

Moving Beyond Merchandise — Japan's Trade in Services —

By Minoru Tanaka

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The question of service trade liberalization encompasses a broad range of fields, from banking and communications to legal services. Indeed, the focus of attention in international trade is shifting from goods to money and services. However, it is admittedly more difficult to establish international rules for service trade than merchandise trade. This is because service trade encompasses such a wide range of concerns, including shipping, insurance, payment of royalties for technology, communications, information services, accounting and legal services.

The liberalization of service trade is essential to facilitate merchandise trade. With the growing weight of services in the national economies of many developed countries, freer international transactions in services, as in goods, are unavoidable. In fact, service trade has expanded at a faster pace than merchandise trade in recent years. Many service industries are expected to continue to grow rapidly in the years ahead.

The wider participation of service industries in international trade is expected to contribute significantly to revitalizing the world economy. Accordingly, the Japanese government is stepping up efforts to liberalize Japan's service trade. The Ministry of International Trade and Industry (MITI) and other ministries concerned are preparing a national study on service trade for presentation to the general meeting of the General Agreement on Tariffs and Trade (GATT) scheduled for autumn. Japan hopes to make a major contribution to the international effort to establish global rules for service trade.

Chronic deficit in service trade

Japan's service exports expanded 240% from 1973-82, from \$6,190 million to \$22,163 million. In the same period, service imports increased 310% from \$10,848



million to \$33,779 million. The share of services in overall trade rose from 15.9% to 16.3% for exports and from 28.4% to 29.1% for imports.

Service trade involves shipping, other transportation, travel, and other private and official services. These comprise a non-trade (invisible trade) balance not including investment proceeds.

Japan's share in world service trade in 1982 stood at 5.0% for exports and 7.7% for imports. The nation's service trade balance has remained in deficit since the 1960s. It widened rapidly after the first oil crisis of 1973, reaching \$11,616 million in 1982. This represented an increase of nearly \$10 billion over 1972, although 1982 marked the first time in five years that the deficit declined.

A number of reasons account for the chronic service trade deficit. The first is the large deficit in shipping reflecting Japan's heavy dependence on chartered foreign ships, as well as the high chartering costs and higher loading ratio of Japanese ships, including chartered vessels. In the latter case, payments by Japanese ships at foreign ports exceed those by foreign ships at Japanese ports because Japanese flag carriers handle more cargoes (both exports and imports) than their foreign counterparts.

Second, payments falling under the category of "other private services"—expenses related to overseas branches and offices, and fees and commission such as agency commissions—have increased in parallel with stepped-up international activities by Japanese corporations. The deficits on office expenses and agency commissions attest to the vast marketing network Japanese companies maintain around the world. These overseas bases are used not only to sell Japanese products but also to purchase foreign raw materials and manufactured goods; they also serve as a "window" for third-country trade. By contrast, foreign firms have lagged in expanding their sales networks in Japan. In 1982, office expenses and commissions accounted for 18.5% of the nation's service trade deficit.

Third, payments exceed receipts by a

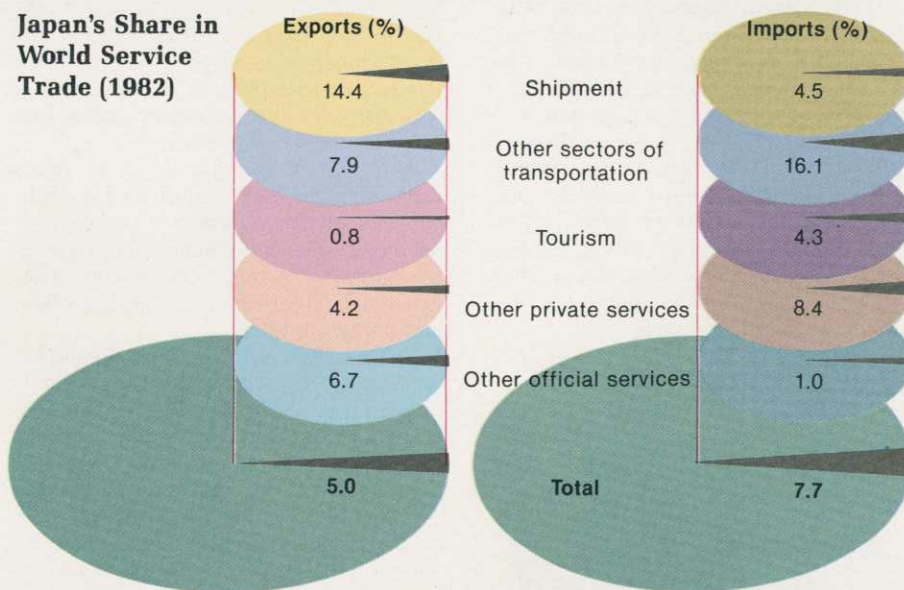
Balance of Japan's Service Trade

(\$ million)

	Fiscal Year (Apr.-Mar.)	Receipts	Payments	Balance
Transportation	1973	4,214	6,343	-2,129
	1982	12,994	16,249	-3,255
Tourism	1973	212	1,386	-1,174
	1982	755	4,096	-3,341
Official services	1973	748	82	666
	1982	2,161	309	1,852
Private services	1973	1,016	3,037	-2,021
	1982	6,253	13,125	-6,872
Investment profits	1973	2,888	2,564	324
	1982	18,016	15,776	2,240
Total	1973	9,078	13,412	-4,334
	1982	40,179	49,555	-9,376
Total (excluding investment profits)	1973	6,190	10,848	-4,658
	1982	22,163	33,779	-11,616

Source: Financial and Monetary Statistics Monthly (June 1974 & June 1983 issues)

Japan's Share in World Service Trade (1982)



Source: Balance of Payments Statistics, 1983

wide margin in technological trade, although the gap has narrowed significantly in recent years. Exports of new items of technology have exceeded imports since 1972, but the balance of payments for patents was \$1,267 million in the red in 1982, or double the figure of 10 years ago.

Finally, the deficit in the travel balance was \$3,341 million in 1982, representing 28.8% of the total service trade deficit. The deficit in the tourist travel balance has widened markedly in recent years, reflecting Japan's higher income level as more and more Japanese take holidays

overseas. The deficit in this category is not likely to drop substantially, although the number of travelers visiting Japan from newly industrializing countries in Asia is expected to rise sharply.

Thus the deficit in Japan's service trade has worsened over the years, in marked contrast to the growing surpluses registered by such nations as the United States, Britain and France. Japan has service trade deficits with every region except the communist bloc. Of the 1982 total deficit, about 25% stemmed from transactions with the U.S. and another 25% from dealings with the European Community.

Services carry increasing weight in the economies and industrial structures of the U.S., Britain and France. A relationship clearly exists between the expansion of service trade and services' greater role in the national economy. The category that has grown most rapidly in Japan's service trade (both exports and imports) is "other private services," which also includes non-merchandise insurance, film rentals, international telegraph and telephone charges, consulting, construction engineering, patent fees and advertising expenses. Between 1973-82, exports of such services expanded 6.2 times while imports rose 4.3 times.

Service trade, including software, has now become the most promising field of trade. In the background is the growing importance of knowledge-intensive industries in industrial structure.

Japan's large deficit in shipping reflects its heavy dependence on chartered foreign ships.



Photo: Asahi Shimbun

Growth of the service sector

Japan's industrial structure was oriented strongly toward heavy and chemical industries in the 1950s and 1960s. This broadened and solidified the production base. At the same time, however, the weight of services in the domestic economy increased, centering on commerce and transport, as distribution improved. The pace of expansion in the service field quickened dramatically in the late 1960s.

By 1982, service sector workers accounted for 54.5% of the total work force compared with 47.3% in 1970. In the same period, the share of the service sector in nominal gross domestic product (GDP) expanded from 50.9% to 58.1%. Of the 6.1 million persons who were newly employed in this period, 72% (4.4 million) were hired in tertiary industries. By contrast, employment grew by only 1.6 million in secondary industries while in primary industries it dropped by 3 million. Production rose 190% in the primary sector, 290% in the secondary sector and 390% in the tertiary sector.

This rate of increase has been much faster than in other industrialized countries. The dynamic growth of Japan's service sector reflects fundamental changes in the demand structure. Service demand has expanded rapidly both at the individual and corporate levels.

The expansion of consumer demand for services reflects a shift in spending priorities from goods to services, such as travel, as personal incomes have risen. Increased leisure time due to the adoption of the five-day workweek by a growing number of companies has also oriented people more toward recreational and cultural activity, while higher female employment has increased demand for food services and other substitute services for housework.

The aging of the population has been another important factor. It has increased demand for medical services and sports activities that contribute to overall physical fitness. At the same time, the growing number of nuclear families has also heightened demand for substitute services

for housework. The diversification of lifestyles is creating new service demands, while the greater number of people with higher education has strengthened the desire for cultural fulfillment, accelerating the growth of education-related service industries.

On the corporate side, meanwhile, the weight of fabrication and assembly industries in the manufacturing sector has increased as basic materials industries decline. This has boosted the role of services in the economy as a whole, as the share of services in total input is higher in fabrication and assembly. Their increasing importance in the production structure has contributed to the expansion of the service sector as a whole.

Stepped-up efforts to supply higher value-added products requires enhanced research and development efforts. This has increased the number of employees in non-production areas and promoted the use of outside service providers such as research institutions.

Progress in office and factory automation by corporations trying to raise their efficiency has also helped services grow. The introduction of robots into factories and computers into offices boosts service-related employment and stimulates the growth of the leasing industry.

Lastly, growing moves by Japanese corporations to strengthen their marketing activities in response to difficult business conditions have led to an expansion in their after-sale service and maintenance divisions, as well as more sophisticated merchandise planning and market research.

These changes in the domestic service market have led foreign service industries to invest actively in Japan. At the same time, outward direct investment by Japanese service industries is also on the rise.

Overseas investment by Japanese service industries

The rising weight of service industries in the Japanese economy and the growth of international service trade encourage



Photo: Asahi Shimbun

Japan's deficit in the travel balance was \$3,341 million in 1982.

direct investment by both domestic and foreign service industries. Direct investment in Japan by foreign service vendors has risen in recent years. At the end of fiscal 1983 the total value of such investment (based on reports submitted by foreign corporations) stood at \$144 million, or 3.5% of aggregate inward direct investments. Cumulative foreign investments in the broadly defined service industry—including intermediary trading, shipping and communications, construction, real estate, and warehousing—topped \$800 million, or about 20% of the aggregate total (figures for investments in banking and insurance are not available).

Meanwhile, direct investment abroad by Japanese service industries reached \$2,717 million at the end of fiscal 1983, accounting for 5% of the total. The share shoots up to nearly 30% when banking, insurance and commerce are included. Reciprocal direct investment by Japanese and foreign service industries is expected to continue to climb as a result of the growing weight of service industries in the Japanese economy.

Unlike goods, services cannot be stored when exported. This is one reason the share of exports in service production remains so much lower than for goods, even though it doubled in the 1970s. International investment exchanges are therefore essential to promote service exports by some industries. Growing international economic interdependence has deepened multilateral relationships not only in traditional merchandise trade but also in investment, banking and other services. It is from this international perspective that the Japanese government is proceeding with the liberalization of domestic financial and service markets.

Toward liberalization of financial and service markets

At a May 1982 meeting of economics ministers, the Japanese government decided to contribute positively to establishing international rules for service trade. In a similar conference in April 1984, the government announced measures to promote the liberalization of the financial and service markets as part of a package of external economic measures designed to further liberalize the domestic market.

In the case of financial market liberalization, various measures were implemented effective April 1984. These included lowering the minimum denomination of CD (certificate of deposit) issues and expanding the issue limit, relaxing standards for residents issuing yen-denominated foreign bonds, and abolishing the real demand rule on forward currency trading.

In the communications field, Nippon Telegraph & Telephone Public Corporation (NTT) is expected to be transferred to private management in April 1985. This will tilt the present communications monopoly toward free competition. Foreign ownership and operation of communications circuits is to be limited to one-third or less of the capital of joint venture companies, while official approval will be required regarding start-ups and charges for the use of circuits. How-

ever, restrictions on foreign operation of value-added data communication and processing networks (VAN) through leased circuits will be substantially eased. In the case of VAN catering mostly to small businesses, for example, foreign entry will be entirely free.

The government is considering liberalizing other specialist services, including a number that have been described as "closed" by American and European critics. Given major differences in customs and legal systems, however, it will be hard to reach quick conclusions in some of these fields. Problems are further compounded by non-economic factors. A case in point is legal services. In the United States, some states qualify anyone who has graduated from a university law department to practice law as an attorney. In Japan, however, one must first pass the national bar examination and then undergo a long period of training. The examination is so difficult that only a fraction of the applicants pass. Nonetheless, the Japanese government is committed to reaching an early settlement that will allow foreign lawyers to practice in Japan.

However it can be very difficult to liberalize service trade involving vital national interests and custom-specific systems.

In the case of the movie industry, for example, Japan imposes no restrictions, legal or institutional, on foreign direct investment. But the Republic of Korea in principle does not allow the import of Japanese movies on the grounds that they would adversely influence South Korean audiences.

Many European countries, meanwhile, are extremely reluctant to liberalize communications, information and data processing. They maintain that the entry of foreign capital could damage national security and violate the right to privacy.

Nevertheless, there is no denying that service trade liberalization is a historical trend. As the world economy evolves, the traditional orientation is shifting from goods toward services. Japan will continue to work to liberalize its service markets, and to participate actively in formulating international rules for service trade. ●