

Japan still matters to the B.C. economy

By Jock Finlayson, Vancouver Sun September 12, 2011

Canadians are coming to recognize that the balance of power in the international economy is shifting inexorably toward Asia. Already home to three-fifths of humanity, the next two decades will see Asia grow to account for half or more of global output.

In recent years, much attention has been given to the implications of rapid economic growth in China and India, and to the emergence of these and other Asian countries - Korea, Vietnam, Indonesia - as expanding markets as well as important participants in global supply chains.

Often overlooked in discussions of what some refer to as the "Asian century" is the country that, until recently, was largest economy in the region: Japan. Interest in Japan by Canadian policy-makers and business decision-makers has been eclipsed by excitement over other, faster growing Asian countries.

The past two decades have been unkind to Japan, as it has grappled with natural disasters, a long period of economic malaise following the collapse of its stock and real estate markets in the early 1990s, deteriorating public finances, and the onset of negative population growth.

Many in North America and Europe appear to believe that Japan no longer matters. But it would be a mistake to discount the Land of the Rising Sun.

Consider, first, that Japan is still the third-biggest national economy, behind the United States and China. It is also a prosperous one: per capita gross domestic product stands at US\$34,000, using purchasing power parity exchange rates. This puts Japan ahead of most European countries and makes it almost five times richer than China (US\$7,600) and 10 times more affluent than India (US\$3,500). The country is highly productive, with a well-educated population, strong manufacturing sector and modern infrastructure. Over the two decades from 1990 to 2009, Japan outpaced all other G7 economies in productivity growth, despite its well-advertised macroeconomic and structural problems.

Japan is an influential trading nation, ranking as the world's fifth largest exporter and the fifth-biggest import market. Endowed with few natural resources, the country has evolved to become a leading global supplier of sophisticated products. Transportation equipment, semiconductors, electrical machinery and chemicals figure all prominently in its export mix.

Japan's success rests in part on a high level of human capital. Adult literacy is just a notch below 100 per cent. High school completion is almost universal, post-secondary attainment rates are relatively high, and the country hosts six of the 100 top ranked global universities.

Two areas of notable weakness are female labour force participation, where it lags behind other advanced economies, and Japan's failure to use immigration as a way to bolster workforce skills.

Japan is home to a significant number of global-scale enterprises. According to Fortune magazine, 68 of the world's 500 largest corporations, including seven of the top 50, are based in Japan. (Canada is home to 11).

Japanese firms are well represented among the ranks of the world's leading producers of automobiles, machinery and equipment. It is also strong in insurance, heavy manufacturing and trading.

Geographically, Japan is ideally situated to benefit from rapid economic growth and ongoing industrial development in the wider Asian region. Since the early 1990s it has expanded and deepened commercial connections with China and other Asian markets, with Japanese corporations now among the most prominent investors in the wider Asian region.

Japan's debt-burdened public sector undoubtedly will act as a constraint on the country's future growth. Gross government debt has reached 225 per cent of GDP, more than double any other G7 nation.

Yet interest rates have long hovered at rock-bottom levels and Japan's government seemingly has no trouble financing its massive debts. It turns out that the Japanese public sector holds very large financial assets which serve to partly offset its aggregate debt, leaving a net debt burden closer to 120 per cent of GDP (not much higher than several European nations).

Moreover, Japan is a low-tax country, with taxes collected equal to about 30 per cent of GDP, the lowest in the G7. This means it has ample room to increase taxes to assist in putting the government's finances on a firmer footing. Finally, while Japan's public sector is indebted, the country as a whole is a net creditor to the rest of the world, in the amount of \$3 trillion.

This reflects its high household savings rate, coupled with a large stock of Japanese investment abroad. On this metric, Japan, surprisingly, is in a better overall financial position than many other nations with proportionately smaller government debt burdens.

As Japan recovers from its earthquake and tsunami, Canadian policymakers and business leaders should pay attention. In 2010 two-way trade reached \$22.4 billion, and trade flows should rebound once Japan overcomes the temporary recession triggered by its recent natural disasters. Japan continues to be an important market for British Columbia lumber and pulp producers. Moreover, if it moves away from nuclear power, Japan may well develop an appetite for B.C. natural gas. Despite unfavourable demographics, Japan's economy should continue to post modest economic gains and it will remain at the centre of the much faster-growing East Asian region.

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