Can Anyone Compete with China? Lessons from Japan

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By Eamonn Fingleton

[*This article by Eamonn Fingleton exemplifies the "Japan as Number One" genre, a type that has become such a rara avis in recent years that it seemed virtually extinct. The conventional wisdom among international economists as well as Japanese neoliberals, is that Japan is washed up and has to learn from America. Using Japan's trade with China as an example, Fingleton raises compelling questions about the failures of American industrial and trade policy.*

Even though the idea that America is the "global standard" is now rarely voiced explicitly in Japan and by globetrotting boosters in business management elsewhere, the belief that what are deemed to be American ways of doing things have simply proved far better than Japan's still underlies much thinking on how Japan should reform its economy. So an article that goes so deliberately against the grain is worthy of notice in part for scarcity value alone.

We cannot confirm whether Fingleton is correct in claiming that Japan is deliberately and skillfully leveraging surplus Chinese labour by transferring low-tech production there and upskilling at home. Certainly Japan's trade surplus is as high as he says it is at a time when the U.S. is awash in debt, and it is also true that Japan runs a trade surplus with China that is the envy of Washington. But if the author has the evidence to show that these results are in large part due to a business and bureaucratic elite that still effectively manages industrial policy, one that puts the needs of the country as a whole over the short-term economic rationality of a given business, it would be important to present it. It seems difficult, though, to square that image of *effective government-led cooperation with credible challenge. Japan Focus reports that the old MITI (now METI) is searching for a role in the wake of losing most of its clout. Fingleton relies too much on a thesis of subterfuge to explain why what appears to be the case is actually virtually the reverse.*

Moreover, if Japan is in fact handily using China's cheap and abundant labour while upskilling its own, then one wonders why there is still high unemployment as well as growing numbers of part-time workers and a widening income gap. Since Japan's population seems already to be entering a period of contraction, and is undeniably producing fewer and fewer young workers, one wonders why the demand for labour isn't strong, in fact white hot. We should not see diverging incomes and declining skills among large numbers of workers in Japan nor should Japanese intellectuals be telling us that much of the Japanese corporate sector is cutting costs by deskilling production and retrenching on lifetime employment. These observations in rebuttal do not, of course, prove that Fingleton's argument is simply wrong or even greatly exaggerated. But they do suggest that we need to look for evidence that Fingleton did not supply as well as consider contrary hypotheses that he chose not to challenge. Japan Focus

Americans believe that the United States is in good company in being hollowed out by China. After all Japan is also suffering badly from Chinese industrial competition -- or so the American press reports. Actually Japan's trade strategy sacrifices neither workers nor high-tech leadership. For more than a decade now we have been told that the world's most advanced economies face a common fate in this era of Chinese economic expansion: massive layoffs in manufacturing and ever-rising trade deficits. Indeed, if American press reports are to be believed, Japan has even more to fear from the Chinese economic threat than the U.S. Supposedly, key Japanese industries such as electronics are being rapidly eviscerated by low-wage Chinese competition. Such reports, suggesting that there is something inevitable and inexorable about the decline of manufacturing in advanced nations, have served powerfully to tranquilize American public opinion at a time when America's trade deficits have gone from merely horrendous to truly disastrous.

It is past time these reports were exposed for the propaganda they are. No nation's trade position has suffered as much from

China's rise as the United States. Quite the reverse. Many of America's key economic competitors have, on balance, strongly benefited from China's industrialization. Of these the most notable example is, oddly enough, Japan.

Consider this little publicized fact: Japan's current-account surplus last year totaled $181 billion. This was a record for any nation in world history. It was more than 2.5 times China's 2004 current-account surplus. More to the point, it was three times Japan's surplus of 1989, the peak year of American concern about Japan's "juggernaut" trade policies.

The truth is that Japan has closely co-operated with China's desire for export-led growth yet it has found ways of doing so that also boost its own exports. Hence another rather significant unpublicized fact: Japan exports more to China than it imports. Its surplus with China in 2004 ran to nearly $14 billion, up 17 percent from 2003.

Just as in the case of the United States, outsourcing to China has played a major role in corporate Japan's production arrangements in recent years. There the similarity ends. Unlike the United States, Japan believes in managing its trade. Although Japanese officials recognize that consumers can benefit from trade, they also recognize that people need jobs and incomes before they can consume. Thus where imports might pose a significant threat to Japanese jobs, the Japanese government works to minimize the damage.

Besides influencing the pace of outsourcing, Japanese policymakers ensure the trend does not entail the leakage abroad of the nation's key production technologies. Thus individual corporations are not permitted unilaterally to transfer advanced technologies to foreign operations.

If this seems impossibly complicated to administer, it isn't. Much of the control stems semi-automatically from Japan's distinctive labor regulation. In principle, employers are foresworn from making layoffs. This principle is applied flexibly: exceptions are permitted in the case of struggling small firms as well as corporate dinosaurs in near-terminal financial difficulties. But as a practical matter, layoffs are not an option for any healthy mainstream Japanese corporation.

Whereas American chief executives are much concerned with pandering to the whims of securities analysts, a typical Japanese chief executive is necessarily focused on long-term production planning. His principal concern is to create new and ever more productive work for his Japanese colleagues at every level, not least the newest recruits who can be expected to be on the payroll 30 years hence. To this end, he will make sure that, among other things, the corporation spends heavily on research and development.

He will also probably try to focus this spending mainly on developing efficient new production technologies, which provide a much more lasting benefit in terms of secure long-term jobs than, say, designing new products.

All this means that a Japanese chief executive's attitude to outsourcing will almost automatically be closely aligned with the Japanese national interest.
Because he cannot easily shed labor at home, he will move production activities abroad only after he has lined up new and better work -- either more capital intensive or more know-how intensive or both -- for his domestic workers.
By way of example, a Japanese television manufacturer might move assembly operations to China only after redeploying its domestic assembly workers to make liquid crystal displays. This latter activity can be at least 10 times as capital intensive as assembling television sets.

As a practical matter, in the early stages of the trend for American corporations to outsource to China, Japanese corporations held back. But lately they have caught up and now outsource almost all routine assembly work. For both Japan and China, this is win-win. In a textbook illustration of the principle of comparative advantage, Japan does the capital-intensive work supplying high-tech components to China's low-wage assembly plants. The net effect has been a huge increase in global output of everything from mobile phones to game machines -- with a resulting benefit to the world's consumers in ever lower prices and ever greater functionality.

In geopolitical terms, the result is that Japan is now far more securely in the lead in advanced manufacturing than it ever was in the late 1980s. This does not show up in American trade statistics because much of what Japan sells to the United States these days comes via final assembly plants in China and thus is counted for American statistical purposes as "Made in China."

While Japan is the most spectacular example of a nation that has secretly leveraged Chinese industrialization to the advantage of its export industries, it is hardly alone. This should be obvious from the fact that China's surplus with the United States exceeds its surplus with the world as a whole. In other words, while China is a huge net exporter to the United States, it is actually a major net importer from the rest of the world.

It is fair to say that, in common with Japan, many of the world's other advanced manufacturing nations are using China as an export pipeline through which to sell to the United States. It is also fair to say that, not for the first time, Uncle Sam is being treated as the world trading system's ultimate patsy.

Why isn't all this better understood? A key factor is the Washington trade lobby. So skilled has it become in spinning the story that it has succeeded in pulling the wool over the eyes of countless analysts at supposedly independent think tanks.

Another factor is the perennial naivety of American foreign correspondents. The problem is particularly acute in Tokyo, where the local English-language press functions shamelessly as the Japanese Foreign Ministry's propaganda arm. The message in recent years has been that Japanese industry is almost ludicrously dysfunctional -- and therefore is quaking in its boots at the rise of Chinese manufacturing. The tone of desperation was nicely encapsulated in an op-ed article recently by corporate chieftain Nobuyuki Idei. Under the headline "Nation's competitiveness must be recovered," Idei bemoaned Japan's allegedly widespread economic inefficiency and a general decline in competitiveness. But how inefficient can a nation be if it boasts the largest trade surplus in world history and pays some of the world's highest wages? (Japanese wages now run about 20 percent higher than American levels.) Idei, of course, did not mention these points. Also left unsaid was the fact that Idei's own corporation has multiplied its dollar-denominated sales nearly fourfold over the last 15 years.

What should the United States do? Clearly it cannot -- and should not -- attempt to emulate everything a highly regulated nation like Japan does. But it could make a start by doing some things that, until recently at least, have always been in the best American traditions -- like being honest with itself.

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