

CHAPTER 7

RECESSION, REFORM AND OPPORTUNITIES

Japan is a nation of sleeping consumers.¹

Introduction

7.1 In the previous chapter, the Committee focused on assessing the effects of the Japanese recession on the Australian economy through trading and commercial links. The Committee also considered some of the barriers to trade with Japan, including tariffs and quotas. In this chapter, the Committee concentrates on the positive effects that developments in contemporary Japan are having on Australia and the opportunities they are creating for Australian business. It emphasises the ways in which Australia, in this changing world, can further consolidate and build on an already solid and friendly trading relationship with Japan.

7.2 The Committee has shown how the nature and composition of trade between Australia and Japan has changed over many years. Australian exports to Japan are no longer limited to strategic raw materials. The strong complementarity that existed from the very beginning of trade between the two countries continues to bind them and provides a solid platform on which both countries can strengthen their relationship. But alongside this established trading pattern, which is based on the exchange of predominantly primary products for manufactured goods, new trading links are developing. There is a reorientation of industry with the growing importance of information technology and, more importantly, services exports such as tourism. Wool, which secured the relationship during the post-war years, is no longer of such significance. Indeed, Japanese tourists are now more important as an export earner for Australia than the traditional wool exports to Japan.

7.3 In addition, the trading environment is changing. Japan's long period of rapid economic growth has come to an end. It is looking for ways to reinvigorate its economy; to encourage new industries. In seeking to lift its economy from the doldrums, Japan has embarked on an ambitious reform program which offers exciting prospects for new or expanding markets. Japan is restructuring its economic system and opportunities are emerging for Australia to broaden its trading horizons. Demographic and technological changes in Japan also present opportunities for new ventures.

1 'Restoration in Progress', A survey of business in Japan, *The Economist*, vol. 35, no. 8147, November 1999, p. 19.

Changes in the Japanese market place

Consumer preferences

7.4 Many witnesses appearing before the Committee drew attention to the noticeable shift in consumer preferences and trends in Japan in recent years. The elderly have become a significant consumer group, as have young women, and, despite the recent economic downturn, there has been, until very recently, a steady increase in income levels. There is a large and growing market for information technology and communication products across all age groups and strengthening consumer preference towards purchasing environmentally friendly products.²

7.5 The *Economist* summarised the extensive sweep of change in Japan:

Younger families want high-quality care for their elderly parents as the extended family breaks down. Parents want choice in education and health. Housebuyers want efficient estate agents and a wider selection of homes. Shoppers want out-of-town discount stores where they can drive with their kids. Women want small cars, better furniture, e-mail, and financial advisers they can trust. Japan is a nation of sleeping consumers.³

7.6 Australia's exporters are in a position to tap this large pool of potential buyers. The importance, however, of sound market research cannot be overstated. With competition fierce, it is important for exporters and investors to read the market accurately. Australians trying to sell into Japan are at a very great risk of missing the buyers' perspective, so they must pay close attention to the vagaries and peculiarities of the market if they want to maximise their potential in this still lucrative market.⁴

7.7 One of the most notable shifts in attitudes is toward a broader acceptance of new products. Japanese consumers who were traditionally 'blindly devoted' to locally made goods, now appreciate the value of imported ones. This willingness to consider new products opens the door for Australian exporters to Japan. Cheese, which is not a traditional part of Japanese culinary culture, is one of Australia's successes. In a period of economic stagnation there has been dramatic growth in exports of Australian cheese to Japan.⁵ In 1998, Australia, now a leading exporter of natural cheese to Japan, accounted for 40% of all Japanese cheese imports. According to a report

2 For example see: Queensland Government, submission no. 18, p. 3; Hiroshi Nakano, Japan Chamber of Commerce and Industry, Sydney Inc, *Committee Hansard*, 3 September 1999, pp. 789–80.

3 'Restoration in Progress', A survey of business in Japan, *The Economist*, vol. 35, no. 8147, November 1999, p. 19.

4 John Longworth, 'Understanding our customers: Hidden socio-political realities in Japan and China which influence trade with Australia', *Australasian Agribusiness Review*, vol. 1, no. 1, May 1993, pp. 25–6.

5 John Sainsbury, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 28 May 1999, p. 662.

published in 1999, 'imports of Australian natural cheese for direct consumption will grow rapidly in the spring of 1999 and thereafter'.⁶

7.8 Mr Gregory Dodds, Executive General Manager, North East Asia Regional Office, Austrade, cited the selling of stockfeed to Japan as another example of changing attitudes towards, and a greater willingness to try, new products. He told the Committee:

People have been trying to sell molasses for a good number of years, and it has just been rejected outright by the Japanese as not being a stockfeed as far as they are concerned. At the beginning of this year, it became a stockfeed for a couple of Japanese. Why?...They have started to look at new ways of doing things and that pre-emptory arrogance that you would encounter in Japan a lot before is being replaced by cautious curiosity in many cases.⁷

7.9 Another example of changing approaches to foreign products and the growing receptiveness for things new comes from the banking sector. Up to a couple of years ago, it was unthinkable for the Japanese public to deposit their money into foreign banks but this is changing.⁸ Given this new found curiosity, the most careful attention, however, should be paid to Japanese preferences. Producers should be thoroughly familiar with the behaviour, sentiments and needs of the Japanese consumer together with the nature of the Japanese market. Cheese provides a good example. JETRO pointed out that 'while it is important to retain the traditional flavour of each nation's cheeses, it is also important to study the taste preferences of Japanese people and devote resources to developing products that accord with those tastes'.⁹

7.10 The challenge for Australian exporters is to entice the Japanese to experiment with a new or different product while winning their approval by meeting their particular taste requirements. The overriding message again is the importance of careful market research—in knowing your customer. Australian rice growers have shown the tenacity and perseverance required in researching and developing a product attractive to Japanese consumers. They have devoted time and resources to producing rice especially for the Japanese market.

7.11 Due largely to their determination, the market in Japan for Australian rice has grown from nothing five years ago to become a significant one. In 1995, Ricegrowers Co-operative Ltd launched a variety of rice called 'millin'—the first Australian bred variety to target the Japanese market. The breeding program for millin commenced in 1981, years before the opening of the Japanese market. This was followed in 1997 by the Japanese short grain variety koshihikari. In March 1999, Ricegrowers Co-

6 JETRO, *Japanese Market Report No. 30—Regulations & Practice—Cheese*, March 1999, p. 5.

7 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 635.

8 Hiroshi Nakano, JETRO, *Committee Hansard*, 3 September 1999, pp. 795–6, 798.

9 JETRO, *Japanese Market Report No. 30—Regulations & Practice—Cheese*, March 1999, p. 14.

operative launched the variety opus, which was the first Australian bred, short grain variety, resulting from a 12-year breeding program—again, started well before the commencement of rice imports into Japan. The Ricegrowers Co-operative Ltd told the Committee that it hopes to expand its exports of Australian short and medium grain japonica varieties to Japan.¹⁰

7.12 The Japanese consumer can be particularly fussy, for example, when choosing produce. Two matters—food safety and quality—are of primary importance to the Japanese. Witnesses could not overemphasise Japanese concern about safety considerations and surveys have repeatedly indicated that the Japanese consumer puts food safety at the top of the list. JETRO cited one such survey taken in 1997 that showed the main reason Japanese consumers shied away from imported produce was ‘concerns over safety.’¹¹

7.13 Moreover, the Japanese tend to regard the local product as safer than the imported one, so overseas exporters, as well as meeting regulatory standards, must also combat the strong bias favouring local goods. Exporters must convince a sceptical consumer of the safety of their product.¹² According to a JETRO report, ‘if overseas producers can reassure Japanese consumers of the safety of their products, they will have no difficulty selling them in Japan’.¹³

7.14 Close attention should also be given to labelling. Products offering assurances of safety, such as organic commodities, or products using only selected high-quality ingredients should be marketable.¹⁴ A strong brand name has strong selling power. Indeed, as part of establishing a name for safety and quality and to improve competitiveness a number of Australian industries are working to develop customer allegiance and to differentiate their product in the Japanese market from those of their rivals. This is one reason why the Australian Ricegrowers Co-operative is keen to develop branded sales to Japan.¹⁵ A brand name associated with safety and quality carries substantial weight in the market place. The Aussie Beef logo is one notable success.

10 Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, pp. 533–4. The NSW Department of Agriculture research station at Yanco developed the ‘opus’ rice variety with assistance from Ricegrowers Cooperative Ltd. Ricegrowers has supported the rice research and development activities of NSW Agriculture for more than 15 years, and it has contributed in excess of \$15 million to rice research over the period, pp. 534 and 542.

11 JETRO, *Japanese Market Report—Regulations & Practices—Fresh Vegetables*, No. 31, March 1999, p. 17.

12 John Sainsbury, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 28 May 1999, p. 665.

13 JETRO, *Japanese Market Report—Regulations & Practices—Jam & Canned Fruit*, No. 32, March 1999, p. 17.

14 See for example JETRO, *Japanese Market Report—Regulations & Practices—Jam & Canned Fruit*, No. 32, March 1999, p. 17.

15 Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, pp. 534, 537.

Aussie Gold logo



7.15 Australia's beef exporters are an example of an industry that has paid close attention to Japanese sensitivities, especially in the area of health and safety and also of meeting Japanese expectations of quality through appearance and presentation. They recognise that, while improved access is important in a high income country such as Japan, consumer decisions as to the quantity of beef purchased are likely to be influenced by quality and safety issues. In most high-income countries, food accounts for only a fairly small part of the household budget. Most of the food bill is made up of the services that are embodied in the food—packaging, processing and advertising.¹⁶

7.16 This point about food safety was made clear in 1996 when, after many years of growth, beef consumption in Japan dropped by about 7% because of consumer concerns over Bovine Spongy Encephalitis (BSE) and particularly E Coli. The United States suffered a loss in Japan's market share.¹⁷ On the other hand, Australia has maintained its health and hygiene status, which is probably one of the biggest value differences that Australia is able to promote in the international market place.¹⁸

7.17 Australian beef exporters have also shown persistence in seeking improved access to Japanese markets and in their willingness to work with the Japanese to promote their product. They keep a watchful and anticipatory eye on their changing market in Japan. Australia was largely a grass-fed beef producer supplying product to a specification and a price. Once the market started to liberalise and customer-based

16 Paul Riethmuller, 'Major Trends Affecting Australia's Agricultural Industries: Have they Taken a Turn for the Worse?', *Economic Issues No. 3*, November 1998, p. 13.

17 Dr Peter Barnard, Meat and Livestock Association, Australia, *Committee Hansard*, 15 April 1999, p. 378.

18 Stephen Martyn, Australian Meat Council, *Committee Hansard*, 15 April 1999, p. 381.

preferences and demands started to come down the marketing chain directly to the producer in Australia, Australian beef exporters were able to adjust production and marketing processes to meet those new needs. The growth in grain-fed beef production demonstrated Australia's responsiveness to changing demands. The Meat and Livestock Association (MLA) believes that before liberalisation, it was about 3% of Australia's total production and has gone up to almost 40% of total production going to Japan, again reflecting customer demand in Japan.¹⁹

7.18 The downturn in Japan's economy has also caused a substantial shift in consumer demand. Over the last four or five years, there has been a broadening in the product mix of Australia's exports to Japan. Originally, beef exports were driven by the demand for high quality chilled beef but now, high quality manufacturing meat is a high growth area. Chilled grass-fed beef exports from Australia have dropped 6 percentage points and chilled grain-fed exports have also dropped, but frozen grass-fed exports have increased substantially, indicating a switch in Japanese consumer patterns, particularly at the lower end of food service. The fast food sector in Japan has grown and their dairy industry, which was a principal supplier of grinding meat in the past, has been unable to meet that demand. Australia has taken that over.²⁰

7.19 The MLA told the Committee that Japanese consumers are increasingly eating less within the home and noted especially the popularity of McDonald's, pointing out that about 80% of all McDonald's hamburger beef comes from Australia.²¹

7.20 The Australian beef exporting industry fully appreciates the importance of intelligent marketing and has reaped the dividends of successful promotional campaigns. Through the MLA and its predecessor, the industry has invested heavily in promoting Australian beef in Japan. Australian beef has won the confidence of Japanese consumers with quality and safety as its major selling points. The Aussie Beef brand is favourably perceived against United States' beef. Careful attention has been given to the presentation of beef in the shops and to the high standards of quality assurance.²² Again, the industry keeps in close touch with its customers needs and changing tastes.

7.21 The Australian Ricegrowers Co-operative Ltd is also very conscious of Australia's health and hygiene status, which places Australian produce at an advantage in the international market place. It understands Japanese concerns about quality and food safety and is working to meet these requirements. Indeed, Australian rice growers are setting very high standards. The Ricegrowers Co-operative explained that because of the crop rotation scheme in Australia, rice is relatively chemical free. Australian rice growers use about one-sixth the amount of agricultural chemicals and

19 Stephen Martyn, Australian Meat Council, *Committee Hansard*, 15 April 1999, p. 383.

20 Stephen Martyn, Australian Meat Council, *Committee Hansard*, 15 April 1999, p. 390.

21 Stephen Martyn, Australian Meat Council, and Samantha Jamieson, Meat and Livestock Australia, *Committee Hansard*, 15 April 1999, pp. 379–80.

22 Gary Humphries, Australia-Japan Foundation, *Committee Hansard*, 19 February 1999, p. 53.

fertilisers that the Japanese farmers use.²³ To underline this point, the Ricegrowers Co-operative submitted:

Japan, with its imports of rice, is currently testing rice for 104 different chemical residues. Certainly we are very proud of the fact that we are showing no detections on any of those residues that they are looking for.²⁴

7.22 The changes in the preferences of Japanese consumers are working to Australia's advantage but, as Australian beef producers and rice growers attest, a commitment and determination to meet the expectations of the Japanese consumer is essential in carving out a place in the Japanese market place.

7.23 Another significant characteristic of Japanese consumers is their keen appreciation for quality and service. Even though the Japanese may well be broadening their tastes, they nonetheless retain an 'impeccable sense of style'. Consumers' decisions are more likely to be swayed by issues such as quality and safety over price. Mr Christopher Pokarier told the Committee that while the Japanese take on board many Western things, they tend to do much better than the original product or process. He argued that Australians start way behind Japanese market expectations and have to go through a difficult learning process to satisfy Japanese standards of quality and performance.²⁵

7.24 Professor Coaldrake shared these sentiments. He believed that:

...the traditional arts have set what I would describe as subliminal standards of quality, industry, behaviour and organisation. One example: Japanese mirror-smooth surfaces on traditional lacquer boxes and bowls set a modern standard for automotive paint finish. The second example: the complicated interlocking wood joints which held historic buildings in Japan steady against earthquakes, storms and the centuries set a standard which explains why doors on Japanese cars do not leak and why there is no water dripping into the Sydney Harbour Tunnel.²⁶

7.25 He stressed that Australians need to be aware of these developments and to anticipate their effects on goods and services.²⁷ To succeed in Japan, Australian companies must be able to equal the standards the Japanese have set for themselves. They must appreciate the high level of quality control and be willing to alter product design and packaging to satisfy market requirements.

7.26 Put bluntly by Mr Terence White, Director, Australia-Japan Foundation based in Tokyo:

23 Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, p. 536.

24 Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, p. 541.

25 Christopher Pokarier, *Committee Hansard*, 16 April 1999, p. 434.

26 Professor William Coaldrake, *Committee Hansard*, 17 May 1999, p. 573.

27 Professor William Coaldrake, *Committee Hansard*, 17 May 1999, p. 573.

Japan is a place where, if you do not have the best product in the world, there is no real point in attempting to compete because they have the money, the purchasing power and the market size to be able to get the best thing in the world.²⁸

7.27 Mr White cited a number of examples where Australian products were meeting or expected to meet these high standards—the lighting decks in computers that control NHK’s halls around Japan; the seats likely to go into stadiums in Japan that will host the World cup and the design for drainage systems and watering control for natural grass stadiums.²⁹

7.28 Again, the Ricegrowers Co-operative demonstrated its understanding of Japanese appreciation for quality. It recognised that the Japanese will pay a premium for quality and asserted ‘that is exactly what we are supplying to them’.³⁰ Australian rice growers, however, were disappointed in early 1999 that they were being denied the opportunity to take advantage of supplying new season’s rice. Because of Australia’s counter seasonal advantage, Australian growers are able to supply new rice at old crop time in Japan. The Japanese look forward to eating new season’s rice but the Japan Food Agency, which controls the timing of tenders, had not given the new season’s advantage to Australian producers. With the way that the tenders are currently held and the timing for the tenders, Australia’s new season’s advantage is dramatically reduced.³¹ This situation was drawn to the attention of Japan in Australia’s submission to the Japanese Government on the Deregulation Promotion Program and needs to be followed up in Australian trade talks with Japan.³² Australian wheat growers are also fully aware of the benefits they derive from supplying Japan with a high quality product and are keen to maintain this reputation.

7.29 Even with the presentation of a product, the Japanese consumer is looking for the highest standards. Packaging, processing and advertising are an important aspect of marketing in Japan. JETRO, in its report on beer, noted that beer cans manufactured overseas generally have only one coating, while two coatings are normally applied in Japan. It stated that ‘even a slight unevenness of color or other minor blemish sometimes is reason enough for products to be returned’.³³

7.30 Although the Japanese are very particular about safety and quality, the recession has sharpened their appreciation of value for money. With continuing intense competition and deflationary expectations in the market, they are deferring some purchases or shopping with a selective eye for less expensive substitutes. They

28 Terence White, Australia-Japan Foundation, *Committee Hansard*, 19 February 1999, p. 46.

29 Terence White, Australia-Japan Foundation, *Committee Hansard*, 19 February 1999, p. 46.

30 Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, p. 535.

31 Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, p. 536.

32 Submission of the Australian Government to the Japanese Government on the Deregulation Promotion Program, see Appendix 4, p. 9.

33 JETRO, *Japanese Market Report—Regulations & Practices—Beer*, No. 23, December 1998, p. 15.

are prepared to accept a certain degree of cost cutting practices, for example, in less elaborate and expensive wrapping and the presentation of goods at the cash register. Without doubt, Japanese consumers are discerning and very canny—they are searching for products which give value for money.³⁴

7.31 This discernment is showing up in relation to certain top-of-the-line consumption-based goods. People are eating in less expensive restaurants and they are being more particular about the kinds of clothes they buy.³⁵ For example, the Australian crustacean market has been quite substantially affected over the past few years by the downturn in the Japanese economy. The decline of crustacean exports is around 22% to that market. The obvious markets to turn to as alternatives are other markets in Asia, which at the moment are not a good alternative.³⁶ The wool industry is another sector that is waiting for the Japanese economy to pick up in the hope that demand for the more expensive wool garment will increase.

7.32 The current recession, however, should not deter Australian exporters from exploring the potential of the Japanese market. Even if the economy shrinks, Japan remains a market of over one hundred million consumers with high disposable incomes.³⁷ The changing circumstances in Japan are creating opportunities but competition is strong and the Japanese market can be difficult. The need for Australian business to understand their customers better and to cater to a particular market cannot be underlined too strongly.

Demographic changes

7.33 Demographic changes in Japan may also provide an opportunity for increased exports of Australian products and services such as those targeted specifically to the elderly—provision of aged care, health care, recreation and leisure services.³⁸ Dr Carolyn Stevens pointed out that in 2025 the number of people requiring long-term care will triple. Therefore, extended and on-going care for bedridden and senile elderly people will become a critical issue in Japan.³⁹

7.34 The ageing population has not only to be cared for but also kept active, both mentally and physically. Their finances must also be managed. This consumer group with abundant savings is generating a strong and growing demand for services to meet

34 Christopher Pokarier, *Committee Hansard*, 16 April 1999, p. 423; Hiroshi Nakano, Japan External Trade Organisation, Sydney Inc, *Committee Hansard*, 3 September 1999, p. 788.

35 Janet Tomi, DFAT, *Committee Hansard*, 15 February 1999, p. 8.

36 Timothy Marney, Treasury Department of Western Australia, *Committee Hansard*, 25 February, pp. 160, 164.

37 See statement by Dr Craig Freedman, *Committee Hansard*, 15 April 1999, pp. 345–6.

38 Queensland Government, submission no. 18, p. 37.

39 Dr Carolyn Stevens, *Committee Hansard*, 17 May 1999, p. 570.

their specific needs. Health care, financial management or hobby services present new and exciting opportunities.⁴⁰

Changes in technology and increasing demand for financial services

7.35 The IT revolution also holds great promise as it expands and pushes into new fields. Business is embracing new technology and the application of IT technologies is spreading across a wider range of the Japanese economy, creating new opportunities in Japan for both foreign and domestic information and communications providers.⁴¹

7.36 Opportunities in areas such as the financial sector, particularly risk assessment, are being generated as the Big Bang reforms start to take effect. Financial services, which are inadequate in Japan, will provide openings for joint ventures. In the professional services area, the need for institutions and companies to benchmark against international standards and improve current practices has created a need for external consultancy services, and this demand will accelerate as deregulation continues in Japan. The door is open for Australian consultancy businesses especially in the area of financial services.⁴² Mr Tadashi Nakamae told an OECD Business and Industry Policy Forum:

Japanese banks and insurance companies are still woefully inefficient, and huge potential exists for financial products that offer Japanese savers a viable alternative to bank deposits. With the interest rate on bank deposits now set at zero, savers are naturally reluctant to put more of their money into the bank. Investment trusts are likely to emerge as the main alternative, but the investment trusts on offer at present, those controlled by Japan's big financial institutions, are not a good investment. When genuine competition is introduced to the investment fund management business, the yield of investment trusts may rise to 5–10%. Then the asset management market will expand rapidly, at the expense of bank deposits.⁴³

7.37 JETRO pointed out that the enormous individual financial assets of the Japanese, estimated at over ¥1.2 quadrillion in value, holds significant appeal for overseas financial institutions. The economic difficulties and the need for corporate restructuring will continue to offer unprecedented opportunities for foreign financial

40 Hiroshi Nakano, Japan External Trade Organisation, *Committee Hansard*, 3 September 1999, p. 788. See also BT Funds Management Limited, Newsletter, *Cherry Picking in Japan*, February, 2000.

41 Professor Peter Drysdale, *Committee Hansard*, 23 August 1999, p. 767.

42 For example see Professor David Allen, *Committee Hansard*, 25 February 1999, p. 181; Dr Craig Freedman, *Committee Hansard*, 15 April 1999, p. 350; Perce Butterworth, New South Wales Department of State and Regional Development, *Committee Hansard*, 15 April 1999, p. 394.

43 Mr Tadashi Nakamae, President, Nakamae International Economic Research, Presentation for the OECD Business and Industry Policy Forum on 'Realising the Potential of the Service Economy: Facilitating Growth, Innovation and Competition', Paris, 28 September 1999, p. 2.

institutions ‘to move into Japan and develop financial services products without hindrance’.⁴⁴

7.38 Overall, the major growth areas in Japan are in medicine and welfare, information and telecommunications, and distribution and logistics. Housing also appears promising.⁴⁵

7.39 The first step to success in the Japanese market is to identify niches where Australian firms have the resources or expertise to secure a foothold. The task of both the business community and the government is to recognise these opportunities and determine how best to capitalise on them.

7.40 Prevailing economic conditions, changes in consumer preferences, the importance of the environment and Japan’s ageing population may provide new market opportunities but they may also harm Australian exports to Japan. The decline in demand for wool and in crustaceans by the Japanese as well as the fall in coal prices reflects the economic downturn. So, it is important for both established and potential exporters to Japan to monitor and accurately assess trends and changes in Japan.

7.41 The overriding message is that Australian business and the Australian Government must be well informed about developments in Japan and be able to analyse such developments to anticipate trends accurately and to identify opportunities.

The Japanese economy—reform, restructuring and opportunities

Reform and deregulation

7.42 The Japanese market offers opportunities for Australian exporters but innovation and careful market research will not necessarily bring success. Importantly, Japan still has in place some hefty obstacles to trade. In the previous chapter, the Committee looked at the tariff and quota system that controls the imports of products such as rice, sugar and beef. But in addition to these barriers, there is also a raft of rules and regulations clogging the economic system. Administrative and regulatory bottlenecks have for many years either created difficulties for, or even discouraged, Australian companies from doing business in Japan.

7.43 Recently, Japan has begun to dismantle some of its barriers to trade. The OECD acknowledged the work being done in Japan:

Tremendous effort has produced real progress in reducing economic intervention in many sectors, among them, large retail stores, gasoline imports, telecommunications, and financial services...There is slow but steady movement toward more transparent and less discretionary regulatory

44 JETRO, *The Changing Service Industries of Japan*, Tokyo, 2000, p. 2.

45 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 641.

practices, partly driven by market demands and partly by recognition of the gap between traditional and international practices. The competition policy framework is stronger. Several initiatives underway to promote the use of international standards will help expand trade flows, to the benefit of Japan's consumers.⁴⁶

7.44 Japan's reform program has already greatly assisted Australian exporters. The liberalisation of Japan's processed food imports has facilitated large-scale exports of Australian dairy products and has made investing in Japan easier and less expensive.⁴⁷ The Committee has shown the benefits that Australian beef and rice exporters have derived from a freeing up of the Japanese market but more work needs to be done in this area.

7.45 Even though Japan has been chipping away at its barriers to trade, difficult hurdles still remain for producers trying to sell their product in Japan. The first obstacle is at Japan's front gate with its tariffs, quota requirements and quarantine regulations.

7.46 With the conclusion of the Uruguay Round Agreement in December 1993, a number of sensitive issues surrounding the access of agricultural and food products were resolved. The Agreement recognised the right of members to take sanitary and phytosanitary measures necessary to protect human, animal or plant life from imported goods provided that such steps were founded on scientific principles. Members were to base their regulations on international standards, guidelines or recommendations, where they existed.⁴⁸

7.47 The Department of Agriculture, Fisheries and Forestry accepted that the harmonisation of international standards was a slow process because of the need for scientific evaluation. It acknowledged that the Japanese processes were basically consistent with the WTO, but they moved very slowly:

We certainly have concerns that some of the processes are not sufficiently quick and timely to ensure that the rights of Japan's trading partners are properly taken into account.

...

...we have succeeded in obtaining new access for Tasmanian Fuji apples and also for easy peel citrus. The processes involved in achieving that access took a long, long period of time. I would be hard-pressed to justify

46 Organisation for Economic Co-operation and Development, *Regulatory Reform in Japan*, OECD, Paris, 1999, p. 15.

47 DFAT, submission no. 32, p. 64.

48 See Articles 2 and 3, 'Agreement on the Application of Sanitary and Phytosanitary Measures' in Agreement Establishing the World Trade Organization.

the long process in terms of the difficult science, and so forth that was involved.⁴⁹

7.48 The issue of obtaining access for Tasmanian Fuji apples and the Japanese concern over fire blight had been around for at least 10 or 15 years before it was finally resolved. Once the Uruguay Round was passed and Japan amended its plant quarantine laws, the path was cleared for the importation of these apples. The first shipment of Tasmanian Fuji apples reached Japan for sale in June 1999.⁵⁰ The Department of Agriculture noted that after the successful conclusion of the Uruguay Round:

...there was certainly a clear indication that the process of proceeding with applications for lifting of quarantine barriers did become more transparent and did speed up quite significantly. Prior to the Uruguay Round it was very unsatisfactory, very slow and obviously used as a trade protection barrier. But following the Uruguay Round there has certainly been a clear indication to us on some of our access issues that there has been far better progress.⁵¹

7.49 Easy peel citrus fruit is another example of where a breakthrough in quarantine requirements has allowed the export of mandarins to Japan. Again, after years of negotiation, the Japanese Government finally in 1999 accepted the efficacy of Australian quarantine treatment for fruit fly.⁵²

7.50 The Japanese are not alone in applying regulations to control imports and, like many countries, still has a long way to go before they adopt regulations that harmonise with international standards, for example, in the food safety area. But, despite the liberalisation measures already taken, a wide variety of implicit trade barriers prevent agricultural and food imports from entering Japan.⁵³

7.51 The Australian Government is working on a number of fronts to encourage Japan to liberalise its trade. In the previous chapter, the Committee noted the importance of Australia's involvement in fora such as APEC and the WTO. There is also much scope for Australia to improve trade flows between Australia and Japan through bilateral negotiations.

49 John Sainsbury and Dennis Gebbie, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 28 May 1999, p. 665.

50 Media Release, Judith Troeth, Parliamentary Secretary to the Minister for Agriculture, Fisheries and Forestry, AFFA99/62T, 16 June 1999.

51 John Sainsbury, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 28 May 1999, p. 665.

52 Department of Foreign Affairs and Trade, Japan, 'Ripe Future for Mandarin Exports to Japan', 15 July 1999. There are a number of examples of further breakthroughs in quarantine regulations. See Media Release, Mark Vaile, Trade Minister, 'Citrus juice exports to Japan set to grow', 26 August 1999.

53 John Sainsbury and Dr Dennis Gebbie, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 28 May 1999, p. 665.

7.52 The Australian Government's strategy through the Supermarket to Asia Council is one way of facilitating trade, especially in expediting some of the processes in clearing products through customs. Under this strategy, the government seeks to provide enhanced opportunity for cooperative resolution of sanitary and phytosanitary issues with Japan. To encourage Japan to accelerate the process of making its quarantine and food standards consistent with its international obligations under the WTO Agreement on Sanitary and Phytosanitary Measures, the government has placed technically qualified plant science and veterinary counsellors in the Australian embassies in Tokyo and Seoul.

7.53 There are also regular bilateral quarantine discussions. The Department of Agriculture believed that these consultations contribute to broadening and deepening the overall bilateral agricultural relationship. It is also working hard under the auspices of the Australia-Japan Ministerial Committee and the so-called partnership agenda developed under that Committee to improve Australia's overall agricultural policy dialogue at a high level with Japan. It concedes that there is still some way to go before achieving the full implementation of the commitments of both governments towards enhancing that policy dialogue.⁵⁴

7.54 The Australian Government can assist exporters in bilateral trade negotiations where a change in rules or regulations will allow the exporter to benefit from a comparative advantage. As an example, and already noted by the Committee, Australian rice growers, who are able to produce new rice out of season, would enjoy a distinct advantage if the government tendering process in Japan was conducted at a time that allowed Australian new rice to be sold in the Japanese market. This is a matter likely to be resolved at a government-to-government level.

7.55 The recent successes of improved or new access to the Japanese market—Fuji apples and easy peel citrus fruit—augured well for a further opening of the Japanese market. But according to the Department of Agriculture, Japan's agricultural sector remains highly protected and is expected to remain so without significant international pressure.⁵⁵

7.56 Australia is also actively involved with the Japanese Government's deregulation action plan. It made a submission in December 1994 outlining regulatory issues that either directly or indirectly affected Australian access to Japan's markets. The emphasis was on diversifying Australian exports towards new items such as apples, melons, mangoes and citrus.⁵⁶ It also provided a submission in 1998 for the first revisions to the Japanese Deregulation Promotion Program (1998–2000). This

54 Dr Dennis Gebbie, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 28 May 1999, p. 659.

55 Dr Dennis Gebbie, Department of Agriculture, Fisheries and Forestry, *Committee Hansard*, 28 May 1999, p. 660.

56 Jamie Anderson, 'Australia's Market Access Agenda Towards Japan', *Pacific Economic Papers*, no. 291, Australia-Japan Research Centre, May 1999, p. 11.

submission highlighted particular problems for Australian exporters and put forward proposals for deregulation in sectors such as housing and construction; telecommunications; agricultural products; legal and financial services; and fast ferries.⁵⁷ (See Appendix 4)

7.57 One of the areas singled out for attention in Australia's submission involved steel-framed housing. Again, one of the main difficulties faced by Australian business in this highly regulated market was the slow-moving bureaucracy and the time and effort required to obtain approval of standards already accepted in Australia.⁵⁸ In its submission, the Australian Government pointed out to the Japanese Government that 'Many Australian companies are using new, innovative steel technologies which allow for much lower thicknesses but exhibit the strength and quality characteristics of much thicker steel.'⁵⁹ Austrade told the Committee that it had spent the last few years seeking Japanese approval for steel framed housing. In April 1999, approval for this steel technology was finally given after eighteen months of consultations and tests and at a cost to Australian business seeking this approval of about \$5 million.⁶⁰

7.58 Lack of information on the details of Japanese building and product standards, codes, rules, regulations and costs also frustrate the efforts of Australian housing companies to move ahead in Japan. Mr Graham Huxley, a representative of Australia Japan Housing Ltd, told the Committee that their main objective, for which they would like funding, is to produce an annual report detailing building costs in Japan. He stated that they wanted to:

...provide members with a document that sets out building materials, labour rates and building costs in Japan for different levels of builders...so that, when builders or building materials manufacturers from Australia go up there, they can look at that document and get an idea of what they are competing with. To get that information is virtually impossible.⁶¹

7.59 Austrade agreed that companies, such as those in the building industry, experience difficulties in trying to establish themselves in Japan. It believed that Australian companies needed to develop a more certain presence in the market than existed at the moment. It also noted that those that had made a start in Japan were quite small companies with limited capacity to push to exploit their gains.⁶²

57 Submission of the Australian Government to the Japanese Government on the Deregulation Promotion Program, 1998, http://www.dfat.gov.au/geo/na/japan/981106_japan_deregulate.pdf (8 February 1999).

58 Graham Huxley, Australia Japan Housing Ltd, *Committee Hansard*, 15 April 1999, p. 361. See also statement by Philip Henry, Department of State, Queensland, *Committee Hansard*, 16 April 1999, p. 419.

59 Submission of the Australian Government to the Japanese Government on the Deregulation Promotion Program.

60 Graham Huxley, Japan Australia Housing Ltd, *Committee Hansard*, 15 April 1999, pp. 359–60.

61 Graham Huxley, Australia Japan Housing Ltd, *Committee Hansard*, 15 April 1999, p. 366.

62 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, pp. 637–8.

7.60 Even so, these small companies are determined to persevere. Japan Housing Ltd made the point forcefully that to succeed in Japan, business must be prepared to be patient and to persist with a long-term commitment to establish themselves as a viable business. While acknowledging that the housing market potential in Japan is 'huge', Mr Huxley stressed that it was not for the 'faint-hearted'.⁶³ In underlining this point and referring to the government's withdrawal of funds to support a secretariat for Japan Australia Housing Ltd, he told the Committee:

That is why we would urge government not to get cold feet and pull the plug on us. We need help. It took the Yanks 30 years to get to the level they are. We have only been there five years.⁶⁴

7.61 The Committee is not in a position to judge the merits of this particular case on funding but it does take the opportunity to underline the difficulties faced by companies, particularly smaller businesses, in establishing themselves in Japan and the importance for the Australian Government to take a longer term view in giving support to these companies.

7.62 It also wishes to draw attention to the Committee's report on APEC, which showed that Australia is taking a prominent role in the area of trade facilitation, particularly in the harmonisation of standards and conformance procedures in the Asia Pacific region. The report drew special attention to and commended the work of CSIRO and the National Association of Testing Authorities, Australia.

7.63 The Committee recognises the efforts of the Australian Government at a bilateral level to further liberalise trade and investment with Japan and to facilitate trade between the two countries. It notes the successes that have been achieved in improving market access but, nonetheless, accepts that there is much more to be done.

Recommendation

The Committee recommends that the Australian Government continue to work with Japan through various programs, including the Supermarket to Asia Council and through Japan's Deregulation Promotion Program, to facilitate trade between the two countries.

7.64 The Committee took special note of the difficulties experienced by Australian companies in obtaining information about Japanese standards and in obtaining official approval for products that already meet Australian standards. Testing and performance

63 Graham Huxley, Australia Japan Housing Ltd, *Committee Hansard*, 15 April 1999, pp. 360, 375. See also Australia Japan Housing Ltd, submission no. 6, p. 3.

64 Graham Huxley, Australia Japan Housing Ltd, *Committee Hansard*, 15 April 1999, p. 376. Also see comments on p. 368.

barriers are particularly severe for small and medium-sized enterprises with their small economies of scale and limited ability to absorb extra costs.

Recommendation

The Committee recommends that the Government persist with its efforts to harmonise standards and conformance procedures with Japan bilaterally and throughout the region.

Distribution system

7.65 One of the main disincentives for people considering selling their product in Japan is the distribution system. Having successfully overcome tariff or quota restrictions and satisfied quarantine, health, safety and other technical standards, exporters may find the prospect of selling their goods in Japan simply too daunting. Japan's complicated distribution chains have long frustrated foreign exporters, who see the web of relationships making up the distribution system as a formidable obstacle to trade. Evidence suggests that barriers to competition seem to restrict market access more in Japan than elsewhere.⁶⁵ The Commission of the European Communities best described the situation:

Newcomers and foreign companies tend to encounter particular difficulties in penetrating the Japanese distribution system. The existence of long-term exclusive or semi-exclusive relationships between established Japanese manufacturers, wholesalers and retailers makes it difficult for merchandise products from alternative suppliers to enter into the distribution network. Analogous difficulties exist in the case of various service industries.⁶⁶

7.66 A number of witnesses raised the matter of non-tariff barriers, saying that Japan still has some very serious impediments to trade, both visible and invisible. The limited sales of Australian-made fast ferries strongly suggest that a number of invisible barriers to imports of sophisticated manufactures are operating in Japan. Dr Mark Beeson argued that, because of the structure of corporate relationships in Japan, there is absolutely no interest in buying fast ferries from outside Japan if they can buy them from another corporate grouping. This is so even if the price is greater than they would pay for the Australian product and the quality of the product is slightly inferior to the Australian one. He told the Committee:

There are a number of barriers like regulations, red tape and corporate relationships that are not always visible things but systematically work

65 Austrade, submission no. 35, p. 9. See also Jonathan Coppel and Martine Durand, 'Trends in Market Openness', *Economics Department Working Paper no. 221*, Organisation for Economic Co-operation and Development, August 1999, p. 5.

66 Commission of the European Communities, *List of EU Deregulation Proposals for Japan*, 12 October 1998, p. 8.

against Australian exporters being able to supply increasing amounts of goods into Japan, even if they produce the sorts of goods that Japan actually wants to buy.⁶⁷

7.67 Impediments to competition in Japan, nonetheless, are being dismantled and, as noted by the Committee in Chapter 4, even ‘the buy Japan policy’ is being undermined. Over the years, distribution options have increased and foreign products are becoming increasingly acceptable.⁶⁸ Not only are Japanese consumers more receptive to new products and Japanese business to new ideas but also the ability to sell goods and services in Japan has improved with changes in access rules and in the distribution system in Japan.

7.68 Japan, however, still retains its forbidding reputation as a difficult market in which to do business. Securing a foothold in Japan is a matter of having the know-how and the right connections.⁶⁹ For many years, advice for exporters to Japan centred on the need to establish close personal relationships with Japanese agents and, where possible, customers.⁷⁰ Many experts advised that people seeking to enter the Japanese market should arrange tie-ups with Japanese agents or form partnerships with Japanese companies for the distribution and sale of their product.⁷¹ Food and agricultural industries in Australia are increasingly linking up with foreign firms or organisations. The establishment in 1997 of a joint venture company between the Australian Wheat Board and Zennoh to market feed grains in Japan is an example of the type of arrangement that is becoming increasingly common. The Australian Dairy Corporation has designated Mitsubishi Corporation, Tomen Corporation, Toshoku Ltd and Mitsui & Co. Ltd as its sole import agents. The Ricegrowers Co-operative Ltd has formed a joint venture with Mitsuhashi Inc.⁷²

7.69 The tie-ups that are being established between producers in Australia and Japanese consumer cooperatives to market horticultural products and livestock products in Japan, although on a much smaller scale, have the potential for growth. These linkages are important for Australian companies because they provide an

67 Dr Mark Beeson, *Committee Hansard*, 16 April 1999, pp. 482–3.

68 DFAT, submission no. 32, pp. 21–3.

69 Professor Teresa Morris-Suzuki, *Committee Hansard*, 24 May 1999, p. 606.

70 For example see Australian Department of Trade, ‘Persistence, Performance and Price’, *Report of the Japanese Market Access Promotion Mission to Australia, November 1984*, AGPS, Canberra, 1985, pp.16–17.

71 JETRO, *Japanese Market Report—Regulations & Practices—Cheese*, No. 30, March 1999, p. 9; see also advice offered in JETRO Reports, no. 10, p, 13; no. 15, p. 23; no. 23, p.19.

72 See Paul Riethmuller, ‘Major Trends Affecting Australia’s Agricultural Industries: Have they Taken a Turn for the Worse?’, *Economic Issues* no. 3, Department of Economics, the University of Queensland, November 1998, pp. 14—15.

established distribution network and a means of obtaining specialised knowledge on the particular requirements of Japanese consumers.⁷³

7.70 There are compelling reasons for Australian producers to seek out the assistance of Japanese agents to help market their products in Japan. But there can be significant disadvantages. The coal industry highlights this problem. Japanese companies, through Japanese trading agents, have a strategic and weighty presence in the marketing of commodities such as coal. This has both a positive and negative aspect for the Australian producer. QCT Resources noted that when it comes to knowledge of Japanese markets, the hand of Australian exporters is held tightly by Japanese trading agents who assist in Japan. The agents, however, are not only assisting Australian exporters but are very close to Japanese industry. QCT Resources explained:

There is no doubt that in the relationships and in the negotiation process we have relied very heavily on the Japan partner in the negotiation. Anybody contemplating entry into Japan cannot do it unless they have a close Japanese partner that is credible and financially stable.⁷⁴

7.71 The NSW Minerals Council also commented on the issue of Japan's trading agents and the possible control of the coal market by Japanese customers. It made clear that the Japanese steel mills and power utilities are not major investors in the Australian coal industry. Further, while they have a certain share in the industry, the Americans, the British, and other European countries have a far more significant investment in the industry than the Japanese customers. It concluded:

The trading houses do have a certain stake in the industry, but I think we can be misled by the fact that there is a high proportion of overseas ownership in the coal industry and by then tying that to some sort of price manipulation.⁷⁵

7.72 The Council also responded to the proposition of introducing a collective approach to coal marketing and pricing. It told the Committee that this would be 'a highly dangerous approach and not appropriate'. In pointing out that the negotiation process for fixing a coal price was very complicated and that there were no simple answers, the Council suggested that the weight of evidence indicated that trying to form seller cartels is a 'very dangerous way to go'. It argued that the customer can place a very different interpretation on the move to a collective approach. If Japanese coal buyers saw their major coal supplier, Australia, trying to form a collective approach, 'that would have a major impact on the way they went about their business,

73 Paul Riethmuller, 'Major Trends Affecting Australia's Agricultural Industries: Have they Taken a Turn for the Worse?', *Economic Issues* No. 3, November 1998, pp. 14–15.

74 Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 16 April 1999, p. 491.

75 Denis Porter, New South Wales Minerals Council, *Committee Hansard*, 14 April 1999, p. 272.

in terms of where they bought their coal and in terms of what share coal would get in Japan as opposed to gas, nuclear and so on'.⁷⁶

7.73 Dr Rawlings went further to note that Australia is not the only supplier of coking coal which also comes from Canada, and the United States and some soft coking coal from Indonesia. He stressed:

...we are not the only country in the world that does have resources in the ground waiting to be developed. I must admit that when I hear talks of, or consideration being given to, there being some ability to control this industry the first thing the Japanese will do is use their considerable financial muscle to invest in another coal resource somewhere else and compete against us...there are very clear reactions to the concept of control and intervention that the Japanese have had a history of being able to implement.⁷⁷

7.74 This tension between Australian commodity producers and Japanese customers came to the fore in July and early August 2000 when Rio Tinto launched an aggressive hostile takeover bid for rival mining group North Ltd. Fearing that their negotiating position could be weakened and that Rio would dominate the iron ore industry in Australia, North's Japanese partners—Nippon Steel Corp, Mitsui and Co. and Sumitomo Metal Industries Ltd—strongly opposed the bid. In an attempt to prevent the concentration of control of the iron ore industry in Australia, the Japanese steel mills retaliated by supporting Anglo American's counter move to takeover Norths.⁷⁸ If successful, this arrangement would keep a third supplier of iron ore in Australia. As economic journalists Ian Howarth and Andrew Cornell explained:

The fight for control of North has triggered a critical battle over Japanese steel producers' historic power to divide and rule among Australia's key suppliers of coal and iron ore.

The steel Cartel see Rio's bid for North as a threat to the survival of the Japanese steel sector, long a protected industry, in its current state.

The Japanese want at least three major iron ore exporters in the Pilbara region of Western Australia.

They are concerned that rationalisation would reduce their ability to play Australian producers off against one another in negotiations on price.⁷⁹

76 Denis Porter, New South Wales Minerals Council, *Committee Hansard*, 14 April 1999, p. 274.

77 Dr Christopher Rawlings, QCT Resources Ltd, *Committee Hansard*, 16 April 1999, pp. 490–1.

78 See David Uren, *Weekend Australian*, 29–30 July 2000, p. 42; Andrew Cornell, Tokyo, *Australian Financial Review*, 19 July 2000, p. 15, 24 July 2000, p. 1 and 13, 27 July 2000, p. 11, 1 August 2000, p. 18; Stewart Oldfield, *Australian Financial Review*, 4 August 2000, p. 46; Jane Counsel, *Sydney Morning Herald*, 4 August 2000.

79 Ian Howarth and Andrew Cornell, Tokyo, 'Cartel wars: Rio targets Japanese in North battle', *Australian Financial Review*, 26 July 2000, p. 1.

7.75 This struggle between Rio and the Japanese mills underlines Japan's desire to maintain its strong position as a buyer and to exercise significant control over Australian iron ore prices.⁸⁰ Clearly, Rio's move to take over a major competitor and supplier of iron ore to Japan has sparked a strong and angry reaction from the Japanese steel cartel.

7.76 A different situation has developed with LNG producers. The Australian LNG industry, in looking for better ways to market its product, is considering multimarketing and diversifying its markets and getting away from the single one-to-one with its product to Japan. According to Woodside, the Japanese buyers seem to appreciate the gas industry's need to reassess its marketing strategy. Nonetheless, Woodside remains very aware of the valuable trading relationship that has grown up between Australia and Japan. It made clear that it is keen to ensure that if their Japanese customers require parts of its project to be dedicated to them, then the longstanding relationship it has with them will continue. Woodside told the Committee:

...we are also looking at innovative ways to market LNG elsewhere. There is a major push on now to present Australian LNG projects with a single face so that confusion in the market place...can be mitigated and reduced and we can present a united front and then worry about which project here produces the LNG.⁸¹

7.77 Witnesses also raised concerns about the extent of Japanese involvement in the marketing and selling of beef in Japan. Dr Mark Beeson argued that when the imports of beef into Japan increased, Japanese corporations responded by immediately moving into Australia where they bought up 'every aspect of the industry in Australia and between Australia and Japan'. He argued:

Japanese corporations basically control the whole beef producing industry from the farm gate to the supermarket shelf. This means that Japanese corporations can shift profits up and down the value production line. They can realise profits in Japan so that Australian producers, the people who actually grow beef, get very little for their product. The profits are realised back in Japan.

...

...it is transfer pricing, and the Japanese corporations are very good at this.⁸²

80 Andrew Cornell wrote an interesting article on the nature of Japan's steel cartel, 'The family nature of Japan's steel cartel', *Australian Financial Review*, 31 July 2000, p. 8.

81 Erica Smyth, Woodside Energy Ltd, *Committee Hansard*, 25 February 1999, p. 207.

82 Dr Mark Beeson, *Committee Hansard*, 16 April 1999, p. 487.

7.78 The Queensland Government expressed similar worries about the Japanese involvement in the beef industry, particularly this practice of price transferring. It submitted:

Several Japanese companies have invested heavily in Queensland abattoirs and cattle properties. Most of the production from these facilities is exported unprocessed to Japan. However, many of these businesses are run at a loss in Queensland with the value-adding and packaging of the product done in Japan.

The bulk of profits in the beef sector are generated by the wholesale marketing chain in Japan. Raw product is supplied into Japan by Queensland but Queensland producers and abattoirs cannot maximise their margins and receive premium prices without value-adding and packaging beef products in Queensland. Therefore, there is a need for Queensland beef to be value-added and pre-packaged in Australia before it is exported to Japan.⁸³

7.79 The current tight economic situation in Japan means that the temptation to shift profits back to Japan is greater. The trading company's first loyalty or primary instinct is to pass the burden on to their suppliers by exerting downward pressure on prices; for example, falls in the negotiated price for iron ore and coal earlier in 1999. Mr Dodds argued that, if the trading companies are too successful in placing the economic squeeze on Australian producers, they will defer some hard decisions that they have to make about their own structuring and behaviour and will be passing on the costs of their own inefficient management to Australian suppliers.⁸⁴

7.80 At the moment, Japanese trading companies occupy a central position in Australia's trading activities with Japan and are reluctant to relinquish their influence. Austrade pointed out that these companies carry just over two-thirds of Australia's total exports to Japan. It submitted that they seek to place themselves strategically in the trading spectrum—they will occupy and control the ground at all stages onward from the quarry or farm gate. Moreover, they encourage Australian companies to assume that marketing in Japan is too hard—and to a degree they have succeeded. Mr Dodds told the Committee that Japan has the largely well deserved image of being a difficult market to work in. So that while Australian companies are prepared to invest in places like China and Vietnam, which are also difficult markets, Japan has 'most people spooked'. According to Mr Dodds, Australian companies are prepared to leave business to the trading companies.⁸⁵

7.81 Clearly, Australian producers rely heavily on Japanese companies to market their product. This close association brings both advantages and disadvantages for Australian producers. It allows them to benefit from the expertise, local knowledge

83 Queensland Government, submission no. 18, p. 34.

84 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 629.

85 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 632.

and the business contacts that Japanese companies bring to the relationship. On the other hand, a Japanese agent, especially one of the large trading companies, can close the Australian producer out of key strategic positions in the production and distribution loop and manipulate the market.

7.82 There are important and fundamental changes, however, taking place in the modes of retailing, marketing and distribution in Japan that should encourage Australian businesses to reassess their marketing strategy. The process of deregulation has made inroads into the established distribution network. The easing of the Large-Scale Retail Store Law, for example, has encouraged larger, more efficient retail outlets.⁸⁶ The corner store is being replaced by major retailers and consortiums.

7.83 The recession has accelerated the pace of restructuring. As explained in Chapter 3, the downturn in the economy has intensified competition in the market place with price conscious consumers diligently comparing prices and producers looking keenly to cut production costs. The search for value for money is increasing downward pressure on prices. As business conditions continue to tighten, there has been a growing urgency to simplify the distribution channels.⁸⁷ Developments such as the increasing popularity of supermarkets and convenience stores, the rapid growth of discounting, and associated direct importing; the emergence of regional markets; the beginnings of an organic food market, and the entrance of foreign companies into the Japanese market are dramatically redefining the way goods are distributed and sold in Japan.

7.84 The gradual collapse of the traditional multi-layer distribution systems creates its own momentum.⁸⁸ The informal cartels within Japan and cross-shareholding, which have made it very difficult for outsiders to secure a presence in the system, are now breaking down. The growing prevalence of larger retailers and wholesalers has meant that they have been able to shoulder their way into the distribution system, increasing their influence at the expense of manufacturers and trading companies. According to Austrade, this growing involvement of large retailers and wholesalers in the distribution chain has:

...further weakened the relationships between firms that had traditionally held a tight grip on their respective markets and allowed foreign suppliers

86 JETRO explained that the Large-Scale Retail Store Law was amended in January 1992 to ease many of the regulations that made it difficult to open large stores. The law has been amended on successive occasions but as of June 2000 will be replaced by a newly enacted Large-Scale Retail Store Location Law. It stated 'Of all the various deregulation policies currently being implemented, it has been among the first sectors to undergo significant change and to have a significant impact on the lives of ordinary people.' JETRO, *The Changing Service Industries of Japan*, JETRO, 2000, p. 15.

87 Hiroshi Nakano, Japan External Trade Organisation, Sydney Inc, *Committee Hansard*, 3 September 1999, p. 788.

88 Austrade, submission no. 35, p. 63.

able to deal directly with retailers or major wholesalers to extract greater profit for themselves from the value chain.⁸⁹

7.85 The practice of smaller companies exercising choice is also loosening the hold of the Japanese trading companies on trade in Japan. Austrade observed:

We are seeing ordinary companies in the Japanese market beginning to change their own purchasing policies in increasing numbers. By that I mean that they are buying directly more and more. They are quite capable of doing it. It is just that the trading companies have successfully manipulated this relationship and now, under recessionary pressures, it is hard to keep that game going.⁹⁰

7.86 The credit squeeze is also forcing the trading companies to release their grip on strategic positions in the trading system in Japan. Japanese trading companies are no longer able to supply export finance at attractive rates on a long-term basis. In Austrade's words, 'their ability to retain that position in the middle as the necessary link between Japanese buyers in Japan and foreign suppliers—a position that they have been very successful at keeping over the past decades—is now coming under real pressure'.⁹¹

7.87 Austrade was concerned that Australian companies could miss out on opportunities to capitalise on the changes taking place in the Japanese trading companies. Mr Greg Dodds told the Committee that he knew of examples of Australian companies, on their own initiative, breaking off their established trading company relationships and selling directly to retailers in Japan. They had chosen to market their products using either a retail brand or an Australian brand. Austrade pointed out that often they decided to mix the labelling—the supermarket chain would obviously brand the product as its own product but the supply from Australia would be a high point.⁹²

7.88 Austrade also pointed out the possibility of one or more of the large trading companies failing and the immediate difficulty that Australian companies relying on that company for their access to the Japanese market would face. It warned companies to be aware of their vulnerability should their Japanese trading company experience financial difficulties or even close its doors.⁹³

7.89 Also of concern to Australia is the number of mergers and acquisitions taking place in Japan. If a buyer of Australian products or a company that has investments in Australia is taken over by an overseas company, there is no certainty that it will

89 Austrade, submission no. 35, p. 63.

90 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 633.

91 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 629.

92 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 634.

93 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 630.

continue to use Australian goods or to invest here. According to Austrade, ‘...there is a distinct possibility that, for their own strategic reasons, they would shift their sourcing to, say, Canada, the US or so on’.⁹⁴ The most recent speculation about a withdrawal from the automobile manufacturing industry in Australia by Mitsubishi after its takeover by DaimlerChrysler highlights the importance of Japanese investment in Australia.

7.90 The slowdown in the Japanese economy may work to the advantage of Australian exporters seeking to improve or increase their involvement in the development and marketing of their product. Austrade believes that a recessionary environment is a good one in which to conduct business in Japan and to present fresh ideas and push new products. According to Austrade, trading with the Japanese during good times is strictly on their terms. During times of economic uncertainty, however, when they are under pressure, they will seriously consider alternatives.⁹⁵

7.91 The Committee believes that Australian exporters should take this opportunity to reassess their business links with Japanese companies. In reviewing the arrangement they have with their agents in Japan, they should keep in mind ‘the whole of chain approach’. They should question the role of the middleman in getting the product onto the shelves and consider the possibility and benefits of becoming more involved in the total process, particularly in the marketing of their products.

7.92 The Ricegrowers Co-operative is aware of the importance of securing a greater say in how their product progresses from the farm gate. In 1994, it formed a joint venture company, the Sunrice Inc, with a large Yokohama based rice miller, Mitsubashi Inc. The Sunrice company is licensed to import only Australian rice. It was formed to enable Ricegrowers Co-operative, through the Sunrice company, to capture more of the margins which accrue at each step in the Japanese supply chain. In explaining the reasons for establishing this company, Mr Milton Bazley stated that they were trying to:

...achieve greater tonnages through having our own company and potential lobbying within the Japanese system. Also, at each stage of the supply chain in Japan, there are huge margins to be made, and by us developing a company that is importing the rice and milling and is packaging the rice in Japan, it gives our shareholders the opportunity to share in those margins within Japan.⁹⁶

7.93 Over recent years, some innovative Australian exporters have availed themselves of the opportunities on offer in Japan and have managed to enter the Japanese market. Wine and cheese makers are good examples.⁹⁷

94 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 639.

95 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 632.

96 Milton Bazley, Ricegrowers Co-operative Ltd, *Committee Hansard*, 17 May 1999, p. 537.

97 Terence White, Australia-Japan Foundation, *Committee Hansard*, 19 February 1999, p. 46.

7.94 Schiavello is a Melbourne furniture company selling about 800 workstations to NTT, the domestic telecommunications carrier. Mr Dodds told the Committee:

Two or three years ago, selling anything to NTT was a nightmare because of the regulations surrounding it. Those were by and large designed to protect the interests of established Japanese suppliers.⁹⁸

7.95 Aside from the opportunity for Australian producers to become more involved in the sale and marketing of their product in Japan, investment potential is opening up for Australian companies.

Australian investment in Japan

7.96 Traditionally, Japan has not attracted significant overseas investment to its shores. In 1997, the Minister for International Trade and Industry, Mr Shinji Sato, observed that the ratio of foreign direct investment into Japan at the end of 1995 was only 7% of Japanese direct foreign investment overseas. He noted this unusually low level when compared to other major industrialised countries such as the 79% for the United States, 78% for France, 77% for the United Kingdom and 41% for Germany.⁹⁹

7.97 In 1998, the Commission of the European Communities noted that while Japan had a formal policy of encouraging foreign investment, high costs in Japan and over-regulation remained a major disincentive for foreign firms. It pointed out:

Factors deterring greater foreign investment in Japan include high business costs, high corporate taxation, difficulties in accessing distribution channels, the general regulatory environment and non-transparent business practices. The recent performance of the Japanese economy has further dampened foreign investment.¹⁰⁰

7.98 This situation is changing and historic difficulties of investing in Japan are disappearing. Austrade told the Committee that the level of foreign investment in Japan is still low but increasing.

7.99 JETRO believed that Japan is definitely becoming a friendlier place for overseas investment now that major problems, such as the effects of high domestic costs and recruitment of staff have been reduced significantly. It maintained that overheads in Japan continue to decline as deflation places downward pressure on prices, along with the flowthrough effects of deregulation. Recruitment too has changed, reflecting not only restructuring and lay-offs in Japanese companies but also the effects of social value changes as employees move away from Japan's lifetime employment ethos. Mr Hiroshi Nakano, Managing Director, JETRO, Sydney Inc,

98 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 636.

99 Shinji Sato, English Translation of Minister Sato's Speech at the Foreign Correspondents' Club of Japan, 16 June 1997, <http://www.miti.go.jp/press-e/f300001e.html> (24 April 2000).

100 Commission of the European Communities, *List of EU Deregulation Proposals for Japan*, 12 October 1998, p. 6.

advised that as the investment trend from the rest of the world is already clearly evident in Japan, Australian companies should not lag behind.¹⁰¹ JETRO has in place various programs to assist Australian businesses including the Export to Japan Program and the Region to Region program.

7.100 Austrade agreed that investing in Japan had become easier, particularly as reforms were beginning to remove major obstacles. It noted that deregulation, such as the relaxation of the foreign currency exchange laws, had given foreign investors who had entered areas, which had previously been dominated by Japanese companies, 'some early and unexpected windfalls'. It submitted:

Sophisticated foreign players have real opportunities to enter the market whether it be through know-how transfer or capital participation, as illustrated by the number of US and European firms that have moved into these sectors in just the past year.¹⁰²

7.101 The slowdown in the economy had also created attractive opportunities for overseas investors. To consolidate their hold over business activity in Japan, the large Japanese companies had, over many years, created a network of subsidiaries to deal with specialist areas of business. This structure is now starting to crumble. Austrade told the Committee that at the beginning of May 1999, the trading companies announced collectively that they were selling off over a thousand of these subsidiaries, a number of which managed the more technical niche market areas of trading companies business, such as software. According to Austrade, such developments offer significant investment opportunities for those wishing to establish a presence in the Japanese market. The Americans are taking this opportunity to invest in Japan.¹⁰³

7.102 Mergers and acquisitions offer particular opportunities for foreign investors. Japanese companies experiencing economic difficulties are now welcoming foreign assistance. JETRO explained that one cause for the growth in mergers and acquisitions was the need for Japanese firms to sell:

The recession since the second quarter of 1997 has hit Japanese firms profits, and they are now restructuring by selling off unprofitable businesses and strengthening their financial structures. This need to sell has coincided with foreign firms interest in buying, hence resulting in more M&As targeting Japanese firms. This is particularly so in the real estate and financial sectors.¹⁰⁴

101 Hiroshi Nakano, Japan External Trade Organisation, Sydney, Ltd, *Committee Hansard*, 3 September 1999, p. 789.

102 Austrade, submission no. 35, p. 9.

103 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, pp. 629–630.

104 JETRO White Paper on Foreign Direct Investment (1999), p. 60. See also Paper 'Prospects for the Japanese Economy', The Japan Research Institute Ltd, Economics Department, July 1999, p. 9.

7.103 Austrade pointed out that ‘Majority acquisitions, joint venture buy-outs—just establishing a minority interest is obviously a sensible first step for people’.¹⁰⁵ An example of a purchase of a significant minority interest was Renault’s 37% purchase of Nissan in 1999. In March 2000, DaimlerChrysler announced that it was taking effective control of Mitsubishi Motors through a 34% holding.¹⁰⁶

7.104 Undoubtedly, the investment environment in Japan is becoming more hospitable for overseas interests. Overall, most foreign firms are finding prejudice against them declining, recruitment problems lessening and legislative controls on business easing.¹⁰⁷

7.105 This friendlier commercial setting together with growing investment opportunities in Japan should encourage Australian business to consider investing there. Austrade was encouraging people at least to consider such investment and offering support to companies contemplating setting up business there. It thought that the message about the possibilities for Australian investment in Japan was starting to filter through to the business sector but needed to be more forcefully, frequently and directly delivered. Officers from Austrade recognised that they needed to drive home this message about opportunities to potential Australian investors and intended to hold meetings with major accountancy and business consultancy firms. Mr Dodds told the Committee:

Part of the message we are delivering here is that investment in Japan in many ways is attractive in its own terms and people should look at it in that way, but it is not really an option to sit back and think ‘...we’ll think about it next year. In the meantime, everything will remain the same’. It might not. There is a chance of losing as well as gaining here.¹⁰⁸

7.106 Austrade, however, noted that Japan is a significantly different investment proposition from many other countries:

The people who are available to invest in by and large are the people who are failures or semi-failures. There is something wrong for a start. Even in Japanese terms, they cannot succeed or stay above water. If they are going to become a good investment proposition, they have to be given a new product and a new way of doing things and led to success...you have to bring something more than money to the table.¹⁰⁹

7.107 Many witnesses reinforced the view that Japan offered great potential for business; that despite the recession in Japan, opportunities were opening up for

105 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 638.

106 *AsiaNow*, 5 November 1999, vol. 25, no. 44.

107 JETRO, *JETRO White Paper on Foreign Direct Investment 2000*, p. 63.

108 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 639.

109 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 639.

Australian exporters and it was time for Australian business to capitalise on them.¹¹⁰ Both Mr Pokarier and Mr Dodds, however, added a cautionary note, reminding Australian producers that even with regulatory reform, there is 'no guaranteed pay-off for foreign firms in the Japanese market'. Mr Pokarier stressed that new comers to the Japanese market must start with a recognition that most sectors are characterised by intense domestic competition. There are hundreds of publicly listed companies in Japan that are world market leaders in their product line including Sony, Mitsui, Nintendo and Sega. These firms are world class and have grown out of intense domestic competition.¹¹¹

7.108 A number of academics at the Australia-Japan Research Centre are also very enthusiastic for Australian investors to become involved in the Japanese market. They identified specific areas such as distribution, processed foods, finance, telecommunications and computer software applications, where changes are occurring rapidly and where Australia has proven expertise and noted success. They stated:

In these sectors, where openings are greater than elsewhere and where other foreign players are acting, it is particularly important that Australian firms reassess the current opportunities for them in Japan and the competitive threats from rival firms who are prepared to invest in the Japanese market.¹¹²

7.109 They, too, issued a word of caution. Despite opportunities in the current circumstances, they urged companies to 'spend time and effort to understand and establish themselves in the Japanese market before undertaking substantial investments there'.¹¹³

7.110 In summary, Japanese consumers are demanding wider choices and better services, traditional business relationships are opening up, regulations are being dismantled or revised, new players are nuzzling in on the previously closed distribution system, and increased foreign involvement is now accepted as inevitable. Moreover, there are Japanese businesses looking to be rescued from their financial difficulties. The Committee believes that it is time for Australian firms to consider establishing a presence in Japan. Continuing reform presents opportunities but Australian producers must be alert, well-informed and motivated.

110 Professor David Allen, *Committee Hansard*, 25 February 1999, p. 181; Dr Craig Freedman, *Committee Hansard*, 15 April 1999, pp. 345–6; Perce Butterworth, New South Wales Department of State and Regional Development, *Committee Hansard*, pp. 394–95.

111 Christopher Pokarier, *Committee Hansard*, 16 April 1999, pp. 423, 432.

112 Peter Drysdale, Toshi Naito, Ray Trewin and Dominic Wilson, 'The Changing Climate for Foreign Direct Investment into Japan', *Pacific Economic Papers*, no. 293, Australia-Japan Research Centre, July 1999, p. 37.

113 Peter Drysdale, Toshi Naito, Ray Trewin and Dominic Wilson, 'The Changing Climate for Foreign Direct Investment into Japan', *Pacific Economic Paper*, no. 293, Australia-Japan Research Centre, July 1999, p. 39.

Value-adding in Australia

7.111 During the course of the inquiry, the issue of value adding to goods in Australia destined for export was raised. Traditionally, Australian exports that have originated in the rural sector have been unprocessed or only lightly processed commodities. These include wheat, raw sugar, skim milk powder and wool. According to Mr Paul Reithmuller:

Most of the value adding activity has occurred in the wool mills of Korea, the flourmills of China and the dairy factories of Indonesia. The prices of bulk commodities have been trading downwards for years and this has been perhaps the main factor behind the move to do more value adding in Australia. The grape industry has probably been the most successful judging by what it has achieved on export markets with wine.¹¹⁴

Cheese is another value-added product that is selling well in Japan.¹¹⁵

7.112 But as noted earlier, unprocessed commodities such as coal, iron ore and grains dominate Australia's exports to Japan. The structure of Japan's overall imports, however, is changing as Japan continues to open its markets and to purchase more value added goods and services. Importantly though, Japan's imports from Australia remain predominantly resources and not consumer goods.

7.113 In other words, while Japan is importing more value-added goods and services, Australia has not shared in this expanding market. This situation also runs contrary to the overall trend in Australia's export trade. In brief, Australia has been increasing its exports of value-added goods and services but not to Japan.¹¹⁶ Mr Panagiotopoulos made the following point:

In 1993 11.5% of Australia's exports to Japan were manufactures (excl Foodstuff) and in 1997 this figure was 13.5%. In 1993, 97.7% of imports from Japan were manufactures (excl Foodstuff) and in 1997 this figure was 97.9%.¹¹⁷

7.114 The Committee noted in the last chapter that the export of manufactures to Japan had peaked in 1988 at 17.7% of total Australian exports to Japan, which fell to

114 Paul Riethmuller, 'Major Trends Affecting Australia's Agricultural Industries: Have they Taken a Turn for the Worse?', *Economic Issues No. 3*, November 1998, p. 14.

115 Paul Riethmuller, 'Major Trends Affecting Australia's Agricultural Industries: Have They Taken a Turn for the Worse?', *Economic Issues No. 3*, November 1998, p. 14; and Terence White, Australia-Japan Foundation, *Committee Hansard*, 19 February 1999, p. 46.

116 Manuel Panagiotopoulos, *Committee Hansard*, 14 April 1999, pp. 215, 219.

117 Manuel Panagiotopoulos, *Japanese and Australian Trade 1988-1997*, Manuel Panagiotopoulos, AJEI Communications, Sydney, p. 19.

14.7% in 1990.¹¹⁸ This pattern of trade where Australia is lagging behind selling value added goods to Japan warrants careful study.

7.115 Witnesses were keen for Australia to do more value-adding to products before exporting. Mr Owen Clare, adviser with Saw James Capel told the Committee that Australians 'have for too long focused on digging it out and selling it, and not adding any value, and we are now paying the price for that, because we are the victim of whatever price these importing countries are prepared to pay for the exports that we want to sell them'.¹¹⁹ Mr Ken Court observed that the iron ore industry stands out as a complete misfire in this area of downstreaming.¹²⁰ He advocated the development of a very large gas-fired steel industry in Australia based on new technology that would have environmental concerns as its strongest selling point. He told the Committee:

...firstly, we have the gas supply and, secondly, we have got the technology now for large scale electric arc furnace production, no longer mini-mills, and it has changed.¹²¹

7.116 Mr Court suggested that the Federal Government should be joining the State Governments in putting infrastructure in place to facilitate downstreaming. The Department of Industry, Science and Resources, in responding to suggestions about companies embarking on value-adding operations, maintained that such decisions were 'a judgment call that individual companies will have to make in terms of trying to attract investment'. It explained that the Australian Government was involved through programs such as, Invest Australia, which is working to attract investment into the downstream processing sector. While acknowledging that at the end of the day the decision to value-add is a commercial one, the Department agreed that the Australian Government 'could be looking at any areas from which blockages to that sort of activity could be removed'.¹²²

7.117 JETRO is actively promoting the export of value added goods to Japan. It, nonetheless, agreed that the decision to value add is a fundamental question of economics. Put succinctly: 'You need to be competitive.'¹²³ Applying this general principle to the iron ore industry, Dr Freedman questioned the economic wisdom of developing more steel producing plants in Australia. He observed:

118 See chapter 5, para 5.55.

119 Owen Clare, Senior Equities Adviser, Saw James Capel Ltd, *Committee Hansard*, 24 February 1999, p. 150.

120 Kenneth Court, *Committee Hansard*, 24 February 1999, p. 144.

121 Kenneth Court, *Committee Hansard*, 24 February 1999, pp. 138, 140.

122 Craig Burns, Department of Industry, Science and Resources, *Committee Hansard*, 28 May 1999, p. 693.

123 Hiroshi Nakano, Japan External Trade Organisation, Sydney Inc, *Committee Hansard*, 3 September 1999, p. 795. See also comments by Manuel Panagiotopoulos who acknowledged that value adding to Australian commodities in Australia was not happening because 'it is not economically viable for corporations to do that here'. He suggested Australians need to ask the right questions to find out why this is not the case, *Committee Hansard*, 14 April 1999, p. 220.

Looking at the world market, the last thing it needs is steel. The Japanese are cutting back. Are we going to be as efficient as the Pohung works in South Korea? No. Is our comparative advantage in steel making? No I think not. I think we would be barrelling into a declining world manufacturing area; we would be coming in there 40 years at least too late.¹²⁴

7.118 In assessing the feasibility of value adding to iron ore in Western Australia, the Western Australian Treasury argued that there are two sets of conditions:

...competitive cost structures domestically—so in that sense the gas pipelines; deregulation of the gas market has been quite profound in setting up the right conditions—and reforms to the labour market, introducing flexibility. In that sense our domestic conditions are now quite well placed to enter into full-scale downstream processing.

7.119 However, the Western Australian Treasury returned to the basic issue of economics—‘you require strong markets, the timing has to be right’.¹²⁵

7.120 There are clear advantages to value adding or downstreaming. It allows the economy a greater capacity to capitalise on its resources and it means more jobs and greater profits. Austrade used the tuna industry to illustrate the benefits that accrue with value adding in Australia:

Take the marine products: rather than just sending tuna off to the market, frozen into things like logs, the tuna has to be cut up and processed here and then sent off to the supermarket in the form it can use on its shelves. If the Australian company is on its toes, it can start talking about doing the packaging in Australia so the product goes off to Japan in a state that can more or less be put straight onto a Japanese supermarket shelf. This employs a lot more people here.¹²⁶

7.121 There are also risks associated with value adding. The Western Australian Treasury pointed out that one of the main trade-offs with downstreaming is narrowing the market for the product.¹²⁷ Overall, Dr Sheales, Manager, Agriculture and Food Economics Branch, ABARE, submitted:

The reason that we are predominantly an exporter of raw materials is that that is what we do best. We have a very clear comparative advantage and that has therefore been reflected in the way our industries have developed. It is not to say that there are not various forms of processing already taking place in this country. The aluminium industry would be a good one where a

124 Dr Craig Freedman, *Committee Hansard*, 15 April 1999, p. 354.

125 Timothy Marney, Treasury Department of Western Australia, *Committee Hansard*, 25 February 1999, p. 166.

126 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 634.

127 Timothy Marney, Treasury Department of Western Australia, *Committee Hansard*, 25 February 1999, p. 166.

fair bit of the alumina we produce is actually turned into metal because we have cheap electricity which is the key other input.

...It really depends on companies making their own commercial decisions within the environment they operate in. To varying degrees they will add value within the country, but for other reasons it is not worthwhile for them to do that.¹²⁸

7.122 Although the decision to value add is a commercial one, Australian exporters to Japan should be fully aware and alert to the gains to be won from value adding to their product. Austrade pointed out that producers need help to identify the opportunities. Mr Dodds told the Committee, 'if they have been going through a trading company they usually do not know where their product goes in the end—and the trading company is singularly unobliging in giving them that information'.¹²⁹

Making Australian products more competitive—infrastructure development

7.123 The decision to value add hinges on comparative advantage as does any commercial decision by Australian producers considering exporting. Japan is a highly competitive market and Japanese consumers set very high standards for the quality of the goods and services they purchase. Domestic policies can help Australian exporters improve their competitiveness.

7.124 The Western Australian Treasury suggested that Australia should consider policies that will foster a domestic environment that will place Australian exporters in a better position. It wanted to highlight the need:

... to ensure Western Australia and Australia's competitiveness is continually enhanced through the provision of appropriate infrastructure as efficiently as possible, through flexible labour markets which enable us, on the one hand, to be competitive and, on the other hand, to be reliable, and through general micro reform to ensure the economy continues to be as competitive as it can be on the international stage.¹³⁰

7.125 Mr Robert Cameron, Chairman, Australian Coal Association, drew attention to a number of changes that have brought direct benefits to Australian exporters, including reform to Australia's industrial relations law and to Australia's national competition policies; the creation of complete electricity markets which have lowered prices for major industrial users; and rail freight reductions achieved in NSW and Queensland. Although he argued that reforms are far from complete especially in regard to rail reforms, he stated:

128 Dr Terence Sheales, *Committee Hansard*, 21 June 1999, p. 741.

129 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, pp. 634–5.

130 Timothy Marney, Treasury Department of Western Australia, *Committee Hansard*, 25 February 1999, pp. 161–2.

The changes...have certainly enabled Australian producers to be more efficient and so better equipped to respond to an increasingly competitive and uncertain market.¹³¹

7.126 This matter of government involvement in fostering a domestic environment that will assist exporters improve their international competitiveness through various means, including infrastructure development, tax policies and labour market reforms is beyond the scope of this inquiry. Nonetheless, the Committee stresses the importance of the need for government, business and the broader community to work together to find ways to nurture a domestic environment that will minimise the costs of production, better use its human resources and improve efficiency for Australian industry.

Research

7.127 One area that holds promise for growth and where Australia may have a comparative advantage is in basic research such as medical research, various scientific research in the field of basic engineering and materials usage. Dr Freedman argued that in these areas Australia has people at the forefront of research—‘that is where Australia can have a leg-up on everyone else’.¹³²

7.128 Reinforcing this view, Mr Peter Hartcher drew attention to Australia’s large pool of ‘creative and technologically savvy people’. He argued that, because Australia lacks a substantial capital base, Australian researchers are without solid commercial backing to exploit fully their skills. In turning from Australia’s strength in this area of R&D, to Japanese vast excess capital, he noted the great opportunity for a productive association between Australian skills and Japanese capital:

...if the hallmark of the last half-century of economic relations between Australia and Japan has been the complementarity between Australian resources and Japanese manufacturing, the potential new complementarity could be complementarity between the Japanese economy that knows it needs to pursue more creativity and more technological fleet-footedness and Australia who can supply that.¹³³

7.129 According to Mr Hartcher, when the Japanese want technological innovation and ideas, they look to the United States. Similarly, when Australian venture companies seek development capital to build on their ideas they also turn to the United States. He saw an opportunity for:

Australia and Japan to exploit the complementarity there by trying to exploit Australia’s potential and Japan’s capital and needs by doing it directly rather

131 Robert Cameron ‘The Australian Coal Industry—Meeting the Challenges’, Fifth APEC Coal Flow Seminar, Yokohama, Japan, 4 February 1999.

132 Dr Craig Freedman, *Committee Hansard*, 15 April 1999, p. 352.

133 Peter Hartcher, *Committee Hansard*, 15 April 1999, pp. 327.

than going to the larger marketplace of the US, where it is a pretty crowded marketplace already.¹³⁴

7.130 He suggested that anything that can be done to bring the private and academic sectors on each side together more often should be pursued with enthusiasm.¹³⁵

7.131 The Committee found that this area of Australian R&D is one that warrants close and serious consideration and certainly should be accorded a higher priority by the Australian Government. The Committee believes that the potential for a more productive partnership in science and technology between Australia and Japan is unrealised. It agrees with witnesses who can see a beneficial marriage between Australian technology and Japanese capital and urges the Australian Government to explore ways to bring together the talent of Australian researchers with the enterprise and backing of Japanese business people.

Regions—think beyond Tokyo

7.132 A number of witnesses urged Australian exporters to look beyond the boundaries of the major Japanese cities, especially Tokyo. They suggested that rather than concentrate on the capital city, export promotion should be deployed on a country-wide basis. Mr Pokarier argued strongly that by targeting the regions in Japan Australian producers could find a range of market opportunities not found in Tokyo.¹³⁶

7.133 JETRO shared this view and stressed the importance of a regional approach to Japan, because ‘not only Tokyo but other areas of Japan are very eager to have foreign companies in their own area’.¹³⁷ Austrade also encouraged Australian companies to consider establishing a presence in a regional area. It noted that areas other than Tokyo are economies in their own right, such as Kansai, the area around Osaka, which is larger than Canada; and Kyushu, the island in the west of Japan which is bigger than the Korean economy. Mr Greg Dodds told the Committee:

The Japanese retail sector is characterised by a couple of very large players like Daiei and Jusco and then hundreds of small to medium sized operators, particularly in the regional level. It would definitely be a strategic option for an Australian retailer. If we were approached, we would suggest they look at buying one of them at a regional level, learn how to make it work in an area like Kyushu or Sendai, where we have an office and could support the process, and then to go national from there.¹³⁸

134 Peter Hartcher, *Committee Hansard*, 15 April 1999, p. 328.

135 Peter Hartcher, *Committee Hansard*, 15 April 1999, p. 329.

136 Christopher Pokarier, *Committee Hansard*, 16 April 1999, p. 437.

137 Hiroshi Nakano, Japan External Trade Organisation, Sydney Inc, *Committee Hansard*, 3 September 1999, p. 798.

138 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, pp. 636, 642.

Austrade offices in North-east Asia



7.134 The experiences of Australian building firms operating in the regional areas bears out this advice. Mr Ian McLean, whose firm has been working in Matsuyama on the Island of Shikoku, which has a population of over a million, knew of the opportunities for Australian businesses. In essence, he stated 'it is so much easier because they want to do business'.¹³⁹ To promote this regional approach, Austrade has expanded its regional representation in Japan. There are now Austrade officials or consuls in Osaka, Sendai, Fukuoka, Nagoya and Sapporo.¹⁴⁰

139 Ian McLean, Australia Japan Housing Ltd, *Committee Hansard*, 15 April 1999, p. 365.

140 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 635.

7.135 A number of cities in Australia have established a sister city relationship with a city in Japan. Although the intention is to promote mutual friendship by developing and strengthening social and cultural interaction between individuals and groups in the two cities, there is great scope for the development of commercial ties that would benefit both communities. The City of Whitehorse Council, the Hastings Council and the Lismore City Council, who have well established sister city relationship with a city in Japan, clearly value their association but are keen to build on their relationship to foster economic and business contacts with their respective sister city.¹⁴¹ The Committee believes that this is an area that provides potential not yet fully realised for Australian business to link up with regional Japan.

7.136 The Committee acknowledges the importance of keeping Australian business informed about the opportunities waiting to be taken up in the regional areas of Japan and of encouraging and assisting Australian business to take advantage of any such opportunities.

Recommendation

The Committee recommends that the Department of Foreign Affairs consult with representatives from cities involved in a sister city relationship to develop strategies that will help them forge better trade ties with their respective sister city in Japan.

Japan's foreign investment in Australia

7.137 The Committee has shown that the decision by Australian exporters and investors to break into the Japanese market depends significantly on their perception of that market. Many in Australia shun the opportunities on offer in Japan because they still regard Japan as a difficult place to do business. The same principle may apply to Japanese considering the potential of the Australian market. Their understanding of Australia might well inhibit their commercial involvement in Australia.

7.138 As a capital poor country that welcomes injection of foreign funds, Australia has a long tradition as a reliable, stable and friendly trading partner. In Professor Rix's opinion, the Japanese would probably prefer to deal with Australian companies more than almost anybody else. Although it is not a formal relationship in the sense of an alliance, the Australia-Japan association has proven to be very beneficial to both countries.¹⁴² Australia's standing as a valuable partner holds it in good stead in the Japanese market place but it does not guarantee continued or expanding investment by Japan in Australia.

141 See Whitehorse City Council, submission no. 2, p. 1; Hastings Council, submission no. 4, pp. 1-2; Lismore City Council, submission no. 11, p. 2.

142 Professor Alan Rix, *Committee Hansard*, 16 April 1999, p. 449.

7.139 Australia must alert the Japanese to the opportunities in Australia for investment. The main aims of Japanese overseas investment since the war have been to secure sources of raw materials and foodstuffs and to improve market prospects for Japanese manufacturing industries. It was the forward contracts offered by Japanese industry that lay the foundations for financing the large-scale mineral projects which unlocked Australia's extensive mineral wealth.

7.140 Since the mid-1980s Japan has invested in a range of industries that has varied according to the changing nature of the Japanese economy. According to Professor Drysdale and Mr Roger Farrell:

While the need to secure supplies of raw materials and energy was a key motivation for Japanese FDI in resource development in Australia, the relatively small domestic market discouraged manufacturing FDI unless import barriers provided an incentive to establish local operations. A considerable part of FDI has been associated with establishing wholesale and retail networks to facilitate bilateral trade and provide a distribution network for locally established Japanese firms.¹⁴³

7.141 Even so, foreign investment has always been a contentious issue for debate in Australia. It has been only a little over ten years since the purchases of real estate by Japanese companies ignited controversy and generated anti-Japanese sentiments in Australia.¹⁴⁴ The Australian economy, however, has benefited substantially from Japanese investment and is well placed to remain a major beneficiary of continued direct investment.¹⁴⁵ Nonetheless, there are many other countries seeking to attract investment from Japan and Australia will have to compete against this wide range of other investment destinations. Austrade told the Committee:

For quite a long time, when we tried to encourage Japanese direct investment in Australia, many Tokyo companies have come back to us with the cost of labour, the cost of land, and these negatives about Australia—not so much the negatives about Australia but the positives of an Asian

143 Peter Drysdale and Robert Farrell, 'Perspectives on Japanese Investment, Employment and Management in Australia', *Pacific Economic Papers no. 290*, Australia-Japan Research Centre, April 1999, pp. 42–3. FDI is the acronym for foreign direct investment.

144 Yukio Satoh, 'From Distant Countries to Partners: The Japan-Australia Relationship', *Working Paper no. 312*, November 1997, Strategic and Defence Studies Centre, 1997, p. 3. See also Purnendra Jain and Donna Weeks, 'Banking on the "Constructive Partnership"', *Current Affairs Bulletin*, vol. 69, No. 9, February 1993, pp. 14–16.

145 For example see Austrade, submission no. 35, pp. 7–8, 16. See also, Peter Drysdale and Robert Farrell, 'Perspectives on Japanese Investment, Employment and Management in Australia', *Pacific Economic Papers no. 290*, Australia-Japan Research Centre, April 1999, pp. 42–3; Manuel Panagiotopoulos told the Committee that 'A large proportion of investment in real estate has since left due to the financial troubles of the parent companies in Japan. However, Japanese investment in Australia is well established and will remain for the long term', *Committee Hansard*, 14 April 1999, p. 215.

destination like Malaysia or Indonesia compared with Australia; that these things were cheaper.¹⁴⁶

7.142 Japanese investment is an area where Australia must create its own opportunities by actively encouraging Japanese interest. The potential to marry Australian research skills with Japanese capital has been noted. But, Australia's business profile in Japan is small in comparison to the size of the trade relationship. JETRO suggested that Australian government and business should have a bigger presence in Japan. This would have two advantages—'it would create an awareness among Japanese about Australia and it would expose Australian business to direct market experience in Japan.'¹⁴⁷

7.143 Even more so, some impressions about Australia's labour productivity including Australia's 'notorious strike record', may still linger, despite improvements over recent years, and undermine Australia's efforts to attract Japanese investment.¹⁴⁸ Mr Manuel Panagiotopolous noted that there are examples of executives in Japan who are basically uninformed. He suggested that 'Their understanding of our country may still be of the Australia of 15, 20 years ago'.¹⁴⁹ According to Mr Seiji Kawarabayashi, Chairman of the Federation of Japan Chambers of Commerce and Industry in Australia:

The perception in Japan...is that Australia is a small, mature market with limited growth potential, mainly in the areas of resources, energy and leisure. It is up to Australia to firmly focus on the future, reinvent itself to compete globally, and benefit from the growth in Asia.¹⁵⁰

7.144 In underlining this point, the Committee for Economic Development of Australia submitted:

...the future must also be our own creation...It is not simply a matter, however, of being good: we must also be known to be good. Impressions count for a great deal.¹⁵¹

The Australia Japan Foundation agreed and urged Australia to do more to engage Japanese attention. It told the Committee:

146 Gregory Dodds, Austrade, *Committee Hansard*, 27 May 1999, p. 641.

147 Hiroshi Nakano, Japan External Trade Organisation, *Committee Hansard*, 3 September 1999, p. 797.

148 See Peter Drysdale and Robert Farrell, 'Perspectives on Japanese Investment, Employment and Management in Australia', *Pacific Economic Papers no. 290*, Australia-Japan Research Centre, April 1999, p. 2.

149 Manuel Panagiotopoulos, *Committee Hansard*, 14 April 1999, p. 223.

150 Quote taken from CEDA, *Japanese Trading Companies: Their Role in Australia's Economic Development*, a study undertaken by INSTATE Pty Ltd, Sydney, 1997, p. 70.

151 CEDA, *Japanese Trading Companies: Their Role in Australia's Economic Development*, a study undertaken by INSTATE Pty Ltd, Sydney, 1997, p. 69. See also comments by Owen Clare, Senior Equities Advisor, Saw James Capel Ltd, *Committee Hansard*, 24 February 1999, p. 156.

...we have to be talking differently about ourselves in the future. We can no longer be kangaroos, koalas and beaches; we can no longer be simply coal, iron ore and primary products. We have to be selling Australian know-how; we have to be selling Australian sophistication; we have to be sending messages to the average citizen in Japan that Australia is equally a target for their interest with the United States, with Europe and with South-East Asia.¹⁵²

7.145 The Australian Government and Australian business need to have a clear understanding of how Australia is perceived overseas and to decide how this perception can be improved. Australia must project a strong positive image as a ‘can do’ nation, able to supply sophisticated goods and services.

7.146 Moreover, within Australia there is a need to promote public awareness and develop a sense of balance in appreciating the benefits of Japanese direct investment. A sound understanding of the nature, extent and benefits deriving from such investment would give a more accurate perspective to the debate and would certainly send a far more encouraging message to potential Japanese investors.¹⁵³

7.147 The Committee accepts Australia cannot take Japanese investment for granted; that Australia must take the initiative and work hard to present itself to the international business world as an attractive investment proposition. The Australian Government clearly has a crucial role in promoting a strong image of Australia as a nation that will reward its investors.

Japan’s understanding of Australia

7.148 The need for understanding and appreciation should flow both ways if the relationship between Australia and Japan is to grow in a balanced and mutually beneficial way. The Japanese people generally have a positive image of Australia. A survey by the Nippon Research Centre showed that Australia continues to rate as one of the most popular and trustworthy countries by the Japanese.¹⁵⁴ The Committee in the course of its inquiry heard evidence that Australia, on the whole, is recognised as a safe, clean and green country, that enjoys stable government and produces mainly primary products such as coal, iron ore, wool, wheat and beef. This reputation while conveying a most favourable impression can be restrictive.

7.149 Although Australia has a good name, the image is often ‘indistinct and dated’. Clearly the predictable and cliched stories of Australia in Japan of beaches, koalas and

152 Terence White, Australia-Japan Foundation, *Committee Hansard*, 19 February 1999, p. 38.

153 See Purnendra Jain and Donna Weeks, ‘Banking on the “Constructive Partnership”’, *Current Affairs Bulletin*, vol. 69, no. 9, February 1993, pp. 14–16 for views on this matter of Japanese investment.

154 NSW Government, submission no. 25, p. 4.

kangaroos and lazy workers who lounge around all day long are misleading.¹⁵⁵ According to DFAT Australia is seen as:

...a collage of a country rich in agriculture and minerals and blessed with sun, surf and space. There is only a limited understanding of Australia's technical capabilities, of its record of innovation and achievement in science and industry or of the extent of Australia's cultural diversity. Unless others know us better, and we others, our relationship will remain limited and the capacity to pursue Australia's national interests diminished.¹⁵⁶

7.150 Research particularly in relation to tourism supports DFAT's assessment of how Australia is perceived overseas. It shows quite clearly that Australia is portrayed typically as a land of surf and sun. The tourist industry recognises the limitations that such a shallow representation can have on attracting Japanese visitors to Australia. But this narrow depiction of Australia spills over into other areas of exchange. Our universities suffer in not being able to attract top Japanese students, Japanese investment in Australia may remain in traditional areas such as minerals, beef, tourism infrastructure and automobiles because Japanese lack an appreciation of Australia's full potential.

7.151 Moreover, as pointed out by QSC, Australia has particular interests that Japan as a major trading partner should be aware of and understand. Our push for the liberalisation of agricultural products is one such matter.

7.152 Perception is a powerful force in shaping relationships and it is important that Australia ensure that its potential is fully understood and appreciated by Japan. The Committee has shown that a range of industries are working very hard to convey positive impressions of their particular product or sector. The coal industry has an established reputation as a reliable supplier and is working toward creating a more environmentally friendly image. Iron ore and LNG producers and rice and wheat growers are consolidating their name as reliable suppliers. LNG is also marketing its product as safe and clean, and the Australian rice, wheat and beef industries are acknowledged as producers of a high quality product. The tourist industry is striving to broaden its image and the education industry has work to do to build a stronger profile in Japan.

7.153 The Committee found that despite the individual efforts of different sectors in the Australian community to promote their particular product, the extent and range of Australia's potential is undersold in the overall understanding of Australia. Mr White of the Australia Japan Foundation believed that it is the responsibility of all who are associated with Japan to work to enhance Australia's image overseas. But he noted that the Australian Government must coordinate these efforts; it must have 'a political

155 For example see David Askew, *Committee Hansard*, 17 May 1999, p. 552.

156 Commonwealth of Australia, *In the National Interest: Australia's Foreign and Trade Policy White Paper*, 1997, p. 78.

will' to bring together all the elements in the community to effectively promote Australia.¹⁵⁷

Recommendation

The Committee recommends that the Department of Foreign Affairs and Trade analyse and evaluate the existing means it uses to promote Australia's image internationally with a view to implementing measures that will raise Australia's profile overseas and convey more effectively an image of Australia that reflects its strengths and potential.

157 Terence White, Australia-Japan Foundation, *Committee Hansard*, 19 February 1999, p. 51. See also views of Philip Henry, Department of State Development, Queensland, *Committee Hansard*, 16 April 1999, p. 410.

EAST ASIAN HEMISPHERE

