

The Japanese View of Eastern Europe

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During 1990 and 1991, mission after mission of Japanese business executives went to Eastern Europe to explore potential business opportunities. Prime Minister Kaifu and other Japanese political leaders also paid visits. By and large, Japanese businessmen concluded that in the next few years Eastern Europe would not loom large in their global strategy.

The total population of Eastern Europe is less than that of the largest province in China, and the consumer market is relatively small by world standards. Eastern Europe has relatively few resources and agricultural goods that it can export, and few of its manufacturing exports are likely to be competitive in world markets in the foreseeable future. Not only are the governments of Eastern Europe riddled with debt, but, in the Japanese view, the transition from socialism to market structures is far from complete. The transition to market thinking is even further behind. The Japanese also know that when opportunities do exist, the Eastern Europeans look more to Western Europe and the United States than to Japan, and that Western European companies, especially German companies, have far more developed networks of business contacts than do Japanese companies.

And yet, Japan will play a significant role in Eastern Europe – as it does throughout the world – thanks to its vibrant economy and powerful global companies with capabilities in manufacturing, finance, service, marketing, and information management. Even with the decline in the Japanese stock markets and real estate markets, Japanese growth rates are likely to continue to surpass those in industrialized Western countries. Many Japanese firms have the capacity to make significant advances throughout the world.

Eastern Europe may loom small in Japanese global strategy, but Japanese activities may nonetheless be very significant for a number of Eastern European countries. In Hungary for example, Japan is the largest creditor, holding 40 percent of total debt, and Japanese bridge loans were absolutely critical in putting together the international package for resolution of that debt.

The Japanese impact on Eastern Europe will be exerted principally through the trading companies.

The Key Role of the Trading Companies

At the center of Japanese efforts in Eastern Europe, as in most parts of the world, are Japanese trading firms. The world's six largest trading firms – Mitsubishi Trading, Mitsui Bussan, Sumitomo Trading, Ito Chu, Marubeni, and Nissho Iwai – are all Japanese. They maintain networks throughout the world, with staffs that understand local politics and economics. Through these networks, they look for business opportunities for companies headquartered in Japan as well as for companies headquartered elsewhere.

The trading companies are involved in all kinds of businesses, from noodles to missiles, and in all phases, from finance, investment, and manufacturing to marketing, sales, and service. In mature markets where other Japanese firms have a large presence, those other firms often have developed their own capacities and have less need for the trading companies. In less mature markets with a smaller Japanese presence – as in Eastern Europe – the trading firms play a proportionately larger role.

The six Japanese trading companies have had a significant presence in the Eastern European market since the late 1960s, when they began opening offices in capital cities or at least stationing representatives in Vienna to make the rounds of the Eastern European countries. By the mid-1970s, these companies had offices in the major Eastern European capitals. Thus, their top officials have two decades of experience in the region. Some have known its current economic leaders from the time when they were section and bureau chiefs, long before the changes of the last several years. Typically the trading companies' Eastern European offices have several native employees who speak English as well as the language of the country and who provide technical and service support. These employees follow local economic developments and serve as liaison to maintain good working relations with local companies and government officials.

At present, few Eastern European capitals can boast more than a few hundred Japanese, including embassy and trading company personnel, whereas cities such as Bangkok and Singapore may have as many as 20,000 Japanese. Despite their relatively small size, however, the Japanese business communities wield considerable clout. They generally form a chamber of commerce in each major city to support local networking, and they maintain excellent communication with their home offices in Tokyo and through Tokyo to worldwide networks. When they discover business opportunities, they can use their networks in Japan to quickly identify appropriate companies to take advantage of them. In the case of Eastern Europe, the search for opportunities has yielded mixed results.

Opportunities in Eastern Europe

Agriculture. Japanese trading companies have been looking for opportunities to buy Eastern European agricultural products to sell in other countries, but they have had difficulty finding products that will produce sizeable sales. They could, for example, buy more Czech hops and malt for use in beer-making if more were available.

Selling Manufactured Goods. Some Japanese firms have already identified opportunities for selling manufactured goods in Eastern Europe. Some Eastern Europeans have accumulated enough wealth to be able to buy Japanese products. However, the Japanese realize that Eastern Europeans are more familiar with Western European products than with Japanese products. Nonetheless, many Japanese are confident that their products will do well in Eastern Europe, as they have done elsewhere. Already, Fuji is selling film there; Canon, Minolta, and Nikon are selling cameras; Sony, National, Hitachi, and Toshiba are selling consumer electronics products; Sharp and Casio are selling calculators; Yamaha is selling electronic organs; and several companies are selling copy machines. Japanese auto companies are beginning to set up sales offices in major Eastern European cities, although they do not expect sales to exceed several thousand in the near future.

In addition, as factories in Eastern Europe begin to be privatized and modernized, some Japanese companies expect to sell producer goods such as textile machinery, generators, steel production equipment, and pollution control equipment. Some hope to sell parts for the more complex machinery that will be produced.

Tourism. The Japanese are also interested in the potential tourist industry in Eastern Europe. Although at present only a few tens of thousands of Japanese visit Eastern Europe each year, Japanese take an interest in its great historic cities. A significant number of Japanese, for example, are studying music in Budapest. Japanese business leaders see considerable potential for Japanese and other tourists' visiting Eastern Europe. There may well be a significant expansion of Japanese-owned hotels, restaurants, and other tourist facilities over the next several years.

The Problem With Local Production

In contrast to their guarded optimism about opportunities to sell goods and services in Eastern Europe, Japanese companies are reluctant to invest in local industrial production and have shown little interest in purchasing state factories that are being privatized. To the extent that the Japanese are interested in manufacturing investments in Eastern Europe, it is primarily to produce goods with low labor costs for export to Western Europe, where they could earn foreign exchange in far larger consumer markets.

Perhaps the main reason Japanese manufacturers have been slow to establish production facilities in Eastern Europe is that they are looking for long-term opportunities and they still see too many uncertainties. When the Japanese invest in a manufacturing plant, they consider it a blow to their image if the plant cannot surmount its difficulties and remain viable for at least several decades. Japanese firms are slow to make initial commitments but very determined once they decide to move ahead.

The overseas offices of Japanese trading companies often advocate that the home office expand the firm's local facilities, and Eastern Europe is no exception. However, the Japanese manager in Eastern Europe must acknowledge that markets are not yet completely open and that the future of reforms remains uncertain. It is not clear even which officials are likely to remain or what policies are likely to be followed. Japanese managers cannot be sure that local officials will help cut through red tape, that workers will be willing to work hard and accept discipline, or that unions will not go on strike. They cannot predict the level of taxes or the foreign exchange rate within a very wide margin. Thus, the trading firm's offices in Eastern Europe have rarely been able to present data that would convince the decision-makers in Tokyo, who must choose among projects in many countries. Japanese investment decisions tend to be relatively conservative and cautious.

It is no accident that the largest Japanese investment in Eastern Europe and one of the three largest industrial investments in Hungary was made by the Suzuki Motor Company, a firm in which the owner can make simple command decisions. Large bureaucratic staffs, such as those in most Japanese corporations, would have had difficulty moving ahead in the face of such uncertainty.

By and large, Japanese manufacturing companies feel that Southeast Asian countries – particularly Malaysia, Thailand, and Indonesia – can now provide labor that is as cheap as or cheaper than labor in most Eastern European countries, and that the market system there is not only well-developed but predictable. Japanese businesses feel that work forces and government officials in these countries are easy to work with. Furthermore, when problems arise, local officials will work quickly and reasonably to solve them. The Japanese do not have the same confidence in the ability of Eastern European governments.

Japanese interest in manufacturing in Eastern Europe will certainly increase if the countries there develop full-fledged market economies with stable political rule that facilitates foreign investment. Japanese interest would also increase if Western Europe should become much more protectionist against Asian goods, which would

make Japanese companies that now produce goods in Southeast Asia eager to shift production to Eastern Europe. Japanese firms believe that Western Europe is unlikely to put up barriers against goods produced in Eastern Europe. They therefore could use Eastern Europe instead of Southeast Asia as a manufacturing base for labor-intensive goods to be marketed in Western Europe. Indeed, some Japanese companies with manufacturing plants in Western Europe are already using Eastern Europe to produce parts and supplies that require labor-intensive efforts and then sending the parts and supplies back to Western Europe.

The Most Favored Nations

To the extent that Japanese are considering manufacturing in Eastern Europe, they find Czechoslovakia and Hungary most promising. To be sure, they acknowledge that the Polish market is potentially larger and that Poland will be a country to consider after market reforms are stabilized. They consider Czechoslovakia promising because of its history of industrial production and the existence of an experienced industrial labor force, the low cost of labor compared to Eastern Germany the low national debt, and the low inflation rate. They find Hungary promising because it has had more experience in market economies and seems flexible in working with foreign multinationals. However, even in these countries, Japanese companies find that fundamentally new attitudes are needed and that often it is better to train new engineers and workers than to try to retrain the experienced ones.

The largest Japanese manufacturing establishment in Europe, Suzuki, hopes to produce as many as 50,000 cars a year by 1994. Suzuki has found a niche producing small cars in various countries of the world, including India, Indonesia, Egypt, Pakistan, and Spain, where it can make a profit with smaller quantities than the large Japanese auto companies consider necessary to gain their economies of scale. Because Eastern Europe lacks experienced parts suppliers, Suzuki has encouraged thirteen Japanese parts suppliers to set up plants in Eastern Europe. Other Japanese companies have found niches in Eastern Europe producing machinery, chemicals, and electronic products. Generally these have been small and medium-sized specialized companies. Honda is beginning to explore possibilities for motorcycle production.

Japanese Assistance to Eastern Europe

The Japanese consider the standard of living in most Eastern European countries too high for them to qualify for aid through Japan's OECF (Overseas Economic Cooperation Fund), but they are beginning to provide some technical training through JICA (Japanese International Cooperation Agency). The Japanese government has also worked with the G-24 to put together loan programs and with international institutions such as the World Bank, the International Monetary Fund, and the European Bank for Reconstruction and Development. In Czechoslovakia, for example, Japan's Export-Import Bank put up some \$200 million, along with \$500 million from Western Europe and \$15 million from the United States, as part of a \$1 billion package.

An important part of the Japanese government aid package to Eastern Europe is an insurance scheme that reduces the risk for Japanese companies. Indeed, the larger Japanese industrial investments in Eastern Europe have generally benefited through loans from concessional financing from Japan's Export-Import Bank and from insurance backed by the Japanese government. In this uncertain transitional period, when the main Japanese interest is in finding sales outlets for goods produced in Japan and Southeast Asia, Japanese governmental institutions work closely with Japanese firms to support a modest level of investment that would not otherwise be possible.

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