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The Role of Japan in Central Europe in an Emerging Multipolar World

Traditionally, Japan has not enjoyed a significant presence in either Eastern Europe (the former Soviet Union west of the Urals), or in Central Europe. However, for a short time during the early Meiji period at the beginning of the 1880s, Japan looked to the Habsburg and Russian empires as appropriate development models[1]. Only in the latter part of the 19th century did Japan turn to the examples of Germany and England to adapt legal, military, and postal systems, and others, to the circumstances prevailing in Japan. In subsequent years, due to geographical distance, religious and cultural differences, and a general lack of mutual knowledge, there were to be very few ties between Japan and Central Europe.

The Cold War era resulted in an artificial separation of the countries of the two blocs, with Japan and the Central European countries belonging to different alliances which had very low levels of political contact. The highly complex nature of Soviet-Japanese relations exercised a diversionary influence upon political relations, with economic relations mostly determined by political and security priorities. Indeed, both in Japan and Eastern Europe, a kind of inward looking economic autarky prevailed, although in the case of Japan this was tempered by a successful obsession with export-led growth.

Recent Trends in Economic Relations

After the 1960s, in line with detente, the first economic, cultural and scientific agreements between Japan and Central European countries were established. This paralleled the accession of Japan to a position of strength among the leading free market economies. Japan had concluded agreements on trade and payments with most Central European countries in the early 1960s, with the result that bilateral trade began to grow, although it did not exceed $10 million per annum until the next decade. The beginning of the 1970s was characterized by the efforts of the five small CMEA countries to open their economies to the West. To promote development they applied for and received foreign credits from, among others, Japanese banks. For political reasons priority was given in the 1960s and 1970s to Romania in offering loans, although later Poland and Hungary became important recipients of Japanese credit.

As a consequence of the second oil shock, which made Soviet crude expensive for the energy-dependent industries of Central Europe, economic stagnation led Poland and Romania to ask for a rescheduling of debts. This coincided with serious political unrest in Afghanistan and Poland, which led in some cases to stricter regulation of trade between America's allies and the countries of Eastern and Central Europe. Nevertheless, increasing trade turnover (with Hungary, Poland and to some extent to Czechoslovakia[2]) led to growing Japanese export surpluses, which, together with an unfortunately static product structure for Central European exports, have been the main features of bilateral economic relations. This was the case during both main phases of the developing relationship, the 1960s and 1970–1989. In effect, the trade pattern continues to reflect disparities in levels of development. 80 per cent of Japan's exports to Central Europe are general machinery, electrical and electronics products, and cars, while imports are dominated by chemicals, agricultural products, and ferrous/non-ferrous metal semi-products.

In 1990, Japan's exports to the five small CMEA countries totalled $888 million, with imports of $654 million. The combined total represented only 0.3 per cent of Japan's foreign trade, which reflects its marginal importance. Correspondingly, in the foreign trade

1 Kumiko Haba, associate professor at Hosei University, has helped with this historical background.
2 In the early 1990s these three (now four) countries, accounted for a 70 per cent share of Japan's total trade with Central Europe.

of Central Europe, Japan is a less important partner than many other countries, although this is slightly less true in the case of Hungary.

Financial contacts between Japan and Central Europe appeared as early as the 1970s, but they began to expand after the mid-1980s. Japanese credits became more widely available in the latter half of the decade, and this was especially true for Hungary, where the National Bank used these resources in its debt policy strategy to switch to long-term credits. As a result, Japan came to account for approximately one third of total Hungarian debt, around $7.5 billion.

It is important to note that the behavior of individual countries in this region with regard to debt repayment has become the decisive factor in Japan's evaluation of these countries' economies. The Japanese standpoint on this issue is far more uncompromising than equivalent positions in the US and Western Europe. Indeed, in the case of Poland, which was a favoured target for Japanese engagement in the region, the rescheduling of Polish debt has caused Japanese interests to re-think their earlier enthusiasm.

As far as foreign direct investment (FDI) is concerned, Central Europe's contacts with Japan are less well-developed than trade links. In 1990, Japanese FDI was $52.7 billion, of which 48 per cent was invested in North America, 25 per cent in Europe, and 12 per cent in Asia. By the end of September 1991, the cumulative value of Japanese FDI in Central Europe was $65 million, which was 0.5 per cent or one two-hundreth of Japan's investment in Europe in that year.

Central Europe and Japan's Economic Strategy in the 1990s

Japan's relationship with Europe as a whole remains relatively distant. Relations have been treated marginally by Tokyo due to differing development strategies and the special character of Japanese relations with Washington, which has meant that Japan has sometimes been perceived in Western Europe as too much a surrogate of the United States[3]. Western Europe has been mainly preoccupied with involvement in multilateral treaty organisations such as NATO and the EC/EU, and content to leave Tokyo in relative political isolation. It was not until the early 1980s that there was a movement in Japan towards greater participation in world politics, and consequently more dialogue with European partners. This was demonstrated by Prime Minister Noboru Takeshita's statement in 1988 which described Japan-European relations as the third pillar of international co-operation.

When considering relations between Japan and Central Europe, it is necessary to distinguish different dimensions, spheres of interests and channels of communication. First of all, in a fairly commonplace classification, there is an official or governmental approach, involving a certain way of thinking and acting. This is exemplified by the Japanese Ministries of Foreign Affairs and International Trade and Industry, as well as MITI's agencies, such as JETRO. Then there is the private sector, which considers official guidance but values above all the short and longer term interests of the enterprise. To understand the growth of Japan's relations with Central Europe both of these perspectives must be considered in turn.

The Japanese Administration's Policy Towards Central Europe

As far as the position of the Japanese government is concerned, there is an important new element: the disappearance of the former bloc treatment. Distinctions between the Central European countries and the successor republics of the Soviet Union are being made. Regarding concrete assistance, it is also significant that the three most advanced countries in the region are receiving the most attention. This new form of attention is based on unspectacular but painstaking research carried out by Japanese experts who are assisting policymakers to formulate their strategies toward individual countries. And, needless to say, it also involves studying the strategies and initiatives of the United States and Western Europe in the same region.

Japan's official involvement in Central Europe has two main elements, financial assistance – using various channels, and the transfer of Japanese know-how to economic policy-makers; in other words, teaching the Japanese lesson. As evidence of one aspect of the special US-Japan relationship, what might be called a division of labour, Japan seems unwilling to take on independently the responsibility and risk involved in offering official loans. It is said that because of the lack of up-to-date and detailed information on the region Japan prefers taking part in multilateral or even bilateral financing. A good example of this trait is the establishment of the Japanese Enterprise Facility, part of the Global Partnership Plan of Action between Japan and the United States. The facility was created to support private sector development in Central Europe in co-operation, as appropriate, with the American Enterprise Funds, on the same conditions. For this purpose, a scheme for co-ordination has been set up between the two facilities, with the Japanese Embassy serving as a contact point in each recipient country.

The sources of funding for the facility are the Japan Export-Import Bank JEXIM for loans, and the Ja-

3 R. Murata: Political Relations between the United States and Western Europe: Their Implications for Japan, International Affairs, No. 1., 1987/8.

pan International Development Organization JAIDO[4] for equity investments. Plans call for increasing the amount of JEXIM loans to approximately $300 million for the whole region. Of these funds, up to $100 million are to be allocated to Hungary, up to $100 million to the Czech and Slovak republics, and up to $100 million to other Central and Eastern European countries, the allocation of which will be determined at a later date. The loans are made available in the form of an untied two-step loan. This means that JEXIM is extending untied loans to the central bank or appropriate government-backed development finance institution of the recipient country so that it can provide loans to individual enterprises. JAIDO's equity investments are made directly to individual enterprises. The Overseas Economic Cooperation Fund (OECF) has provided $10 million in capital to JAIDO and the authorised share of capital recently was raised to nine billion yen. JAIDO has made a further capital injection in 1993, with the money increasingly coming from the private sector.

The other element of official assistance is more indirect and intangible: the Japanese government sponsors missions, workshops and studies to assist policy-makers to formulate new methods to develop the market economy. Studying Japanese know-how in industrial policy-making is considered by many economists in Central Europe to be crucial in this transition period[5]. There were many elements of industrial policy pursued by Japan in the 1950s and 1960s which Central European countries with similar ambitions can reasonably attempt to adopt, even though economic and political circumstances are now of course quite different. In this context, some recent indications have suggested that the advice of Japanese experts is getting through, not only to independent economists in Central Europe, but also to policy-makers.

The Japanese Private Sector's View of Central Europe

This dimension of the Japan-Central Europe relationship is the most interesting, and at the same time the most delicate. With regard to short and long-term considerations it is also quite clear that Central European countries are eager to seek a long-term engagement from the Japanese side, principally through attracting capital investments. This does not mean that there is little interest in enlarging trade relations as well. Japanese products, both industrial and consumer goods, are necessary and welcome, but the likely increase in imports will need to be monitored in terms of the growth of prospective exports to Japan.

In the present transition period Central Europe is characterised by a lack of domestic capital, a very low technological level of industry, an outdated industrial structure, and the collapse of the most important former market, the Soviet Union. Foreign capital from any country is therefore urgently required. It is expected that this foreign capital will bring new technology, as well as more efficient management and work practices, while simultaneously opening up new marketing channels. As Japanese goods have high prestige in all industrial economies, capital investment from the same source, however tentatively it emerges, will be welcome. Moreover, it is hoped that Japanese participation might preserve economic sovereignty through a greater diversity of foreign investors, dominated up to now by German companies.

These expectations have not yet been fully realised, however. Although the last two years have witnessed a certain increase in new investments, Japan's share of total FDI has remained rather low. Indeed in Hungary, the country with the greatest share of Japanese direct investment among the countries of Central Europe (about $80 million), the share of Japanese FDI in the total from all countries has remained under five per cent. It is apparent also that the recent establishment of South Korean companies in this region has provided an interesting basis for comparison, reflecting perhaps a different approach to the realisation of investment opportunities between these two Asian countries.

One of the arguments used by Central European countries to attract inward investors is that the region has a central location in the heart of Europe. A further argument is that, despite the shortcomings of the present economic situation and quality of infrastructure, there are many long-run advantages associated with the region. Foreign companies generally decide to invest in this region to get an early footfold in a market that has enormous future potential. The quality of human capital is also important, given the high level of education and experience of much of the local labour force. Stressing cheap labour and production costs is becoming less important than a focus on the quality of the workforce, especially as the majority of investors are seeking longer-term profits as local purchasing power increases.

Despite the low level of direct investment in Central Europe by Japanese firms it should not be forgotten[6] that none of the Japanese investments are speculative, something that could not be said with regard to all the German, Austrian and American projects in

4 JAIDO was set up jointly by the government and Keidanren to provide industrial assistance to developing countries.
5 In the framework of a project recently sponsored by Japan Foundation and organized by the Japan – East and Southeast Asia Research Center in Budapest the present author prepared a study under the title Japan's Industrial and Investment Policy – Lessons to be Drawn for Hungary.
6 Early in 1990, in a study prepared on behalf of the Institute of the World Ecomony of the Hungarian Academy of Sciences, the present author had already expressed this view.

the same region. As far as the manufacturing sector is concerned, companies receiving Japanese capital benefit from high-technology inputs and produce high quality and internationally-competitive outputs. Particularly in the case of the Magyar Suzuki project, one of the most important long term gains has been technology transfer into the Hungarian economy. Furthermore, Suzuki's assembly plant is not insulated from the local economy, having developed links through its establishment of a network of sub-contractors. Indeed, the short-term advantages stemming from Japanese direct investment in Hungary derive from this substitution of local inputs for costly imports, together with the parallel generation of foreign currency inflows arising from increased exports.

Japanese Responses

Japanese businessmen have spoken frankly about the advantages and disadvantages of operating in Central Europe. Many opinion polls and surveys, initiated by organisations such as JETRO and ROTOBO, have outlined the Japanese firms' evaluation of market and investment opportunities. To summarize their thoughts about operating in Central Europe, a number of points are evident.

Firstly, the starting point is always the present situation of the Japanese economy, and against this background, the situation of private firms. Because of the current recession in Japan and elsewhere, Japanese companies are continuously reviewing their overseas operations. In concrete terms this means that they are postponing investments even is such important markets as the United States. Thus, they are in no mood to expand activity in new, and potentially more risky, markets; the current priority being to protect present positions. The appreciation of the yen is nevertheless changing the investment strategy of Japanese companies, making the establishment of foreign production bases more profitable. A surge of Japanese investment since 1993 may have been a consequence of this.

Secondly, Japanese people, and in particular businesspeople, greeted the political and economic changes of 1989–90 with sympathy, and with some interest in the possible implications for international business. This perhaps encouraged a short-term boom in exports to the more developed fringes of the region around 1990, but this has been followed by a slump since 1991.

A third point to consider is the traditional strategy of Japanese companies wishing to expand overseas. This begins with some export of goods, followed shortly after by the establishment of marketing and service networks which test a local market and gather market information. A decision concerning direct investment usually follows only after a significant lapse of time, even if general business conditions are favorable. Many Japanese companies, among them branches of the sogo shosha or general trading companies, have established offices in Central European capitals and have continued to maintain them even in years when local business activity has been slight. This would seem to reflect the long term approach of many Japanese companies.

Fourthly, the traditional linkages of Japanese companies need to be recognised as principal factors in determining where, when, why and how much capital is invested. Much has been spoken and written about this subject, and in the view of one Japanese executive Japanese foreign direct investment is essentially protective investment with the aim of keeping traditional export markets. This characterises Japanese multinational strategy in East Asia, where lower labour costs permit the establishment of sub-contracting investments. In the USA and Western Europe however, the trade policy of host economies has forced Japanese companies to invest if they wished to retain or expand markets. At the same time, towards Latin America, the former Soviet Union and Central Europe, a kind of wait and see attitude can be detected. The reason for this is the conflict between Japanese companies' natural preference for longer-term relations and what is perceived as an unstable business environment often subject to excessive local regulation and administrative interference. In Hungary there has been some evidence of these negative factors, and the change of regime, although welcomed, was to introduce a new factor of uncertainty, especially when it became necessary to establish contact with new decision-makers. Objective obstacles such as changes in the legal framework, the tax system, property rights and infrastructure have added to these difficulties.

As a fifth factor, we should note that there is at present little interest in joint ventures with Central European companies. Significantly also, Japanese companies are keeping their distance from privatisation, being unwilling to buy shares of Central European companies.

Sixthly, the liberalization of trade, now almost complete in Hungary, has created unprecedented competition for locally-owned firms and foreign investors alike. Indeed, some recent investors from countries which stress the importance of introducing a market economy into Central Europe have requested local protection from imports.

It is accepted that Japanese firms would prefer greenfield investment, rather than taking control of existing plant facilities. This is the seventh point to consider. As a consequence of this the only major investment to date has been Suzuki's car assembly plant in Esztergom, on the Hungarian border close to Slovakia. This project is something of a test-case for the future of Japanese manufacturing investment in Central Europe, and is perceived as such by Japanese business circles, as well as local interests concerned with industrial development. There is therefore a joint vested interest in ensuring the success of the project. It is as well to remember, however, that the Suzuki project is the product of former circumstances, conceived in a period of increasing consumer demand and limited opportunities in Central Europe to purchase high-quality sub-compact cars. These circumstances have become less valid in the mid-1990s.

Another consideration, the eighth, is that Japanese investors making cost/benefit calculations naturally assess the size of markets and market-access for products produced in foreign locations. With this in mind not only the Hungarian market, but also the whole Central European market may seem rather limited. In Hungary, and also in some neighbouring states, there is a widespread image of the country as a bridge between East and West. This is reinforced by the associate-member status, and anticipated full-member status, that Hungary, Poland, the Czech Republic and Slovakia enjoy in their relations with the European Union. Significantly, this enables these countries to channel goods to Western Europe under favorable conditions. Moreover, the collective experience of these four nations in doing business with the former Soviet republics, and continuing contacts, mean that production for a huge market in the easternmost part of Europe may one day make Central Europe a particularly attractive production base for foreign investors. Nevertheless, many Japanese businessmen express profound doubts concerning the foreseeable future prospects, both political and economic, of the former Soviet republics. The existence or lack of a market economy, rather than the population size, was recognised as crucial.

This is well understood in Japan. Japanese companies rapidly increased investment in EC countries (above all in the UK and Germany) after the mid-1980s to establish bases within a potential Fortress Europe. Hungary (and Poland, the Czech Republic and Slovakia) have therefore to compete not only with each other in attracting Japanese investors, but with better developed West European economies. Among these, Spain and Portugal have low operating costs, as well as greater political stability and much better infrastructure. Understandably, the issue of bad infrastructure in Central Europe, whether in transport, communications, or the financial sector, has been a major concern of Japanese companies.

As a final point, and perhaps the most striking with regard to the prospects of Japanese engagement in Central Europe, several Japanese businessmen have indicated to the present author that Japan is unwilling to create a new field of confrontation with its Western partners in this region. Experience of confrontation in other regions, leading to trade friction, has led Japan to be wary, especially given the uncertain prospects and unfamiliarity of the territory involved. For this reason Japanese companies may well prefer to co-operate rather than compete with American and West European firms, and try to develop a joint or indirect approach to investment in Central European countries, once they have developed their presence beyond a certain point.

To summarize therefore, it would seem that a tangible gap exists between the expectations of Central European countries and the likely degree of Japanese support for processes leading to required political and economic reforms. This is to some extent understandable, being in part a result of unrealistically inflated expectations in Central European countries, as well as a cautious approach on the part of Japanese interests that would generally prefer to wait and see how the situation is likely to develop in the region. This being so, Central Europe is unlikely to become a major arena for confrontation involving Japan-West European or Japan-US rivalry, but is more likely to emerge as a region of understated co-operation aimed at ensuring the success of democratic and market reforms. Such a situation would offer Japanese interests a chance to develop a higher profile in the region and buttress its presence in a more integrated European Union which is likely to include, before too long, Central European countries as full members.

Concluding Remarks

The most important lessons to be drawn from the interviews and studies carried out in preparation for this essay are threefold. Firstly, this decade will be a period when Japan is striving to strengthen its regional leadership in East Asia in both economic and political spheres. In accordance with its Global Partnership Plan, Japan will defer to the United States with regard to its future presence in Central Europe. This bilateral co-operation – even though of considerable importance for the region – will not however counterbalance the scale of involvement of West European countries, especially Germany, in the backyard of these advanced market economies. One reason for this resides with the attitude of many Central European countries, which despite having had decades of unhappy unilateral linkages followed by a professed wish for a balanced participation of powers' in the region, still find it more comfortable to give preference to European interests and contacts. This aspect should not be overlooked, notwithstanding the desire for more Japanese engagement in its own right.

Secondly, there is an active circle of scholars, bureaucrats and businessmen in Japan at present working to enlarge and deepen relations with Central Europe. They have the intellectual and financial resources, in universities and in powerful ministries such as the Ministry of Foreign Affairs and MITI, to promote increased Japanese investment in Central European human capital. These influential people believe that this investment is among the most important types of assistance in the long run. Scholarships, fellowships and reciprocal missions of Central European policy-makers and Japanese economists with industrial policy-making backgrounds help the development of this human resource. The experience of Japanese businessmen and managers working in foreign operations is also recognised as a valuable source of knowledge transfer. Moreover, agencies of the Japanese government carefully observe how these initiatives are received, and consider them an important criterion for deciding where and when to allocate official financial assistance.

Finally, the main lesson to be learnt from the tentative growth of Japanese involvement in Central Europe is that the wait and see approach may be an affordable luxury for Japanese international business, but Central European countries are not in a position to hesitate or relax. They have to make considerable efforts to create a domestic environment for the inward investor which is stable, welcoming and profitable, and to do this at the same time for locally-owned enterprises. In short, the investment climate which is required to attract foreign capital clearly requires an economy and society which is agreeable both to live in, and to work in.

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ÖSSZEFOGLALÓ

Japán szerepe Közép-Európában, egy „feljövő" multipoláris világban

Az 1970-es években, az enyhülés irányzatával párhuzamosan kezdte az öt kis KGST-ország megnyitni gazdaságát a Nyugat előtt, s a potenciális hitelforrások között a japán bankok is ott voltak. A kereskedelmi és pénzügyi kapcsolatok a nyolcvanas évek közepétől élénkültek meg újra. Azonban 1990-ben az öt kis KGST-országba irányuló export a japán kivitelnek mindössze 0,3 százalékát tette ki. 1990-ben a japán közvetlen befektetések mintegy negyede irányult Európába, s ennek mindössze 0,5 százaléka realizálódott Közép-Európában.

Japánnak az 1990-es évek elején Közép-Európára irányuló stratégiájában két fő terület különböztethető meg: a különböző csatornákon csordogáló pénzügyi hozzájárulás, és a gazdaságpolitikai know-how átadása. Az elsőt illetően azonban meg kell jegyezni, hogy a régióra vonatkozó részletes információk hiánya és más okok miatt a japánok előnyben részesítik az USA és mások részvételével is járó multilaterális, de legalábbis bilaterális finanszírozást. Ugyanakkor a japán kormány különféle olyan programokat, szemináriumokat, tanulmányokat finanszíroz, amelyek célja, hogy megismertessék a politika- és gazdaságpolitika-csinálókat a piacgazdaság fejlesztésének új módszereivel. Ez kulcsfontosságú az átmenet éveiben a közép-európai országokban.

A japán magánszektornak Közép-Európáról alkotott véleménye a másik fontos kérdés. Nyilvánvaló, hogy a közép-európai országoknak rövid és hosszú távon egyaránt szükségük van Japán partnerségére, elsősorban a tőkebefektetés területén. Ez nem jelenti a kereskedelmi kapcsolatok lebecsülését, de az átmeneti szakaszban ezen országok gazdaságára a hazai tőke jelentős hiánya, az ipar alacsony technológiai szintje, az elavult ipari struktúra a jellemző.

Sürgős szükség van külföldi tőkére, bármely országból érkezzék is. Várható, hogy e külföldi befektetések technológiai megújulással járnak, hatékonyabb munkavégzési és menedzsmentmódszerek meghonosítását jelentik, valamint segítik új piaci csatornák megnyílását is. Amennyire nagy presztízsnek örvendnek a japán termékek, annyira üdvözlendő a Japánból érkező tőke is, mely ráadásul a túlnyomóan német befektetői dominancia oldásával a gazdasági függetlenség megőrzéséhez is hozzájárul. Bár az utóbbi években a japán beruházások a térségben növekedtek, részarányuk a teljes FDI-ben meglehetősen alacsony maradt. Valójában Magyarországon is, mely az első helyen van a Közép-Európába irányuló japán befektetéseket illetően, a teljes tőkebehozatal 5 százaléka alatt marad a japán tőkeimport aránya.

A közép-európai országok a kedvező földrajzi elhelyezkedés mellett többnyire azzal érvelnek, hogy a jelenlegi, több területen lesújtó gazdasági helyzet dacára a régióban számos hosszú távú előny kínálkozik. Ez utóbbit akceptálják a beruházók is, amikor gyakorta az vezérli őket, hogy korán megvessék lábukat egy ígéretes piacon. Az alacsony termelési és bérköltségek kezdenek kisebb szerepet kapni a döntésekben, s előtérbe kerül a munkaerő minősége, főként azon