The European Union and the Japanese Market

By Dr. Jörn KECK

Times have changed and so has the attraction of the Japanese market for European companies. Twenty years or so ago the feeling was that entering the Japanese market required special skills, stamina and qualifications, comparable to those required of a mountain climber scaling the famous north face of the Eiger mountain in Switzerland. There was an equally strong feeling that Japanese companies entering European markets had it much easier, comparable to the effort required to scale Mount Fuji, which any determined and healthy person can accomplish. Not that the feeling that it is a difficult market for newcomers—not only foreign but also Japanese—to penetrate has disappeared, but over time, market access barriers have been lowered and with them, from the perspective of a European company, the merits of engaging and investing in a commercial presence in Japan have increased.

Merits of the Japanese market

Indeed, there are many good reasons why companies from the EU should be interested in the Japanese market. To name only a few: in Japan, European business has its second largest external market in the world. It is equivalent to two-thirds the number of U.S. consumers. The Japanese market is also rather homogeneous, certainly far more homogeneous than the European single market. It has a reputation for welcoming new products. It is also a market in transition.

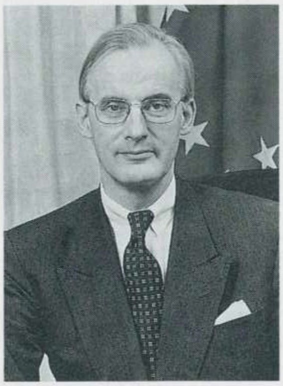
Greater familiarity among Japanese consumers and companies with European and foreign products and the relentless rise of the yen have, over time, led to a significant change in purchasing habits.

In the past, purchases of non-Japanese manufactured products tended to be limited to luxury goods, products with a technological edge built-in, or products otherwise not readily available in Japan. It is gratifying to see how consumers and other users in Japan have become more conscious of, and interested in, the whole range of goods and services that the rest of the world can offer. Strong demand during the years of the "bubble economy" certainly contributed to this. However, the bursting of the bubble and, more recently, the Great Hanshin Earthquake have had an equally great impact on both consumers and industry. Value for one's money rather than conspicuous consumption has become the watchword. Price comparisons, particularly with price levels in other countries, are often made and publicized. Consumers are increasingly attracted to high-quality but competitive products from abroad. This, too, has recently helped European exports to Japan.

From a corporate strategy perspective, a company's presence in Japan also means competing in one of the world's most innovative and competitive markets, a "leading edge" market in many fields. In this sense, Japan presents a challenge to European industry to improve its overall competitiveness. Being able to compete in this sophisticated environment helps European companies stay one step ahead in the world market. Furthermore, many European companies consider a presence in Japan and cooperation with Japanese companies as a stepping stone for further expansion into the markets of North- and Southeast Asia; others see it as part of their global presence. Business relations are stable and reliable. Recent inquiries among European companies established in Japan confirm the experience that Japan can provide good, long-term profit. In fact, some studies argue that the rate of return of foreign direct investment in Japan is even higher than in many rapidly developing countries.

EU deficit with Japan

The usual way to measure the "success," so to speak, of trade relations is to look at trade statistics. While the EU's trade deficit with Japan had shown an increasing trend—in 1992 it reached its peak of US$30.3 billion—it is worth noting that in relative terms this deficit has declined slowly but steadily ("relative" here means the trade deficit compared to overall trade, i.e. the sum of



Dr. Jörn KECK

exports and imports). The other good news is that 1993 and 1994 showed significant decreases in the deficit. In 1994 this was based on a 20% increase of European exports to Japan to a level of nearly US$27 billion. Figures to date on 1995 trade suggest a further increase that for the whole year could amount to about 30% growth. These are most encouraging figures. The sharp appreciation of the yen in early 1995 has undoubtedly helped, but the greater responsiveness of imports to changes in currency values also suggests that the Japanese economy has become more open compared to the past, when exchange rate fluctuations were not always reflected in corresponding movements in trade flows. However, whether 1995 export increases will lead to a further reduction of the EU deficit with Japan is not guaranteed.

Japan's exports to the Union have been picking up in light of the good growth performance of the European economy as a whole. Since there is still a strong imbalance in the mutual trade flows, relatively normal Japanese export increases can, in value terms, outweigh high growth figures in European exports to Japan. On the other hand—statistics on service transactions are not necessarily comparable and definitions are sometimes arcane—the EU seems to enjoy a substantial surplus with Japan, through transport and tourism, insurance and processing services. In 1994, according to Japanese data, the EU achieved a surplus to the order of US$12 billion.

Problems still lurking

The question, then, is whether everything is the best of all worlds, or whether European companies still face problems in regard to access to the Japanese market. The answer to the latter is yes: outside companies do still face problems in access to the Japanese market. In this aspect, though, we find that, fortunately, European views are increasingly shared by Japanese authorities and political leaders, as intensive dialogue and cooperation on the question of deregulation *inter alia* has shown.

The European Commission said in a recent report on relations with Japan that it considers the bilateral deficit with Japan, while it reflects Japan's overall global trading position, unacceptably high. This phrase can be interpreted in different ways, but it certainly means two things: European companies are not doing as well in the Japanese market as they should be and secondly, since Europe is not prepared to accept this deficit, it is ready to do something to reduce it.

The first point, in all fairness, asks for an evaluation showing whether European companies in the Japanese market are prevented from achieving their full export potential. This is a complex question but the EU has at least two ways to come to a view on the issue. The first approach is to look case by case at specific factors that make market access difficult. We have done so over many years and are continuing to do so. The Japanese government well knows the problems and demands regarding European market access as these have been conveyed and discussed at expert levels frequently and in detail.

The process has indeed shown that in a considerable number of cases the Japanese authorities have shared the view that a number of regulations or requirements are unnecessary. Consequently, they have eliminated or modified some.

It is also no coincidence that a considerable number of market access issues also fall under the question of "deregulation," since regulatory barriers, at least as far as European companies are concerned, constitute the majority of specific market access problems. After the European Commission and Japan agreed in an exchange of letters between Japanese Prime Minister Murayama Tomiichi and Commission President Jacques Delors on a dialogue on deregulation in 1994, the EU's first deregulation request list was presented in October of the same year. The Japanese government's deregulation measures of March 1995 dealt positively with more than 40% of our market access requests. Even though this did not fully satisfy our demands, we welcomed this as a step in the right direction.

The official reaction also proved that Japanese authorities and politicians in a number of instances shared the European view that there exist barriers to market entry—for everyone, not only foreign exporters—that need not be there. On November 7, 1995 the Commission presented a further list of deregulation proposals—184 items —which we hope will receive a forthcoming response when amendments to the original package are proposed at the end of March 1996.

The EBC paves the way

In the context of identifying market entry problems in Japan, the EU and, more specifically, the Delegation of the European Commission in Japan, works closely with the European Business Council. The European Business Council is a most valuable partner in the network of support of European business in Japan. Its composition, experience of doing business in Japan and its understanding of Japanese business practices make it uniquely well placed to advise organizations such as the Commission and individual companies. The European Commission will continue to work closely with the EBC, drawing on its direct business experience to help identify and remove obstacles and create more opportunities for doing business in Japan.

The Council of the European Business Community in Japan was established in 1972, under the name of the EC Steering Committee, to promote closer coordination between the National Chambers of Commerce, formalize networking and the exchange of information and to ensure the European business community spoke to the Japanese government with one voice. The EBC is a non-political organization which promotes the interests of European companies and industries in Japan with governmental and business organizations. Major issues can be raised by the EBC directly with the Japanese government on behalf of their member companies and industries without fear of retaliation. A member of the EBC is, together with a member of the American Chamber of Commerce in Japan (ACCJ), represented in the Deregulation Subcommittee of the Administration Reform Board, a leading player in the Japanese deregulation process.

The EBC operates through 28 sectoral committees whose members are professionals in their sectors. Companies of all sizes participate in this committee work, reflecting a wealth of business experience in Japan. Membership now includes more than 1,000 companies. Through committee activities, market access problems are brought to the attention of the European Commission or member states' embassies. They are directly related to difficulties experienced in setting up operations, investing or marketing in Japan and as such relate to specific issues that prevent or hamper better market penetration. Similarly, specific requests that are brought up in the committees by EU member states in Brussels that deal with trade policy issues or in expert groups often reflect company-specific difficulties of market access in Japan.

That approach, however, leaves out of consideration the export potential for companies that have, for a number of reasons, never "dared" to enter the Japanese market. In order to find out where and why European industries or segments thereof are not represented at all, or are under performing in Japan, the European Commission, in close collaboration with the Japanese government, has developed and refined a "Trade Assessment Mechanism (TAM)" which analyzes trade flows between the EU and Japan.

TAM on top of trade flows

The TAM analysis is based on two indicators of market performance. The first compares the performance of EU exports in specific sectors and product groups on the Japanese market with that of other comparable trading partners (the U.S., Canada, Australia and New Zealand). The other compares and calculates the EU's performance on the Japanese market with how the same products perform in the EU. It has proved useful in analyzing trade issues in terms of their relative economic importance to the Union, putting the discussion of these issues on an objective basis and preparing the ground for political decisions taken in other fora. The method is non-confrontational, allowing both sides to join together in an objective analysis of the factors affecting the comparative performance of given products in each other's markets. No preconceived agenda exists; problem areas emerge from objective analysis.

This process has generated a positive atmosphere and created a good communication channel between the two sides. In developing TAM it was agreed to include "success stories" (pharmaceutical goods, leather clothing industries) in the analysis and the possibility of introducing trade in the service industry is now under consideration. The identification of success stories is of particular interest in order to learn about how one succeeds in the Japanese market. It should not be forgotten that the EU has some outstanding successes in the Japanese market. TAM is an important tool in identifying potential trade issues and in analyzing their probable causes. The mechanism works in both directions, and the Ministry of Trade and Industry (MITI) has taken an active role in identifying possible difficulties in the European market.

That leads to another issue: what should be the EU's action to help European companies better penetrate the Japanese market and how can increased exports to this country help to reduce the trade deficit?

One of the answers already given implicity is that the European Commission and member states have over many years, worked to reduce specific problems of market entry. Beyond that we have also looked at broader issues that have a bearing on trade imbalance. This is not because the European Commission takes the view that bilateral trade has to be balanced, because that is not what we believe. What we have been striving for bilaterally and multi-laterally is the maximum free trade possible, free of restraints and impediments.

Competition issues—the degree of enforcement of rules dealing with collusive market behavior, restrictions of competition and dominant monopolistic market positions—have recently come increasingly into the focus of international trade discussions. The European Commission has for some time engaged with Japanese authorities in discussions on competition issues (like those held with the U.S.). These discussions with Japan are now held annually at the ministerial level and also at the sub-cabinet level. The latest of these high-level meetings took place between Commissioner Karl Van Miert, responsible for Competition, and the chairman of the Japanese Fair Trade Commission, Kogayu Masami, on November 22, 1995, followed by the sub-cabinet meeting on November 24, 1995. In the past three years these meetings have also featured a seminar on competition involving companies and experts on competition issues.

It is not by chance that the Japanese deregulation program of March 31, 1995 pointed to the need to strengthen the role of the Fair Trade Commission in competition policy in general as an important means of opening up and reinvigorating the Japanese economy. This is not only to the benefit of foreign exporters but also, especially, to new market entrants from within the country. The European Commission welcomes and supports this approach wholeheartedly. On broad issues, the Commission is engaged in an exchange of views about macro-economic issues with the Ministry of Finance and the Economic Planning Agency. The view that the Economic Planning Agency is taking on sectoral issues in drafting the new five-year plan for the Japanese economy will certainly have a bearing on the deregulation debate and on the further opening of the country.

Export promotion activities

The member states of the EU, including the European Commission, have long since worked with considerable effort to promote exports to Japan. In regard to the Commission, we have been operating a three-tiered program of export promotion activities known as EXPROM, complementary to the export promotion activities of the individual member states, since 1979.

One of the first initiatives under EXPROM was the creation of the "Executive Training Program in Japan" (ETP) which aims to build up a pool of European managers to spearhead the European export drive to Japan. The ETR was established in recognition of the fact that penetration of the Japanese market would be greatly facilitated if there was a pool of people able to speak Japanese with first-hand practical understanding of Japanese society and business. A total of 580 European executives have so far been given the opportunity to participate in this 18-month program, 12 months of which are spent on language training, and six in-house with a Japanese firm which we organize with the help of Keidanren, Japan's leading industry association. This latter feature is one of the most powerful and attractive features of ETP. There is little doubt that this program, now in its 15th year, is one of the biggest successes in our cooperative relations. Many of the graduates stay on in key positions in Japan and use their training to further economic exchange between us.

As the second tier of its export promotion activities, the Commission conducted, after ad hoc programs assisted by European industry associations, a three-year pilot campaign called "Export to Japan." This was completed in late 1993. The second campaign, entitled "Gateway to Japan," was launched in both Brussels and Tokyo in February 1994. Unlike its predecessor, it focuses mainly on capital and intermediate goods. The sectoral approach is flexible and kept under review in light of developing demand in Japan. "Gateway to Japan" promotes mainly midsize European companies' participation in trade fairs in Japan in selected market sectors. The European Commission provides partial financial support and also a range of public relations activities. Trade missions are organized in the same sectors along similar lines.

An important aim of the "Gateway to Japan" campaign is the building of synergies between the export promotion activities of the EU and those of the Member States as well as the import promotion activities conducted by MITI and Japan External Trade Organization (JETRO).

The third part of the Commission's export promotion activities covers sectors that are not part of the integrated promotion campaign. On the basis of incoming proposals, the Commission co-finances activities that are complementary to its general export promotion objectives. These include trade missions, exhibitions and other promotional activities. In addition, the Commission is able to sponsor conferences and seminars in order to facilitate network-building among parties interested in Japan.

Earnest efforts towards mutual interests

One of the positive developments in EU-Japan relations on trade issues is that MITI and the European Commission agreed in 1994 to establish a Trade Cooperation Committee to look at subjects of mutual interest. This discussion not only concentrates on our own markets but also looks at trade in third markets. The Trade Cooperation Committee is a useful forum for stocktaking, discussing new ideas and understanding developments in the thinking of MITI and the EU. It has already been showing its worth by helping to stage European promotion efforts better than would otherwise have been possible. The Commission's activities in the field of export promotion quite obviously only represent a part of the picture. EU member states have their own campaigns and programs.

Equally, specific programs aside, trade and industry ministers from EU member states have come to support trade by their national companies on a number of occasions, accompanied by company representatives that have an interest in the Japanese market. For the Commission, Vice-President Sir Leon Brittan came in June with about 20 European businesspeople to discuss deregulation and market access issues. From the Commission's point of view, the visit was a success and it is considering a further one in 1996.

The dialogue among European and Japanese industrialists through the "Industrial Round Trade Conference" in February and November 1995, contact between *Keizai Doyukai* (The Japanese Association of Corporate Executives) and the European Business Forum in September in Tokyo and the Keidanren mission to Europe in November 1995 have also dealt with deregulation issues. We are convinced that discussions will benefit the further opening up of the Japanese market for European products and investment.

One final word on investment. There is clearly an imbalance in direct investment activities between Europe and Japan. The problem is not so much Japanese investment in Japan. On the contrary, Japanese investment in Europe is welcome. All European member states and many regions and municipalities are actively seeking Japanese direct investment. Indeed, we are concerned that Japan's interest in investing in Europe appears to have decreased. The problem is, rather, too little European investment in Japan. The problems, be they regulatory or relating to differences in business practices, have meant *inter alia* that foreign companies encounter considerable difficulties in mergers with and acquisitions of existing Japanese companies. Deregulation might be only part of the answer and so improve the situation. Too little investment obviously has a bearing on trade and is one of the factors that has slowed down European companies' penetration into the Japanese market.

The above describes the European approach to market access in Japan and was intended to demonstrate two things. First, European governments and other authorities and European companies take the Japanese market seriously and despite all the current euphoria about other markets in Asia they will continue to treat this market as a priority. Secondly, it shows that Europe has chosen the route of discussion based on precise argumentation and cooperation to achieve results. Even if conflicts cannot always be avoided—the alcohol tax issue is such a case—that does not change the basic European attitude.

We expect fair and even-handed treatment. There is often worry that politically significant deals in highly visible purchase areas like aircraft and selected aeronautics products, high-technology products related to government procurement and telecommunications products have often gone to our competitors for reasons we have found difficult to understand. We have been encouraged by a statement of the Japanese government made at the ministerial meeting with the Commission in November 1994 to the effect that the Japanese government did not seek to influence private-sector purchase decisions, which should be made solely on a commercial basis. The government stressed that it wished its private sector not let any political considerations affect its commercial decisions.

It is in this spirit that the European Commission and other authorities of the EU will encourage industry to seize the opportunities the Japanese market is increasingly offering. JJTI

H.E. Dr. Jörn KECK is Ambassador of the Delegation of the European Commission in Japan.