town Development Promotion Project Utilizing Historical Resources" is one example. Some regions are increasing the number of visitors by creating websites in English and other languages to inform foreign visitors to Japan of the regions' attractions and to explain how to access the regions from major airports. It is essential for the government and the private sector to work together to build on these efforts, as well as to make efforts to increase the number of repeat visitors to Japan.

c) Eliminate low productivity

The key to attracting wealthy foreign visitors is to raise the low productivity of accommodations and other facilities through mechanization/IT by introducing new technologies.

d) Human resource development

A major challenge in attracting wealthy foreign visitors will be to develop human resources who can respond in English, as well as to improve accommodations and other facilities. It is necessary to establish a system whereby remote education and training programs can be provided by public institutions, and people can learn free of charge. In addition, it is also necessary to provide easy-to-use translation software that can be converted into other languages by

smartphone at any time, for example, for terms commonly used in the service industry.

e) Addressing overtourism

Finally, to address the issue of overtourism, the national and local governments should improve their efforts to improve infrastructure (increase the number of buses, cabs, trains, etc.). In addition, dynamic pricing (variable pricing system) could be used to equalize the number of passengers.

(3) Measures

a) Innovation

- Shift from "pinpoint tourism" that only requires a visit to "experiential tourism" that allows people to enjoy the experience itself, such as trekking and fishing. Capture the needs of the younger generation for self-improvement and the needs of the older, affluent generation for classic luxury.

- Renewal of tourism industry leaders

In addition to traditional tourism industry players such as accommodation facilities, restaurants, transportation companies, and souvenir shops, non-tourism industries such as finance, real estate, consulting, and advertising companies will be brought together to form a Destination Management Company (DMC) that will set the direction for "tourism town development".

b) Digitalization

- Designing cities with tourism promotion in mind using data and AI
- Design using data and AI to realize large-scale pedestrian spaces in cities and co-create them with tourists. This will solve the problem of overtourism and at the same time increase sales of restaurants and retail stores in pedestrian spaces, which will affect high value-added tourism. Data analysis will be conducted to determine how pedestrian spaces should be set up to maximize added value, which will be reflected in future urban planning and tourism management. In

TABLE 1

Travel consumption (2014-2023)

(Unit: trillion yen)

	2014	2015	2016	2017	2018	2019	Year 2020	Year 2021	Year 2022	Year 2023
Japanese domestic overnight travel	13.9	15.8	16.0	16.1	15.8	17.2	7.8	7.0	13.7	17.8
Japanese domestic one-day trips	4.5	4.6	4.9	5.0	4.7	4.8	2.2	2.2	3.4	4.1
Japanese domestic overseas travel (domestic portion)	1.1	1.0	1.1	1.2	1.1	1.2	*1 0.3	*1 0.1	*1 0.6	0.9
Foreign travel to Japan	2.0	3.5	3.7	4.4	4.5	4.8	*2 0.7	*2 0.1	*2 0.9	5.3
Total	21.6	24.8	25.8	26.7	26.1	27.9	11.0	9.4	18.7	28.1

*1 "Overseas travel by Japanese nationals (domestic portion)" is estimated due to the impact of the new coronavirus infection.

*2 "Foreign travel to Japan" is estimated due to the impact of the new coronavirus infection.

Source: Travel and Tourism Consumption Trends Survey 2023 Annual Values (Fixed Report)

addition, the introduction of a tourism tax will enable the creation of a system that will allow the implementation of various policies while securing financial resources for local governments.

c) Human capital investment

- Develop advanced human resources by improving communication skills, including English language skills, and training professional guides for tourist attractions. For example, it is possible to increase the number of high-level human resources by creating a free remote education system by public institutions.

d) Addressing specific challenges

- Appropriate reflection of quality services such as “hospitality” in prices
(Note) Moving away from cheap and good service.
- Introduction of dynamic pricing
When demand for services varies significantly by season and time, it is important to equalize demand.
- Responding to overtourism
Establishment by local governments of public infrastructure facilities’ rental fees for tourists, including transportation infrastructure.
- Expand medical tourism through collaboration with the medical industry
Realization of collaboration between Japan’s advanced medical technology and tourism (details to follow in the Medical Inbound chapter).
- Short-term technology acquisition program
Short-term courses for foreigners to learn advanced Japanese technology.
- Educational support programs
Establish training courses in areas where Japan has strengths (crafts, animation, etc.). Create an intensive program, for example, a two-week course, so that participants from overseas can enjoy both

tourism and educational support in Japan.

Entertainment Culture as a Growth Industry

(1) Current condition

a) Expanding online market

Since the early 2000s, the Japanese content industry, including manga, anime, and video games, has served as a gateway for foreign interest in Japan, and the government has focused on it as a growth industry. In the past few years, the market has been on a further expansion trend, with an estimated market size of approximately 14 trillion yen for content in 2023. In particular, the online content market, including online distribution, has grown from about 13% of the total market in 2011 to 46.5% in 2023 (Chart 8).

b) Overseas market expansion

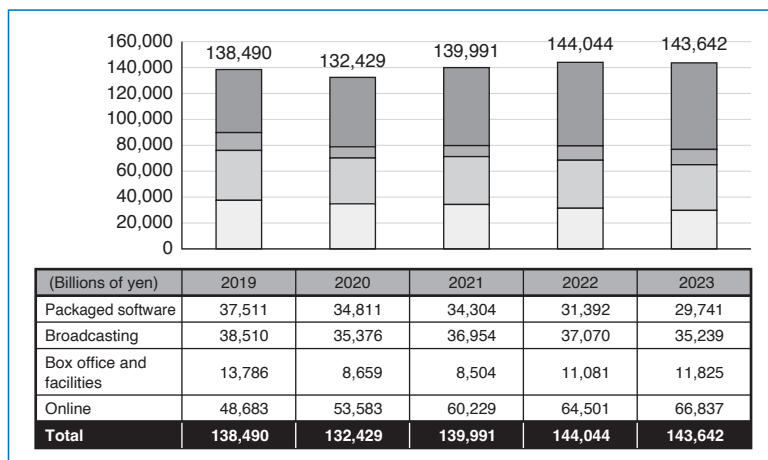
Growing in tandem with the expansion of the digital online market is the overseas market. Over the past 10 years, the Japanese content industry has grown 3.3 times, and the value of exports has reached 4.7 trillion yen. In terms of the scale of exports of domestic industries, it has reached a point where it can be compared to steel and semiconductors. However, Japan’s share of the global content market, including exports, will be around 7% in 2022, which is still small compared to the US (43%) and China (19%). However, there is room for significant growth (Chart 9). Animation and home video games (software) account for 90% of the 4.7 trillion yen export value, of which online accounts for more than half, indicating that digital is driving the overseas market.

c) Growth of related industries

The total market for character products, amusement facilities, tourism, and education using content is estimated to be 57 trillion yen, more than four times the size of the entire Japanese content market (Human Media, Inc. estimate). This is 10% of Japan’s GDP, which is close to the amount invested in construction. In other words, the content industry has a large ripple or external effect on related industries. Efforts should be made to use the content industry as a catalyst to enhance brand power and image, and to grow related industries by promoting Japan’s various regions, cultures, and products abroad, for example by using Japanese consumer electronics in content, including Japanese food products and scenery from Japanese tourist destinations.

CHART 8

Japan content market by media from 2018 to 2023



Source: Human Media, Inc.

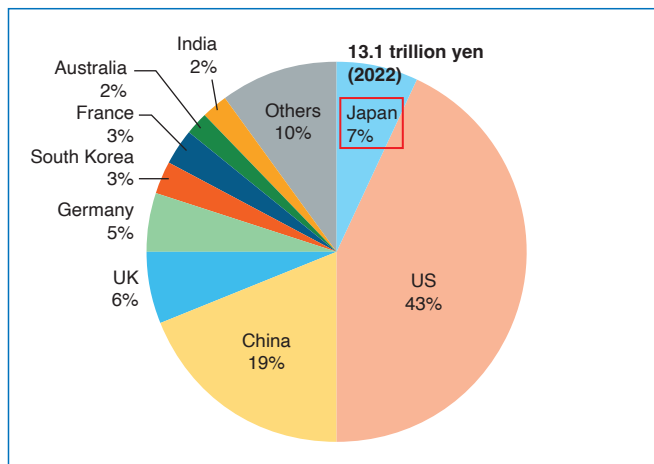
(2) Issues

(a) Overseas expansion

While overseas expansion has been steadily increasing due to support for overseas development through investment from the fund “Cool Japan Organization” (established in 2013), expansion of government subsidies, support through the development of Internet platforms, and other means,

CHART 9

Global content market size, 2022 (estimate)



Source: Human Media, Inc.

and the effect of government announcements, further expansion is an issue. In light of the increasing number of tourists interested in animation, collaboration with the tourism industry will be important. It is also expected that Japanese products will be purchased and used by visitors to Japan and that the quality of Japanese products will spread overseas through the Internet.

b) Digitalization

Online issues such as distribution include anti-piracy measures for manga. At the same time, it is important to promote overseas distribution such as Netflix for animation, cloud computing by Google and others for games, and overseas platforms such as Spotify for sound. It is also necessary to cooperate with international organizations and countries to develop an international system to crack down on illegal use overseas. The same is true for cyber-attacks, and international partnerships need to be built up to ensure that overseas criminals cannot get away with them.

c) Integration with other fields

Another major business strategy is the fusion and matching with other fields. Synergistic effects from cooperation with fashion, food, tourism, and other industries should be fully exploited. For example, inbound tourism can be fused with food, as in “people come to Japan to eat something called ramen that they saw in a comic book.” Other national strategies are also needed, such as including in the content the attractions of various regions of Japan and including in the content scenes of the use of products from various fields in Japan.

d) Human resource development

Japan has a very large number of creative artists, and fans who support them, but there is a lack of human resources for producers who can develop overseas as a business. In addition, “how to sell good products at high prices” is an important marketing strategy, for which human resource development is also essential.

(3) Measures

a) Innovation

- Integration of tourism and animation

Learn from the successful example of Disneyland, for example, and build facilities such as “Ghibli Land” or the “Dragon Ball Theme Park” being planned by Saudi Arabia, both domestically and internationally. Use of “digital policy forums” (online platforms) to examine integration with tourism and other sectors, as well as the fostering and development of the content industry, as in the case of the Korea Content Promotion Agency (KOCCA) in South Korea and the former Department of Digital, Culture, Media and Sport (DCMS) in the UK. The goal is to establish a system that can oversee and promote multiple areas such as the fostering, development, overseas expansion, promotion of digitalization, and collaboration with other industries.

- Promotion of overseas expansion

It is important to develop human resources capable of producing content that can be used overseas. Furthermore, measures to induce SMEs to expand overseas, support for overseas distribution, and overseas development of theme parks also have great potential. The government needs to provide assistance for overseas expansion. First, the government should identify needs from overseas countries, support the overseas expansion of service providers who can meet those needs, and extend support to ensure that business demand will grow steadily and generate stable earnings after overseas expansion.

b) Digitalization

- Anti-piracy measures
- Convergence of telecommunications and broadcasting
- Development of new areas such as e-sports
- Fostering AI literacy

As a result of the Copyright Amendment Act of 2018, which nudged the development of AI by making machine learning of data not a copyright infringement, AI content may be generated automatically in an explosion, making human-created content scarce. As competition in the use of AI intensifies, the literacy required to use it will become more important, and it will be important to establish an educational system for this purpose.

- Develop rules for processing music copyrights.

c) Human capital investment

- Enhance the Information Management Innovation Professional University (iU)

This university produces innovators and artists who make full use of digital technology. The most important feature is that all students will start their own businesses, and the goal is to create many content-based companies.

- It is important to develop producers and marketing strategy specialists who can develop overseas operations, and to assign appropriate human resources.

New Frontier in Medical & Nursing Care Services

[Medical inbound activities (including medical tourism)]

(1) Current condition

A drastic review of medical inbound activities is needed, but it is difficult to achieve in the current situation

One of the pillars of the late Prime Minister Shinzo Abe's growth strategy was to promote the international expansion of health and medical care. The main activities for overseas expansion in this strategy included inbound as well as outbound activities to form partnerships between overseas medical professionals and related companies and the Japanese medical community. For example, international expansion is an issue, such as sending cancer patients who were detected in early stages overseas but for whom surgery is difficult to perform locally to Japan for treatment. Outbound and inbound should be combined to internationalize medical care.

However, the actual situation of medical inbound activities in Japan is extremely challenging: the number of foreign tourists is expected to exceed 30 million annually in 2019, of which an estimated 20,000 to 30,000 will visit Japan for medical purposes, a figure that is one or two digits lower than other Asian countries such as Singapore (Table 2). So there is room for significant growth in this field.

There is a need for Japan to provide advanced medical care, and the public and private sectors must work together to develop nurses, doctors, medical equipment, and medical facilities to meet this need.

(2) Major benefits of medical inbound activities

Medical inbound care is not covered by public medical insurance and private practice. An increase in this number is expected to have the effect of increasing the sustainability of medical services to domestic patients through increased revenues. It will also help improve Japan's image as a health powerhouse.

Inbound patients are exclusively targeted as the wealthy, but there are also high expectations for the middle class in countries with high medical costs, such as the US. High-quality, reasonably priced Japanese healthcare is attractive. Japan should do a better job of communicating that Japanese medical care is attractive to a diverse range of people. Even at present, there is a high need for Japanese medical care, such as particle beam therapy for cancer.

(3) Issues

Breaking away from the concept "private medical care = preferential treatment for the rich"

The reason why medical inbound activities have not progressed is that the universal healthcare system set up in 1961 is now at its limits. While it has undoubtedly contributed to Japan's medical care and healthy life expectancy, reimbursement has been substantially negative in real terms, and hospital management is under pressure. Japan is too much under the spell of "medical care should be covered by public insurance". Japan needs to break free from the mindset that "private medical care = preferential treatment for the rich".

(4) Measures

a) Innovation

• Promotion of medical tourism

The entire country should support the medical tourism industry as a national policy, emphasizing the importance of the medical tourism industry, which combines Japan's advanced medical technology with its rich tourism resources.

• Construction of wellness resorts

In order to expand the medical inbound market, create wellness resorts with high unit prices and added value for foreigners who would stay for a week or so for the primary purpose of preventive medical checkups using the physical checkup system. It is also important to

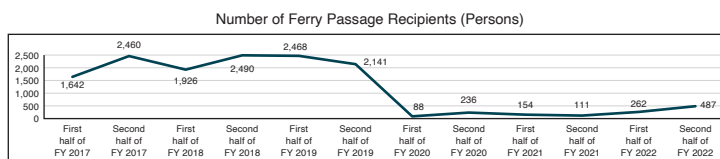
TABLE 2

The dismal state of Japan's inbound medical tourism

Country	Foreign tourists (2019)	Estimated number of visitors (2019)
Japan*	30.19 million	Estimated 20,000-30,000
Singapore**	19.1 million	500,000
South Korea**	17.5 million	500,000
Malaysia**	26.1 million	1.2 million
Taiwan***	12.2 million	300,000

The State of Inbound Medical Tourism in Japan (2019)

- Although the Japan International Hospitals (JIH) certified by MEJ and the Ministry of Health, Labor and Welfare's "Survey on the Actual Number of Foreign Patients" exist, there is no data on how many tourists actually come to Japan for medical treatment at clinics, etc.
- The JIH reported 4,069 people per year (for one day in Bangkok).
- 1,653 people obtained medical stay visas
- China 3,841, Vietnam 322, Russia 81, Indonesia, Mongolia, etc. (very few from Europe, US, Middle East)



Source: Compiled by MEJ, *Ministry of Health, Labour and Welfare, "Survey on the Actual Conditions of Acceptance of Foreign Patients in Medical Institutions in Fiscal Year 2022", statistics.jnto.go.jp/graph/#graph-inbound-travelers-transition, **"Strategy to Facilitate Attraction of International Patients", Ministry of Health and Welfare, South Korea, ***Medical Excellence TAIWAN. www.oecd-ilibrary.org/industry-and-services/oecd-tourism-trends-and-policies-2022_a8dd3019-en, <http://www.stb.gov.sg/content/dam/stb/documents/statistics-marketing-insights/Quarterly-Tourism-Performance-Report/STB%20Q4%202019%20FA%20v7.pdf>, admin.taiwan.net.tw/upload/contentFile/auser/bl/annual_2019_bmlen/01_2_Taiwan-Tourism-Market.html

establish the concept of high unit prices for high quality products.

b) Digitalization

- Medical inbound is private medical care. In order to create incentives for private medical care in the medical field, it is important that hospital management is streamlined. Digitalization of hospital management and administration is a prerequisite for this.
- As a mechanism for early transfer of patients from foreign hospitals, it is necessary to establish a common data format among hospitals and a digital infrastructure as a tool for close and smooth information exchange with foreign hospitals.

c) Human capital investment

- Diversification of medical human resources, including inviting foreign physicians
- Training of personnel capable of triage to determine whether or not a patient from a foreign country should be accepted for treatment
- Establish an emergency response system in case of inappropriate treatment.
- Training of hospital management professionals based on the premise of “private medical care”

d) Addressing specific issues

- Cooperation between the Japanese medical industry and the travel industry is essential for the smooth realization of medical tourism. If it is just a matter of bringing tourists from overseas to Japan, the overseas travel industry can handle the task. However, in order to link diagnosis and treatment with tourism in Japan, the Japanese travel industry, which is well versed in the Japanese medical industry, must play a major role.

[Aging Society and Care Robot Innovation]

(1) Current situation – decrease in the number of active elderly and rapid increase in nursing care costs

A major problem in the aging of Japanese society is that the number of healthy elderly people is decreasing and the number of people certified as requiring support or nursing care is increasing (Chart 10). As a result, the gap between supply and demand for human resources for long-term care is widening and the cost of long-term care is increasing (Chart 11).

(2) Issues

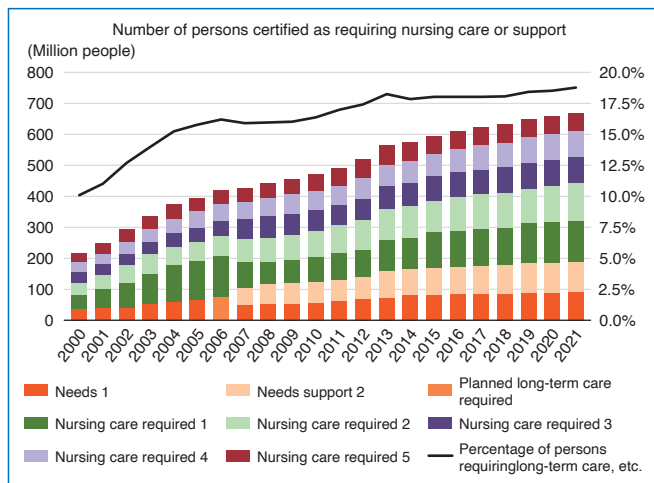
a) Standardization and customization of technology

The key issue for expansionary use of caregiving robots is development cost reduction and customization of technology to the needs of an individual aged person.

The Japan Agency for Medical and Development (AMED)/Ministry of Economy, Trade and Industry (METI) “Project to Promote the Development and Introduction of Robotic Nursing Care Equipment” which has been implemented since 2013, supports the development and diffusion of robotic devices in six key areas (transfer support, mobility support, removal support, monitoring and communication, bathing support, and nursing care work support) for assisting the elderly in their daily lives. Effective social implementation of these technologies, especially promotion of commercialization, is an urgent issue. It is essential to build a comprehensive ecosystem from development to social implementation, in which both standardization to reduce costs and customization to meet the diverse needs of the elderly are required. How to achieve this compatibility will be an important research issue in the future. In addition, it is also important to establish a system for the effective use of newly developed equipment in the nursing care field. It has been pointed out that useful equipment is not being fully utilized due to a lack of technical

CHART 10

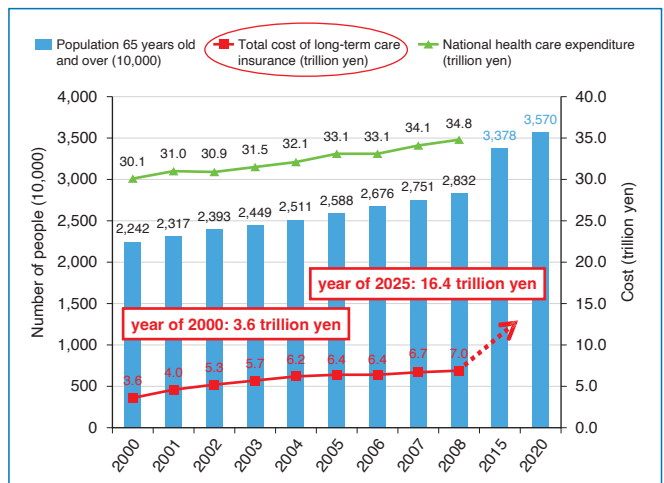
Decrease in the number of healthy elderly people is the biggest challenge.



Source: Ministry of Health, Labour and Welfare, “Monthly Report on Long-Term Care Insurance Business Status (Provisional Version)”, April 2000 to February 2021

CHART 11

Social problems that need to be solved: Rapid increase in care costs



Source: Ministry of Health, Labor and Welfare, Japan

personnel and budget constraints.

b) Creation of new industries

Another major challenge is to capitalize on the potential for the creation of new industries. The nursing care robot technology that Japan has pioneered will be a valuable solution for countries around the world with aging populations. Safe and secure nursing care robots designed with a human-centered philosophy have a large potential market as a new export industry.

In addition, the development and diffusion of independence-assistive robotic devices will create a new industrial sector aimed at preventing nursing care and extending healthy life expectancy. The creation of such a healthy life extension industry will also contribute to reducing medical costs and improve the sustainability of the social security system.

Furthermore, the development of the nursing care robot industry will encourage the establishment of R&D and manufacturing bases for related technologies, contributing to the revitalization of regional economies and the creation of new jobs.

To this end, it is important that technologies developed in Japan, such as care robots, be recognized as “global standards”, and support by the public sector is essential. In smartphone technology, it is said that technology developed in Japan has failed to win global standardization and has fallen behind other countries. If technologies originating in Japan are not recognized as global standards, advanced technologies will miss the opportunity to be used around the world.

(3) Measures

a) Innovation

- Like airplanes and automobiles, care robots should be modularized so that various capabilities can be added by modifying the software.
- Caregiving is a lifestyle innovation for daily life. If the challenges are solved, it could become a next-generation industry following consumer electronics and automobiles. The next challenge for technological development will be to create situations that not only complement physical functions but also lead to the happiness of the person. Japan's aging population offers an excellent opportunity to advance the development of nursing care-related technologies. The technological needs on the medical and nursing care fronts are becoming clearer, and Japan is well-positioned to develop equipment to address these needs.
- By integrating robot technology and AI, it is possible to develop comprehensive nursing care solutions with AI-enabled operational know-how. This is expected to create a new business model of care support (Care as a Service) that goes beyond mere equipment sales.
- Care robot technology is a cross-sector innovation, integrating technologies from diverse fields such as medicine, IoT, AI, and materials science. This is expected to promote cross-sector innovation and have a ripple effect on other industries.
- Deregulation to promote such innovation and international standardization activities to increase international competitiveness are important. Disseminate Japan's nursing care robot technology to the world and establish a presence in the global market through

international cooperation and technology transfer.

- It is necessary to establish a system to accelerate R&D and practical application through the cooperation of universities, research institutes, companies, and government.

b) Digitalization

- Promote digitalization of nursing homes (e.g., online interviews with family members). Ensure that daily health index changes are recorded digitally.

c) Human capital investment

- It is important to develop human resources who can use nursing care robots. Education related to engineering and digital literacy is needed in the nursing care field (the Ministry of Health, Labor and Welfare is creating a living lab).
- There is an urgent need to establish a system for training a diverse range of human resources to support the new industry, including nursing care robot technicians, operators, and maintenance personnel.

d) Addressing specific challenges

- The company will promote both educational activities to increase social acceptance of the daily use of robots and AI, and product development that pursues ease of use.

[Medical device startup]

(1) Current situation – diagnostic equipment, competitive to some extent, but weak treatment equipment and low self-sufficiency

The global market for medical devices is approximately 60 to 70 trillion yen (of which the Japanese market is approximately 4.4 trillion yen; the global medical equipment market is 53% therapeutic, 26% diagnostic, and 21% others). Japan's international competitiveness is relatively strong in diagnostic devices such as ultrasound, endoscopes, magnetic resonance imaging (MRI), and computed tomography (CT), and has a high share of the global market (for example, Japan has almost a 100% share in diagnostic flexible endoscopes), but in therapeutic devices (artificial joints, stents, radiation therapy and pacemakers), its global market share is currently almost zero. Therapeutic devices are more expensive and have higher profit margins, and increasing this share is important for the development of the Japanese industry as a whole. In terms of trade balance, the trade deficit for medical devices is approximately 800 billion yen to 1 trillion yen, while the trade deficit for pharmaceuticals is approximately 3 trillion yen. Japan's overall market for medical devices is approximately 4.4 trillion yen, with imports increasing year by year, and the domestic self-sufficiency rate has recently reached approximately 50%. Among these, about 80% of treatment equipment relies on imports, and the domestic self-sufficiency rate is about 23%, indicating a very low self-sufficiency rate in a field that holds the very foundation of life. The medical industry is a major industry that can contribute to the future growth of the Japanese economy. If patents can be obtained and new medical devices can be developed that can

be used in overseas medical facilities, this is a field that has the potential to become a major export force. If there are problems with regulations, market practices, and insurance reimbursement prices, it is necessary to eliminate these barriers and establish a system that facilitates the development of medical technologies.

(2) Issues

Comparing Japan, which has universal health insurance, and the US, where private insurance is the norm, expensive medical equipment is used in the US, where insurance reimbursement prices are higher. In Japan, reimbursement prices for medical equipment are lower than in the US. In terms of providing equal medical services, Japan is superior with lower out-of-pocket costs for patients, but in the US, where the gap between the rich and the poor is normalized, inequality is progressing. The wealthy in the US are more likely to enjoy quality, cutting-edge medical care. The current trend will be further strengthened by the depreciation of the yen, which will greatly reduce the attractiveness of the Japanese market for US companies and thus increase the likelihood that they will not expand into the Japanese market. Particularly in the field of therapeutic devices, there is a risk that the latest technology and equipment will no longer be available in Japan, and Japanese will not be able to receive the latest medical care.

Another factor that may have contributed to the failure of the therapeutic device industry to grow in Japan is the fact that, in the case of therapeutic devices, the death of a patient would cause significant social damage, whereas such concerns are unnecessary in the case of diagnostic devices. In the case of US companies, there is pressure from shareholders for high profit margins, even if there is risk, and they tend to choose to develop therapeutic systems with high profit margins.

(3) Measures

a) Innovation

- There is room for rethinking Japan's universal public medical insurance system from the perspective of innovation. In order to stimulate innovation, it is necessary to create a role model for doctors and researchers to start their own businesses and succeed, as at Stanford University in the US. In general, such a culture of entrepreneurship will not emerge in a growth model of lifetime employment and seniority.
- Public medical insurance should provide generous coverage for serious illnesses, but it is important to distinguish between public medical insurance and private medical insurance. It is necessary to examine whether Japan's private life insurance system can cover the portion of medical expenses beyond the amount that can be covered by public medical insurance.
- In Japan, where research funding in academia and elsewhere is scarce compared to Europe and the US, measures are needed to raise private funds for research through corporate donations and crowdfunding, and to enable researchers to continue their research through donation-type funding. Kyoto University continues to receive endowment-type funding, as called for by Prof. Shinya Yamanaka, and we believe a similar approach is feasible.

b) Digitalization

- Promotion of hospital digitization is a prerequisite for smooth utilization of state-of-the-art diagnostic and treatment equipment. Medical treatment collaboration and data sharing among different hospitals is important, and for this purpose, system compatibility and standardization of database structure should be promoted.
- It is important to facilitate the operation of the regional medical information coordination network that is being established.

c) Human capital investment

- In order to promote the development of therapeutic devices, it is important to have a smooth supply of first-in-men (investigators) to serve as the first experimental subjects. Currently, the Ministry of Health, Labour and Welfare (MHLW) is investing national funds to study this issue in the core clinical trial hospitals. Efforts should also be made to make transparent the explanation of the content of clinical trials to be reviewed by the Clinical Trial Review Committee for foreign investigators.

d) Dealing with specific issues

- In order to promote the latest medical equipment, it is necessary to reconsider Japan's universal public medical insurance system.

[Drug lag, drug loss and drug price reform]

(1) Current condition

Clinical development of new drugs in Japan has stagnated, and the number of new drugs approved in Europe and the US but not yet approved in Japan has increased, and the percentage of unapproved drugs now accounts for about 70% ([Chart 12](#)).

For example, avapritinib, a treatment for GIST (Gastrointestinal Stromal Tumor, a rare cancer), is one of the most important anticancer drugs, but it is currently not available in Japan. The current situation is not so much a drug-lag situation as a drug-loss situation.

(2) Issues

The main reason for this is that, compared to Europe and the US, drug prices are very low at the time they are listed on the insurance market. Furthermore, the financial capacity of the medical insurance system is limited for expensive drugs with large sales, which puts pressure on insurance finances, and drug prices are lowered at the time of biennial drug price revisions through the use of various exceptional calculation standards, such as market expansion re-calculation, to keep prices within insurance financial capacity. As a result, incentives for the development of innovative drugs are severely hampered.

(3) Measures

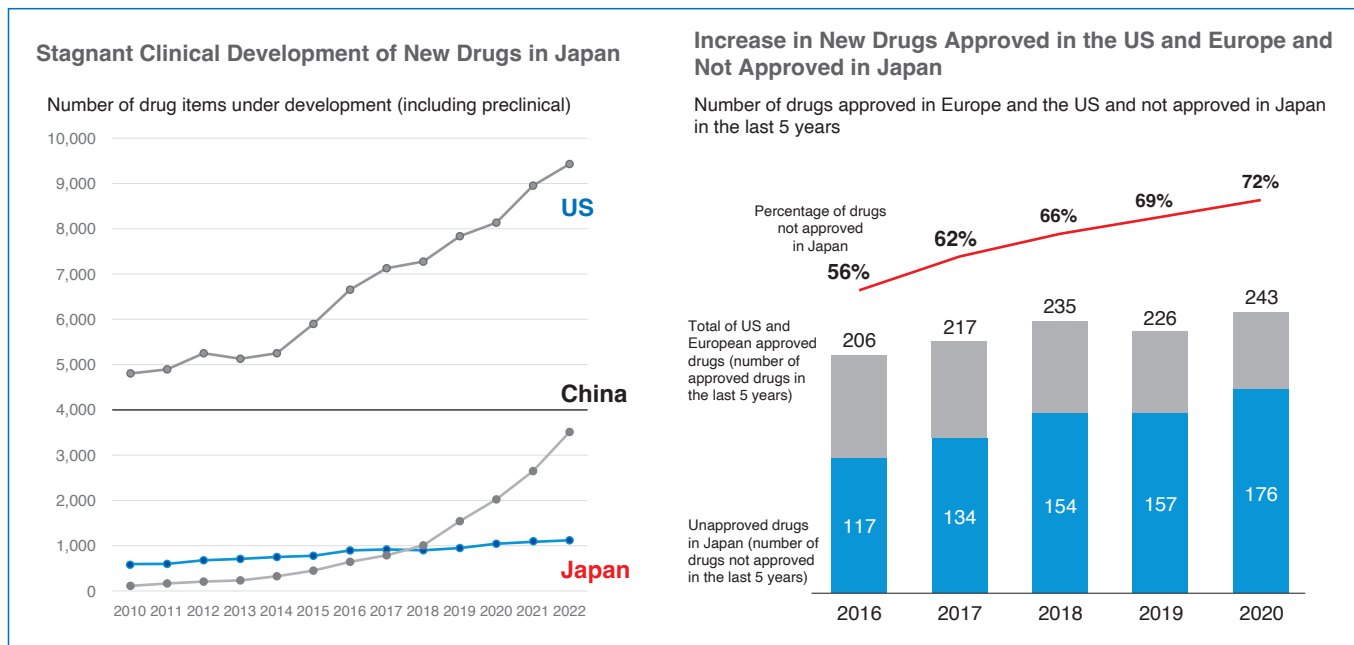
a) Innovation

Combining medical big data and next-generation AI to make drug discovery super-efficient and productive.

b) Digitalization

Developed a therapeutic application that promotes and treats

CHART 12

Drug lag/loss problem ①

Source: PharmaProject

Source: Office of Pharmaceutical Industry Research

behavior change through personalized messages and videos.

e) Human capital investment

The knowledge and skills of pharmaceutical companies and researchers involved in drug discovery need to be enhanced with respect to digital technology, AI, and big data.

d) Addressing specific issues

It is problematic that innovative new drugs are not reaching Japanese patients due to drug loss. While establishing firm rules for the growth of total drug costs, it is necessary to review the market expansion recalculation and its special provisions, including the formulation of new rules for the NHI drug price listing system, which will properly set prices commensurate with value. In such cases, a study group of pharmaceutical manufacturers, private insurance companies, patient groups, academics, and others should examine what kinds of drugs could be substituted for private insurance in areas beyond the amount covered by public medical insurance, in cooperation with private life insurance.

If there are other invisible barriers in the medical/nursing care field, it is also necessary to create a system that allows people to try using devices created through research and development in medical/nursing care settings.

Possible measures to promote clinical trials include simplifying the clinical trial procedures, strengthening the personnel of the Pharmaceuticals and Medical Devices Agency (PMDA), which is in charge of reviewing the approval of clinical trials, and promoting educational activities on the benefits of clinical trials.

Conclusion

Japan's service industries have tremendous potential. Each sector has the potential to transform itself into a key industry if the public and private sectors focus a little more effort on digitalization, strengthening overseas-oriented activities, and human resource development, in line with these recommendations. In particular, the fact that the majority of Japan's service industries are limited to domestic activities is considered to be a major impediment to their development.

In order to strengthen the international competitiveness of the service industry, it is necessary to have a wide range of strategic moves when expanding overseas, including bilateral negotiations, multilateral negotiations, and negotiations with international organizations. Otherwise, if Japanese service industries attempt to expand overseas, they will be rounded up and their overseas expansion may be blocked. Policymakers should also become professionals in their respective service fields and reach a level of knowledge accumulation in these fields that is second to none. Furthermore, it is necessary to develop policymakers who can consider the consistency of policies from a macro perspective.

There are many aspects of overseas expansion on the part of individual service companies that are difficult for the private sector alone. A public-private partnership on the policy and political fronts is essential, including support from the local JETRO (Japan External Trade Organization) and negotiations with the partner country's government and international organizations through public-private partnership.

As Japan's exports to foreign countries decline, globalization of the service industry is an urgent priority.

Strategies for Japan's service industry: making the service industry a source of prosperous growth

	Service industry as a whole	IT-related services	Tourism	Entertainment
Present	<ul style="list-style-type: none"> Both value-added and worker share increased. Important sectors! (GDP share: 52% 1970 → 73% 2020) Suffering from low productivity (50% of US 2017) and balance of payments deficit 	<ul style="list-style-type: none"> Software is the mainstream instead of hardware. Furthermore, cloud services are predominant (efficiency of traditional software development declining). Low productivity of IT companies due to low mobility of human resources (sales per employee: 30 million yen in the US, 19 million yen in Japan / AI adoption ratio: 72% in the US, 50% in Japan) 	<p>Steady recovery of inbound tourism from the corona virus disaster and increase in inbound consumption, which is expected to reach a record high of 33.1 million in 2024. France is at 100 million. Japan's government target is 60 million. (2030)</p>	<ul style="list-style-type: none"> Content, online market expansion, (global market share: US 43%, China 19%, Japan 7%, South Korea 3%) Overseas Market Expansion Fostering related industries
Issues	<ul style="list-style-type: none"> Low prices that do not reflect quality Low labor productivity Sluggish domestic investment opportunities Improving services balance of payments deficit 	<ul style="list-style-type: none"> Low and stable multiple subcontractor structure entrenched without organizational reform Expanding digital trade deficit 	<ul style="list-style-type: none"> High value-added Revitalization of local economy Elimination of low productivity in accommodations, etc. Human resource development Responding to overtourism 	<ul style="list-style-type: none"> Overseas Expansion Digitalization Integration with other fields Human Resource Development
Countermeasures	<p>Aggressive measures</p> <p>a) Innovation promotion b) Digitalization c) Human capital investment</p> <p>Environmental Improvement Measures</p> <p>a) Regulatory reform b) Exit facilitation c) Maintain population agglomeration d) Ensuring employment mobility e) Development of digital infrastructure</p>	<p>a) Innovation</p> <ul style="list-style-type: none"> Productivity improvement through standardization and componentization in non-competitive areas and in-house production in competitive areas Utilization of AI revolutionary trends <p>b) Digitalization</p> <ul style="list-style-type: none"> Utilization of AI, promotion of cloud computing with ICT investment <ul style="list-style-type: none"> Cultivation of AI startups to replace GAFA <p>c) Human capital investment</p> <ul style="list-style-type: none"> Training to improve the competence of engineers Mobilization of quality engineers to make it easier for AI to enter the organization 	<p>a) Innovation</p> <ul style="list-style-type: none"> Creation of high value-added tourism Cultivation of DMCs (tourism strategy planning companies) that bring together diverse players <p>b) Digitalization</p> <ul style="list-style-type: none"> Improving service efficiency and designing tourist cities with data and AI <p>c) Human capital investment</p> <ul style="list-style-type: none"> Improvement of English and other communication skills Cultivate high-level human resources such as professional guides to meet the needs of wealthy foreign tourists <p>d) Addressing specific issues</p> <ul style="list-style-type: none"> Raising service prices in line with higher value-added services Leveling of demand through the introduction of dynamic pricing Addressing overtourism through infrastructure development, etc. 	<p>a) Innovation</p> <ul style="list-style-type: none"> Integration of tourism and animation (e.g. construction of Dragon Ball theme park in Saudi Arabia) <p>Promotion of overseas expansion</p> <p>b) Digitalization</p> <ul style="list-style-type: none"> Anti-piracy Fusion of telecommunications and broadcasting <p>Developing new areas such as e-sports</p> <ul style="list-style-type: none"> AI literacy development Development of music copyright processing rules <p>c) Human capital investment</p> <ul style="list-style-type: none"> Development of Information Management Innovation Professional University (IU) Cultivation of producers and marketing strategy specialists capable of overseas expansion

Source: Compiled by the Study Group on the Service Industry in Japan, Nov. 12, 2024

Strategies for Japan's service industry: making the service industry a source of prosperous growth

Medical Care Services				
	Medical inbound	Nursing robot	Medical equipment	Medical supplies
Present	Utility is great, but disastrous (500,000 Singaporeans, 500,000 South Koreans, 1.2 million Malaysians, 20,000-30,000 Japanese)	Decrease in the number of healthy elderly people and rapid increase in nursing care costs (Nursing care expenses: 3.6 trillion yen in 2000 → 16.4 trillion yen in 2025)	Low self-sufficiency in therapeutic equipment is serious. (In diagnostic equipment, endoscopes have a certain level of competitiveness, with a 99% share of the global market, but the share of therapeutic equipment is almost 0%)	Stagnant clinical development of new drugs. In addition, the number of new drugs approved in Europe and the US but not yet approved in Japan is increasing (the ratio of unapproved drugs in Japan is 72%)
Issues	Breaking free from the psychological bondage of “free medical care = preferential treatment for the rich Singapore has a population of less than 6 million, but is surrounded by hundreds of millions of wealthy people.	Reducing the cost of care robots and customizing the technology to the individual needs of the elderly	Reimbursement prices are lower than actual prices in other countries , which prevents medical devices from being introduced in Japan (device gap) and also prevents innovation due to reimbursement prices that do not cover domestic development costs.	Price of a new drug is too low at the time it is covered by insurance → Hampers incentives for drug discovery
Countermeasures	a) Innovation <ul style="list-style-type: none"> • Promotion of medical tourism • Construction of wellness resorts (integration of physical checkups and tourism) b) Digitalization <ul style="list-style-type: none"> • Rationalization of hospital management, unification of medical data standards, collaboration with overseas hospitals c) Human capital investment <ul style="list-style-type: none"> • Invitation of foreign doctors • Training of personnel capable of triage (selection of appropriate responses), emergency response, and hospital management experts d) Addressing specific issues <ul style="list-style-type: none"> • Cooperation between the medical industry and the travel industry 	a) Innovation <ul style="list-style-type: none"> • Development of various robots through modularization, etc. b) Digitalization <ul style="list-style-type: none"> • Digitalization of nursing homes c) Human capital investment <ul style="list-style-type: none"> • Education to increase digital literacy to use nursing care robots 	a) Innovation <ul style="list-style-type: none"> • Create role models for physicians and researchers to start successful businesses • Considering treatment of advanced medical care through the use of private insurance similar to that in Europe and the US • Expanding the market for advanced treatment opportunities b) Digitization <ul style="list-style-type: none"> • Digitize data for effective use, ensure compatibility of data utilization in systems between hospitals (promote utilization of data from over 100 million people) • Activation of regional medical information networks c) Human capital investment <ul style="list-style-type: none"> • Smooth supply of first-in-man (investigator) for clinical trials d) Addressing unique challenges <ul style="list-style-type: none"> • The need to rethink Japan's public health insurance system with universal health coverage 	a) Innovation <ul style="list-style-type: none"> • Combining medical big data with next-generation AI to make drug discovery super-efficient and improve productivity b) Digitization <ul style="list-style-type: none"> • Development of therapeutic applications c) Human capital investment <ul style="list-style-type: none"> • Spread digital literacy and AI literacy d) Addressing specific challenges <ul style="list-style-type: none"> • Introduce a price matching system (consider a subsidy system like that for EVs [electric vehicles]) • Consideration of substituting private insurance for the portion beyond the amount covered by public insurance (consider subsidies for income groups below a certain level)

Source: Compiled by the Study Group on the Service Industry in Japan, Nov. 12, 2024

The Japan Economic Foundation (JEF) initiated the Study Group on the Service Industry in Japan with prominent Japanese experts in May 2024 and will conclude its role by publishing recommendations in early 2025.

R oundtable on Making the Service Industry a Source of Japan's Soft Power (Jan. 30, 2025)

By Japan SPOTLIGHT

Participants: Prof. Masami Morishita, Professor, Faculty of International Tourism Management, Toyo University
 Dr. Ichiya Nakamura, President, Professional University of Information and Management for Innovation (iU)
 Dr. Kenji Shibuya, Chief Executive Officer, Medical Excellence JAPAN (MEJ)
Moderator: Masakazu Toyoda, Chairman & CEO, Japan Economic Foundation (JEF)

Participants



Prof. Masami Morishita



Dr. Ichiya Nakamura



Dr. Kenji Shibuya



Masakazu Toyoda

Introduction

Toyoda: It is said that as an economy matures, the share of its service industries usually increases. The share of service industries in Japan's GDP increased from 52% in 1970 to 73% in 2020. Unfortunately, Japan's labor productivity is not necessarily high. Compared to the United States, Japan's productivity in the manufacturing industry is about 70%, but in the service industry it is said to be about 50%.

The service industry is now a major part of the Japanese economy, and the challenge is how to increase productivity. Japan has a current account surplus of approximately 20 trillion yen as of 2023, but in addition to a trade deficit of 6 trillion yen, there is a deficit of 3 trillion yen in the services sector. In this context, travel and tourism services have a surplus of about 4 trillion yen, and entertainment services are expected to grow significantly and now have a surplus of about 270 billion yen. Medical inbound services are also expected to grow.

In travel and tourism services, Japan is ranked 12th in the world and third in Asia after China and Thailand, according to pre-pandemic 2019 statistics. The Japanese government is aiming for 60 million foreign visitors by 2030, but the current rate of 60 million is

comparable to China and Italy, which are in fourth and fifth place, respectively.

Entertainment services, although not yet showing a big surplus, have great potential given the popularity of Japanese anime and games. Furthermore, in terms of medical inbound services, we are currently looking at 20,000 to 30,000 visitors to Japan in 2019, though this is still an insignificant level compared to Malaysia's 1.2 million and Singapore's 500,000 visitors. However, given the popularity of tourism in Japan and the high level of medical care in Japan, we feel that with some ingenuity it could be dozens of times higher.

I believe there are common challenges that need to be addressed to increase the productivity of these service industries. The first is the promotion of innovation, the second is the evolution of digitalization, and the third is human capital investment. In addition, I believe that each industry may have its own specific problems and unique challenges.

Today, I would like to discuss these issues with experts from three service industries. For the travel and tourism industry, we have asked Prof. Masami Morishita of Toyo University; for the entertainment industry, we have asked Dr. Ichiya Nakamura, president of the Professional University of Information and

Management for Innovation (iU); and for the medical inbound industry, we have asked Dr. Kenji Shibuya, chief executive officer of Medical Excellence Japan (MEJ).

Although these are different service industries, we would like to discuss these issues from the perspective of common challenges. First, I would like to ask you to discuss what are the challenges in your respective industries in terms of promoting innovation. I would like to ask Prof. Morishita to speak first. When we consider travel and tourism services, we can think about creating high value-added tourism, or fostering tourism strategy planning companies that bring together diverse players. What do you feel is important in terms of promoting this innovation?

Promotion of Innovation in Each Industry

Morishita: Tourism can be surprisingly confusing or different from what you may have in mind, so I would like to start with a brief overview of what the tourism industry is.

Generally speaking, the tourism industry includes travel, transportation, accommodation services, souvenirs, theme parks, and event conventions. The environment surrounding the industry has changed dramatically over the past 20 years, though it may be the same with other industries.

There are two major changes. It is not a question of whether to innovate or not, but rather an environment in which we have no choice but to change. One is, as you mentioned, digitalization. Stores are no longer needed, and distribution methods have changed dramatically, such as connecting customers with industries without the need for a travel agency. The way customers themselves approach information has also changed dramatically. This is a rather major change that affects the very foundation of the industry.

The other major change is the market. This has also changed over the past 15 years or so. Until now, the tourism industry mainly served the Japanese market. One point is that there has been a major shift to inbound tourism, and the customers themselves have changed.

In addition, until now, the tourism industry has been more of a method of attracting large numbers of customers and then leveling them off to lower prices, but that approach is no longer working, since large amounts of diversified tourism-related information are now available. So some of the challenges cannot be summed up in the tourism industry as a whole.

And there is also the high value-added aspect. Until now, the tourism industry has not had much of a mechanism for customers to spend money on tourist attractions. The tourism industry is an industry that is equivalent to a distributor or manufacturer, so it has been supplying raw materials from tourist attractions; in other words, it has been collecting and sending tourist resources, such as culture and nature, to customers. But nowadays this has changed drastically with the emergence of private lodging accommodations and ride-sharing.

Generally, when we talk about high value-added, we are talking about luxury hotels, first-class hotels, and the like. However, what is

needed now is to add value to the raw materials of tourist attractions. In other words, the existence of DMOs (tourism region development corporations) and DMCs (tourism region development companies), which organize tourist attractions, is becoming more and more important in order to create a system that allows a little more consumption in areas where money has not been spent so far.

Conventional tourism was centered on “seeing”, so there was no mechanism for spending much money. There was the problem of overtourism, in which only customers came to enjoy tourist spots and the surroundings, and residents there were burdened with the costs for it. This has changed a bit recently. What is called “experience tourism” with consumption is becoming popular. However, experience tourism is only practiced at a particular point, and in order to make it a high value-added product it is necessary to make it more of an area-based product. For example, we need to set a proper theme within a certain region, decide on the target customers, and provide them with the right combination of what to do, what kind of story to tell, and what kind of things to consume.

In the world today, those who support high value-added tourism are those who are looking for luxury stays and services on the traditional upscale route, and those who are a bit younger in terms of generation and engage in high consumption. There is a growing number of customers around the world, especially in Europe and the United States, who want to have authentic experiences, who want to enter a certain area to experience different things, and who want to improve themselves by doing so. Targeting them as potential tourists to Japan could produce value-added tourism that does not lead to overtourism. If DMOs and DMCs do not play a role in this process, it will be difficult to encourage consumption.

Toyoda: Now Dr. Nakamura, in terms of innovation in the entertainment industry, you recently mentioned the construction of the Dragon Ball theme park in Saudi Arabia. I think the fusion of tourism and animation is important. In particular, what do you think about the possibility of overseas expansion?

Nakamura: There are efforts to increase inbound tourism by using anime as a trigger in many areas. An organization called the Anime Tourism Association has selected 88 locations throughout Japan to promote tourism called “pilgrimages to sacred places”. To cite a few specific examples, Sakaiminato city in Tottori Prefecture, the birthplace of Shigeru Mizuki, one of the greatest Japanese authors of manga, has become the largest tourist destination in the San'in region, with 178 bronze statues of “Gegege no Kitaro” ghost characters invented by him, placed throughout the city.

Then there is Washinomiya Shrine in Saitama Prefecture, the setting of the “Lucky Star” anime, which was visited by 420,000 people, the second-largest number in Saitama Prefecture, on *Hatsumode* (the first prayer to the Sunrise on New Year's Day) in 2009. These have been in place for 15 years now. The anime “Girls und Panzer”, which is set in Oarai, an area hit by the Great Eastern Japan Earthquake, has had such a positive effect that local retail stores have increased their sales by more than 20% from what they

were before the disaster, according to some data.

Similarly, Japanese pop culture is gaining popularity overseas. The Japan Expo held in Paris every July attracts 250,000 Japanese content lovers. The Anime Expo in Los Angeles attracts even more, around 350,000 people.

Such Japanese cultural events, so to speak, are held all over the world. Some data indicate that the total number of people who attend these events exceeds 20 million every year. However, most of the events held overseas are organized locally and it is difficult to say that Japan is making the most of them as a business.

When considering the economic impact of pop culture such as animation, the ripple effect is important. If direct sales of animation are counted as 1, then sales of toys and other products, related equipment and other sales, and sales of peripheral industries, in addition to tourism, add up to about 10. In other words, the annual sales of the content industry, including animation, movies, manga, and music, are about 13 trillion yen according to data from the Ministry of Economy, Trade and Industry (METI), but if ripple effects are included, the total is estimated to exceed 100 trillion yen. Such a large external effect is the basis for policy support for the industry.

We call this policy “Cool Japan”, which aims to expand peripheral industries, including tourism, with this kind of content as the core, to raise the overall scale of industries. Until now, the focus of Cool Japan has been on domestic industries, but the policy is now moving in the direction of increasing the size of the overall pie, including overseas industries.

Toyoda: Dr. Shibuya, I feel that the concept of medical tourism is lacking in Japan. I believe that there is a great need for the fusion of medical checkups and tourism.

Shibuya: First of all, medical tourism has been practiced in Japan for a relatively long time in the form of medical support for inbound tourism. Initially, the focus was on addressing the needs of foreign tourists who came to Japan for sightseeing and faced sudden illness or accidents, rather than people coming to Japan specifically for medical treatment.

The terms “promotion of medical inbound tourism” and “growth of Japan’s medical industry” were included in the government’s “Basic Policy Plan” released last June, as well as in the Global Health Strategy formulated by then Minister of Health, Labor and Welfare Keizo Takemi, in August last year. It is very rare for the Ministry to use the term “industrialization of healthcare.” Traditionally, the medical community has been based on public insurance, and since hospital inbound services are basically provided through private-pay and not covered by public insurance, the concept of coming to Japan for medical purposes under private-pay services was difficult for the medical community, especially the Japan Medical Association (JMA), to accept.

That being said, small and medium-sized hospitals are facing financial difficulties due to negative revisions in fee schedules, leading to a rapid closure of hospitals, particularly in Tokyo. There are growing voices from the frontline saying, “If we don’t provide

private-pay medical services, we won’t be able to survive.” This trend, combined with the element of tourism, has brought medical tourism into the limelight.

I believe that medical services that involve life are the ultimate high-value-added services. However, the scope of medical tourism is very broad, ranging from wellness services such as yoga, preventive medicine, and medical checkups to cutting-edge services such as regenerative medicine and heavy particle radiotherapy. The former can generally be managed through Japan’s e-commerce market, which is one of Japan’s strengths. The latter, however, faces various regulatory challenges and requires further hospital system development. The government has decided to promote medical tourism, and medical associations are basically not opposed to it as long as the patients are foreigners. Therefore, I think it will accelerate quickly.

Toyoda: I feel that there is very great potential. I would like to ask you to lead the industry as a whole.

Now on to the next topic. I would like to ask you to speak from the perspective of the progress of digitalization. Let me start with entertainment, Dr. Nakamura. How would you describe the fusion of the entertainment industry with the telecommunications and broadcasting industry? Or, recently, I think there are possibilities for the development of new areas such as e-sports. On the other hand, we must also do our best to deal with piracy. What are your thoughts on this digitalization?

Utilizing Digitization

Nakamura: I believe that the entertainment industry faces two challenges: overseas expansion and digital expansion. Overseas sales have grown more than 3.3 times in the past 10 years and have now reached just under 5 trillion yen. This has reached a point where it is on a par with exports of steel and semiconductors. This is the reason why the government is paying renewed attention to the content industry.

Meanwhile, digital development is also progressing. Japan recognized the importance of digital distribution during the pandemic and the entertainment content industry also took advantage of the pandemic that forced people to stay at home: anime distributed to them online created a major growth opportunity. Online sales accounted for about 13% of total content sales in 2011, but by 2023 they had grown to 46.5% or about half of total content sales. While the analog content industry, such as books and newspapers, is shrinking, the digital and online sectors are responsible for most of the growth in content.

In 2021, there was news that online advertising exceeded the total of the four media (TV, radio, newspapers, and magazines). TV and newspapers are now lumped together as the four media, and those four media are considered as a whole as the rival of Internet business. However, the online media is dominated by American IT companies and digital platforms such as GAFA and Netflix. In Japan, neither the broadcasting nor the telecommunications industries have

succeeded in integrating with the content industry. Such fields should have invested strongly in content from around the year 2000, when the Internet began to grow, but Japanese broadcasters at that time were negative toward the Internet. This still resonates today.

It is also important to develop and nurture new areas such as e-sports, but in fact Japan has been a backward country in e-sports. The reason for this is that Japan has had too much success with TV games, and has lagged behind in the development of PC and Internet games. However, Japan has a solid foundation in the fields of manga and music, and is rich in production capabilities, so there is great potential to capitalize on these strengths. In this light, e-sports is also growing rapidly in Japan.

As you mentioned, the headache is piracy. In each genre of entertainment, such as manga, anime, and games, their profits are being siphoned off by overseas online piracy. This is why the Cabinet Office established the Piracy Task Force in 2018. I co-chaired the task force with Keio University Prof. Jun Murai, and we brought together relevant ministries and agencies from related industries to formulate comprehensive measures. As a result, the countermeasures to deal with piracy were strengthened. Since then, we have seen some positive results, such as the arrest of criminals overseas and the imposition of penalties. However, there is still a need for further action.

In addition, one of the current digital issues is the response to artificial intelligence (AI). Japan has revised its copyright law to make it free for AI, or computers, to learn – a strategy not seen anywhere else in the world. While both Europe and the US have moved in the direction of regulating AI, Japan has taken the lead in promoting its use, and we expect that AI will produce new entertainment contents.

On the other hand, there is a movement among creators who fear infringement of their rights, and in fact, when I asked university officials to what extent AI should be used, their responses varied from school to school, and their policies are not yet clear. How to deal with AI will be an important theme for some time to come.

Toyoda: Next, I would like to ask Dr. Shibuya whether digitalization of hospital management is sufficiently advanced? How much progress has been made in unifying medical data standards and collaborating with overseas hospitals?

Shibuya: I think that the medical industry, like other sectors, is still lagging behind in digitalization. The reason for this is that there are some stakeholders who are resistant to change, even though it would be much easier if it were digitized in a conventional manner. In other words, many people do not want their medical practice to become transparent. There are also those who prefer not to embrace digitalization. This is why progress has been slow.

However, with the working population decreasing, rural areas are losing more and more people even when offering higher salaries, and it is becoming increasingly difficult to attract nurses and other healthcare professionals. I think that digitization is a necessity, but it is still not progressing as it should.

In the context of medical tourism, diagnosis and treatment data

from overseas are often still brought on paper or DVDs. This creates an additional burden on doctors in the field, as they must also translate the data. These are the areas which medical institutions should not be responsible for, and it takes up a significant amount of time.

There are many people who would oppose the sudden implementation of personal health records (PHRs) for patients in Japan, so I believe that it would be quicker to start using PHRs for foreigners who come to Japan for medical tourism. I have a feeling that if foreigners can successfully use the system, progress will be made, as the process would ultimately be the same for both Japanese and foreigners.

The reason why I am promoting medical tourism is to avoid opposition from the medical community, especially from the JMA, by introducing the concept of private-pay medical care for foreigners first. In the end, what Japanese and foreigners do is the same, so once the system is established, Japanese people will also be able to use it. I believe that leveraging medical tourism by foreigners is one of the opportunities to reform Japan's rigid system.

Toyoda: How about AI?

Shibuya: I think AI can be used in various ways for diagnostic decisions and back-office support. In medical practice, of course, generative AI has significantly better diagnostic capability than ordinary doctors, so it should be used to support diagnostic decisions to a great extent. Even though final judgement must still be made by a physician, AI can be fully utilized in a doctor's back office or in image diagnosis. Even if we do not go as far as AI, if someone wants visit a certain region in Japan at a certain time, and inputs their medical condition, medical tourism can be facilitated in that region. I believe it is possible to create numerous apps that provide information on medical institutions, doctors, and costs for medical tourism in the area. This should be done from the user's perspective first and foremost.

Currently, in medical tourism, there are intermediaries such as agents and travel agencies involved in the process of obtaining a visa and transferring information to medical institutions. Even within medical institutions, there are various fragmented and disjointed systems. I believe that it would be better to create a kind of web portal that users can go to first, and that is what we are aiming to develop this year.

At the moment, the environment forces each user to handle every step of the medical tourism process separately. The receiving side in Japan is based on a supply-side logic and lacks a user perspective entirely. I would like to fundamentally transform this and focus on the user's perspective instead.

Toyoda: I would like to ask Prof. Morishita if it is possible to use AI to design a tourist city, as in Barcelona, using AI?

Morishita: In terms of digitalization, as well as AI, I think factual developments preceded the tourism industry's own efforts. In other

words, another industry, not the tourism industry, has entered into the reservation system field, whereas the tourism industry itself was behind the trend of digitalization in this area. One of the most common uses of digitalization is to simulate flow lines, such as the flow of customers. When there is overtourism, there is inevitably a concentration of customers in the same place at the same time, or the customers move in the same flow, so we actually use this to see how we can disperse them to other places.

I think it is a fact that the tourism industry is particularly short of labor, and if we do not use these things, we will not be able to keep up. In addition, there are so many players in the tourism industry. Without objective data, it is impossible to reach a consensus. So in order to create data for consensus building among many players, we are now promoting Digital Transformation (DX) and taking data. The Japan Tourism Agency is also subsidizing this.

In terms of high-value-added travel, in reality we cannot and will not be able to capture only high-value-added customers. In that sense, I think there are both “mass” and high value-added segments. For the so-called mass segment, I believe that AI-based travel proposals and planning proposals will advance and will have to be implemented. However, as things stand now, customers do not need AI very much. In other words, there is a lot of information available, and they have pinpointed the places they want to go, so rather than compounding this information and using AI to make suggestions, many customers go where they want to go based on what they see on social networking sites. Therefore, there is a mismatch with their needs in this area, and I think there are some areas where AI is not necessarily needed.

Toyoda: What you just said was about using digitalization as a countermeasure against overtourism. Can digitalization be a successful solution?

Morishita: Overtourism is happening only in so-called famous tourist destinations such as Kyoto and Tokyo, and we are talking about a limited number of areas. In these areas, it is necessary to first understand how the flow lines of customers work before conducting community development. Kyoto, Takayama, and other cities have already begun to introduce this system. However, we have not yet reached the point where we can make concrete plans for urban development. We are still in the process of collecting data, but the specifics of how to distribute the data and at what times of the day are still in the early stages of development, as there are not that many experts in this area. But the local governments and the national government are subsidizing the collection of data in this area, so I think the first step is to get the data ready.

Toyoda: I feel that human resources are important in both innovation and digitalization. My third question is from the perspective of human investment. I would like to ask Dr. Shibuya first. In the field of medical care, I believe that communication will not proceed smoothly if the language is not well understood. It is a matter of course to learn English, but how about inviting foreign doctors to

Japan? Also, from the perspective of training professionals, such as those who can triage, i.e., select priorities for medical treatment, those who can respond to emergencies, and hospital management, is the world of medicine progressing well?

Importance of Human Resource Development

Shibuya: In the medical and nursing care sector, human capital is crucial because, ultimately, no matter how much digitization is implemented, human hands are still involved in the process. This is especially true in medical tourism, where the target is primarily the middle class and above, and there are many areas that cannot be handled solely by machines.

First of all, I believe that the only way to create a private medical care sector is for private operators, global insurance companies, and other consumer service providers to take the lead. Ultimately, this can be achieved by establishing hospitals specializing in private medical care.

As for language support, we are not only focused on English, but also targeting wealthy Vietnamese, wealthy Chinese, and eventually people from India and the Middle East. In terms of multilingual services, medical interpreting differs from regular interpreting, as it requires considerable expertise, particularly in areas like safety assurance. Qualifications for medical interpreters and telephone interpreters have already been developed for the Tokyo Olympics, and I think we should actively utilize such qualifications.

On the other hand, there are so-called coordinators, but their role is not just to connect patients with medical institutions. It is difficult for machines to determine which hospital is best suited for a patient's needs and medical condition, and in what medical and socioeconomic context. There are very few coordinators with clinical experience, or health concierges as they should be called, and we are currently in the process of training such professionals.

Medical care cannot exist without human resources, so human capital is the key. In particular, we need people who can add value, not only by connecting existing services, but also by creating new services from existing ones, along with individuals who can manage these processes. The medical community has traditionally been able to function with public insurance, so I expect that fostering connections between personnel in the medical and the private sector, especially from the standpoint of high-value, user-centered private medical care, will positively influence the public insurance system.

Toyoda: Do you have any kind of human resource training institution? Is it the training of personnel to support doctors rather than doctors themselves?

Shibuya: Nowadays, to be honest, it is extremely burdensome for the frontline workers, such as doctors and nurses. Ideally, healthcare professionals on the frontlines should be placed in an environment where they can provide the best possible service to any patient in front of them, whether Japanese or foreign. However, for example,

whether it is language support, dealing with patients, or handling data that comes in paper form, healthcare professionals are burdened with unnecessary tasks that go beyond their primary responsibilities. The most important point is to eliminate as much of that extra work as possible. To achieve this, we need more than just medical personnel. This is where the medical coordinator personnel I mentioned earlier comes in, and of course DX also plays a key role.

Toyoda: Is there still resistance in Japan to inviting foreign doctors themselves?

Shibuya: We must convince doctors to refer their patients to Japan, so I believe that we must definitely foster medical exchanges, although this is a process that needs patience. If doctors in other countries do not perceive the added value of sending their patients to Japan, the patients will not come on their own. Although medical treatment cannot be performed without a Japanese medical license, remote diagnosis, demonstration of medical procedures, observation, and training are possible, so I think we should actively promote medical exchanges, especially in advanced medicine. In special economic zones, it may be possible to do so without a license, but I think there are still challenges to overcome.

Toyoda: Dr. Morishita, I know this is elementary, but some people say that Japanese tourism personnel lack English and other communication skills. What is the actual situation? And what do you mean by “highly-skilled” human resources who can meet the needs of professional guides and wealthy foreign tourists? What about the development of educated personnel?

Morishita: Language skills are of course necessary and indispensable, but I don't think they are the first requirement. As for translation, although it is not digitalization as I mentioned earlier, it is already quite advanced and can be done to a certain extent with a single smartphone. Securing human resources is a matter of both quantity and quality.

If you are talking in terms of quantity, the tourism industry, as you know, has low salaries and not very good working conditions. And we have now come to a point here where the cost of lodging has skyrocketed. Everyone says it's tough, but I think the industry has finally established a base from which salaries can be raised. The reason why people don't stay is because the working conditions are poor and they are not respected, so first of all it is difficult to secure a quantity of workers. That is one point. It is not only about salaries, but unless the industry is made to be respected a little more, human resources will not stay in it.

In terms of quality, including language skills, we are talking about the two groups I mentioned earlier: those who come to Japan via social networking do not need a guide of that caliber. On the other hand, for affluent travelers who want high value-added travel, it is necessary to have a proper guide. Guides are also not well respected. Of course, it depends on the country, but in general, hiring a guide for eight hours a day in other countries, especially in Europe, costs

more than 100,000 yen, but in Japan, even if you hire a guide for one day, the cost is as low as 20,000 to 30,000 yen. On the other hand, there are also volunteer guides, and I think this is where the difficulty lies.

However, the world of tourism is not just about being able to guide; in the end, you need a coordinator. In order to deal with wealthy people who want to go trekking in an area, for example, you need to have knowledge of trekking itself, as well as miscellaneous knowledge about the area. Naturally, hospitality is also necessary. You need to know what they are looking for and be able to respond to them by telling them that they are tired and should move on to the next one. In this case, the cost of the tour would have to be quite high to make it worthwhile, but since the price does not go up very much, there is no one to be a guide.

There are qualifications such as guide interpreters, but they do not increase salaries to any great extent, and it is not only a matter of language skills. Now that there is a clientele coming in from overseas in the form of high value-added tourists willing to pay a certain amount of money, I feel that the cost of guides will rise a little due to external pressure.

Toyoda: One point, you used the word “respect”. Internationally, for example, is the tourism business respected in the US and Europe?

Morishita: The tourism industry has been seen as more of an entertainment industry worldwide until now, so it is not only in Japan that the tourism industry itself is not respected in that sense. However, in the case of other countries, they receive a certain amount of expenses, so I think that this part of the industry makes a certain amount of difference.

Toyoda: Why are they willing to pay the fees abroad?

Morishita: I think this is partly because the overall cost of living is high, but also because, as in the case of high value-added tourism mentioned earlier, there is a large number of visitors who want to learn about the area and enjoy a good trekking experience, even if they have a guide. As in Japan, people who come to a place after learning about it through social networking do not need a guide; they tend only to take pictures and leave.

Toyoda: Dr. Nakamura, if overseas expansion is important, I think it is important to develop producers, marketing strategies, and specialists who can realize this. I have heard that South Korea is very enthusiastic about this. What is the situation in Japan?

Nakamura: In the content field, human resource development was considered the most important issue. About 25 years ago, when the government launched its content policy, the main issue was how to develop human resources for production, creators and artists. At the time, there were no film schools or other institutions of higher education in Japan. Various schools and faculties have since been established.

Before that, Japan had created a model that did not exist anywhere else in the world through initiatives that included compulsory education and high schools, such as light music clubs and manga clubs, so the people on the creative side and the human resources were already in place. However, like tourism, content also has the problem of what to do about low wages.

On the other hand, the current issue is that there are not enough people to develop overseas business, i.e., people who sell rather than people who make, producers and managers. However, there does not seem to have been visible improvement in this. The Ministry of Economy, Trade and Industry holds the “Entertainment and Creative Industries Policy Study Group” and we have been hearing from related industries such as games, animation, manga, and music for a long time, and the one thing that comes up unanimously from all industries is securing international business personnel. The current situation is that each content company has been developing its human resources through on-the-job training, and there are few schools or faculties that specialize in this area, even at universities. I do not know of any Japanese economics, business administration, or MBA schools that focus on this area.

In fact, that is what I myself am trying to set up right now. There is an entertainment MBA program called Thunderbird, which is based in Hollywood, and my university, iU, is trying to attract them to Japan and establish a Japanese school in cooperation with the Japanese entertainment industry and the government. iU has been working with the Japanese entertainment industry and the Japanese government to establish a school in Japan. We are planning to conduct a trial this year and start an MBA course next year. This is one small trial. We believe that we need to increase many such movements.

Toyoda: Thank you very much for your comments, and I was thinking that in a sense, medical tourism is connected to tourism, and that it would be very useful to establish a school where medical care, tourism, and entertainment can be well connected to each other.

This brings me to my last question. I think that each industry has its own problems and challenges. Let me start with you, Prof. Morishita. From the perspective of tourism, what are the specific issues that Japan is facing today? You have talked a little about overtourism, but when you think of specific problems in the industry, what kind of problems come to mind?

Challenges Specific to Each Industry

Morishita: Although there are many detailed issues, I believe that the biggest issue for tourism in Japan at present is the need for a proper direction on how to position tourism. The number of tourists will increase more and more, regardless of Japan’s efforts, because the external environment is very favorable. But I believe that unless we establish a proper policy of how to position the tourism industry, we may just be swept along by the market and wonder what is left at the end of the day. We must consider how each municipality thinks

about tourism in its own region, and not simply how to attract visitors.

Tourism is inevitably focused only on the economic benefits. Of course, the economic benefits are a great advantage, but for local residents, overtourism may mean that nothing good comes from having people come to the area. I often say, “It’s good for all sides.” This means that the tourists are happy, the businesses are happy, the residents are happy, and the environment is happy. Unless each recipient of tourism is willing to think about how to realize these goals, I believe the market will simply carry the tourism industry along with it. In addition to the economic benefits of tourism, I believe that a grand design should be properly drawn up, such as passing on local culture.

Regarding overtourism, the United Nations World Tourism Organization issued guidelines a long time ago. There are about 12 guidelines on what should be done. It also says that we should disperse and give back to the residents in a visible way. However, as I mentioned earlier, it is important for the community itself to choose its own customers, and for us to properly choose what kind of customers we want to see in our community.

What if the first priority is to make money? If we don’t properly position ourselves, including balancing whether we want to carry on our own culture or not, we will be swept along just because the market is good, and we will end up only responding to that, which is a matter of great concern.

Toyoda: While a national strategy is a matter of course, we also need a strategy that makes the most of the individuality of local regions.

Morishita: That is right. As for the national strategy itself, the fourth Basic Plan for the Promotion of a Tourism Nation was being formulated in 2023. The plan calls for sustainable tourism. Sustainable tourism means not only the return of nature, but also the return of industry, and the securing of human resources, rather than their leaving the country.

In addition to sustainable tourism, high value-added tourism is coming to the forefront. Until now, the number of visitors was only a target of 60 million, but the high consumption value and sustainability are coming to the forefront. However, since inbound tourism has only started to increase extremely in the past 12 or 13 years, it is still a follow-up measure, and I think the current situation is that a grand design has not been drawn up yet.

Toyoda: Although the challenges are great, the opportunities are also great, aren’t they?

Morishita: That is correct. The market is growing rapidly, so I think the question is how to make the most of it.

Toyoda: Now, Dr. Nakamura, in the entertainment industry, Japan’s share of the world market is 7%. With the US at 43% and China at 19%, what are the key issues for Japan to increase its share?

Nakamura: As you say, the potential is great. What we should do, I repeat, is focus our efforts on overseas and digital. On overseas expansion, I mentioned that the export of contents has grown more than 3.3 times in the past 10 years, and 90% of exported contents are animations and games. The industrial structure is such that animation accounts for 30% and games for about 60%.

Recently, too, Japanese popular music has grown overseas, with artists such as Yoasobi and Fujii Kaze gaining popularity on the Internet, and in the case of movies, *Godzilla-1.0* won an Academy Award and *Shogun* won an Emmy Award. and so on. I think we have a great opportunity to spread through the Internet. This is a different trend from what we have seen in the past.

In terms of overall Japanese strength, it is characters. An American company's survey of the world's top 25 selling characters shows that of the top 25 characters of all time, 10 are Japanese: Pokemon is No. 1, Hello Kitty is No. 2, and Anpanman is also high on the list. The industry believes that concentrated growth in these areas will be the strategy for the future.

What is lacking, then, is the development and securing of human resources to develop this as a business. In this case, the human resources are those who can formulate strategies to link this to tourism or medical tourism, for example, and that is what is said to be lacking. I think this is something that we need to consider on today's theme.

Another is digital readiness: Japan does not have its own platform like GAFA or Netflix. The Sony Group acquired an American company called Crunchyroll for online distribution of anime, if there is such a thing. So it is difficult for Japan to make a game-changing move in that area, i.e., the online business. I believe that the digital and IT market is almost completely cleared. So one thing we can do is to compete in the area of characters. If this is possible in the future, AI will have a great impact on this field. If this is the case, the next theme will be how to formulate a strategy and how to create a business that utilizes AI.

Toyoda: Thank you very much. Just as there are many resources for tourism, there are character resources, and young people who come to Japan are first drawn to anime, so I think there is great potential.

Finally, I would like to ask you something, Dr. Shibuya. I heard that Japanese patients feel uncomfortable when there are many foreign patients. What should we think about that? I have also heard that there is a suggestion to make it easier to obtain a visa for medical-related visits to Japan. What are your thoughts in this area?

Shibuya: Perhaps you are referring to the future. First of all, there has been an overwhelming influx of inquiries from various organizations since the release of last year's "Basic Policy" and the Ministry of Health, Labour and Welfare's Global Health Strategy. However, we must understand the situation where patients are not coming to Japan in the first place.

We conducted a survey this year in Vietnam and found that there are actually many people who would like to receive treatment in Japan. This made me realize that healthcare is a powerful asset for

Japan. However, there are high barriers to actually reaching people who want to come to Japan. For example, there are many people wanting to come to Japan who face a month-long process to apply for a Japanese visa, so they end up choosing to go to Singapore, where they can get a visa in just a week. Additionally, as I mentioned earlier, the barriers to accessing medical facilities are too high and not designed from a user's perspective, which is a common issue across the tourism industry. We need to resolve these issues step by step.

To begin with, the industry has not conducted thorough market research. What are the strengths of Japanese healthcare? How are competing countries such as Singapore, Malaysia, and South Korea doing? What kind of people do they actually want to attract? What are they looking for, and what kind of patient journey are they seeking? Public medical insurance reimbursement is uniform across the country, but the benchmark for medical tourism is three times that amount – is that enough to cover costs? We have not yet established such a basic market strategy, so we need to focus on that first. I believe that maintaining the status quo will not lead to success, which is why I am trying to create as many successful cases as possible with individuals who are determined to bring about change.

Finally, unless we break free from the spell of public insurance and create an atmosphere where it is acceptable for medical care to generate revenue – as it is also a service – the medical industry as a whole will decline. This is because everyone is doing good work without making money, eventually leading to exhaustion by long working hours.

Therefore, the first step is to properly price services according to their value and experience firsthand so that this will lead to reinvestment in the next step. This will improve user services, the overall environment, and provide incentives for us. I believe that medical tourism can be a breakthrough for private medical care for this purpose. That is exactly the kind of momentum we are experiencing right now, and I believe we should not let it slip away.

Toyoda: Thank you very much. I think that content, tourism, and medical tourism all have great potential, but I feel that the common issue is that there is not yet a sufficient strategy. Of course, METI is developing various policies, but I feel that those in charge need to be motivated. The Japanese service industry in general has great potential, but I believe that these three industries are also important to help Japan contribute to world peace as a soft power. I wish you all the best in your further contributions and development. Thank you very much.

JS

Written and translated by Naoyuki Haraoka, editor-in-chief of *Japan SPOTLIGHT*, with the cooperation of Tape Rewrite Co.

Roundtable with Dr. Yutaka Matsuo, Akiko Murakami, Chizuru Suga & Masakazu Toyoda
(April 4, 2024)

Is AI a Friend or Foe of Humans?

By Japan SPOTLIGHT

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Akiko Murakami, Executive Director, Japan AI Safety Institute (AISi)
Chizuru Suga, Director, Digital Economy Division, Commerce and Information Policy Bureau,
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Dr. Yutaka Matsuo



Akiko Murakami



Chizuru Suga



Masakazu Toyoda

Introduction

Toyoda: As a specific example of generative AI, the chatbot ChatGPT has been publicly acknowledged and is said to be a great invention comparable to that of the internal combustion engine or the Internet due to its great convenience, and it is said that the fourth AI boom has been arriving. While it can not only answer various questions, but also write scenarios and easily create composite films, some say that this could bring about a crisis for human civilization and that it is a devilish invention comparable to a “nuclear bomb”. Others say that it will take away people’s jobs, provide false information, create confusion at elections, and possibly even cause wars. New technologies have advantages and disadvantages, and I think there is a loud call for certain regulations to strike a balance between the two.

So what kind of regulations are appropriate? Although the invention of the automobile has greatly increased convenience as a means of transportation, it can also cause traffic accidents and take human lives. No one doubts the need for traffic regulations. Over-regulation hinders the further development of technology, while under-regulation leads to chaos. We understand that the “Hiroshima AI Process”, which Japan played a key role in formulating, aims to

achieve “safe, secure, and reliable AI”. Will Japanese companies remain users or contribute as developers in the AI boom? So far, I feel that the contribution of Japanese companies in the post-Internet era is unfortunately limited. Why is that so? Large companies are bound by past successes and seem timid about the risk of change.

On the other hand, some say that the reason why Japan has lacked an environment conducive to nurturing startups is because of the limited mobility of labor. It is said that talented people tend to fail to utilize their competency fully in large companies where the lifetime employment system and seniority system remain dominant. The Japanese government is also beginning to focus on supporting startup companies. Will Japanese companies be able to contribute to the development of AI as developers in the AI boom?

International collaboration on AI development and utilization is also said to be making progress, and a US-Japan joint research framework on AI development was announced during Japanese Prime Minister Fumio Kishida’s visit to the United States in April 2024.

The opportunities and challenges posed by the AI boom for Japan are many, and today we have gathered three experts to discuss these issues. Joining us will be Dr. Yutaka Matsuo, professor at the School

of Engineering, the University of Tokyo, a developer of AI and chairman of the government of Japan's AI Strategy Council, which compiled the Hiroshima AI Process; Ms. Akiko Murakami who, while being a proponent of the use of AI as chief digital officer of Sampo Japan Insurance, Inc., a large non-life Japanese insurance company, has also been looking at the safety side of AI as the executive director of the Japan AI Safety Institute (AISi) since February 2024; and Ms. Chizuru Suga, director of the Digital Economy Division of the Commerce and Information Policy Bureau at the Ministry of Economy, Trade and Industry (METI), who is in charge of policy. So let's begin our discussion.

Benefits of AI

Toyoda: First, the merits of AI. I would like to hear from each of the three experts about the “technological singularity” at which AI surpasses human intelligence, including what this means for humanity and for Japan in particular. I would like to start with Dr. Matsuo, who is an educator and developer.

Matsuo: I do not think it is necessarily a good idea to start from technological singularity, as it would be somewhat divergent. First of all, there are many areas where the current generative AI technology can be used industrially and where industrial productivity can be improved, so I think it is important to make sure that in such areas the use of AI is advanced and AI fully utilized. There is no doubt that the technology will spread throughout society in the span of five, 10 or 20 years, and I believe there will be several more major breakthroughs in the level of the technology.

Murakami: From the corporate side, the technology is advancing very quickly, and there is a risk of a technological singularity in the future, but at this point I believe that AI has more advantages for companies than disadvantages. In particular, it is certain that the labor force will decrease in the future, and in order to compensate for this shortage I think it will be necessary to supplement the workforce in a technological way. At that time, it will no longer be possible to cover only simple tasks by mechanically delegating them, as has been the case up to now. I think it is very important to cover labor other than simple tasks with advanced AI technology.

On the other hand, AI technology nowadays seems on the surface to be usable by everyone, but there is still a bit of a gap in order to put it into practice, and I think there is a big division between companies that can do it and those that cannot. This is where the difference in competitiveness comes into play, and I think it poses a threat to the industry.

Suga: I think the best way to understand AI is that a new engine has been developed that will support what we want to do. I have heard that when printing technology first appeared in ancient society, some experts of the time expressed concern that the sudden introduction of such technology into the world of oral tradition would corrupt human beings and that printing technology would surpass human memory. In reality, humans have not become creatures that do not memorize, and the technology of printing has been of great use to human society, including expanding human capabilities and preserving unmemorable amounts of data in various forms for the future.

When new and disruptive innovations appear in society, people have all sorts of imaginative fears and grand dreams. However, the important thing is how to incorporate them into business as usual. What is important is what strategies will be adopted, both for the company and for the country, based on the assumption that the competing companies and countries will also be trying desperately to master the technology.

Disadvantages of AI

Toyoda: I would like to ask you to talk about the disadvantages of AI. It may be too early to discuss demerits at this stage, but I would like to hear about them from Ms. Murakami, who is in charge of both promotion and safety assurance.

Murakami: I think this is true for all technologies, not just AI. I could list as many bad points as I want to. With AI, for example, it is often said that there is a risk that news and news images produced by a generative AI may induce untruths, or that the company cannot fully control the predictions of the output produced by generative AI, so it may lie and be subject to corporate liability, I suspect. Also, the question arises who would be responsible for an accident that could result in loss of human life, such as with automated driving. I think the list of risks is really endless.

However, there are significant advantages in complementing labor shortages or expanding human activities, so not using AI may in itself be a risk for both companies and individuals' economic activities. I believe that not using AI because you are afraid of the disadvantages while others are using it is in itself a risk of falling behind the competition.

Humans have the greatest fear of what they do not understand, and they tend to estimate the risk as being greater than it really is. Therefore, I think it is important to organize where risks are manifested and what needs to be addressed, and to create an environment in which this information can be understood by people who are not cutting-edge engineers or researchers.

Toyoda: Some have voiced serious concerns from the perspective of employment, social stability, or security. As someone in charge of policy, I would like to ask Ms. Suga to tell us about this. And after that Dr. Matsuo, as a developer and an educator.

Suga: Since everyone is currently experimenting with generative AI globally at the same time, it is very important to learn from each other what kinds of risks others have identified and faced, in addition to the risks that can be recognized by using systems on one's own. We share risk information with various companies in Japan and also globally. In other words, I believe that risk recognition and handling should be addressed in a coordinated manner as much as possible, both among companies and among nations. That is why, as a country, we are taking the initiative and making efforts to create a platform for companies to share risk information, or to issue guidelines for sharing risk information and coping methods.

Matsuo: I think there are various forms of risk that need to be addressed. From a technical point of view, for example, we need to make it clearer what kind of data we are learning from, and there are many technical issues such as how to control and put in a guardrail system to prevent inappropriate output that could lead to danger or discrimination, and so on. I think we need to conduct research and development on such issues.

Appropriate Regulation & Governance

Toyoda: I think this is exactly the kind of research that needs to be done, but then I would like to ask what kind of regulation is good and how should it be governed? I think the government's position is to promote AI from the perspective of maximizing benefits and minimizing risks, but what is generally said is that Japan is relatively reluctant to regulate and is steering clear of excessive regulation. I would like to hear the government's position from Ms. Suga, who is in charge of policy.

Recently, newspapers have reported that the European Union has introduced a bill to comprehensively regulate AI. On the other hand, the Japanese government has compiled the Hiroshima AI Process. I would like to ask you to introduce the contents of each of them and talk about how the Japanese government thinks about governance.

Suga: Regarding governance, Japan was chairing the G7 Summit in 2023 when generative AI suddenly became a hot topic, and Prime Minister Kishida proposed the Hiroshima AI Process as his initiative. This has enabled Japan to acquire an overview of various information on each nation's trials and errors in regulations. This was thanks to the accumulation of contributions made by the

Ministry of Internal Affairs and Communications (MIC) and others to global discussions on AI to date, which helped Japan gain the trust of other countries in presiding over sensitive discussions as the chairing country.

While each country has its own political agenda, it is significant that while reaching a consensus on the fundamental scheme of AI governance to be shared by the G7 in dealing with various arguments, the G7, which is closest to the developers of AI and the largest user of AI, agreed on a direction for using AI with the same sense of values.

In parallel with the Hiroshima AI Process, we also issued AI business operator guidelines in Japan. These are a single set of guidelines that integrate and substantially update those which had been issued by the MIC and the Ministry of Economy, Trade and Industry (METI) from different perspectives on AI, in response to the emergence of a new and powerful AI called generative AI. Considering the discussions in the Hiroshima AI Process, we have created a large network of experts from industry and academia in Japan, and have had numerous dialogues with them, taking care to show the most advanced risk recognition and the most sophisticated ways to deal with the risks.

In preparing these guidelines, more than 100 experts with knowledge of generative AI were invited to join the same mailing list, and a number of discussions among those experts have been held on the basis of the shared information with the joint secretariat of the MIC and METI. The AI Business Operator Guidelines were first tabled for discussion at the AI Strategy Council, chaired by Dr. Matsuo, at the end of 2023, and a finalized version was released in April 2024, taking into account further public comments.

For a country where there are not so many companies on the cutting edge of development, I think we have done well by supplementing the amount of information we have input.

Toyoda: As the chairman of the Strategy Council, Dr. Matsuo, looking at the two positions of Japan and the EU, how do you see the two compared from a developer's point of view?

Matsuo: In general, I think Japan's response to AI is very impressive. The EU has taken a strong regulatory position, and with both the US and the United Kingdom having different agendas, I think Japan is in a very good position to make its presence felt. With the EU taking a strong regulatory position and the US focusing on innovation, I think Japan and the UK are striking a balance. Also, while each country has a strong political appeal aspect to its AI policy, we have to think about how to really make it work for the economy. In this sense, I think Japan is doing very well now.

Toyoda: I would like to ask Ms. Murakami to tell us what the appropriate regulations should be from the standpoint of a company and from the standpoint of a person whose job is to ensure safety. You mentioned that Japan is taking a position between the US and the EU.

Murakami: First, speaking from a corporate perspective, while not using AI is becoming a risk, I believe that Japanese companies are struggling with how to use AI for economic development, as not all companies can afford to have AI engineers.

A situation in which people are allowed to do things completely freely may, on the contrary, encourage fear. Therefore, if there are some guidelines, companies can use AI with peace of mind, because it will indicate that it is not safe to go beyond a certain point. This can be compared to the installation of guardrails.

I think it is advantageous for companies promoting AI to be able to look at their risks not only from their own perspective, but also from a larger global perspective. AI has no borders. Therefore, both user companies and companies that provide technology may have to spend time researching regulations overseas while Japanese companies should also expand globally. It would be easier for companies to do business by centralizing that research rather than having individual companies do it.

Speaking as the executive director of AISI, I too believe that Japan is in a very good position, as you both have mentioned. We will not move to major regulations that would stop innovation while fulfilling guardrails for companies to utilize. In my personal opinion, there is a time gap between when a law is issued and when it is enforced, so if regulations are too inflexible, it will be very difficult to catch up with modern technology. I think the ideal situation is not a law, but rather guidelines showing that the government thinks this way at this point in time, and which are then updated in a timely manner as technology changes. Then both business and academia can provide input for the government on the current situation, so that we can all evolve together.

AISI is working with national ministries and agencies to unify the guidelines, and we are also planning to have many companies that promote innovation participate in the project, so we would like to include input from these companies. In addition to the AISI in the UK and the US, we will also collaborate with organizations in other countries to provide information equivalent to a guardrail, so that overseas developments can be fed back to those businesses that will develop the Japanese economy.

Competitiveness of Japanese Companies

Toyoda: I think the Japanese ideas that you have mentioned will

probably be very helpful to many countries. Next, I would like to ask you about the competitiveness of Japanese companies. It is often said that Japan is behind in the development of information services. I would like to ask Dr. Matsuo, who has been leading the way in terms of AI development and use in Japan, what we should think about the limitations of Japanese companies' activities from the first to the third AI boom to date. Why are they and how we can expect them to be active in the fourth boom this time around?

Matsuo: The premise is that Japan is completely behind the rest of the world in the digital field. Most of the products and services we use are made overseas: Zoom is a US startup, Word and PowerPoint are from Microsoft, and Mac is from Apple, etc. AI is a new digital technology, so we are starting from a place where overseas companies are strong and Japan is not in a position to compete. We need to recognize this starting point.

In this context, I believe we are fighting the good fight when it comes to generative AI. Appropriate measures are being taken, and while the gap has not narrowed, we are not far behind, and the use of generative AI is progressing in Japan. In terms of development, even though the computational resources are not as strong as those of other companies, a large number of developers are working on the development of AI, and at the same time they are taking steps to strengthen their computational resources, and in this sense they are continuing to make the best moves.

The winners in this game will build on their current competitiveness so as to create the next competitive edge. But the strategy of the loser, I think, will be to continue to make the best moves and wait for some opportunity to present itself. I believe that Japan is continuing to make its best moves now, and depending on the situation, when the US administration may change, there may come another time when Japanese companies will be able to grow globally.

Toyoda: I would like to know what Ms. Murakami thinks from the standpoint of user companies and their competitiveness in terms of development and utilization.

Murakami: I also think it is true that Japan is a little behind in the digital area as Dr. Matsuo just mentioned. On the other hand, it is in the area of AI that Japanese researchers and developers have made their presence felt. I have wondered why this is.

I was in R&D at a global company in my previous position, and compared to other research fields, Japanese people were very active and had a strong presence in the language field. American companies are mainly English-speaking. In the case of image and voice, for example, speech recognition is a little different, but when it

comes to semantic understanding, you cannot develop globally without thinking about multilingualism. However, inevitably, native English-speaking engineers tend to do jobs only in English. Meanwhile, Japanese people need to think about doing jobs in both English and Japanese first, not only Japanese. Then, when going multilingual, it will be easier to go to other languages if you understand the difference between English and Japanese. In this sense, I personally believe that Japanese companies have the ability to consider the risk of only doing English from the beginning, which I believe is where Japan can win.

On the other hand, this can also be a risk. When using AI, Japanese companies must always use Japanese, and the fact is that most Japanese users, even for work within their companies, have a hard time accepting tools in English, and therefore cannot use the most advanced in the world. This is how I think there is also a drawback. The fact that Japan is not an English-speaking country could be a strength in terms of competitiveness. But at the same time, there are many Japanese who are not very good at English, which is another area of concern regarding competitiveness.

However, when I look at young Japanese people now, they are not at all afraid of reading English. This is because the technology can translate automatically. Considering the fact that they are able to read a volume of literature in English that was completely unthinkable when I was young, the English barrier has been greatly reduced. When developing AI, Japan, which is what we call a linguistic minority in the world, will have opportunities to find the best moves.

Toyoda: I would like to ask Ms. Suga what are your thoughts on the competitiveness of Japanese companies?

Suga: I think all countries other than the US and China are lagging behind. In digital and platform services, the hegemonic countries are still strong, but Japan is quite competitive in many other industries. So I think there is a strong tendency to view Japan as a failure because it is struggling in digital, but in the digital field Japan is rather fighting the good fight in a difficult situation. I think this is a correct assessment.

Although they are fighting the good fight, many Japanese companies seem to be trying to do everything on their own out of a big-company mindset in order to be strong in the domestic market. If we understand that Japan is in a position where it could become a small country or a country that does not have much, the optimal strategy will change. I think it would be good to see more moves toward defining the field in which we should compete by broadening the scope of our cooperation with domestic as well as international companies.

I think the relationship between startups and large companies is

also a matter of crisis. Large companies often lament the lack of digital talent or AI talent in the country, but such people do not go to large companies because they do not get due recognition. On the other hand, the reality is that those people, because they are in startups, are having a very hard time acquiring resources that would normally be easily available to larger companies. I often wish we could see who has the most essential understanding of the new technology of generative AI and who can serve as a pilot, regardless of age or other attributes. Some of the younger people who are doing well in startups are the ones I wish could be entrusted to head large divisions of a company.

It is a shame that there are both companies that have the resources but cannot entrust them to young people, and people who have the motivation and ability but must struggle to obtain sufficient resources.

International Cooperation in Policy

Toyoda: METI is now beginning to support startup companies, and I hope that we can reconcile these two dilemmas that Ms. Suga mentioned.

As the last part of our discussion, I would like to ask how international cooperation on policies should be positioned, and whether there is any meaning to international cooperation in order to catch up. First of all, Ms. Murakami, please tell us how international cooperation can be positioned for the success of Japanese companies in terms of utilization, and what you would like to see the government do, or what you think companies should know on their own.

Murakami: Borders are disappearing both for companies that use AI to provide services and AI itself as an innovation. Both are expanding globally. Many people in Japan think that they are not good at global expansion, but in fact there are many Japanese companies that are quite active on a global scale, even outside of the well-known companies we are familiar with.

While such companies provide services around the world, the regulations in each country are changing by the minute. We believe that it would be a waste of resources for individual companies to keep track of all of these regulations, even the differences between soft law and hard law, which are changing every minute. In order to update the latest information quickly, I think it would be helpful if Japan as a whole cooperates so that companies provide the Japanese government with the knowledge they have gained and the Japanese government redistributes this knowledge to all the companies. Such mutual support would lead to success for Japanese companies.

I believe that there are competitive and non-competitive areas with regard to corporate activities. Since technology itself is a competitive area for companies, I do not think it is necessary to give out the substance of technology, but information on the situation in each country to deploy it should be shared among companies through cooperation, and in order to protect what Japan should protect, information in non-competitive areas should be shared among companies and cooperation between companies and the government should be promoted. I believe this would lead to the development of Japan's economy and the success of Japanese companies.

Now, comparing Japanese and foreign companies, Japanese companies are very bad at cooperating in non-competitive areas. I used to work for IBM, and I was surprised to find that American companies are not afraid to exchange information with their rivals in non-competitive areas, cooperate with each other, and collaborate with each other in appealing to the government. However, Japanese companies are often reluctant to disclose information to other companies to the extent that they are not in the competitive area. If Japanese companies can improve on this, I believe they will be able to make their presence felt in the world.

Toyoda: I would like to ask Dr. Matsuo to share his thoughts on whether there are any policies that are necessary for startup companies from the perspective of development.

Matsuo: In Japanese companies, the people in charge of various areas do not take responsibility for themselves. This occasionally ends up in failure to achieve innovation. For example, there is a discussion around me right now about whether Singapore's copyright law would apply to the use of cloud computing for AI learning, when the cloud server itself is physically located in Singapore. There is an argument that this would be subject to Singapore copyright law. If that is the case, then we are talking about whether all companies using the cloud are subject to the laws of each country, and which may apply. It is just a possibility, and there is almost no actual risk of that happening, but when you are told that, it makes things harder for the person in charge.

Then, to give another example, there is the question of whether large-scale language models (LLMs) trained with personal information are actually personal information. If it is personal information, the law requires that it must be treated as such, but no matter how removed, the data set may still contain personal information. When asked if all LLMs created must be treated as personal information, the legal experts can only say that this is a possibility. Then in the end, nothing can be done.

It is very important to set a precedent for such a situation and have a legal expert comment in such a way that each person in

charge does not have to take responsibility; for example, that such a decision can be made in such a case, or that a precedent has been set for a project being conducted in the country. I think it is important to arrange it so that each person in charge does not have to take responsibility for any project. I would like the government to tackle this.

Keywords for the Future of AI

Toyoda: In terms of promoting international cooperation, I thought that it may indeed be important to share the arrangement of risks in areas beyond national borders.

Finally, I would like to ask all of you to say a few key words about what is important to link the development and use of AI to the development of the Japanese economy.

Matsuo: I think the current AI policy situation is very good, and I think that means we will continue to move forward.

Murakami: I think it is important for companies to cooperate in non-competitive areas. I believe that cooperation is needed for each company or individual to get through this AI era, as we all have to get through it together.

Suga: I am very much looking forward to the AI Safety Institute, of which Ms. Murakami has agreed to be the first executive director, as I think it has the potential to become a very important and interesting framework among the moves Japan has made. Dr. Matsuo is also going to support the institute, which has the potential to become a center for the smartest possible designs by working together in a coordinated manner in the name of "AI safety".

Toyoda: Thank you very much for your time. I wish you all the best and look forward to working with you in the future.

JS

Written and translated by Naoyuki Haraoka, editor-in-chief of *Japan SPOTLIGHT*, with the cooperation of Tape Rewrite Co.



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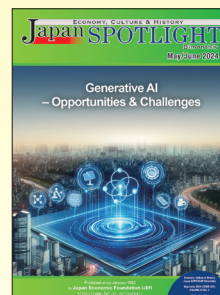
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