

Japan's Automotive Industry and Its Strategies

By Hamano Takayoshi



Photo: Kyodo News Service

The car talks ended in a tentative accord, averting anti-Japan sanctions at the last minute.

"Of many trade issues that our two countries have dealt with, this one was the most contentious and the most vituperative," Mike Mansfield, a former U.S. ambassador, wrote about the auto negotiations. And, he adds, "In many regards, the auto talks were a model of how not to conduct trade negotiations. (August 16, 1995 *The Daily Yomiuri*)."

In June 1995 Japan and the U.S. finally settled their ongoing wrangle over the automotive sector, averting a dangerous showdown between two economic behemoths who together make up 40% of the world's GDP. However, combined with subtle corollary repercussions on the future stability of the Japan-U.S. relationship, it will also greatly affect Japan's economy through its impact on future strategies adopted by the automotive industry, which, simi-

lar to the electrical machinery sector, has played a central role in propelling the Japanese economy.

These ongoing negotiations were part of the Japan-U.S. framework talks that began with discussions between then Prime Minister Miyazawa Kiichi and President Bill Clinton in April 1993, but even after accords had been reached in other sectors, there were no prospects for a resolution of the bilateral dispute over cars and car parts. Claiming that Japan's market for cars and auto parts was closed, the U.S. eventually announced in May 1995 that it would implement sanctions under Section 301 of the Trade Act if Japan did not open up. After the U.S. imposed a June 28 deadline for the activation of these unilateral sanctions, last minute negotiations resulted in a down-to-the-wire

agreement, heading off the application of punitive 100% tariffs on Japanese luxury car models.

The talks focused on the issue of expanding Japanese car manufacturers' purchases of foreign car parts. The U.S. demanded that Japan provide target amounts for parts purchases, while Japan strongly resisted, for the reason that setting numerical targets would be the equivalent of government-managed trade. In the end, the U.S. appeared to accept Japan's assertions, but in parallel to the closing stages of the bilateral negotiations, Japan's five leading car manufacturers each announced "voluntary" pledges regarding overseas production, among other efforts, in their "Global Vision"

plan. The Japanese government clearly indicated that it had no part in the manufacturers' announcements, but the Americans praised them, treating the Japanese car manufacturers' independent plans as "further reinforcement for the pact and declaration" following the car accord concluded between the U.S. and Japan in August.

Moreover, arbitrary American estimates specified figures for the number of vehicles to be sold in the future. Further, 17 clauses related to objective criteria, including the number of foreign vehicles imported by Japan, were written into the accord to determine the extent to which the contents of the agreement had been implemented. On this basis, the two countries' governments decided to conduct an inspection once a year.

Therefore, despite assertions that numerical targets had been avoided, the car manufacturers' announced moves to implement voluntary plans and targets did not mean that responsibility for rectifying the extreme disparities in Japan-U.S. automotive trade could be side-stepped. Reviewing Japan-U.S. automotive trade in 1994 in this connection, 91,643 American vehicles, a mere 1/13 of the 1.209 million Japanese vehicles sold in the U.S., were sold in Japan that year.

Global Vision plans' orientation

The Global Vision plans independently announced by the five leading car manufacturers when the negotiations had reached the final stages on June 28 provide an idea of the Japanese car industry's future international strategies. One essential point is that overseas production of fully assembled vehicles will be accelerated and localization will be stepped up not only in the U.S., but also in Europe and Asia.

In one of those announcements, Toyota specifically noted its intention to raise the ratio of vehicles manufactured and sold overseas from 48% (in 1994) to 65% in 1998, boosting production capabilities at the plants it now has in the U.S. from 900,000 units in 1996 to 1.1 million in 1998 and establishing a new plant with an annual production capacity of 100,000 vehicles at start-up.

Second, local component procurement would be promoted and special efforts would be made to increase local production of engines, transmissions, and other primary parts. On the assertion that merits of scale could not be obtained without larger lots of parts, these parts had mostly been exported from Japan. Honda announced that it would increase the number of engines manufactured in the U.S. from the current 500,000 to 750,000 in 1998, while Nissan, Mazda, and Mitsubishi all announced organizational restructuring to increase their local parts manufacturing. Nissan has established an "imports procurement team," Mazda a "committee to promote overseas procurement," and Mitsubishi an "overseas procurement headquarters."

Third, imports of foreign-manufactured vehicles and Japanese models made in the U.S. are to be expanded. The manufacturers have thus announced the orientation of their respective overseas corporate activities. Even with moves to implement these measures, however, instant eradication of the substantial surplus in the car trade will undoubtedly be difficult, but with efforts in that direction Japan's car and parts imports will steadily increase, enabling gradual rectification.

However, if further declines in domestic manufacturing accompany these moves, the manufacturers' operations will not only become more difficult; there will be no slight impact on other, affiliated industries.

Ongoing automotive industry slump

Before looking at future Japanese automotive industry developments, let us review the current situation.

In preparation for the biennial Tokyo Motor Show, which will be held from the end of October through early November this year, the manufacturers began announcing a stream of new models from summer. The aim is to capture consumers' hearts with new designs and reinvigorate domestic sales. In the first half of the year domestic car sales showed signs of reverting to favorable growth, but subsequently returned to a stalemate situation in which it was one step forward, one step back. With cloudy prospects for the Japanese economy due to the repercussions from the rising yen, consumers are seen to have become cautious. Nevertheless, because there was a slight correction to the strong yen, the Tokyo Motor Show might serve as the impetus for a different trend in the future.

Domestic sales were greatest during the peak of the "bubble" economy in 1990, when 7.78 million new-model cars were sold. The bubble period was characterized by flat exports in the latter 1980s due to the adoption of "voluntary" restraints on U.S.-bound exports from 1981, so manufacturers concentrated on domestic sales, releasing a succession of luxury models, and a gen-

eral shift to demand for cars with more displacement occurred. This led to greatly increased sales, with 9% annual growth from 1988 to 1990.

However, sales again began to decline with the collapse of the bubble economy, falling to 6.47 million units in 1993. Demand began to recover in 1994 with sales of 6.53 million vehicles, but customers' interest in the outdoors led to burgeoning demand for recreational vehicles and other distinctive models.

On the other hand, the erosion in exports continued, from 6.73 million units in 1985 to 4.46 million vehicles in 1994, 560,000 below the previous year. Because domestic sales were almost at a standstill and exports were falling, automobile production lagged the year before for four years running, from 13.49 million in 1990 to 10.55 million in 1994, a decline of around three million units from the peak.

Reviewing the history of Japan's automotive industry, the continuing pattern has been sales increases in pace with growing incomes and exports compensating for stagnating domestic sales at such times as the two "oil shocks." However, battered by the first recession since the end of the war, domestic sales and exports have both declined for three consecutive years since the collapse of the bubble economy. In 1980 Japan surpassed the U.S. to become the world leader in car production volume, but with the resurgence of America's Big Three in the last couple of years the Japanese share of the U.S. market has fallen and the domestic market has also been sluggish. The automotive industry's investment in plants and equipment has been confined to less than half of what it was during the peak period in 1990-91 and the industry can no longer sufficiently fulfill its leadership role.

A mid-term forecast

So, where does Japan's automotive industry go from here? The point that the car industry will "hollow out" should there be increasing moves to shift from exports to overseas production of fully assembled vehicles is a particular concern. According to the LTCB Research Institute Inc., forecasts of industry conditions through 1999

"Survey of the Automotive Industry" (*Soken-chosa* 38), released in July, Japan's car industry will maintain a certain measure of international competi-

tiveness. It notes that the ratio of overseas manufacturing will increase, but at a few million units in scope will not amount to a major overseas shift, so there will not be much concern about "hollowing out."

In other words, Japanese manufacturers' overseas production capacity of 5.71 million units as of April 1994 will come to 8.07 million by 1999, including the portion added in their Global Vision plans, meaning that 1999's production volume of 6.89 million units will be an increase of 2.03 million over 1994.

As a result, it is estimated that the percentage of overseas production, that is, the ratio of all Japanese cars produced overseas, worldwide, will increase from 31.5% in 1994 to 39.4%.

In contrast, the report says that from now on exports of fully assembled cars will decline by nearly one million, to 3.48 million vehicles in 1999. It further forecasts domestic sales of 7.55 million units in 1999, noting that sales will not recover to their 1990 peak. It forecasts that imports will make up around 4.1% of this figure.

In short it notes that, if only as far as cars are concerned, there should not be much concern about hollowing out leading to spreading nervousness regarding domestic employment. In particular, vehicles fully assembled overseas will not be made with 100% foreign parts even

if more are manufactured overseas. A rough calculation shows that overall production cuts will amount to 1.2 trillion yen over a five-year period because the production of parts to be sent overseas will increase.

Even so, the survey points out that, if overseas production picks up, some parts manufacturers will be able to follow fully assembled vehicle manufacturers overseas, but secondary and tertiary subcontractors who cannot will find business tougher and so will either have to diversify into sectors outside the car industry or will be pressed to restructure drastically.

Certainly, employment has not been affected much whenever exports of fully assembled vehicles have fallen up to now thanks to the allocation of parts for the share of additional overseas manufacturing. Toyota's figures for the period ended June 1994 show that each vehicle exported cost ¥1.42 million, but that the ¥530,000 in sales profits from parts associated with each vehicle manufactured overseas compensated for nearly 40% of each fully assembled vehicle's costs. Even if exports fell by one million vehicles from now through 1999, that 40% would add up to the equivalent of guaranteed sales of around 800,000 vehicles if overseas manufacturing increases by 2.03 million units, so there is not much need to worry about a serious impact.

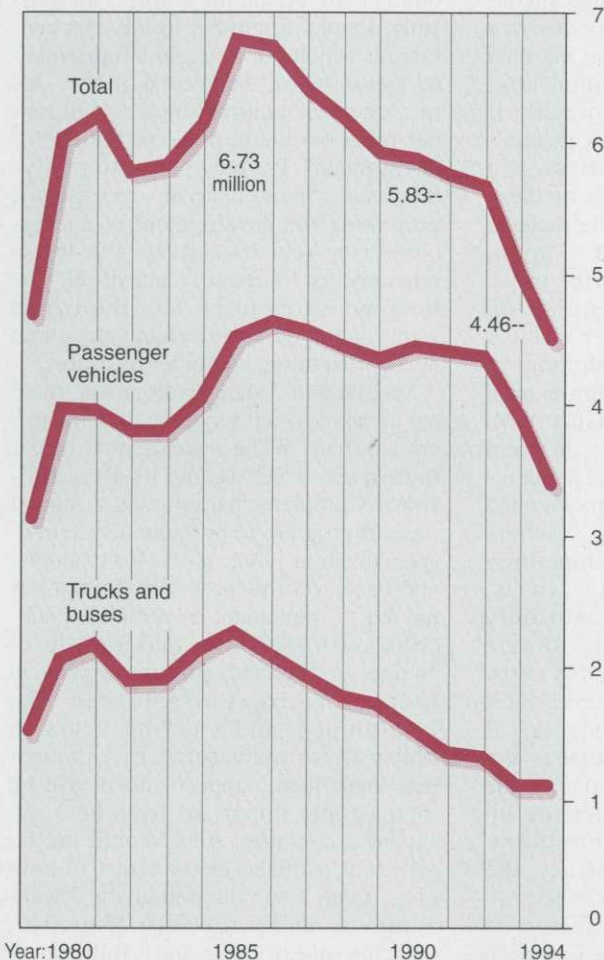
Future exchange rate trends render forecasts difficult and hollowing out could possibly surge with the onset of a strong yen phase in which the yen rises to 80-to-the-dollar, for example.

Future issues

The recession that followed the bubble's collapse has been without precedent in the half century since the end of the war and the Japanese economy has turned in nearly zero growth for three years in a row. Unable to ascertain which way the economy is headed, many corporate leaders also appear to feel as if they have run into a road block. In the midst of this the automotive industry, which has been in the forefront of the Japanese economy up to now, is at an impasse. What should be

Exports of Four-Wheeled Vehicles

Number of vehicles in millions



Year:1980

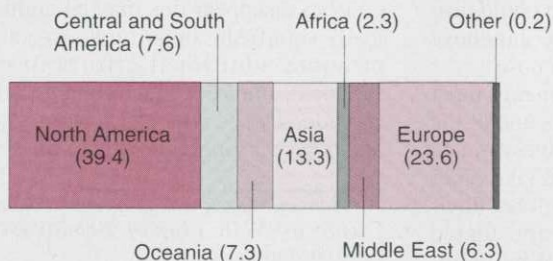
1985

1990

1994

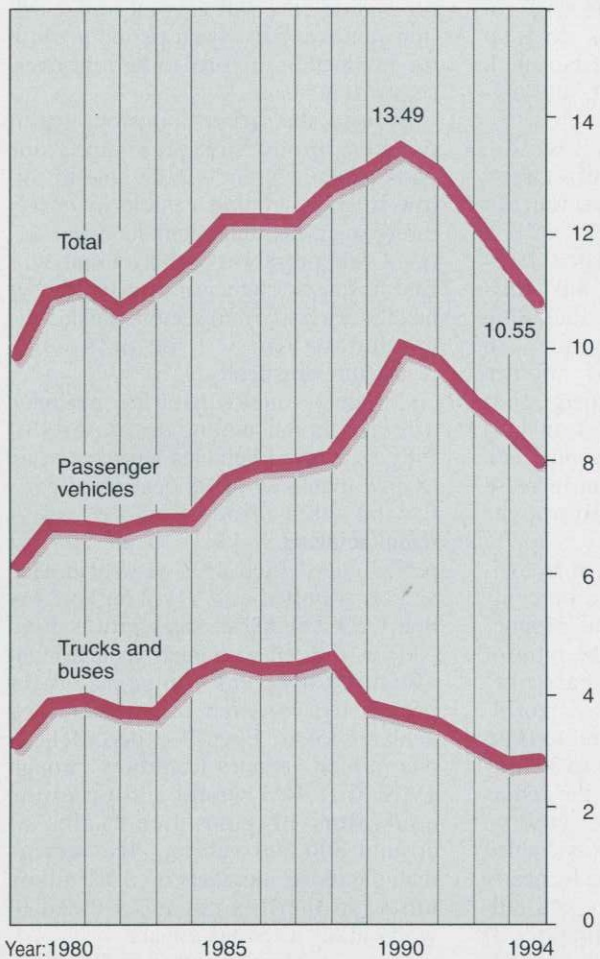
Source: Japan Automobile Manufacturers Association survey

Export Destinations (1994)



Production of Four-Wheeled Vehicles

Number of vehicles in millions



Source: Japan Automobile Manufacturers Association survey

done to restore the car industry's ability to power Japan's economy?

For one, the industry must undoubtedly maintain the intensely uniform competition that served as the basis for its expansion up to now, using it as the driving force for growth into the 21st century.

Initial protectionist government policies and rising income levels in Japan were factors that led to the Japanese automotive industry's success and the establishment of overseas sales networks could also be noted, but the intense competition among the 11 manufacturers of fully assembled vehicles was one large factor not seen in other


countries. Unlike European-style niche manufacturing of different quality vehicles, this was a coequal contest to create the same types of vehicles. In the late 1960s manufacturers sought (now inconceivable) intra-industry alliances because national mergers and capital link-ups were unavoidable if the industry was to challenge the American Big Three, and some of these fell apart after the mergers were agreed upon. However, while those merger and acquisition experiments later resulted in the establishment of links with foreign capital firms, such as Isuzu-GM, Mitsubishi-Chrysler, and Mazda-Ford, each manufacturer firmly maintained its independence, resulting in continued competition among the 11 firms. Manufacturers not only fought furiously to pare domestic production costs, they kept an eye on their competitors' moves and if one moved overseas the others would step up to the challenge by setting up overseas operations themselves, repeating the

intense competition, and this is seen to have been one of the main factors in their growth. Compared to the European example, it is extremely doubtful that, if they had merged into a few companies, they would have seen the success that they have to date.

That cut-throat competition could also be valuable in restoring the Japanese economy's sense of direction now.

Sweeping safety improvements must be made on future car models and at the same time there is an absolute need to reduce exhaust emissions and take other steps to prevent harm to the global environment. Cars developed and tested with those aims in mind will be publi-

cized at the Motor Show, but the question will be how to build them practically, at the lowest cost. Above all, it is thought that a stratum of car-buying consumers will emerge in East Asia in connection with Asian economic growth. The 600 million vehicles now on the road around the world could possibly double in number in the 21st century, at which point urgent environmental measures will be needed, if only due to concern that current models will render it impossible to preserve the earth's environment. We must move to resolve this issue without delay by, specifically, promoting the development of energy-conserving vehicles and cars able to use other energy sources in place of oil, various measures to protect the ozone layer, increased scrap vehicle recycling, noise prevention, and other measures.

Speaking of Asian development, there are areas in which Japanese manufacturers can help in the development of car industries. ASEAN has its Brand-to-Brand Complementation plan, a mutual support program to promote a system of specialization in car parts, for example, and based on this program, Toyota has moved to implement a specialized subcontracting system, making diesel engines in Thailand, gasoline engines in Indonesia, transmissions in the Philippines, and steering gears in Malaysia for mutual use. It is thought that these local support efforts will be increasingly important from here on. Japanese manufacturers should not be reluctant to make every effort to help raise Asian automotive industries' technology to uniform levels. Moreover, vehicles sold overseas must fulfill local customers' expectations and the promotion of local development is important in that sense. As the scars left over from the Japan-U.S. automotive negotiations of 1995 disappear this may be an historically significant opportunity to actively promote additional efforts to open Japanese markets that other countries consider closed and attempt to cooperate locally through globalization. 

Hamano Takayoshi is a news commentator at NHK (Japan Broadcasting Corporation).