Miñambres García, Ignacio José

JAPANESE CAPITAL INTERNATIONALIZATION AND ITS REGIONAL LEADERSHIP IN SOUTHEAST ASIA

Revista de Economía Mundial, núm. 42, 2016, pp. 109-127
Sociedad de Economía Mundial
Madrid, España

ISSN: 1576-0162

Japanese Capital Internationalization and its Regional Leadership in Southeast Asia

La internacionalización del capital japonés y su liderazgo regional en el Sudeste Asiático

Ignacio José Miñambres García
National Cheng-Kung University of Taiwan
nachovalladolid@yahoo.es

Recibido: mayo de 2015; enero de 2016

Resumen

Tras mantener un perfil bajo en los años 90, Japón se reafirmó internacionalmente después de la crisis financiera asiática y proyectó su capital de nuevo al resto de Asia al mismo tiempo que afrontaba la emergencia de China como un nuevo competidor por el liderazgo regional. En este artículo analizamos la influencia de los intereses de política exterior del gobierno japonés en su inversión extranjera directa y defendemos que las ambiciones políticas de liderazgo regional han jugado un importante papel en las decisiones de inversión en el exterior de las empresas niponas. Esto ha dado lugar a una internacionalización caracterizada por un gran peso de la IED estratégica en países en desarrollo, la adopción temprana de la externalización al extranjero en redes horizontales de producción, así como un constante retorno al sudeste asiático como el área natural de expansión del capital japonés.

Palabras clave: IED; Sudeste asiático; Regionalismo asiático; Hegemonía regional; Globalización.

Abstract

After a low profile international role in the 1990s, Japan has reasserted itself since the Asian financial crisis and is projecting capital again over the rest of Asia, at the same time that it tackles the emergence of a new competitor for regional leadership in China. In this paper we study the influence of government foreign policy objectives in shaping Japanese FDI and argue that Japan's political ambitions of regional leadership have played an important role in the international investment decisions of its enterprises. This has in turn resulted in a particular structure of internationalization characterized by heavy presence of strategic-seeking FDI in developing economies, early adoption of cross-national outsourcing and horizontal production networks and a recurrence return to Southeast Asia as the natural area of internationalization for Japanese capital.

Keywords: FDI; Southeast Asia; Asian Regionalism; Regional Hegemony; Globalization.

Clasificación JEL: F15, F21, F54.

1. Introduction

Japan's foreign direct investment (FDI) has traditionally focused on expanding in Asia, to the point that Japan's modern-day economic strategy has even been dubbed as "empire building" (Sheridan 1995, 489), meaning economic forces are submitted to political objectives. However, recent literature on Asian regionalism has not paid attention to how FDI flows interact with regional leadership aspirations through the establishment of a certain division of labor (Doner 1993).

Traditionally, theoretical and empirical FDI studies considered that the bulk of FDI is market-seeking investment from developed countries, with the size of the target market as its driving factor (Nunnenkamp and Spatz 2002). This assertion was confirmed by data consistently showing that most FDI flows took place among developed economies, although it is undergoing a deep structural change at present.[1]

In this paper we argue that the recent resurgence of Japanese FDI flows towards Southeast Asia, together with investment liberalizing treaties, connects with a recurrent interest in regional leadership (Katada 2002). We shall also show that, from early on, Japan developed a unique pattern of foreign investment. By focusing on underdeveloped Asia and becoming the first OECD country to favor investment in developing countries over other industrialized economies early in its internationalization process, Japan spearheaded the creation of transnational production networks that are now a feature of the present era of globalization.[2]

Along the text, we shall make a broad use of the term Southeast Asia to include in it the whole purported area of influence of Japan encompassing the new industrializing economies (NIEs, namely Taiwan, South Korea, Singapore and Hong Kong), while reserving the term ASEAN to refer to the 10 countries that nowadays form said group of Southeast Asian nations.

The paper is divided into three parts. In the first one we analyze the colonial past of Japan that serves as background to present policies, then the evolution of Japan's FDI in the region, and finally the links between FDI and government

[1] While the developed world remains the main source of FDI outflows, their share has steadily declined from over 90% of world total in 2002 to 60% in 2013. More importantly, their share of the inflows has fallen from 71% in 2002 to just 39% in 2013.
[2] See for example the debate on Global Value Chains (Ravenhill 2014).

policy. In the second part we focus on the particular way in which Japan's capital has shaped its production and expansion abroad. The third section presents conclusions.

2. Japan FDI and southeast asia

2.1. The colonial past of japan in asia

At the turn of the nineteenth century Japan was involved in a process of expansion of its trade and economic activities in its recently acquired colonies (Taiwan, Manchuria) and the rest of Southeast Asia. The economic advance in Indochina commenced in Singapore, where Japanese migrants established themselves during the British colonial regime in the service industry, revolving fundamentally around prostitution (Hirakawa and Shimizu 2002, 6), spreading into the Malayan peninsula and spearheading the arrival of Japanese products, investment and firms. As for the Malay islands, Japanese migrants were lured into the Philippines as well as in Indonesia, seeking jobs or as divers for the pearl industry of the Netherlands East Indies.

On the heels of colonial expansion in Korea and China, Japanese investment abroad grew sharply between 1900 and 1930 (Higuchi 1949). Prior to 1914 Japan suffered from difficulties in raising credit for investment, but during the First World War its corporations boosted their profits from Asian markets opened to them with the withdrawal of European products due to the Great War.

The initial distribution of Japanese FDI in Asia resembled colonial patterns common to many Western empires, with important investments for resource exploitation (particularly mining) and development of local infrastructure (railways), particularly in Manchuria (Beasley 1987: 133). Investments in Southeast Asian territories where Japan was not yet expanding colonially were of small quantity (albeit growing) and represented around 6% of its total investment, mostly in commerce, agriculture and mining in Malaya, Indonesia and the Philippines (Beasley 1987, 223).

After WWI Japanese investment diversified. New companies entered Manchuria and smaller businesses opened to service them through joint-ventures with local Chinese companies (Beasley 1987, 139-140). In ASEAN, Japanese trading companies landed in Singapore starting from 1916, establishing offices there. From trading in Singapore, they expanded and diversified their activities, supported by the arrival of Japanese shipping companies and banks, which opened branches first in Singapore and then in other major cities of ASEAN, providing financial assistance to the expanding Japanese firms (Hirakawa and Shimizu 2002,72).

Such economic adventurism was not at all due to private efforts alone. It was also the result of a very active governmental policy encouraging expansion in the region. The Ministry of Agriculture and Commerce provided subventions to Japanese fishing companies operating in the colonies, while the Ministry of Colonies subsidized the construction of an ice factory and refrigeration plant to meet the increasing demand generated by the rise in Japanese fishing (Hirakawa and Shimizu 2002, 97). In April 1918 a commercial museum opened in Singapore with a subsidy of ¥112,000 from the Japan Ministry of Commerce and Industry. The Japan Foreign Ministry also created a program of "commercial trainees" for trading companies abroad.

During the Second World War, the Japanese established their military and economic Southeast Asian capital in Singapore (which they renamed as *Shōnan)* and ruled the region for three and a half years, imposing a severe control on the economy and stimulating the arrival of numerous Japanese firms both in manufacturing and the service industry. By 1 May 1944, 140 Japanese companies were functioning in *Shōnan*. The military government favored the arrival of big department store firms and Japanese trading companies, already present before the war, were each granted monopoly for domestic and foreign trade in a certain product.

Singapore was not the only city where Japanese companies thrived under military rule. Kuala Lumpur also saw the arrival of Japanese investors, both in services as well as some industry in the form of engineering works for the army. Furthermore, the use of the region as a source of raw materials during World War II boosted investment by Japanese companies in mining and manufacturing, accumulating around JP¥ 3,5 billion by the end of 1944 (Beasley 1987: 248).

Japan's economic penetration into Southeast Asia halted with its defeat in the Pacific War. Japanese capital lost all of its foreign assets, its businesses closed down or taken over by locals, and was forced to make a fresh start.

2.2. Japan's Continued Investment In Asia

We have seen already how prior to WWII most Japanese investment was geared towards Asian countries in coordination with the country's colonial expansionism in the region. After the War, fearing shortages of foreign reserves and in the need to concentrate resources on national reconstruction, the government imposed severe restrictions on outgoing foreign investment. Under the Control and Exchange Law of 1949, projects were judged on a case-by-case basis and had to be approved by the Ministry of Finance (Krause and Sekiguchi 1976). Japanese investment in the fifties consisted mostly of government-promoted, large-scale projects aimed at securing a stable supply of resources to feed an economy in need of high growth for recovery (Lee 1999, 463).

The years stretching between the end of the Pacific War and the Korean War are usually considered the "void period" of Japan's economic relation with Southeast Asia, when the country had no economic policy towards the rest of the continent (Yano 1975). The bulk of Japanese investment concentrated in market-seeking in North America. Japanese firms opened representative commercial offices as well as a few manufacturing industries in the US oriented for export.

However, authors like Hirakawa and Shimizu (2002, 147) have disputed this view and defended the idea that the Japanese government never gave up on an economic return to its "area of influence".[3] During the 1950s, and into the 1960s, most of Japan's investment in Asia was resource-seeking. Banks, insurance, shipping and trading companies also returned to Southeast Asia in the 1950s, as well as some industries that set up their own production centers in the region (Hirakawa and Shimizu 2002, 173-177).

Japan's private capital presence in Asia remained at low levels until the acceptance of Japan in the OECD in 1964, coupled with the Normalization Treaty with South Korea in 1965, modified the international situation of the country. The recovery of Japan's economy pushed the Japanese government to promote imports and relax their control over investment abroad.

As shown on Table 1, Japanese FDI increased constantly throughout the sixties, and so did the importance of Southeast Asia as its destination. Capital invested abroad tripled compared to before its entry in the OECD and generated the first Japanese foreign investment boom. The region became the most important target of Japanese investment in 1971 for the first time since the end of the Pacific War.

During its high growth period, Japanese capital projected abroad with a dual strategy of both export-oriented and market-seeking investment in developing Asian countries. This pattern remained in place until the first half of the eighties (Sakurai 1992, 100-01), when it was exhausted due to the revaluation of the yen. Japanese companies took then a step further and proceeded to globalizing their production networks in advance of other developed economies.

In the early 1990s Japan "reversed the outward orientation of its economy to ratchet up new capital investment in domestic industry" (Westra 2012, 702). Then in the 2000s (as seen in Table 2), Japan's outward investment flows recovered and accelerated while, at the same time, re-focusing on Asia as a main destination.

It has been argued (Akyüz and Gore 1996) that until the eighties Japanese FDI complemented rather than substituted local accumulation of capital, and it then transitioned from trade reliance to investment reliance. This means that Japanese FDI became increasingly at odds with exports and domestic investment. The transition completed in the 1990s when FDI became the main source of Japanese global production. After several years of FDI outflows outpacing exports, in 2008 "sales by foreign subsidiaries substantially exceeded Japanese exports" (Ito 2011, 1) for industrial products in both high and low labor intensive sectors. At this point we can consider that the multinationalization process of Japanese corporations was complete.

[3] For example, it made a contribution of US$50,000 in 1954 to the Colombo plan, a US$1.5 billion project promoted by the US to build infrastructure in the region (Lee 1999, 477).

Table 1: japanese fdi by destination in us$ million

Fiscal Year		1965-69	1970-74	1975-79	1980-84	1985-89	1990-94
Latin America		301	1,989	3,071	7,440	23,835	18,293
Europe		284	1,880	1,708	5,179	35,899	44,896
North America		524	2,291	5,191	13,268	87,523	93,698
Asia		431	2,534	5,526	9,385	22,437	35,751
East Asia		420	2,519	5,490	9,255	22,213	35,073
	China	0	0	14	173	2,287	6,254
ASEAN10		341	1,673	4,054	6,451	10,716	19,876
	Brunei	86	3	6	12	3	15
	Cambodia	0	0	0	0	0	0
	Indonesia	159	996	2,705	4,121	2,420	6,546
	Lao PDR	0	0	0	0	0	0
	Malaysia	22	213	254	541	1,461	3,850
	Myannmar	0	0	0	0	0	0
	Philippines	20	146	346	295	491	1,496
	Singapore	9	198	574	1,133	3,785	3,821
	Thailand	45	117	169	348	2,557	3,916
	Viet Nam	0	0	0	0	0	233
Asia NIES (excl. Sing)		79	846	1,422	2,631	9,210	8,942
	Hong Kong	11	253	666	1,860	5,266	5,816
	Korea	16	479	607	447	2,305	1,415
	Taiwan	52	114	149	324	1,639	1,712
Other		342	1,295	3,648	4,358	12,770	17,073
TOTAL		1,883	9,989	19,141	39,628	182,464	209,710

Source: Japan External Trade Organization.

Table 2. Japanese fdi by destination in us$ million

		1996-2000	2001-2005	2006	2007	2008	2009	2010	2011	2012	2013
Latin America		16,195	20,903	2,547	9,482	29,623	17,393	5,346	11,287	10,454	10,197
North America		46,624	47,913	10,188	17,385	46,046	10,889	9,016	15,166	35,768	46,505
Europe		27,145	52,239	18,396	20,965	23,068	17,830	15,043	39,841	31,017	32,227
Asia		34,620	47,722	17,167	19,388	23,348	20,636	22,131	39,492	33,477	40,470
East Asia		32,609	46,893	16,610	17,814	17,558	16,927	19,238	37,105	30,631	38,133
	China	6,774	21,197	6,169	6,218	6,496	6,899	7,252	12,649	13,479	9,104
Asia NIES		7,123	9,193	3,518	3,806	4,753	3,026	3,057	4,810	6,477	5,410
	Hong Kong	3,322	2,936	1,509	1,131	1,301	1,610	2,085	1,509	2,362	1,785
	Taiwan	1,347	2,330	491	1,373	1,082	339	-113	862	119	330
	S.Korea	2,454	3,926	1,517	1,302	2,369	1,077	1,085	2,439	3,996	3,296
ASEAN		18,711	16,503	6,923	7,790	6,309	7,002	8,930	19,645	10,675	23,619
	Thailand	5,522	6,793	1,984	2,608	2,016	1,632	2,248	7,133	547	10,174
	Indonesia	4,764	2,955	744	1,030	731	483	490	3,611	3,810	3,907
	Malaysia	1,624	1,010	2,941	325	591	616	1,058	1,441	1,308	1,265
	Philippines	2,455	1,910	369	1,045	705	809	514	1,019	731	1,242
	Singapore	3,473	3,072	375	2,233	1,089	2,881	3,845	4,492	1,566	3,545
	Vietnam	853	853	467	475	1,098	563	748	1,859	2,570	3,266
Other		3,738	7,458	1,864	6,263	8,716	7,903	5,687	9,947	11,638	5,652
World		127,928	175,724	50,165	73,483	130,801	74,650	57,223	108,808	122,355	135,049

Source: Japan External Trade Organization

2.3. Government promotion and investment in Asia

The objectives of Japan's government in international political economy have consistently included the creation of an Asian sphere of influence as envisioned since Meiji industrialization. The rhetoric of a paternalistic Japan helping its poorer neighbors in their economic development dates back to the nineteenth century and has taken several forms. From the *Daitoa Kyoeiken* (Greater East Asia Co-Prosperity Sphere), to the Flying Geese Paradigm created by Akamatsu and developed into a model for regional development centered in Japan by Kojima (Oizumi and Muñoz 2011, 205). Not less importantly, the "Fukuda Doctrine", a set of commitments towards ASEAN put forward by Prime Minister Takeo Fukuda advocated the building of close economic and trade relations with countries of the block (Yano 1978, 61).

Under this logic, in the sixties and seventies, reflecting Japan's position as a strong US ally in the Pacific region during the Cold War, a stream of funds were delivered as Official Development Assistance (ODA) to countries in ASEAN. Sizeable projects were financed by Japanese credit and ODA in developing countries in order to diversify sources for energy and raw materials.

Japan tried to capitalize on the integration attempts by ASEAN and presented the idea of an "Asian New Deal", aimed at supporting self-sufficiency in food for targeted developing countries. The proposal included subsidies for agricultural sector-related projects such as damns, or fertilizer and food processing plants. The initiative was supported by official visits including the highly-publicized tour of Premier Tanaka Kakuei in January 1974 to Thailand, the Philippines, Malaysia, Singapore and Indonesia. During the visit, he and other government officials guaranteed "full-scale cooperation in development programs" with those developing nations (Koyano 1976a, 50).

In more recent times, Japan made a considerable effort to help Southeast Asia recover from the 1997 financial crisis by providing over US$80 billion in aid along with other financial support (Johnstone 1999). This was probably due to the high exposure of Japanese banks to Southeast Asia when the crisis started (Katada 2002, 90). ASEAN remained the largest recipient of Japan ODA as well in following years, including a remarkable effort when several ASEAN countries were hit by a devastating tsunami in 2004 and Japan assisted them with over JP¥ 24.6 billion.

Despite all its development assistance and its soft-power approach, Japan's involvement in Southeast Asia was met with considerable suspicion by nations with painful memories of Japan's past colonial ventures. For years, critics of Japan's foreign policy accused the Japanese government of mostly providing for its own private investors through economic assistance in ASEAN, and they were not very off-track in considering so.

The funds for infrastructure investment in the Colombo plan of 1954 were tied with commercial loans that forced the recipient countries to purchase from Japanese producers. When Prime Minister Kishi Nobusuke visited Singapore in November 1957, he discussed with Chief Minister Kim Yew Hock about the promotion of Japanese firms' investment in it. Both programs allowed Japan to shift from the NIEs to ASEAN as suppliers of raw materials, while integrating the region economically.

As Lee (1999, 478) points out, Japan's reparation and aid programs were both foreign and economic policy tools. The Japanese government totally liberalized FDI in 1967, eliminating all exchange and outward capital controls. The document "Long-Term Vision of Industrial Structure" (MITI 1975), outlined a national strategy to encourage FDI by the government, particularly in Southeast Asia.

Projects were not to be decided solely at the firm level, but would be part of sectoral strategies backed by the Ministry of International Trade and Industry (MITI) through multiple instruments (guarantees, "bond insurances", etc.). A Joint Committee was created, together with ASEAN, for business leaders on both sides in order to encourage and coordinate common investments. "A Vision of Industrial Policy in the 1980s", another document by MITI, also addressed the need for FDI promotion, particularly in Asia, as an objective of the Japanese government.

Japanese corporations' investment in ASEAN countries in natural resource extraction and infrastructure was linked with development projects, coordinated by the Japanese government in an example of the "consultative arrangement" policies that were implemented domestically (Lee 1999, 446). The public sector funded them through its aid agencies and supported them through measures like insurance for political risks in the host country, or low interest loans by government financial institutions (especially the Japan Export-Import Bank) that were also accounted for as economic assistance (Yoshihara 1978, 11-12). In the seventies, construction and infrastructure (with a special focus on ports in the case of Southeast Asia) rose consistently with a 50% public-private fund established by MITI to "assure contracting for large scale construction work overseas" (Koyano 1976b).

Japan was creating, and at the same time taking advantage of, opportunities for investment across Southeast Asia. Some of the Free Trade Zones created in Malaysia, Taiwan and Singapore in the seventies with Japan's aid loans, would later host mainly Japanese capital with Japanese firms amounting up to 90% of all present companies (Nakano 1977, 33).

In the eighties, production of polluting, labor and energy-intensive industries was transferred to neighboring countries in Asia that provided cheap labor, thus giving birth to Japanese corporate networks. The government continued to support the relocation of Japan's small and medium enterprises (SMEs) through instruments such as the Small Business Corporation, the Peoples' Finance Corporation and the Central Bank of Commercial and Industrial Corporation.

Overcoming the relative passivity of the nineties, when Japan's government and capital were too busy with the country's economic woes to pay attention to international projection, the Asian financial crisis generated a renewed activism by Japan's government in relation to Asia. After many years of a strong commitment to multilateral negotiations and institutions for trade and capital liberalization, the problems encountered in the WTO to complete agreements on certain areas (among which FDI was an important case in point) took Japan and other developed countries, (Siddique 2007) to pursue bilateral agreements in order to close ties with developing countries. Japan signed Economic Partnership Agreements (EPAs) mainly with Asian countries[4] as part of Japan's national interest of regaining its influence in the region (Yoshimatsu, 2006). The first regional agreement was the "Japan-Singapore Economic Partnership Agreement" signed in 2002.[5]

Japan's rush to sign EPAs with ASEAN was not unrelated to the advances of China in the region (Hale 2011, 311). Beijing had signed a free trade agreement (FTA) with ASEAN in 2001 (which entered into force in 2010) and in 2002 it was also the first non-ASEAN country to sign ASEAN's Treaty of Amity and Cooperation (Yoshimatsu 2006, 498). China's approaches modified the status quo in the region and Japan's Ministry of Energy, Trade and Industry (METI) voiced the concern among Japanese authorities that "other countries are already taking advantage of the rich potential of ASEAN" (METI 2002).

While Free Trade Agreements are in themselves a means for securing FDI (Arnold 2006), Japan's EPAs are even more ambitious. Investment receives very different treatment in each text, since attitudes by developing countries towards its liberalization vary the most. Beyond the EPAs, Japan has in recent years drawn from common interests with the US to gain leverage in its rivalry with China. In October 2010, then Prime Minister Kan Naoto declared the willingness of Japan to join negotiations for the Trans-Pacific Partnership Agreement (TPP), in a new attempt to lead a regional leadership process hand-in-hand with its Western allies (Hirakawa 2012). China has been absent from TPP since its earliest stages, and US president Barack Obama has made explicit the marginalization of the Asian giant in recent declarations.[6]

3. A particular internationalization of japanese capital.

In the years of high growth, Japan developed a unique pattern of foreign direct investment that anticipated the globalization of production seen in present–day global value chains. In the seventies Japan was the only OECD coun-

[4] "The government's Free Trade Agreements (FTAs) priority seems to be placed primarily on FTAs with ASEAN, Korea and Mexico as the Ministry of foreign Affairs and Ministry of Economy, Trade and Industry indicated" (Okuda 2004).

[5] This would be followed by other EPAs with Malaysia (2006), Philippines (2006), Thailand (2007), Indonesia (2008), Vietnam (2009), Brunei (2010), and a "Comprehensive EPA" with the ASEAN block that entered into force in 2009.

[6] "If we do not help to shape the rules so that our businesses and our workers can compete in those markets, then China will set up rules that advantage Chinese workers and Chinese businesses", Bloomberg Politics, 17 April 2015, 6:47 p.m. www.bloomberg.com/politics/articles/2015-04-17/obama-warns-china-will-fill-void-if-u-s-can-t-reach-trade-deals

try delivering more than half of its FDI to countries in the developing world in search of cost advantages, instead of market-seeking investment.

In the sixties, Japan's domestic economic structure was going through deep changes and companies faced new challenges (Ozawa 1982, 4): scarcity of labor was becoming an important problem in Japan. To attract this scarce workforce, Japanese companies narrowed wage differences and Japanese wages increased 8% between 1955 and 1965, then doubling with a 16% increase in the period between 1965 and 1975 (Nester 1992, 56-59). Meanwhile environmental problems caused by rapid industrialization were also turning into higher costs for companies, forced to reduce pollution due to social pressures and new laws.

The dollar value of Japanese wages further increased as the yen appreciated against the dollar following the termination of dollar convertibility to gold on 15 August 1971. Japanese businesses shifted to a strategy of increasing investment into developing countries to avoid rising labor costs at home[7]. Taking advantage of their experience in investing in the NIEs as suppliers for parts and components (Yang 1972), Japanese industries made extensive use of the Free Trade Zones created by the governments of Taiwan and South Korea.

Southeast Asian countries lacked the industrial base to produce domestically the goods which imports they were restricting and carried a policy of attracting foreign capital. In order to access local markets and avoid restrictions, such as high tariffs and quotas on imports of finished products, Japanese firms engaged in export-replacement FDI, focused on producing light consumer goods to sell domestically (such as textiles in ASEAN). Manufacturing became the highest share of Japanese FDI (Tsurumi 1976). This kind of investment was characterized by the high participation of Japanese trading companies (*Sōgōsōsha*) in spearheading Japanese capital's presence abroad. Commerce, both wholesale and retailing, was a first step before the arrival of productive investment by Japanese multinational corporations[8].

The experience the *Sōgōsōsha* had already acquired in Southeast Asia prior to WWII no doubt helped pave the way for the later comeback of Japan in the post-war period. The trading companies entered the region in the form of joint ventures in the 1960s to serve as project organizers for incoming large investments in infrastructure and manufacturing, thereby playing a key role in attracting Japanese capital in the region as organizers, consultants and financiers of investments made by SMEs.[9]

[7] A poll by the Ministry of International Trade and Industry (MITI) conducted in 1977 concluded that "a growing portion of overseas investment by Japanese Business is motivated by the desire to exploit the wage gape between the host countries and Japan" (cited in Nakano 1977: 40).
[8] These companies represented 60% of all Japanese FDI between 1951 and 1987 (Lee 1999, 475).
[9] Phongpaichit (1990) points out that trading companies were unique "in their management style, strong links with government, sense of a national mission [...] and most importantly, the ability to combine and mobilize the various advantages into a formidable integrated system which undertakes foreign direct investment".

Around 80% of Japanese manufacturing foreign investment was located in Asia (MOF 1974) and was carried by SMEs. In Japan, these companies played a large role in the manufacturing industry and were strongly dependent on the export market. Faced with increasing protectionist policies from industrialized markets, Japanese SMEs invested in the NIEs to use them as export bases for overseas markets in Europe, Australia and the US, taking advantage of the preferential schemes in customs and trade they offered to developing economies.

Such export-oriented Japanese investment appeared around 1970, and consisted mostly of electric machinery and electronic products that had become an export industry in Japan due to saturation of the domestic market (Hirakawa and Shimizu 2002, 218). Their export-oriented investment abroad maintained many of the characteristics of the early manufacturing investment of the 1950s: labor-intensive processes continued to be transferred to cheaper countries while retaining research and development activities and high value-added industries in Japan (Prasartset 1991, 63).

Later, Japan emerged relatively unscathed from the second oil crisis compared to other developed economies, and Japanese companies reinforced their presence in Asia through complementary investments in their facilities, completing their regionalization. The interrelation of Japanese and Southeast Asian economies presented a high level of mutual but unbalanced dependency, with Japan at the top while its Asian neighbors endured bilateral trade deficits in what could be interpreted as the final building of a Japanese "sphere of influence" in Asia (Allen 1979), not far from the expected results of the flying geese model envisioned by Kojima (Oizumi and Muñoz 2014, 216).

A key event took place on 22 September 1985, when Germany, Japan, the United Kingdom and the United States signed the Plaza Accord in New York in order to devaluate the US dollar via a concerted intervention in currency markets. The agreement would shape the future of Japan's economy for years to come, as it caused a steep raise in the yen unlike any other experienced before. The US dollar fell from JP¥250 to JP¥201 within one year, and Japan's currency continued appreciating until 1988, when the yen value of the dollar was half that of early 1985.

Fueled by the availability of cheap credit at home, and as foreign assets and labor became cheaper with the revaluation of the yen, Japan experienced its sharpest surge of outward FDI in history. Soon, Japanese enterprises faced increases in costs, land prices and a resurgence of domestic labor movements that pushed up wages, suffering a loss of competitiveness (Yamashita 1991, 8). Imports from other Southeast Asian countries competing with local industries increased as they became cheaper for Japanese consumers (Ishida 1999, 161-69).

To remain competitive, Japanese companies at first reduced yen prices and profits. However, stimulated by the high growth of the economy during the bubble, they quickly resorted to investing heavily both at home and in the target markets in developed countries. In only a few years, Japan became the world's third highest investor in stock after the US and the UK, while other forms of capital export increased as well in all directions. This FDI boom had two characteristics: it was particularly strong in the manufacturing sector and it concentrated on export industries (Phongpaichit 1990, 23).

While traditionally Japanese companies had often invested abroad for the production of parts and components that were transferred for final assembly in Japan, after the Plaza Accord the manufacture of final products started to be relocated abroad as well. Factories in Southeast Asia were used as export bases and, rather than driven by market size, Japanese FDI was heavily conditioned by the competitive advantages of the receiving countries (ADB 1992).

In the first phase of the boom (1986-1988), FDI concentrated on Korea and Taiwan. As wage levels started to rise in these economies as well from 1988, Japanese industry extensively relocated its labor-intensive production towards ASEAN countries[10]. Coincidentally, at this point ASEAN countries were switching their strategy from import substitution to export promotion. They removed restrictions placed upon foreign investment and sought to attract it by investing in infrastructure and technological upgrading (Ang Beng Kiat *et al.* 1998).

Since developed countries also increased their demand for products in which the region was used as an export base, ASEAN enjoyed high flows of investment which fueled the growth of their markets. Nevertheless these countries remained production bases for the lower-end processes of Japanese manufactures (Hirakawa 1993, 23-24). Those industries that relied on higher technology and high human capital stayed competitive and could produce in Japan. In fact the highly demanding requirements in infrastructure and human capital of some sectors often implied that their production could not be transferred abroad.

The expansion of Japanese industry abroad came to a dramatic halt in the years after the burst of the Japanese asset bubble in 1989, with stagnating FDI flows in the early nineties that turned into a deep drop in the second half of the decade (see tables 1 and 2). However, reinvestment from branches of Japanese corporations in Southeast Asia had been rising until it exceeded Japanese direct investment into the region in 1992 (Terry 2002, 120). Through these investments Japanese companies were creating complex international production networks in the Asia-Pacific region (JETRO 1996).

Until 1991, major corporations had represented the bulk of Japanese investment using Southeast Asia as a base for production, but a new revaluation of the yen in 1993 pushed many SMEs to follow their bigger corporate clients into the lower cost ASEAN economies (Salleh 1995, 139). Dunning *et al.* (2007) have pointed out that in the 1990s Japanese FDI flows deepened their horizontal nature as opposed to the vertical internationalization of the 1970s. This is not, however, an exclusive characteristic of Japan since it affected most developed economies (García and Solis 2013, 153).

[10] The process is aptly described by Hirakawa (1993: 22-23): “By the early 1980s Japanese capital had already transferred export-oriented, labor-intensive industries to the NIEs.[…] The subsequent rise in value of the currencies of the NIEs diverted investment towards manufacturing bases in ASEAN countries.”

At the turn of the century, the final process of multinationalization of Japanese capital was to bring back China into its economic network. While in the early eighties 51% of Japanese FDI into Asia flowed to the NIEs, and by 1991 ASEAN was the highest recipient with 34%, in 1995 China was already receiving 66% of Japanese investment in Asia (Hirakawa 1999).

High interdependence with Japanese manufacturers has been a blessing but at the same time a risk and weakness for ASEAN industry. ASEAN is now vulnerable to the economic cycles of the global North since its production is devoted for export to developed countries (Abe 2009, 114).

In parallel, following the tertiarization of developed economies, world foreign investment flows at the beginning of the century have been shifting towards tertiary activities also in developing countries (UNCTAD 2004), and Japanese banks have multiplied their activities abroad, becoming the biggest international lenders in 2011 (McKinsey Global Institute 2015, 87). Investments into the NIEs since 2007 have focused more on services, and particularly in the financial sector. Investment in services in ASEAN is mostly concentrated in Singapore, which has consistently been the main recipient of Japanese FDI in this sector as well as a main destination for Japanese FDI in general since 2006.

Japan has reasserted itself as an international player in this new international environment. Revaluation of the yen caused a new spree in mergers and acquisitions by Japanese corporations abroad that almost matched the levels of the bubble peak (McKinsey and Compay 2012). In the meantime, many of the most well-known brands of Japanese miracle economy are struggling to survive in a very competitive environment in which new comers from emergent economies are taking over their markets. However, a whole industrial base of *hidden champions*[11] in highly technological, upstream sectors with large market shares and pricing power is forming.

The earthquake that shook Northern Japan in March 2011 generated concerns that year about the power supply and a contraction in domestic consumption, which led to a new expansion of manufacturing facilities abroad, with special emphasis in new emerging markets in Asia (JBIC 2012). Domestic demand recovered in 2012 under the stimulus the economy received from the monetary and fiscal expansion of the new cabinet of Shinzo Abe, but their effects proved short-lived and private consumption has remained stagnant since 2013.[12] Household consumption continues to remain at values below its 2013 peak and the economy saw very little growth in 2015, driven mostly by private investment and exports.[13]

Weak demand at home and the need to manufacture in proximity of customers have also contributed to the expanding relocation of Japanese produc-

[11] Hidden Champions (Simon 2009) are small and medium-size firms with little-known brand names, but which boast large shares of their respective markets. Japan is said to harbour somewhere between 200-250 of these kind of companies, 95% of which are in the manufacturing sector (Murphy 2014, 206).

[12] See for example GDP data from the cabinet office at: http://www.esri.cao.go.jp/jp/sna/data/data_list/sokuhou/files/2015/qe153_2/__icsFiles/afieldfile/2015/12/04/gaku-mk1532.csv

[13] Data on the component distribution of GDP can be found on http://www.esri.cao.go.jp/jp/sna/data/data_list/sokuhou/gaiyou/pdf/main_1.pdf

tion abroad, in this case near their customers. The main targets of this trend have then been North America and, in second place, China followed closely by Southeast Asia. The industry that has most importantly participated in this tendency has been the automobile sector, followed by electronics.[14]

These trend show a recent tendency of Japanese companies to focus on market-seeking investment once global value chains have been created, and their internationalization is in an advanced state.

4. Conclusions

After the end of the Asian financial crisis of 1997, Japan entered a period of reassertion in Asia taking the initiative in a series of regional proposals that aimed at increasing its importance and allegedly boosting its perspectives as a leading economy in the area, and Japanese FDI flows have recovered contemporaneously with that process. The internationalization of Japanese capital has played an important role in creating regional production networks and Japan's aspirations for regional leadership.

This paper has analyzed the interaction between government policy and private capital behind Japan's increased involvement in Southeast Asia through FDI, and how it could lead to the creation of a "sphere of influence". Japan's government has been building soft power in Asia since the end of the Pacific War, with development aid and assistance to Asian neighbors that have continued into the present. It has also used those interventions to pave the way for its firms in the region.

Looking at the history of Japanese FDI in Southeast Asia, a recurring pattern of public-private collaboration in expanding Japanese capital throughout the region emerges. However mixed the results may be from a political point of view, the process has ended up inextricably binding Japanese and Southeast Asian economies in a complex web of production linkages. The building of these networks shaped the internationalization of Japanese capital in a particular way: Japanese corporations pioneered the process of transferring production to developing countries, and the country hollowed out its industrial base according to conditions that were as much created by market forces as provoked by official policies, both at home and abroad. This process that was later carried on by other multinational corporations in what are known as Global Value Chains (Ravenhill 2014) was, in the case of Japan, geographically circumscribed to Southeast Asia and, with the coming of the new century, China.

[14] A summary of the METI data that shows this can be found in the following report by Bloomberg: http://www.bloomberg.com/news/articles/2015-07-06/japanese-companies-keep-moving-factories-overseas

References

Abe, S. (2009): "Philippines' Competitiveness and Global Financial Meltdown: A Question of Japan's Role", Doshisha University, CCAS Working Paper Series n. 22. Kyoto.

ADB (1992), *Asian Development Outlook: 1992*, Asian Development Bank, Manila.

Akyüz, Y. and Gore, C. G. (1996): "The investment–profits nexus in East Asian industrialization", *World Development* 24, 3, 461–70.

Allen, T. W. (1979): *ASEAN Report*, Dow Jones Publishing Company for Asian Wall Street Journal, Hong-Kong.

Ang Ben Kiat, S., Silva, M. S., Sivanesan, S. and Alex Tan T.H. (1998): "The Geese Flying South", in *Japan—ASEAN Relations: Implications for Business*, edited by Tan Teck Meng, Choo Teck Min, John J. Williams and Chew Soon Beng, Prentice Hall, Singapore.

Arnold, D. (2006): "Free trade agreements and Southeast Asia", *Journal of Contemporary Asia*, 36, 2, 195-216.

Beasley, W. G. (1987), *Japanese Imperialism 1894-1945*, Oxford University Press, New York.

Beeson, M. and Y.oshimatsu, H. (2006): "Asia's Odd Men Out: Australia, Japan and the Politics of Regionalism", *CSGR Working Paper* no. *196*.

Doner, R. (1993): "Japanese foreign investment and the creation of a Pacific Asian region", in *Regionalism and Rivalry: Japan and the United States in Pacific Asia*, edited by Jeffrey A. Frankel and Miles Kahler, 159-216, University of Chicago Press, Chicago.

Dunning, J., Kim, Z. K. and Lee C. I. (2007): "Restructuring the regional distribution of FDI: the case of Japanese and US FDI", *Japan and the World Economy*, 19, 1, 26-47.

Frankel, J. (1993): "Is Japan Creating a Yen Bloc in East Asia and the Pacific?", in *Regionalism and Rivalry: Japan and the United States in Pacific Asia*, edited by Jeffrey A. Frankel and Miles Kahler, 217–48, University of Chicago Press, Chicago.

García, A. S. and Solís, V. (2013). "Comercio Internacional: Cadenas Globales de Valor. Una Aproximación Desde la Teoría de Redes", *Revista de Economía Mundial*, 37, 151-180.

Hale, T. (2011): "The de facto preferential trade agreement in East Asia", *Review of International Political Economy*, 18, 3, 299-327.

Higuchi, H. (1949) *Nihon no taishi tōshi kenkyū* [Study of Japanese Investment in China]. Seikasusha, Tokyo.

Hirakawa, H. (1993): "Investing in Asia", Pacific-Asia Resources Center, *AMPO Japan-Asia Quarterly Review* 24, 4, 22-27, Tokyo.

Hirakawa, H. (1999): "East Asia Industrialization and the Currency and Financial Crisis Within the World Economy", *Journal of International Economic Studies*,13, 1-23.

Hirakawa, H. (2012): "The TPP and Japans Response", Information and Communications Publishing House, *International Conference on Trans-Pacific Partnership Agreement: Prospects and Implications*, edited by Hoang Van Chau. Hanoi.

Hirakawa, H., and Shimizu, H. (2002): *Japan and Singapore in the world economy: Japan's economic advance into Singapore 1870-1965*, Routledge, London.
Ishida, K. (1999): "Japan's Foreign Direct Investment in East Asia: Its Influence on Recipient Countries and Japan's Trade Structure", in *East Asian Development: Will the East Asian Growth Miracle Survive?*, edited by Gerard F. Adams and Shinichi Ichimura, Praeger, Westport.
Ito, K. (2011), "FDI in Emerging Economies: Analysis in a firm heterogeneity model", Research Institute of Economy, Trade and Industry, *RIETI Discussion Paper Series* 11-E.055, Tokyo.
JBIC (2012): *FY2012 Survey (the 24th): Report on Overseas Business Operations by Japanese Manufacturing Companies*. Japan Bank for International Cooperation, Tokyo.
JETRO (1996): *White Paper on Foreign Direct Investment: Increasing Foreign Investment in APEC and Japan's Response – Summary*, Japan External Trade Organization,Tokyo.
Johnstone, C. (1999): "Paradigms Lost: Japan's Asia Policy in a Time of Growing Chinese Power", *Contemporary Southeast Asia* 21, 3, 365-385.
Kamikawa H. (1973), "Japan's Monroe Doctrine", in *Japan's Greater East Asia Co-prosperity Sphere in World War II: selected readings and documents*, edited by Joyce C. Lebra, Oxford University Press, Kuala Lumpur.
Katada, S. N. (2002): "Japan and Asian Monetary Regionalisation: Cultivating a New Regional Leadership after the Asian Financial Crisis" *Geopolitics*, 7, 1, 85-112.
Koyano, T. (1976a): "Japan Overseas Investment: A Shift to Strategic Projects", Pacific-Asia Resources Center, *AMPO Japan-Asia Quarterly Review* 8, 1, 50-53, Tokyo:
Koyano, T. (1976b): "Japan's Overseas Investment: Building Big in Asia", Pacific-Asia Resources Center, *AMPO Japan-Asia Quarterly Review* 8, 2, 35-37. Tokyo.
Krause, L. B. and Sekiguchi, S. (1976): "Japan and the World Economy", in *Asia's New Giant: How Japanese Economy Works*, edited by Hugh Patrick and Henry Rosovsky, 438-58, Brookings Institution, Washington DC.
Lee, Y. I. (1999): "Political economy of Korean and Japanese foreign direct investment", *Journal of Contemporary Asia*, 29, 4, 462-493.
McKinsey and Company (2012): *A Yen for Global Growth*, www.mckinsey.com/~/media/McKinsey%20Offices/Japan/PDF/A%20yen%20for%20global%20growth.ashx
McKinsey Global Institute (2015): *The Future of Japan: Reigniting Productivity and Growth*, www.mckinsey.com/~/media/McKinsey/dotcom/Insights/Growth/How%20a%20private-sector%20transformation%20could%20revive%20Japan/Future_of_Japan_Full_report_March_2015.ashx
METI (2002): *White Paper on International Trade 2003: Revitalization of the Japanese Economy through Importing the Overseas Dynamism*, Ministry of Economy, Trade and Industry, Tokyo.

MITI (1975): *A Long-Term Vision of the Industrial Structure*. Council on Industrial Structure, Tokyo.
MOF (1974): *Manual of Foreign Direct Investment in Japan*, Ministry of Finance and Foreign Department, International Finance Bureau and Bank of Japan, Tokyo.
Murphy, T. (2014) *Japan and the Schakles of the Past*, Oxford University Press.
Nakano, K. (1977): "Japan's Overseas Investment: Patterns and FTZs", Pacific-Asia Resources Center, *AMPO special issue, Free Trade Zones and Industrialization of Asia*, 33-50. Tokyo.
Nester, W. R. (1992): *Japan and the Third World: Patterns, Power, Prospects*, St. Martin's Press, New York.
Nunnenkamp, P. and Spatz, J. (2002): "Determinants of FDI in developing countries: Has globalization changed the rules of the game?", *Transnational Corporations*, 11, 2, 1–34.
Oizumi, Y., and Muñoz, F. F. (2014): "Kaname Akamatsu and the Japanese Industrial Development Model", *Revista de economía mundial*, 37, 201-224.
Okuda, S. (2004): "Deepening Interdependence in East Asia: Deepening Intra-industry Trade of Japan and its Bilateral FTAs", Institute of Developing Economies*, IDE-JETRO APEC Study Center Working Paper Series* 03/04–2, Tokyo.
Ozawa, T. (1982): *Multinationalism, Japanese Style*. Princeton University Press, Princeton.
Phongpaichit, P. (1990): *The New Wave of Japanese Investment in ASEAN: Determinants and Prospects*, Institute of Southeast Asian Studies, Singapore.
Prasartset, S. (1991): "The Global Context and the New Wave of Japanese Investment in Thailand", in *Transfer of Japanese Technology and Management to the ASEAN Countries*, edited by Shoichi Yamashita, University of Tokyo Press, Tokyo.
Ravenhill, J. (2014): "Global value chains and development", *Review of International Political Economy*, 21, 1, 264-274.
Sakurai, M. (1992): "Japanese Direct Foreign Investment and Asia", in *The US-Japan Economic Relationship in East and Southeast Asia*, edited by Karou Okuizumi, Center for Strategic and International Studies, Washington D.C.
Salleh, I. M. (1995): "FDI and Technology Transfer in the Malaysian Electronics Industry", in *The New Wave of Foreign Direct Investment in Asia*, edited by Nomura Research Institute and Institute of Southeast Asian Studies, 111-130, Singapore.
Sheridan, K. (1995): "Japan's direct investment, its development pattern and future direction", *Journal of Contemporary Asia*, 25, 4, 473-491.
Siddique, M.A.B. (2007): *Regionalism, Trade and Economic Development in the Asia-Pacific Region*, Elgar, Cheltenham, UK and Northampton, USA.
Simon, H. (2009): *Hidden champions of the twenty-first century: The success strategies of unknown world market leaders*, Springer Science & Business Media, New York.

Terada, T. (2010): “The Origins of ASEAN+6 and Japan’s Initiatives: China’s Rise and the Agent-structure Analysis”, *The Pacific Review*, 23, 1, 71–92.

Terry, E. (2002): *How Asia Got Rich: Japan, China and the Asian Miracle*, M. E. Sharpe, Armonk.

UNCTAD (2004): World *Investment Report 2004: The Shift Towards Services*, Geneva.

Wesley, M. (1999): “The Asian crisis and the adequacy of regional institutions”, *Contemporary Southeast Asia*, 21, 1, 54-73.

Westra, R. (2012): “The Japanese Economy in the Crossfire”, *Journal of Contemporary Asia*, 42, 4, 697-706.

Yamashita S. (1991): “Economic Development of the ASEAN countries ad the Role of Japanese Direct Investment”, in *Transfer of Japanese Technology and Management to the ASEAN Countries*, edited by Shoichi Yamashita, University of Tokyo Press, Tokyo.

Yang, Y. (1972): “Foreign Investment in Developing Countries: Korea”, in *Direct Foreign Investment in Asia and the Pacific*, edited by Peter Drysdale: 242-257, University of Toronto Press, Toronto.

Yano, T. (1975): “*Nanshin” no Keifu* [The Genealogy of the “Southward Advance”], Shuo Koronsha (Chuko Shinsho), Tokyo.

Yano, T. (1978): “The” Fukuda Doctrine” And Its Implications For Southeast Asia: A Japanese Perspective”, *Southeast Asian Affairs 1978*, 60-64.

Yoshimatsu, H. (2006): “The politics of Japan’s free trade agreement*”, Journal of Contemporary Asia*, 36, 4, 479-499.

Yoshihara, K. (1978), *Japanese Investment in Southeast Asia*, University Press of Hawaii, Honolulu.