Here Come the NICs

By Takashi Sato

Historians may record 1987 as the year in which the Asian NICs—the newly industrializing countries of Asia—began making inroads into the Japanese market.

These industrial newcomers have been mounting an export drive to sell their products in Japan ever since the Plaza Accord of September 1985—an international agreement reached by the Group of Five to readjust exchange rates. The yen has since appreciated sharply against the dollar, making dollar-denominated imports into Japan vastly cheaper in yen terms.

Exports to Japan from the Asian NICs are likely to accelerate in the years ahead. That the change is not already obvious, and indeed, that the trade imbalances between Japan and these countries have shown little improvement, is due largely to the so-called J-curve, which temporarily widens the dollar-denominated trade gap. It is this effect, caused by delays in the self-correcting mechanism of exchange rate adjustment, that is also responsible for the continuing growth in the nominal Japan-U.S. trade imbalance.

But Japan's chronic trade surplus will begin shrinking in due course. And that is when the NICs will have their day. It is even possible that the balance of trade between Japan and the Asian NICs, if not the United States, will be reversed in the 1990s. Japan, ironically, could find itself running trade deficits with its neighbors.

A surge of NIC imports

The yen's rise is not the only factor contributing to the surge of NIC imports. True, these countries now enjoy a distinct advantage in trade with Japan because their currencies have depreciated markedly against the yen. Not a few Japanese products have already lost or are beginning to lose their competitive edge over other Asian products. Garments made in Asian countries are pricing Japanese products out of the home market, with the exception of high-grade items and specially designed fashions. Apparel from South Korea, Taiwan, Hong Kong, Singapore and even China, now dominate supermarket apparel corners.

South Korea is already running ahead of Japan in the volume of new orders for shipbuilding. Until last year, the Japanese shipbuilding industry held the largest share of the world market for new ships. In the first half of this year, however, that position changed, with the South Korean shipbuilders snatching the largest volume of orders.

Garments and ships are not the only Japanese products losing out to Asian products at home and overseas. Asian producers are increasingly taking over from a number of Japan's traditional industries. In short, the changes now under way are part of a historic trend toward international industrial realignment. The appreciation of the yen has only accelerated an ongoing process.

Some of Japan's old-line industries—textiles, shipbuilding, steel, shipping and certain home appliances—were already unable to compete effectively against foreign products even before the G-5 agreement. The yen's surge has only given further impetus to the decline of these industries.

The NICs in Asia have strengthened their underlying international competitiveness as their industrial power has grown both qualitatively and quantitatively. In the past, NIC products fell short of Japanese expectations because of uncertainties about stable supply and quality. Japanese producers, trading companies and distributors were not willing to import such products on a long-term basis.

In the past few years, however, such uncertainties have been greatly reduced, if not entirely dispelled. There has been a marked improvement in the industrial competitiveness of the Asian NICs, while the yen's turnaround has further improved their position in export markets. Thus the sharp appreciation of the yen, coming at a time when the industries in the NICs were already sharpening their competitive edge, was bound to accelerate the influx of their products into the Japanese market.

Videotape free-for-all

The inroads the NICs will make could be heavy indeed. In fact, some of their products are already carving out substantial niches in the Japanese market. A case in point is videotapes made in South Korea. The videotape market in Japan is already saturated, with domestic makers such as TDK, Hitachi Maxell, Fuji Photo Film, Sony, Victor Co. of Japan, Matsushita Electric Industrial waging a cut-throat sales war. Now the price of a tape has plunged to as low as ¥700 (about $4 or $5 at the rate of ¥150/$). Now that South Korean producers have thrown their hats into the ring, the market is locked in a price-cutting free-for-all.

Imports from South Korea are about ¥100 cheaper than Japanese videotapes, and three Korean makers—Sunkyong Chemical, Saehan Media and Goldstar Magnetech—are taking full advantage of the difference. Goldstar Magnetech, the latest participant, began selling its products here in late 1986.

South Korean videotapes are said to be in no way inferior to Japanese standard products. Tapes made by Goldstar Magnetech, for example, have done so well that they have been billed as hit products at major discount stores. Contributing to the brisk sales of made-in-Korea videotapes is the fact that buyers make their choice by price, without much regard for brand loyalty.

Last year, South Korean videotapes claimed an estimated 2% to 3% of the Japanese market. This year these im-

Takashi Sato is a staff writer with the Toyo Keizai Shimpo-sha, a leading publisher of economic journals and books.

ports, particularly standard types, are expected to take 5% to 6% of total Japanese demand, or an estimated 130 million cassettes.

Low-grade audio products such as radio cassette players are also crowding into the Japanese market. Most of these products are assembled by Japanese producers at factories in the Asian NICs for export to Japan. In the case of radio cassette players, an estimated 30% to 40% of the 4.5 million sets sold in Japan now come from Taiwan, South Korea and Singapore.

Japanese audio products makers have made it clear that they intend to import products of lower value-added from the NICs or produce them abroad themselves instead of in expensive Japan. Eventually, their domestic production will be confined largely to higher value-added products such as CD players and high-class component stereo systems.

Sony has long been cautious about importing products made in NICs. Now, however, it is planning to expand purchases of both finished products and parts from South Korea and Taiwan. Aiwa, likewise, is expanding its plant in Singapore and is trying to make full use of its capacity. Aiwa's imports of finished products produced at this plant—from small radios to radio cassette players and pocket-size cassette players—are estimated to reach ¥30 billion in fiscal 1987 (April 1987 to March 1988), exceeding the original estimates for the year of ¥25 billion. Victor Co. of Japan, Clarion and Kenwood all began importing parts and components from Asian NICs in 1985. This year, even more companies have started buying parts made in Taiwan and South Korea.

Shipbuilding companies are also looking to NICs for parts and materials. Mitsui Engineering and Shipbuilding and Ishikawajima-Harima Heavy Industries already station representatives in South Korea. Last spring, Mitsubishi Heavy Industries joined them with a representative office in Pusan.

Develop and import schemes

Another notable development in trade between Japan and the Asian NICs is the efforts of major supermarket chains in Japan to expand purchases from these countries under a "develop and import" formula. Under this formula, companies import products made to their own specifications, and all the products developed in this way are destined for the Japanese market. In fiscal 1986, for instance, Daiei imported ¥57 billion worth of such products, followed by AIC Inc., a joint purchasing firm set up by Jusco and three other retailers, at ¥46 billion. Jusco itself followed at ¥33 billion, then Ito-Yokado at ¥24 billion and Seiyu at ¥17 billion. Each company boosted its imports of these goods by more than 10% from the year before, and the rate of growth is expected to rise even further.

Jusco is the most active company in this field. In May this year, the company began selling large quantities of home appliances made in South Korea. In particular, playback-only videocassette recorders priced at only ¥39,800 (about $270) proved so popular that they sold out in a month. Jusco placed an additional order for several thousand units but could secure only 200 units. The South Korean producer was simply unable to meet the sudden demand. Jusco imports six other products including 14-inch color TV sets and three-door refrigerators, from South Korea's Samsung Electronics. It also sells two appliances imported from Taiwan.

Major supermarket chains have been importing apparel, one of their main commodities, from Hong Kong, Taiwan and South Korea for years. Now, however, they are relying increasingly on develop and import schemes to create fashionable, inexpensive products of their own design. For example, Seiyu is planning to market Thai silk underwear this autumn. The silk is actually Chinese, but it is sent to Thailand for dyeing and sewing. Similarly, Seiyu's alpaca sweaters use alpaca wool produced in Peru but processed in Hong Kong.

Major trading companies are also ac-

Manufactured goods from NICs attract consumers with good quality and low prices.

tive in the fashion field. C. Itoh and Tomen have relocated their main planning and manufacturing operations for garments to Hong Kong. They are using the productive power of the NICs to export finished products to Japan, the United States and other large markets.

Sumitomo Corp. has set up a joint venture company in Japan with West Germany's Otto, the world's largest mail-order house for women's garments. Sumisho Otto, capitalized at ¥1 billion, is now selling such products by mail order. The main line is fashionable garments that the German partner markets worldwide. In Japan, they are imported directly from Otto's manufacturing base in Hong Kong. Garments are manufactured in Hong Kong and other Asian NICs for sale through Otto Group companies in Japan, Western Europe and the United States. While products made in Japan still acount for half of the sales of Sumisho Otto, all products are expected to be imported in the future. In short, Sumisho Otto will become a mail-order company for made-in-NICs apparel.

NIC producers aim for Japan

These examples show how Japanese producers and distributors are taking the initiative to utilize the productive power of the Asian NICs. Yet, as in the case of the videotapes mentioned earlier, there are also growing moves on the part of NIC producers themselves to carve out a stake in the Japanese market.

Cement offers a perfect example. Two years ago, cement imports were virtually nonexistent. In fiscal 1986, Japan bought about 1.5 million tons, or more than 2% of its domestic needs (69 million tons), from South Korea and Taiwan. The volume of imported cement, two-thirds of it from South Korea and one-third from Taiwan, continues to expand. Cement produced in these countries was said to be ¥1,000 to ¥2,000 per ton cheaper than Japanese products, and the price gap has widened since because of the strong yen. South Korean cement in particular can be transported to some Japanese factories for even less than Japanese cement because South Korea is so geographically close to Japan.

Yet even more important has been the steady efforts South Korean cement producers have been making to secure a share of the Japanese market. Many of Japan's South Korean residents make a living by making and selling premixed concrete. These Korean residents are hired by Korean enterprises in Hokkaido and other areas to which cement made in South Korea is shipped. Premixed concrete made in these locales is then shipped to domestic customers through distribution routes also managed by South Koreans. These concerted efforts are now bearing fruit.

At the port of Otaru in Hokkaido there are silos for cement imported from South Korea. These silos, put up by a South Korean producer, supply 5% of the cement used in the region. The Korean product is transported to Otaru by Korean boats across the Sea of Japan. South Korean companies are now expanding their unloading and other receiving facilities and are bolstering their distribution network in Japan. Ssangyong Cement of South Korea, which now has import bases in the Kinki region and Hokkaido, is planning to build two silos in the Kanto area, two more in Hokkaido and one in Nagoya.

Cement imports to the Kanto area are still relatively small because of the inadequacy of import facilities. If such facilities are expanded, however, large volumes of NIC cement could soon find use in this region. Cement imports this year are forecast to reach 2 million tons at least. Their share in total domestic sales is expected to reach 5% within the next few years.

Made-in-NICs goods threaten domestic industries

Japanese steelmakers also face a growing competitive threat from foreign producers. In the past, imports from South Korea, Taiwan and Brazil temporarily dropped after a promising beginning as domestic demand increased as a result of economic expansion in their own countries. Now, however, South Korea and Taiwan have begun expanding their exports to Japan again in parallel with the expansion of their own steelworks. The South Korean steelworks at Pohan in particular are believed to pose a serious challenge to the Japanese steel industry. In 1986, Japan's steel imports reached 2,880,000 tons, or more than 5% of total domestic demand.

Until recently, steel made in the NICs and other developing countries received relatively low quality ratings. Now, however, South Korean makers are seeking approval to use the JIS (Japan Industrial Standards) mark for their products. South Korean steel is likely to make further inroads into the Japanese market in coming years.

Even Japan's automakers face the prospect that cars made in South Korea will someday debut in Japan, although when that will happen is still a matter of conjecture. Small trading companies are already reported to be trying to import the Pony, a small passenger car produced by Hyundai Motor. The Pony has been such a big hit in Canada and the United States that it seems only a matter of time before it hits the Japanese market as well. One hurdle to be cleared by the South Korean maker, however, is how to meet Japanese exhaust gas standards, which are the most exacting in the world. Another question is whether the Pony will be able to compete favorably with Japan's own minicars.

Following in the footsteps of Hyundai in the United States is Kia Industrial Co., which has a tie-up agreement with Mazda of Japan. This year Kia began supplying subcompacts to Ford. In addition, Daewoo Motor, a General Motors affiliate, is also exporting cars to the United States. There is speculation that Kia may be the first South Korean carmaker to expand into Japan.

As for Taiwan, subcompacts built by Yue Loong Motor, in which Nissan has a 25% interest, are likely to start appearing in Japan this autumn at the earliest. The cars will likely be sold by an import subsidiary of Tokyo Nissan Motor, a major Nissan dealership.

Semiconductors made in South Korea are still little known among Japanese users since they claim only a minuscule share of less than 1% of Japan's market. Yet that share is likely to expand in the future, given the high production levels in South Korea. South Korean makers obviously want to expand their sales in Japan as they try to avoid too sharp an increase in the U.S. market share lest they trigger trade friction with the United States. Nonetheless, Samsung Electronics currently turns out 5 million 256K DRAM chips a day, making it the third largest chipmaker in the world after Texas Instruments Japan and NEC.

Another development worth noting is the establishment of a chip design center in Japan by Goldstar Electronics. The move is strategically important in the sense that it is aimed at the Japanese market for applications-specific integrated circuits (ASICs), which are expected to be strong growth products in the years ahead. Clearly, the Asian NICs are serious. They are moving steadily to penetrate the Japanese market, even in areas where Japanese producers have long boasted great advantages over their foreign competitors. This year could well mark a turning point in the history of trade in Asia. ●