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Plazza Acord and the "explosion" of the Japanese FDI

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Abstract

As the name already states, the present article proposes to analyze the advancement of Japan's FDI, caused by the yen's strong appreciation (after the Plaza Accord-1985). The increasing of the Japan's currency and the disputes with western states, caused by the trade surplus, made the aggressive export policy harder to accomplish. Therefore, they had to find a new paradigm of growth, which could provide a sustained economic development. They tried to expand the investments abroad, which were considered the adequate solution at that time. The aim of this study is to analyze the evolution of the FDI, its allocation by regions/countries, by sectors (manufacturing, nonmanufacturing ones) and also the consequences on the Japanese economy.

Keywords: Japanese FDI, Japanese economy, yen's appreciation, Plaza Accord, Endaka

1. Methodology

Regarding the methodology of the paper, I tried to present two intersecting perspectives. Besides the economic approach, there will be a short reference to the historic one. The economic view, which is the most important and renown, is assisted by the others that are using it to better explain the flexibility and the dynamic character of the Japanese economy, before and after the economic crisis of Japan.

Of all scientific methods and procedures, this article will especially include the analysis and the synthesis. Both have been used to analyze foreign direct investments (FDI) in Japan in the period succeeding the Plaza Accord.

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The interpretation of the charts will be divided in two periods: before the Great Japanese Crisis (1982-1990), and the following years (1991-2013).

Regarding the scientific documentation of this paper, after verifying the sources, I have gathered the data, studied the documents and followed out with the charts for highlighting and making the analysis easier, at the end all these have been used for the draw up of the present article.

2. Literature review

The literature with reference to the Japanese FDI is vast. Ozawa Teramoto, describes in more articles, the catch-up model called the "flying-geese" who supported the rise of Japan,. Regarding the relations with the United States and China are distinguished some empirical studies: Shinji Tagaki & Zhongying Shi wrote about the Japanese investment in Asia (1987-2008) and especially in China; Cheng Saoming created an empirical model to examinte the changes for the Japanese capital because of the reorientation of chinese development strategy to interior area from the coast; Salike Nimesh made a panel to observe the fact that the Japanese FDI in China took a considerable spring.

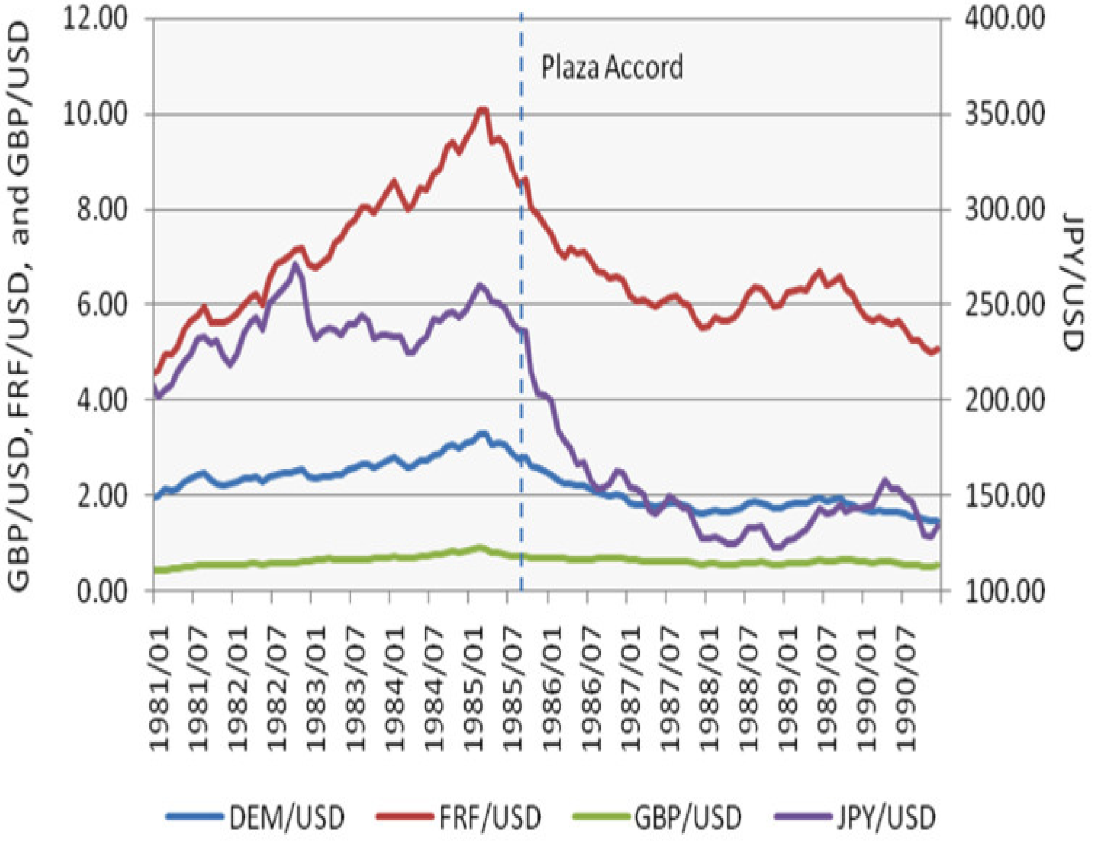
3. Introduction

Shattered to pieces after The Second World War, Japan managed to become in 1968, due to a 10 years plan of doubling the national income (achieved in 7 years) the third world economic power. After only five years, the country hit another obstacle: the first petrol shock. The fast pace of the petrol's price growth (from 2,18 dollars in 1971 to 11,65 dollars in January 1974) drastically affected Japan's economy, who was a great consumer of such resources. The Japanese quickly realized that they had to adapt and acted accordingly: Japan started to give up on the great industries, starting to specialize on those with a higher added value, achieving better economic performances than other developed countries.

As a consequence of the first oil shock, being poor in natural resources, the country's imports bill grew exponentially and the Japanese market was close to saturation, the only option left was to take by storm the external markets in order to succeed in equilibrating the commercial balance sheet. Outside the border sales grew significantly (for example, if at the beginning of the '60s Japan was exporting 7.000 cars in 1980 the country was exporting 3.9 million cars) and Japan's burst could not be stopped by the commercial partners who's deficits grew deeper (the ratio between the U.S. and Japan was over 50 billion dollars in 1986).

The remarkable performance achieved by Japan in "its golden decade of exports" could not let the powerful western countries just sit by, as they saw their economic growth being threatened, they had a constantly increasing unemployment rate, an amplification of mass pressure, etc. Thereby, the middle of the nineteenth century would bring the signing of the Plazza agreement, and with it, Endaka, representing a significant appreciation of the yen.

As we can see in Figure 1, if at the beginning of 1985 one U.S. dollar amounted to 260 yen, its value soon dropped towards 130. Therefore, with a doubling of the value of the yen, Japan suffered in terms of competitiveness, and moreover, it had to deal with an extremly important aspect, namely the " self-limiting of exports". Subjected to significant pressure from the Western countries, the Japanese archipelago had to accept a more limited export of cars to the United States and Europe (specifically France).



Source: http://www.research.stlouisfed.org/fred2/series/STLFSI/downloaddata?cid=3457

Fig.1. Exchange rate evolution of the dollar, compared with the yen, the French franc, the German mark and the British pound: 1981-1990

After initialing the agreement on the "voluntary restraint" of exports mentioned in the previous paragraph, a resigned Seiichi Yamashita from Keizai Doyukai (Japan Committee for Economic Development) stated:"We are at a turning point. Our partners in the United States and the Common Market give increasingly harsher criticism on the expansion of our exports, showing that we are creating difficulties for them in balancing the payments balance and in unemployment absorption. We must now adopt another strategy where the primary focus shifts from exports of manufactured goods to exports of capital and technology towards developed countries".

Therefore, the Japanese dignitary announced Japan's entry into a new era: one of capital export and of direct investments abroad using a comparative advantage recycling to attempt an industrial and market recycling. Accumulated capital surplus at the time, coupled with the appreciation of the yen, allowed the Japanese to overcome the tariff and non tariff barriers imposed by Westerners, by implanting production units precisely in this region of the globe.

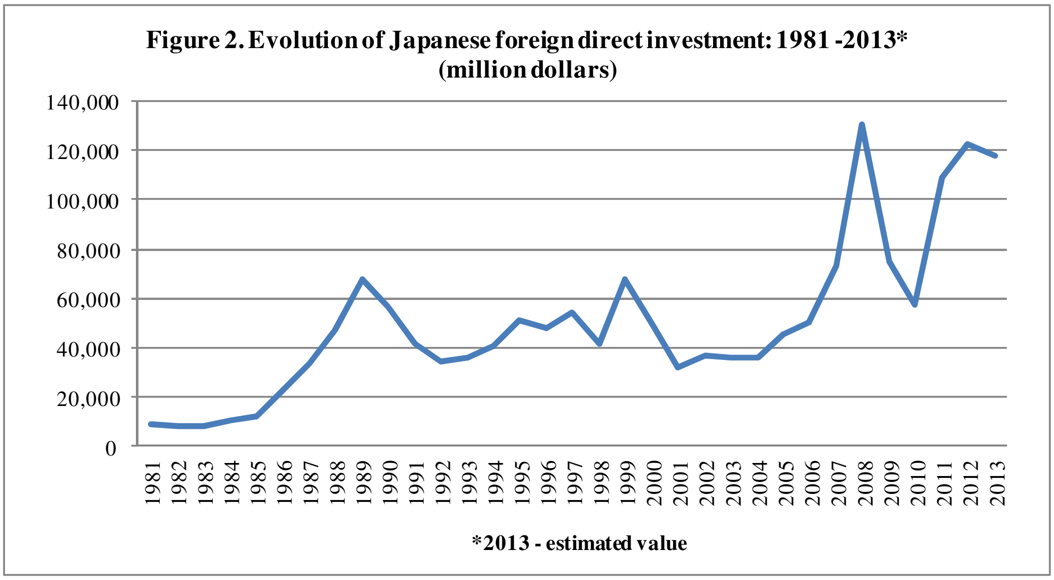
Besides this advantage, this decision granted Japan three more benefits: first, it increased its financial benefits, second, it maintained its ethnic and cultural homogeneity by not importing immigrants to work in their country, and third, it compensated for the reduced surface of the territory (Gibney, 1996, 135). Regarding the stages of Nippon foreign direct investment, as Ozawa Teramoto (Teramoto, 2001, 4) showed, they passed through several stages: searching for low wages, discovering resources, components, accessories, seeking alliances.

The goal of the Nippon companies was to maintain their market shares, even if they could not export. With the help of FDIs, they were producing directly in the markets where they were installed. In general, the Japanese market was trying to produce inside the borders; and the "outside" production was therefore the programmed extension of the one within national territory.

As shown in Figure 2, we can observe that after a relatively linear evolution in 1982 - 1985, 1986 brought a boom in Nippon foreign direct investment, marking a relative increase of 82.67% over the previous year. 1987 followed the same trend, marking a relative increase of 49.48%.

This was the annual relative increase margin of Japanese FDIs, until 1990, when, as a result of challenging imbalances in the Japanese archipelago, it started to follow a negative trend. In 1985-1989 foreign direct investment registered an increase of over 450%, thus confirming the new era Japan was entering. Japanese transnational had the highest rate of global investment in '90s. We can note, as Shinji Takagi and Zongying Shi concluded (Shinji & Zongying, 2011), the Japanese FDI to Asia was very little affected.

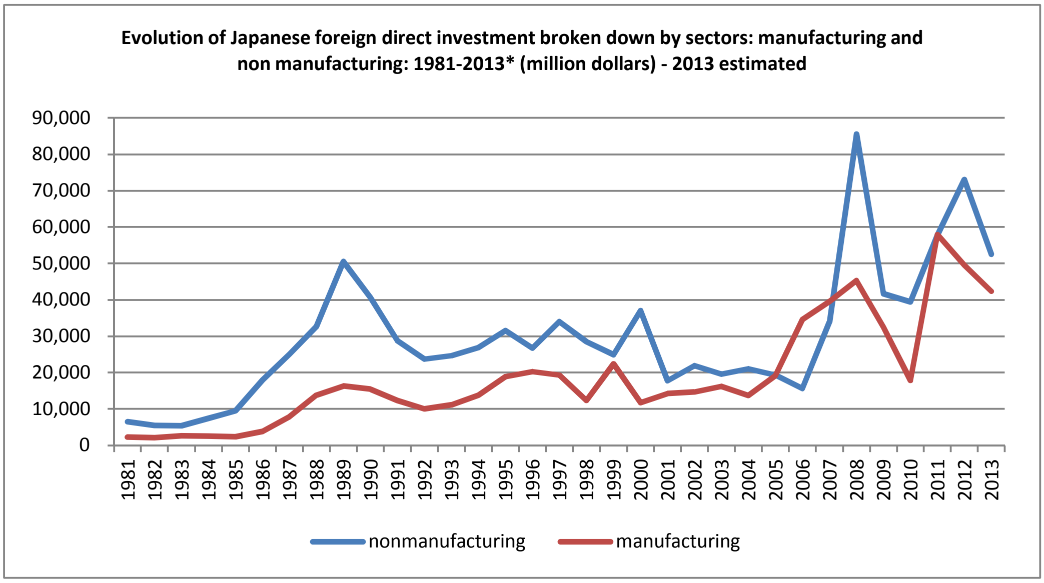
With the beginning of the Japanese crisis one can observe a decrease of Foreign Direct Investments that lasted more than a decade, this trend reversed only in 2006 (surpassing the level of FDI in 1989 only after 17 years). The subprime crisis's consequences can also be seen at this chapter, in two years the amount assigned to the FDIs lowering with almost 60%, than a change of scenery can be seen.



Source: http://www.jetro.go.jp/en/reports/statistics/

Fig.2. Evolution of Japanese foreign direct investment: 1981 -2013 (million dollars)

4. Japanese foreign direct investment by industry



Source: http://www.jetro.go.jp/en/reports/statistics/

Fig. 3. Evolution of Japanese foreign direct investment broken down by sectors: manufacturing and non manufacturing: 1981-2013* (million dollars) – 2013 estimated value

Figure 3 shows the fact that the nonmanufacturing sector took a considerable spring, growing with almost 1000% in half a decade, before The Great Japanese Crisis. Same aspect can be noticed before the subprime crisis, when between 2006 and 2008 the FDIs grew with almost 500% almost like a premonition that something was about to happen in the world of international finances. These aspects are not to be neglected and they say a lot about the role of financial speculations regarding economic crisis outbursts. In 2011, as a consequence of the international financial cool off, the foreign direct investments in manufacturing softly exceeded the nonmanufacturing ones.

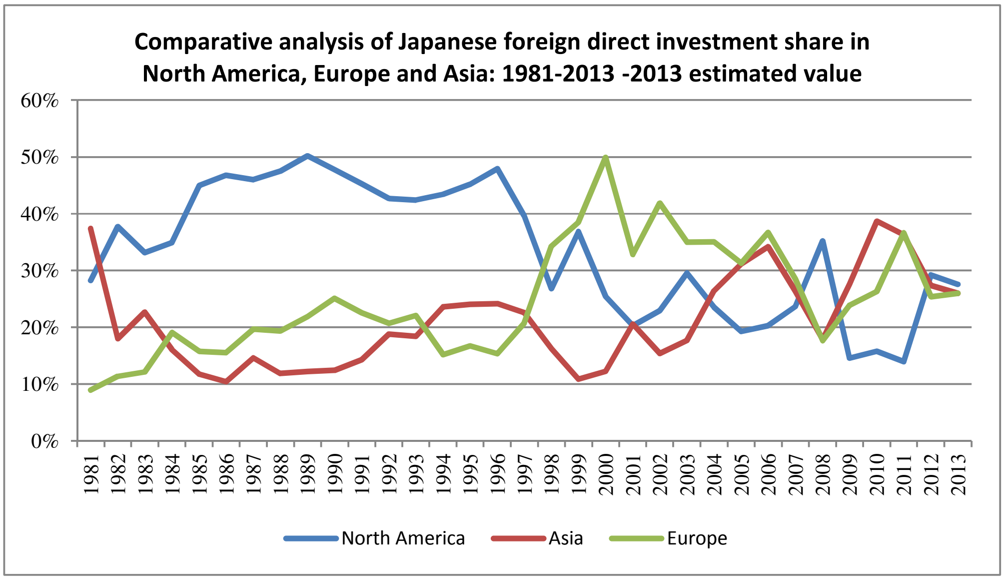
The manufacturing sector had a growing course until 1989, maintaining almost the same level until 2004, than started an accelerated growth until the outburst of the economic crisis.

5. Japanese foreign direct investments by continent / country

As shown in Figure 4, and as expected, Japanese investments were mainly directed to the North American continent, their share ranging between 40-50% of total in 1985-1990. The second destination of Japanese capital was the Old Continent, with a share of 20%, followed by Asia. Thus, a series of Japanese products “made in USA”,”made in Germany” etc., appeared on the market.

After almost two decades in which the North American continent represented the main partner Japanese investments would go to, this tendency changed at the end of the 90s, Europe taking its place. Japan focuses its attention on west European markets.

As we can observe in Figure 4, of the three main partners only Asia’s share was decreasing, which shows that most of the financial resources were directed towards North America and Europe, who had imposed”voluntary restraints”, and where they had to produce in order to maintain their market shares; therefore, the share of both continents was maintained, with a continuous growth during the studied period.



Source: own calculations by http://www.jetro.go.jp/en/reports/statistics/

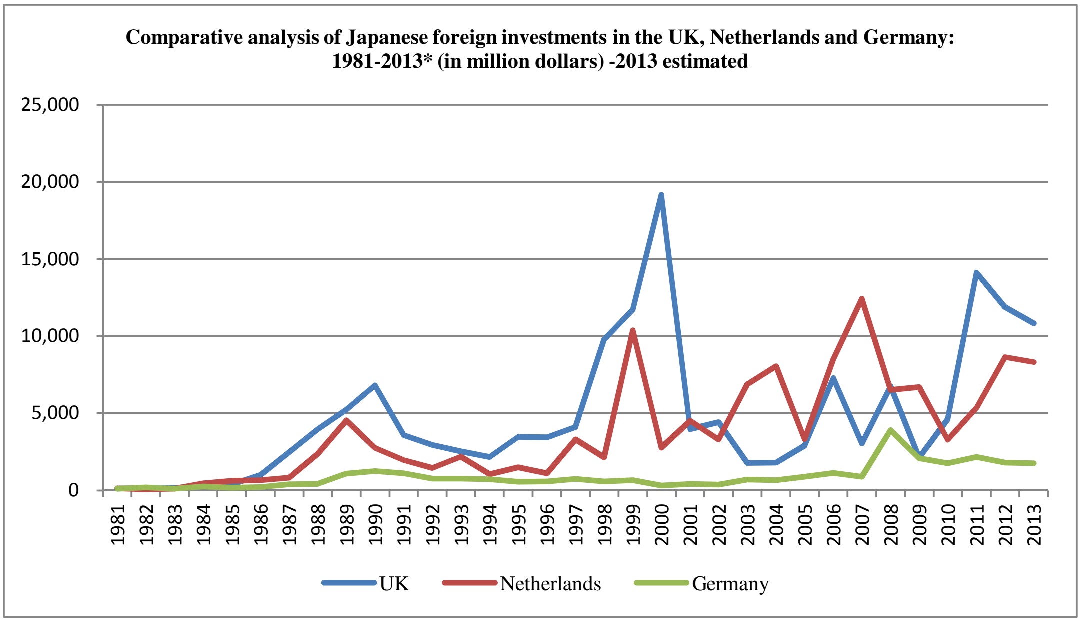
Fig. 4. Comparative analysis of Japanese foreign direct investment share in North America, Europe and Asia: 1981-2013* -2013-estimated value

Regarding the Asian partners, these have occupied the third position in Japan’s FDIs top for almost the entire analyzed period of time. The cheap labor force found in the neighboring countries was losing its appeal, as Japan was rather searching for strategic partnerships or maintaining markets which were obtained with difficulty and which generated important profits. Moreover, a very rapid financial expansion would have been frowned upon in Asian views, who were already remembering the Mutual Prosperity Area before World War II.

With regard to the evolution of Japanese FDIs in North America, it practically merges with the United States, which has a share of 95-98% of the total FDI in the continent. Japanese economic surpluses were channeled toward this country and at some point it seemed like Japan was trying to buy the whole. Investments were directed towards all sectors, but the large amounts were channeled towards the financial world, and Japan became the second largest external player (after Great Britain).

A more detailed analysis of Japanese FDIs directed towards Europe shows that the main destinations in 1981-2013 were, in order, Great Britain, Holland and Germany.

Generally, the financial resources directed toward the first two countries represented financial investments (30% of loans in the UK were provided by Japanese banks), while in Germany the amounts were directed towards the manufacturing sector, particularly towards the automotive industry.



Source: http://www.jetro.go.jp/en/reports/statistics/

Fig.5. Comparative analysis of Japanese foreign investments in the UK, Netherlands and Germany: 1981-2013* (in million dollars) -2013 estimated value

Regarding the Asian destination for Japanese FDI, we can find the main partner countries in Figure 6. They would relocate the industries with low added value in Japan that were renounced since 1985. It concerns in particular the textiles, shoes and so on industries, because of the cheap labor force available in these countries.

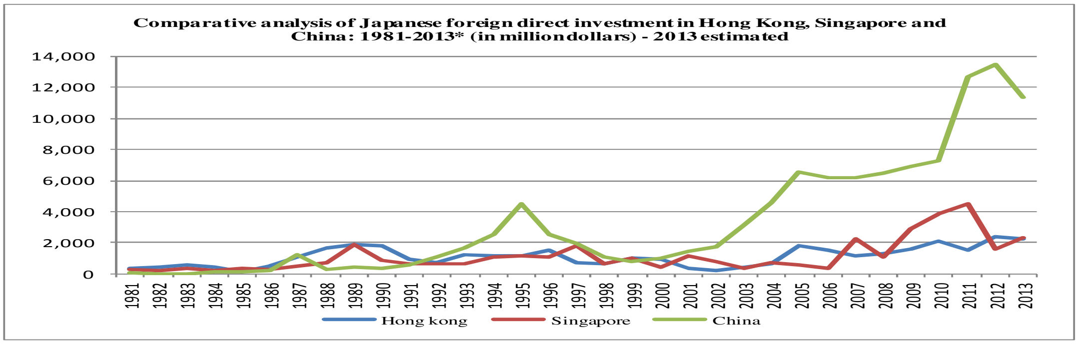


Fig. 6. Comparative analysis of Japanese foreign direct investment in Hong Kong, Singapore and China: 1981-2013* (in million dollars) 2013 - estimated values

We can also notice the rise of foreign direct investment in China, after "the opening" of this country. From 226 million dollars in 1986 the amount of 165 million dollars was reached in 1990 and to 13500 in 2012.

“China effect” (Salike, 2010) was a win-win situation for both countries: Japan would take advantage of the cheep work force and of the close geographic position to China, while the second would develop with the amount of money that came from the Japanese (for more information see (Shaoming & Stough, 2006), (Cheng, 2008)).

6. The evolution of Japanese economic growth between 1981-2013

At an economic growth level, Japan has felt the Endaka shock in 1986, until it managed to devise a new strategy, posting an advance of only 2.5%. Afterwards followed the years of 1987 and 1988 that brought more than satisfactory figures of over 4% respectively over 6% growth. In 1989 and 1990 the growth level went up with almost 5% (http://www.stat.go.jp/english/data/chouki/03.htm).

When analyzing Japanese growth in the above mentioned period it is interesting to also note its performance relative to other economies. Japan registered an advance of nearly 50% than both the United States and Great Britain, which once again demonstrates the power of the Japanese archipelago on that period (http://databank.worldbank.org/data/views/reports/tableview.aspx).

Due to the crisis at the end of the 80s, Japan could no longer achieve the economic growth it used to after the second World War, on the contrary alongside the recessions the country struggled with, by the end of the 1990-2000 period, it had an average growth rate of only 1%, this period being called by many “the lost decade”. In 1996 when Japan shown signs of a positive comeback the country got struck by the 1997 Asian Crisis. The beginning of the third millennium did not bring great changes, financial improvements could only be seen in 2005-2006, but shortly after the subprime depression came out fatally injuring the Japanese economy (a 5% decrease in 2008). This was the first time, since the World Wars, when Japan could not adapt and was unable to produce significant economical increase (http://www.stat.go.jp/english/data/chouki/03.htm).

7. Conclusions

After the World Wars, the Japanese economy was able to cope with all challenges, proving itself to be adaptable and dynamic. Same thing happened when due to the signing of the Plaza agreement and the significant appreciation of the yen, Japan was losing its export competitiveness which helped her succeeded so amazingly in the decade before. If we add to this the decision to "restraint" the exports, the only solution the Japanese had at that time was to increase the FDI, the value of which increased by over 450% only between 1985 and 1989.

In terms of distribution by industry note that throughout the period under review the non-manufacturing system has exceeded the manufacturing one, but the number of the latter one increased rapidly by almost 600% in just 4 years especially after the Plaza agreement; And so the production in markets where products are consumed has began.

By analyzing the distribution of Japanese foreign direct investments by regions, we note that the amounts allocated to the North American continent (which absorb roughly half at global level) have grown exponentially, the amounts allocated in 1989 being more than 5 times larger than the amounts of 1985. The following partner was represented by Europe, absorbing more about 20% of the total Japanese worldwide investments and who registered in its turn an increase of over 600% in the above-mentioned period. We can note that it is on these two richest continents, where the Japanese ware faced with a multitude of export barriers, that they decided to prodoce, directly on the territory of the consumer states. While there they were investing with the aim of maintaining or increasing the market shares, in Asia (the third Japanese partner), the main goal was to seize raw materials, but also to use the cheap labor force.

As we have seen, in regard to economic growth, although affected during the year when the Plaza Agreement was signed, Japan was able to overcome this impediment, recording a net advantage over other international powers, such as the United States or Great Britain. Thereby, Japan was able, for the thrid time in the postwar period, to transform a disadvantage in an advantage.

Unfortunately for Japan, after an economic period when the country seemed to be taking over the world, starting with the late 80s crisis, it got into a shadow in which it seems to be struggling up to this day, without being able to pull itself back into the light. Due to the unfavorable international environment (the 1997 Asian crisis and the 2008 world crisis) Japan does not manage to find the key to resolve the problems of its economy. If between 1952 and 1989 the country represented the ideal example to follow, regarding economic accomplishments, after this period Japan embodied the incapacity of development.

I want to notice also the fact that the nonmanufacturing sector took a considerable spring, before The Great Japanese Crisis growing with almost 1000% in five years. This aspect can be observed also before the subprime crisis, when in only 2 years the FDIs grew with almost 500%. Those show the link between financial speculations- economic crisis outbursts and could be an indicator who can help us to detect new crisis.

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