BOOK REVIEWS

1992 JETRO Hakusho: Toshi Hen
(1992 JETRO White Paper: Investment Volume)
Japan External Trade Organization
(Tokyo, JETRO, 1992), 520 pages.

Since 1972, the Japan External Trade Organization (JETRO) has been publishing a pair of annual white papers, *JETRO Hakusho: Boeki Hen* (*Trade Volume*) and *JETRO Hakusho: Toshi Hen* (*Investment Volume*), to document the rapidly changing nature of the internationalization of the Japanese economy and to give a broad perspective of its future course. *Hakusho: Toshi Hen* discusses recent trends in foreign direct investment (FDI), main developments in the international economy affecting such investment and the role of Japanese FDI in the world economy. *Hakusho: Toshi Hen* is considered to be an authoritative source of information related to Japanese FDI and is widely cited by Japanese academics and the press.[1]

Hakusho: Toshi Hen consists of two parts. Part I is devoted to an analysis of trends in FDI, recent developments in FDI policy and two special topics, namely, FDI and economic development and the expansion of overseas networks of Japanese firms and FDI inflows to Japan. Part II is mostly descriptive; it summarizes economic and political developments, FDI in and from Japan and the regulatory framework of host countries and regions. The country reports cover 58 countries in five regions (North America, Latin America, Asia and Oceania, Europe and the Middle East and Africa). The extensive world-wide branch network of JETRO makes *Hakusho: Toshi Hen* one of the most comprehensive and up-to-date sources of data of its kind. The present review focuses primarily on part I, which contains four chapters dealing with world direct investment in transition; FDI and economic growth; the expansion of overseas networks of Japanese firms and FDI inflows to Japan; and the development of the world economy.

Confirming UNCTC (1991), *Hakusho: Toshi Hen* observes that the sharp increase in Japanese FDI outflows, as well as steadily rising flows of FDI from and into Western Europe and the United States during the 1980s,

[1] The other principal sources are the Ministry of International Trade and Industry, *Wagakuni Kigyo no Kaigai Jigyo Katsudo* (*Japanese Firms' Activities Abroad*), and Toyo Keizai Shimposha, *Kaigai Shinshutsu Kigyo Soran* (*Japanese Multinationals: Facts and Figures*), both of which are published annually.

have created a triad in FDI and a clustering of investments in East Asia and the European Community centred around the three members of the triad. The increase of FDI flows during that period was mainly attributed to the expansion of the world economy, the sharp depreciation of the dollar, the boom of real-estate investment and mergers-and-acquisitions activity and trade frictions. According to *Hakusho: Toshi Hen*, FDI flows decreased considerably during 1990 and 1991, and this tendency is expected to continue in 1992, owing to the slow-down of the world economy, the end of the mergers-and-acquisitions boom, a tightening of liquidity of firms, a credit crunch by financial institutions and a deteriorating world investment climate owing to the Gulf War.

Japanese affiliates in the United States were hit the hardest by these deteriorating conditions: profit rates among Japanese affiliates declined sharply and were reported to be lower than those of their European counterparts.[2] Unlike European firms (most of which invested in the United States through mergers and acquisitions), the majority of Japanese FDI took the form of joint ventures, the construction of new plants or the expansion of existing plants. Besides, 60 per cent of Japanese manufacturing plants in the United States were established after 1985. This might suggest a lack of experience on the part of these new entrants. All of this translates into lower short-term profits and higher investment expenditures. Faced with an economic slow-down in the United States, Japanese affiliates are now forced to change their production, sales and investment strategies in the United States. Most of the Japanese affiliates operating in the United States regard localization, that is, an increase in local content, as the most important element of their business strategy (localization includes support for part suppliers, feedback from suppliers as regards product design, acceleration of local employment and the establishment of research-and-development centres). Japanese affiliates have also indicated that they intend to strengthen their relationships with their business partners and will promote joint ventures, thereby diversifying risks, multiplying sales channels, facilitating mutual understanding between Japanese affiliates and local companies and accelerating technological development.

The section on trends in world financial flows warns that the gap between global investments and savings is widening and that the majority of countries are experiencing increasing trade deficits. Under these circum-

[2] See also Tejima (1992) for a discussion of the performance of Japanese affiliates and an evaluation by parent companies of their investments in each region.

stances, it is crucial to devise a mechanism that facilitates smooth flows of capital. To tackle the problem, *Hakusho: Toshi Hen* proposes: encouraging savings and reducing fiscal deficits; the effective utilization of international organizations to achieve an efficient allocation of scarce capital resources; and the promotion of FDI, which does not create debt and can transfer technology and managerial skills to host countries.

Chapter 2 focuses on the impact of FDI on economic development, citing three major effects. First, FDI upgrades the activities of firms and industries through the transfer of managerial know-how and skills, such as technological skills and marketing methods (this can be best observed in East Asian countries). Second, localization of production and the resulting internationalization of firms can create a new pattern of international flows of goods and services. Third, it is likely that FDI flows to a host country accelerate the growth of that country, since it has been observed that growth in countries that experienced lower inflows of FDI during the 1980s is stagnant.

As examples of the effects of trends and impacts of TNCs, *Hakusho: Toshi Hen* lists five cases: the triad in FDI, the restructuring of European industry and steps towards the formation of a European Economic Area, the growth of East Asia, NAFTA and Latin American policies towards foreign capital and economic reforms in Central and Eastern Europe. JETRO predicts that the creation of NAFTA will not force North American TNCs to move production from East Asian countries to Mexico, except in the case of labour-intensive activities. This is because recent FDI in East Asia is based less on cost considerations and more on TNC strategies, which emphasize expansion of high-technology investments and investments for supplying domestic consumer markets.

The early 1990s saw a steep decrease in FDI flows from Japan and, in particular, FDI outflows to the United States (discussed in chapter 3). Foreign direct investment to Europe and Asia also fell, but by smaller proportions. Foreign direct investment in the manufacturing sector declined by only 5 per cent, in spite of a sharp drop in outflows in steel and non-ferrous products and food products. Several large investment projects in the electrical industry, as well as a steady FDI outflow in textiles, prevented an even greater decline of FDI outflows from Japan.

According to *Hakusho: Toshi Hen*, two important characteristics of Japanese FDI abroad during the late 1980s have been the expansion and

deepening of overseas networks of foreign affiliates and an increasing involvement of small and medium-sized firms in outward FDI activity. Japanese TNCs have strengthened strategic alliances with European and United States firms, creating a division of labour in production and sales based on four poles: Asia, Europe, Japan and the United States (network expansion). They have also increased local-content ratios and have actively established research-and-development centres (network deepening). *Hakusho: Toshi Hen* further notes that the Japanese FDI boom in the late 1980s was, in a sense, supported by small and medium-sized firms, since more than half of the FDI projects during that period originated from these firms.[3] Small and medium-sized firms were particularly active in services, such as commerce. These firms not only increased the amount of FDI abroad, but they also succeeded in diversifying their activities over different countries and industries. They switched their manufacturing investments from light manufacturing, such as toys and shoes, to electric and transport equipment, and diversified from the Asian newly industrializing economies to the other members of ASEAN, to China and to North America. The movement to invest abroad was partly the result of the appreciation of the yen during that period and partly the outcome of strategic considerations of these firms, aiming at securing market share by being present in all three regions.

Regarding FDI inflows to Japan, *Hakusho: Toshi Hen* notes four recent trends: an increase in FDI from Europe; a rapid rise of non-manufacturing FDI; the shift within manufacturing FDI from chemicals to machinery; and a shift of FDI to the services sector, especially commerce, business services and construction. Furthermore, according to *Hakusho: Toshi Hen*, joint ventures were replaced by wholly foreign-owned affiliates as the major form of FDI; in fact, several joint ventures and strategic alliances were dissolved. This reflects the competitive relationship that exists between Japanese firms and foreign affiliates in Japan and a change in the strategies of the latter, which increasingly consider the Japanese market as part of their globalization strategy. The growth of design-in alliances (that is, alliances in which suppliers of parts contribute to improving the design of the product sold by the final producer) for computer chips and automobiles is likely to help the promotion of sales of these products in Japan in the medium and long term. It is noticeable that, on average, foreign affiliates in Japan enjoy higher prof-

[3] JETRO does not provide data on the value of investments of small and medium-sized TNCs. However, it has been estimated that the share of these firms in total new equity investment from Japan was about 51 per cent during the period 1985-1989 (TCMD, 1992a).

it rates than domestic firms, owing to the strong emphasis placed on profits, as opposed to increasing market shares. The corporate strategies of foreign-based TNCs demand high profits in exchange for the high costs involved when they invest in Japan and encourage imports of commodities to take advantage of the strong yen.

In the last section of chapter 3, *Hakusho: Toshi Hen* makes a few suggestions for facilitating the increase of FDI inflows to Japan. Foreign-based TNCs are urged to take several steps in the following areas: development of new products that satisfy Japanese local standards and needs; creation of a solid and extended system of customer service; greater participation of Japanese staff in management; and the establishment of medium- and long-term strategic goals. Typically, foreign firms that did not succeed in the Japanese market had three characteristics: they tended to regard the Japanese distribution system and business practices as a symbol of the backwardness of the country; they did not trust Japanese managers and employees (the lack of trust resulted in the exclusion of Japanese staff from the decision-making process of the company); and they underestimated the size and dynamism of the Japanese market. JETRO suggests that overcoming these shortcomings and combining the managerial system developed by foreign-based TNCs with that of Japanese companies may be one way to be successful in the Japanese market.

Hakusho: Toshi Hen also mentions some barriers on the Japanese side. These include difficulties in recruiting capable staff, the opacity of various legal and administrative procedures and the exclusiveness of business practices, all of which require foreign-based TNCs to have a vast and detailed knowledge of the Japanese market and business practices. The first barrier reflects the rigidity of the labour market, the lifetime employment practice and a general labour shortage in Japan. The second and third barriers often lead foreign affiliates to the belief that they are being discriminated against by the Government of Japan and by domestic firms. *Hakusho: Toshi Hen* emphasizes the importance of alleviating those problems in order to secure a more dynamic growth of the Japanese economy.

Chapter 4, in conclusion, makes reference to emerging trends in the investment environment and to Japanese strategies to promote FDI. The current investment environment is characterized by a slow-down of the world economy, a widening gap between savings and investment, the growth of regional integration treaties in the face of increasing globalization and interdependence and the need for the establishment of an international order

regarding FDI. It warns that a European Economic Area and NAFTA have the potential of distorting flows of FDI and should be closely watched in order to prevent the emergence of "fortress" regional blocks. Regarding the role of Japan as an outward investor, *Hakusho: Toshi Hen* suggests that Japanese TNCs promote cooperation and industrial restructuring in Europe and in the United States; continue to support growth and development in East Asia; and pay special attention to the vast demand for foreign capital in Central and Eastern European countries, Latin America and socialist countries in Asia.

Hakusho: Toshi Hen, rich in data, is an indispensable source for understanding trends in Japanese FDI and its role in the world economy. It is interesting to note that the topics chosen by the report, such as the triad in FDI and FDI and economic development, are the same as those of *World Investment Report 1991* and *1992*, respectively. The concept of development used by JETRO, however, is much wider than the concept of economic growth used in the *World Investment Report 1992* (UNCTC, 1991 and TCMD, 1992). Some readers might feel that even though *Hakusho: Toshi Hen* sheds some light on several complexities in the institutional framework and business practices of Japan, the discussion could have been more specific on how to remove structural obstacles to inward FDI. Some more concrete proposals are certainly needed to tackle these problems. Finally, it would be very desirable if an English version of *Hakusho: Toshi Hen* were available to familiarize a wider readership with the Japanese perspective on FDI issues.[4] ■

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[4] It is not rare to have Japanese discontent expressed about the exclusion of Japanese views from English publications. Watanabe (1991), for example, argued that Japanese opinions on the issue of low FDI inflows to Japan should be adequately reflected in English publications. This issue is thoroughly discussed in *Hakusho: Toshi Hen*.

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Global Shift: The Internationalization of Economic Activity

Peter Dicken

(New York, The Guilford Press, 1992), second edition, 492 pages.

Paul Krugman, one of the young Turks of the economics profession, once remarked that he had spent his whole professional life as an international economist writing about economic geography without being aware of it. Peter Dicken, the author of this book, is one of the few who are actually economic geographers, and his book is a testament to both the strengths and the weaknesses of his profession.

Through a thorough review of trends in the shift of production and other value-added activities and by case studies of the textiles, automobile, electronics and financial services industries, Dicken synthesizes much that is known about the twin processes of internationalization and industrial change. Little that he says is new or additional, but the mere fact that he has been able to synthesize such a vast pool of statistics and research makes his book a vital source of information on the subject.

Several interesting points emerge from his discussion. Much of the growth of foreign direct investment (FDI) in the 1980s came from small and medium-sized transnational corporations (TNCs) while larger ones mostly consolidated their positions. Much of the decline in employment in traditional manufacturing within the industrialized world has come through technological change and productivity improvements and not from a shift in production to lower-wage countries in the developing world. A mere ten countries produce more than two thirds of all manufacturing output of developing countries. Most of those countries are in East Asia, though Mexico and Brazil also figure prominently. These ten countries appear again and again throughout the case studies as the only ones to benefit significantly from the internationalization of economic activity orchestrated largely by TNCs. Perhaps because the rest of the developing world has not played a large role as hosts to TNCs, it receives little attention in this book. Some discussion of why most of the developing world has been left out would have been useful, rather than focusing simply on the success stories.

In spite of this shortcoming, Dicken's review of internationalization trends is clearly presented and avoids the usual hype and mystery attached to the word globalization. His book should be read by anyone interested in

these trends, especially by economists who are still entrenched in the spatially frictionless world of international trade.

Economic geography is a vital component of economics that has been ignored for too long, and which is only slowly beginning to reassert itself within the economics profession. But, by itself, it is inadequate to the task of analyzing the welfare implications of the growing internationalization of business. Dickens is perhaps better placed than many economists to describe these changes and to explain why they have occurred, but he is less able to explain what they mean. He speaks in Luddite terms of the threat that technological change poses to employment, but it is not clear what he would do about it. Would we be better off if technological change had not occurred? In his attempt to steer between criticism and praise of TNCs, he utters such platitudes as "A comprehensive restriction on overseas investment by domestic firms might make a national economy worse, rather than better off. On the other hand, wholesale outflow of investment must surely be detrimental to home country interest" (p. 417). Those readers interested in the economic implications of global shift should perhaps look elsewhere. ■

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