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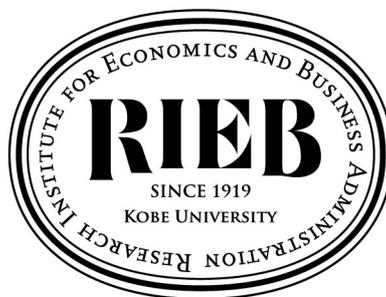
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**Reappraisal of Japan-LAC Trade
and Investment Relations Amid
China's Ascendance***

Mikio KUWAYAMA

October 1, 2019

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Abstract

Though LAC's bilateral trade with Japan has not been as buoyant as that with China in recent years, Japan's trade relations with the region is more diversified and balanced in terms of trading partners, product composition, and trade balance. Furthermore, business activities of Japanese subsidiaries operating in the region are conducive to employment creation, export expansion (especially to third-country markets), and global value-chain developments in the region. In addition, Japan's FDI flows to LAC fare quite well when compared with those from China in both quantitative and qualitative respects: Japan's FDI stock is high and is diversified among targeted industries, thereby contributing to technological transfer and human resource development. Moreover, Japan has been a significant source of development finance for the LAC region; the present scale of JBIC's operations in Latin America rivals those of Chinese policy banks. The nature and scope of JICA's activities in LAC suggest the relationship between Japan and the LAC region has transformed from "Japan as donor and LAC as recipient" to "Japan-LAC global partners." As a result of the preceding, LAC nations are increasingly viewed by Japan as essential economic and political partners as Japan promotes its model of cooperation and economic governance in the Asia-Pacific region and globally. In short, cooperation has been an integral part of the Japan-LAC relationship, demonstrating how interactions in the private sector open space for government-to-government cooperation and vice versa. Strengthening commercial relations with Japan by reciprocally applying the public-private partnership (PPP) principle will assist LAC countries in addressing some structural problems and challenges of long data.

*/ This paper has been prepared by Mikio Kuwayama, Research Fellow of the Research Institute for Economics and Business Administration, Kobe University (RIEB) and Managing Director of the Japan Association of Latin America and the Caribbean (JALAC), for the Seminar "The Role of Japan-LAC Partnership in Restoring a Fragmented International Order: Toward Enhanced Cross-Pacific Connectivity", cohosted by JALAC and the Inter-American Dialogue (IAD), September 27, 2019, Tokyo, Japan. The views expressed in this paper are of the author and do not necessarily reflect those of JALAC. The author is responsible for any errors or omissions. This paper has not undergone formal editing. Please do not cite or distribute without permission of the author.

I. Introduction

For decades, Japan has been an important trading partner, lender, investor, and provider of official development assistance (ODA) in Latin America and the Caribbean (LAC). While China's ascendance has overshadowed bilateral merchandise trade between Japan and LAC in recent years, Japan was the largest Asian trading partner for a majority of LAC countries up to the turn of the century. Furthermore, Japan has been a major investor and provider of development finance for the region over more than five decades. In addition, when overseas activities by Japanese companies' subsidiaries and affiliates operating in the LAC region are taken into account, it becomes clear the economic and commercial relationship between Japan and LAC is much deeper and diversified than simple trade and investment statistics might suggest. Merchandise trade and investment flows to and from Japan do not capture all facets of the bilateral economic and commercial relationship.

Japan's long-standing ties to LAC and its decades-long commitment to the region's economic development are distinguished from other East Asian nations (Myers and Kuwayama 2016; Myers and Hosono 2019). Japan's trade relations, its finance provided mainly by Japan Bank of International Cooperation (JBIC) and ODA by Japan International Cooperation Agency (JICA) have targeted increasingly diverse and technologically intensive sectors in the region, facilitating technology transfer, skills development, and employment. Japan's FDI, which has likely acted as a substitute for trade in some cases, brings significant benefits for LAC countries: cutting-edge technology, know-how, employment opportunities, and foreign exchange earnings (Kuwayama 2015; IDB 2013; IDB 2016).

In some cases, Japanese companies have transformed into major exporters from their production bases in LAC not only to Japanese markets but also to third countries including China, the United States, the European Union (EU), and the proper LAC region. Specifically, exports to third-country markets by Japanese companies' subsidiaries and affiliates operating in the region exceed by far LAC's bilateral exports to Japan. This contrasts the case of China, where a number of studies have shown that significant market penetration by Chinese imports often pose a direct competitive threat for LAC manufacturing producers, especially in sectors such as steel products, textiles and clothing, footwear, domestic appliances and tires, in both domestic and third markets (ECLAC 2011, 2018b). Moreover, Japan has worked for many years to integrate the LAC industry into its global value-chains (GVCs) through targeted investment and technical cooperation. These initiatives are supportive of both Japanese and LAC exports of manufactured goods and natural resource-based products.

Japan has been a significant source of development finance for the LAC region. The

scale of JBIC's operations in LAC has rivaled those of major multilateral institutions and Chinese policy banks. Though a strict comparison is difficult, the stock of loans and equity investment funded by JBIC equals that of Chinese policy banks. The distribution of finance by recipient countries and sectors is more diversified for JBIC than Chinese policy banks. In turn, the LAC has been a target for JBIC: The region has accounted for 20% of JBIC's annual outstanding commitments in recent years. While a considerable percentage of JBIC overseas lending supports the acquisition of energy and mineral resources by Japanese firms, Japan's official loans to LAC also support manufacturing, and its share is increasing. JBIC has shown a strong disposition towards governments with market-friendly economic policies. It should be reminded, however, that JBIC's contributions represent only a fraction of aggregate Japanese finance in the LAC region; Japanese commercial bank interests in LAC are substantial and rising.

Despite some obstacles, Japan sees considerable value in enhanced engagement with the region, both from an economic perspective and as part of a broader, global effort to build consensus on a rules-based international order. Japan maintains bilateral trade agreements known as economic partnership agreements (EPAs) with Chile, Mexico, and Peru, and will engage with these three countries and other nations along the Pacific Rim through the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP, or commonly known as TPP11), which took effect on December 30, 2018, without US participation. The Japan-EU EPA entered into force on February 1, 2019, before the United Kingdom supposedly leaves the EU. The entry into effect of both agreements sends the world the message that with concern over the global rise of anti-globalism and protectionism, Japan is prepared to play an active role in preserving the multilateral trading system (Kuwayama 2019b). In a sense, CPTPP is likely to fill, to some extent, a geopolitical vacuum created by the retreat of US global leadership, which is unlikely, at least for now, to be filled by China's "state-driven" trade liberalism. In addition, very recently, there has emerged a possibility of signing an EPA with the Mercado Común del Sur (Mercosur).

The type of EPAs signed by Japan was established from the premise that a free and open trade regime is not enough to bring about sustainable development and that trade liberalization must be complemented by cooperation (Kuwayama 2015, 2019a). The Japanese authorities are increasingly aware that greater market-driven economic integration will not happen without measures to promote and support it; it requires not only trade liberalization and harmonization of disciplines and rules, but also cooperation directed towards market development, industrial amalgamation, and enhancement of comparative and competitive advantages. The Japanese ODA model that has been applied in Asia and elsewhere emphasizes those typical elements of ODA such as infrastructure improvements and human resource training, with a view to transform the production sector and to promote trade and investment.

This paper will argue not only the LAC region has become an essential target for the Japanese business community over the years, but also the nature and scope of business implemented by the Japanese companies operating in this region, and elsewhere for that matter, is much more globalized than Japan-LAC bilateral trade and investment statistics might suggest. Chapter II will highlight the main features of Japan's trade and investment relations with LAC, analyzing in detail 1) bilateral trade flows, 2) foreign direct investment (FDI), 3) business operations of Japanese companies' subsidiaries and affiliates in the region, and 4) loans and investment by JBIC in relation to those of Chinese counterparts whenever such comparison is possible. Chapter III will examine Japan's ODA-related activities in recent years and highlight some ODA projects in conformity with the new guidelines for cooperation toward the LAC region recently announced by the Japanese authorities. Chapter IV provides concluding remarks and policy recommendations.

II. Trade and investment relations between Japan and LAC

A. Bilateral Trade

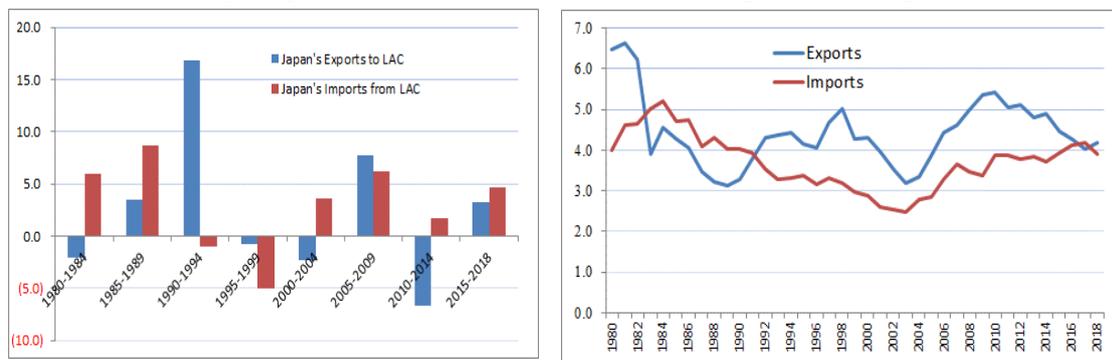
Japan and LAC have been important trading partners for decades, a sharp contrast to LAC's trade with its neighboring countries in Asia, whose trade has only reached significant levels since the turn of the present century. Although the ascendancy of China as a major force in LAC trade has overshadowed, to some extent, the dynamics of Japan-LAC trade and investment relations, commercial ties between Japan and LAC have evolved and diversified over five decades (ECLAC 1986, 1990, 1996; Stallings 1990; Horisaka 1993). From an initial focus on minerals and agriculture, the relationship now encompasses a much broader spectrum of trade-cum-investment links and government-to-government cooperation that have laid the foundations for the development of various sectors in the LAC region.

As observed in LAC trade with other countries and regions, Japan's trade performance has been heavily influenced by both business cycles of trading partners and external factors. LAC's importance as a trading partner for Japan has evolved accordingly in relation to the business cycles and economic-financial crises (Kuwayama 2015; Hamaguchi 2018). Despite ups and downs, however, the LAC market accounts for 4-5% of Japan's total exports and 4% of the country's imports over 35 years (see Figure 1A and 1B). In recent years, the share of LAC in Japan's imports has been on the rise. Therefore, the region continues to be Japan's significant trading partner; in 2018, Japan's exports to and imports from LAC (based on Japan's official statistics) amounted to US\$ 30.8 billion and US\$ 29.2 billion, accounting for 4.2% and 3.9% of the country's total exports and imports, respectively.

Figure 1: Japan's Trade with Latin America and the Caribbean 1980-2018
(percentages)

A: Annual growth rate averages,
(five-year periods)

B: LAC share in Japan's total
exports and imports



Source: Author's elaboration based on JETRO statistics.

It should be noted that Japan was the largest Asian trading partner (both in exports and imports) for the LAC region as a whole until 2003, when China, for the first time, displaced Japan as Asia-Pacific's main trading partner in that region. Specifically, Japan accounted for 51% and 57% of total LAC exports and imports with the Asia-Pacific region in 1991, respectively. In 2002, Japanese bilateral trade (exports and imports) with LAC totaled US\$ 23 billion, surpassing US\$ 20 billion of Chinese trade with LAC that year. As seen in Figure 2A and 2B, the displacement of Japan by China was accelerated during LAC's "Golden Age" (2003~2008) and in the post-crisis period until 2013, when LAC's exports to China started to slow down in relative terms.

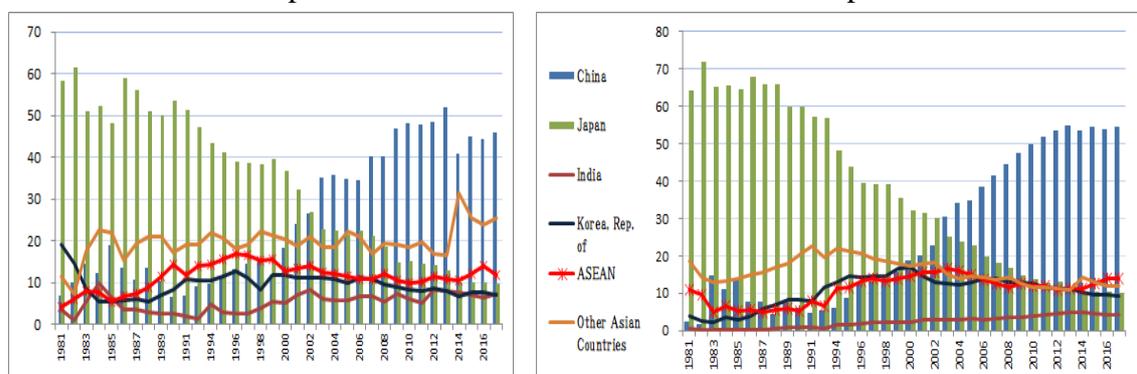
In 2017, Japan's share in total LAC exports to and imports from Asia stood at 9.6% and 10.6%, respectively, slightly below the figures recorded by the ASEAN countries. LAC's bilateral trade (exports and imports combined) with China reached US\$ 256 billion in 2017, almost five times Japan's trade with the region of approximately US\$ 50 billion, or ASEAN total of US\$ 49 billion. Japan's trade, however, surpassed South Korea's total of US\$ 42 billion and India's total of US\$ 28 billion (Figure 2A, 2B). In short, whereas Japan was the main trading partner (both supplier and buyer) from the region in the 1980s and 1990s, China is currently the dominant partner for LAC, especially in the region's imports. In terms of imports into LAC from Asia, China's penetration is unparalleled: Roughly 60% of LAC imports from Asia originate from China.

Figure 2: Shares in total LAC trade with Asia, by major trading partners, 1981-2017

(In percentages of total LAC exports/imports to and from Asia)

A. Exports

B. Imports



Source: Author's elaboration based on INTAL/IADB (Institute for the Integration of Latin America and the Caribbean) database.

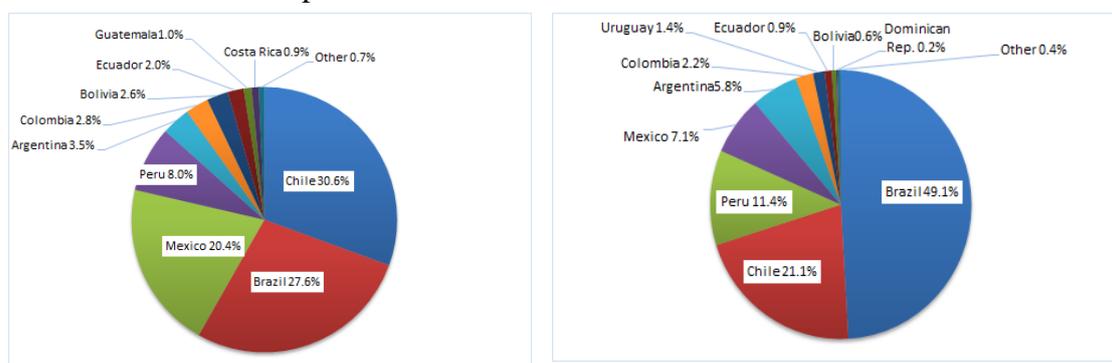
Despite the preceding observations, LAC exports to Japan are more diversified than to China; Chile, Brazil, Mexico, and Peru, by order of importance, together accounted for 87% of LAC total exports to Japan during 2015-2017 (see Figure 3A). Similarly, in the case of LAC exports to China, the same four Latin American countries figure as the top four LAC exporters with a combined share of 89%. In addition, the export structure to China is more concentrated; Brazil accounts for half of LAC's total exports to China (Figure 3B). In contrast, in the case of LAC's exports to Japan, Chile has overtaken Brazil as the largest LAC exporter in recent years, while the share of Mexico (20%) has markedly risen. In contrast, China has not experienced a significant change in its export market diversification process in recent years.

Figure 3: LAC Exports to Japan and China, by major exporting countries, 2015-2017 Average

(In percentages of total LAC exports to Japan and China)

A. To Japan

B. To China



Source: Author's elaboration based on INTAL database and other sources.

It is of considerable significance that LAC trade is more balanced with Japan than with China. During 2015-2017, LAC countries reported an annual trade deficit of US\$ 11.9 billion on average with Japan, much smaller than that with China of US\$ 76.8 billion. For some Latin American countries, the trade balance with Japan was positive, and when it was negative, the deficit was much smaller than with the Chinese case. During 2015-2017 on average, Bolivia, Brazil, Chile, and Peru registered a surplus with Japan. Chile's annual trade surplus amounted to US\$ 3.7 billion during the same period on average, while Mexico's deficit is reaching US\$ 14.2 billion.

By comparison, Chile, Brazil, and Peru also registered a surplus with China; Brazil's annual surplus with China amounted to US\$ 12.3 billion during the period. Among the LAC countries that recorded a deficit with China, Mexico's deficit was the largest with US\$ 65.6 billion (as annual average), followed by Colombia (US\$ 7.4 billion), Argentina (US\$ 5.3 billion), Ecuador (US\$ 2.9 billion), Paraguay (US\$ 2.9 billion), Costa Rica (US\$ 1.9 billion), and Guatemala (US\$ 1.8 billion). The increasing deficits with China have resulted from the rapid penetration of Chinese industrial goods into LAC domestic markets. Although Mexico exports more to China than to Japan, Mexico's rapidly growing imports from China results in an increasingly large trade deficit for the Azteca country. Almost 85% of China's total trade deficit with LAC (US\$ 76.8 billion) originates from Mexico. In sum, South America's overall trade balance with China sits close to the equilibrium point, while given their different export specialization, Central America and Mexico report an overall deficit with China and the size of that deficit is increasing rapidly (ECLAC 2018b).

Moreover, LAC's export basket to Japan is much less concentrated by product than the region's exports to China. In Japan's case, copper ores, iron ores, petroleum, meat and edible offal of poultry, zinc ores, coffee, frozen fish, meat of swine fresh chilled or frozen, maize (corn), and accessories and parts of the motor vehicles comprise the ten major export products, accounting for 58% of total exports to Japan in 2017 (Table 1). In the case of China, the ten major products including soybeans, copper ores, iron ores, petroleum oils, refined copper, chemical wood pulp, bovine meat, offal of fish, crustaceans, and poultry represented more than 82% of LAC's total exports. Though LAC's overall export baskets to Japan and China are similar, in the case of China, soybean exports alone account for almost a quarter of total exports. Another critical difference between the two countries lies in fuels; these products account for roughly 11% of LAC exports to China, whereas exports to Japan, the corresponding figure is 5%. In turn, LAC exports to Japan have a larger agriculture and fishery component.

Table 1: LAC Exports to Japan and China, by major product groups, 2017, Harmonized Schedule 2 digits
(In US million dollars and percentages of total LAC exports to Japan and China)

		LAC exports to Japan			LAC exports to China					
Ranking	HS (heading)	Product description	Value	Share in	cumulative	HS (heading)	Product description	Value	Share in	cumulative
			(US millions)	total (%)				(US millions)	total (%)	
1	2603	Copper ores and concentrates	4,191	21.4	21.4	1201	Soya beans	23,223	24.9	24.9
2	2601	Iron ores and concentrates	1,564	8.0	29.4	2603	Copper ores and concentrates	15,020	16.1	41.1
3	2709	Petroleum oils	1,033	5.3	34.7	2601	Iron ores and concentrates	11,502	12.3	53.4
4	0207	Meat and edible offal of the poultry	912	4.7	39.4	2709	Petroleum oils	9,991	10.7	64.1
5	2608	Zinc ores and concentrates	758	3.9	43.2	7403	Refined copper and copper alloys unwrought	7,632	8.2	72.3
6	0901	Coffee	740	3.8	47.0	4703	Chemical wood pulp soda or sulphate	3,522	3.8	76.1
7	0303	Fish frozen excluding fish fillets	617	3.2	50.2	0202	Meat of bovine animals frozen	1,973	2.1	78.2
8	0203	Meat of swine fresh chilled or frozen	537	2.7	52.9	2301	Meat offal of fish, crustaceans molluscs	1,447	1.6	79.8
9	1005	Maize (corn)	461	2.4	55.3	7402	Unrefined copper	1,393	1.5	81.3
10	8708	Parts and accessories of the motor vehicles	435	2.2	57.5	0207	Meat and edible offal of the poultry	895	1.0	82.2
11	8517	Electrical apparatus for line telephony	414	2.1	59.6	2616	Precious metal ores and concentrates	804	0.9	83.1
12	0304	Fish fillets and other fish meat	406	2.1	61.7	8703	Motor cars and other motor vehicles	797	0.9	83.9
13	7601	Unwrought aluminium	388	2.0	63.7	8517	Electrical apparatus for line telephony	791	0.8	84.8
14	7202	Ferro-alloys	347	1.8	65.4	7202	Ferro-alloys	724	0.8	85.6
15	4401	Fuel wood ; wood in chips or particles	341	1.7	67.2	2608	Zinc ores and concentrates	691	0.7	86.3
16	2613	Molybdenum ores and concentrates	293	1.5	68.7	7404	Copper waste and scrap	612	0.7	87.0
17	2836	Carbonates; peroxocarbonates (percarbonate)	227	1.2	69.8	4104	Leather of bovine or equine animals	549	0.6	87.6
18	2204	Wine of fresh grapes	223	1.1	71.0	2607	Lead ores and concentrates	531	0.6	88.1
19	4703	Chemical wood pulp soda or sulphate	213	1.1	72.1	8708	Parts and accessories of the motor vehicles	428	0.5	88.6
20	2009	Fruit juices and vegetable juices	199	1.0	73.1	4702	Chemical wood pulp dissolving grades	421	0.5	89.0
		Others	5,266	26.9	100.0		Others	10,204	11.0	100.0
		Total	19,565	100.0			Total	93,149	100.0	

Source: Author's elaboration based on INTAL database and other sources.

In addition, LAC's exports to Japan consist not only of traditional commodities and their processed goods but non-traditional primary products of higher value-added such as salmon, wine, meats, orange juice, fresh flowers, processed wood, and other products. LAC countries such as Brazil, Mexico, and Chile have become a major source to satisfy the import needs of chicken and pork meats in Japan. Mexico, together with Peru, is a major supplier of asparagus, avocado, and mango to the Japanese market. Almost 60% of imports of salmon and trout, fish of the largest domestic consumption in Japan, are met from Chile, far greater than that from Norway (22%). Sushi shops in Japan are increasingly dependent on Mexican tuna supplies and Chilean salmon products. Colombia has become a major provider of fresh flowers for Japan, in addition to coffee, product of which the country is the third-largest exporter to Japan after Brazil and Viet Nam. Also, LAC has established undisputed positions as suppliers of non-traditional minerals and metals. Two-thirds of Japan's increasing demand for molybdenum is being satisfied from Chile and Mexico. Japan meets most of its lithium needs from Chile and Argentina.

Over the years, Japan has established in LAC a strong manufacturing base in sectors such as automobiles and electronics. Japanese companies operating in these sectors serve

both the domestic and third export markets, contributing to employment and boosting LAC's trade balance and foreign exchange earnings. As analyzed in more details later in this paper, overseas transactions by Japanese companies' subsidiaries and affiliates do not figure in LAC-Japan bilateral trade statistics. For example, Japanese automakers accounted for nearly 30% of Mexico's car production in 2018, of which 76% were exported to the United States (Tajitsu et al. 2019). Nissan, Toyota, Mazda, and Honda together produced some 1.3 million units of passenger cars and exported approximately 950,000 units that year.

The preceding means the Japanese automakers accounted for 27% of passenger cars exported by major automakers operating in Mexico in 2018, including General Motors, Ford, Fiat Chrysler, Volkswagen, Kia, and others (see Table 2). In Mexico, the automotive sector was the most important export product to the United States in 2018; exports of passenger cars (US\$ 93 billion) accounted for 28% of total Mexican exports (US\$ 344 billion) to the United States, followed by electrical machinery and equipment, where Japanese companies have also heavily invested in Mexico over the years. Overall, exports by Japanese automakers in Mexico are responsible for almost 10% of total Mexican exports to the United States.

Table 2: Number of vehicles produced in and exported from Mexico to the United States, by automaker, 2018
(Units of vehicles, as percentages in total %)

	Production		Exports	
	Units of vehicles	Share in total (%)	Units of vehicles	Share in total (%)
General Motors Co	834,414	20.2	811,954	23.5
Nissan Motor Co Ltd	762,408	18.4	496,333	14.4
Fiat Chrysler Automobiles NV	639,022	15.4	630,967	18.3
Volkswagen AG	435,373	10.5	377,437	10.9
Kia Motors Corp*	294,600	7.1	231,695	6.7
Ford Motor Co	280,499	6.8	273,009	7.9
Toyota Motor Corp	191,978	4.6	187,569	5.4
Audi AG	173,098	4.2	172,232	5.0
Mazda Motor Co	149,589	3.6	137,463	4.0
Honda Motor Co	147,158	3.6	130,542	3.8
Daimler AG**	230,000	5.6	-	-
Total	4,138,139	100.0	3,449,201	100.0
Japanese automakers	1,251,133	30.2	951,907	27.6

Notes: */ South Korean automaker stated production includes 55,978 Verna small cars made for affiliate Hyundai Motor Co. **/ The group last year opened the COMPAS plant in Aguascalientes, which it jointly operates with Renault-Nissan, to produce its A-class sedan. Originally, the plant targeted annual production of up to 230,000 vehicles, whose ramps have faced technical difficulties.

Sources: Reuters (2019), "Factbox: Auto, other industries' manufacturing presence in Mexico, ". The original data cited in this article are taken from the Mexican Automotive Industry Association

Destinations of exports from Mexico have diversified to include South America, Europe, and even China. In Brazil, Japanese automakers have also developed important export platforms, exporting to a few South American countries from their plants in Brazil. Some of these automakers have established plants in neighboring countries such as

Paraguay to supply Brazilian-based assemblers and Central America to supply Mexican production (IDB 2016). As can be appreciated from the above, a rapidly consolidated presence of the Japanese companies in the automotive sector and others suggests some Latin American countries are beginning to integrate into the extensive supply-chain networks prevalent in the Asia-Pacific, North America, and Europe. LAC's engagement with Japan should further facilitate this process. In turn, Japan has been contributing to GVC development of Mexico and Brazil across the Pacific Rim.

Another feature that differentiates Japan-LAC trade from that of China is the important role that large general trading companies (*sogo-shosha*) play in moving merchandise and services between LAC and third countries. These companies, either directly or through subsidiaries operating in the region, play a critical intermediary role in moving raw materials such as minerals and grains from their source in the region to destination countries in Asia, especially China (ECLAC 2010a; IDB 2013). As the trade war between China and the United States intensifies, China has increasingly satisfied its soybean needs from Brazil against the backdrop of diminishing imports from the United States. Some *sogo-shosha* are reported to engage in this type of third-country trade between China and LAC. As shown later in this paper, the scale of business implemented by subsidiaries of these companies in the LAC region is significant but not necessarily reflected fully in LAC's bilateral trade statistics with Japan.

More importantly, these companies also act as investment banks, participating directly in the management of the firms they invest in or co-finance projects with other firms of Japanese or non-Japanese origins. Examples of investment projects financed by these companies in LAC abound. A significant part of their global business resources is sourced from third countries, and this often leads to underestimating the magnitude of investment by Japanese companies in the LAC region. In addition to boosting trade between LAC and third countries, these companies bring not only logistical, marketing, and distribution expertise but also significant investment and finance resources to the region (ECLAC 2010a; IDB 2013). However, activities of these companies with third-country markets and LAC's domestic markets are not captured in the LAC-Japan bilateral trade and investment statistics.

An interesting feature of trade relations between Japan and LAC is the Japanese public sector has played a major role in introducing non-traditional exports by Latin American countries to Japanese and other markets. Government activities have often taken the form of cooperation projects to help firms in the region develop export potential and develop capacities to supply Japanese and other markets. In fact, Japan has been behind some of the region's emblematic export success stories, such as Chilean salmon (Hosono, Iizuka and Katz 2016), Brazilian soybeans and maize (Hosono et al. 2015) and agricultural product supply-chain projects in Paraguay (JICA/ECLAC 2014) in addition to the

development of local supply chains in Mexico's automotive sector. Such achievements are a result of efforts based on interactions between Japan's public-private partnership (PPP) efforts and those of Latin American counterparts. Governments on both sides have played a catalyst role in shaping the bilateral (or even triangular) relationships, ensuring that opportunities will diversify by sector and market and that trade and investment in new areas be materialized.

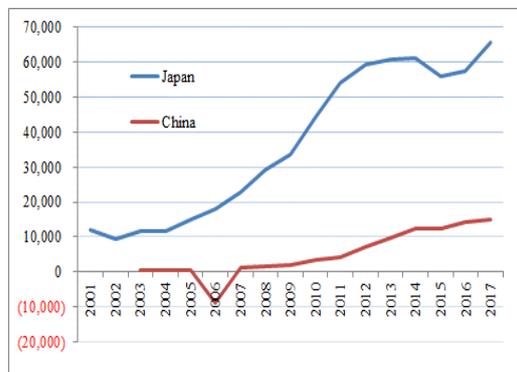
B. Foreign Direct Investment (FDI)

Identifying the country of origin of FDI flows based on national accounts tends to be very imprecise, as this shows only the immediate bilateral source of investment funds, and does not identify transactions conducted through third-party markets, including those via subsidiaries located in territories offering tax benefits. As in the case of trade statistics, FDI flows from third countries, particularly from subsidiaries of Japanese firms in the United States, are not included in these figures. This omission leads to a significant underestimation of investment by Japanese companies in the region. Another serious defect of FDI statistics is investment amounts are most often based on "announced" investments, not actual "materialized" investments. Moreover, in the case of both Japan and China as well, the inclusion of these "tax heaven" financial centers as FDI destinations grossly overestimate actual flows and stocks (net accumulated flows). In addition, all these figures are based on historical prices (not constant prices), so that Japanese FDI flows of long data, which sometimes go back 50 years, tend to be severely underestimated in current dollar terms.

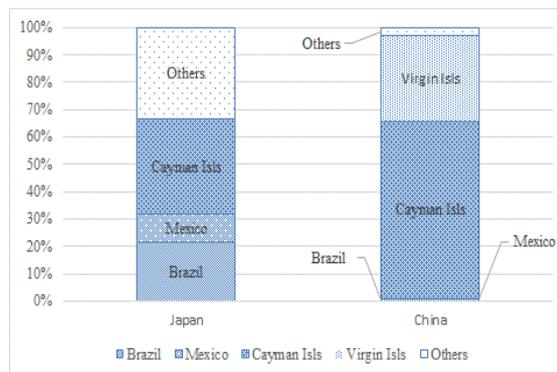
Keeping in mind the problematic methodological aspects mentioned above, official statistics of both countries indicate Japan's FDI flows to LAC fare quite well with those from China. Japanese official FDI figures are based on balance-of-payments, which also include those FDI flows to financial centers such as the Cayman Islands. Japan's FDI stock including FDI to the Cayman Islands reached US\$ 101 billion in 2017; when FDI to the Cayman Islands is excluded, that stock amounted to US\$ 68.9 billion, with the financial center accounting for 36% of the total. On the other hand, data from the Ministry of Commerce of the People's Republic of China (MOFCOM), which include two principal financial centers (Cayman Islands and the Virgin Islands) as FDI destinations, show both financial centers representing 96% of the FDI stock (US\$387 billion) in the LAC region in 2017 (Figure 4A). Thus, FDI to non-financial centers represented only 4% of total stock (approximately US\$15 billion). Moreover, China's FDI stocks in Brazil and Mexico are minuscule, where Japanese companies have heavily invested over the years.

Figure 4: Japan and China FDI stock in LAC, by official statistics
(US\$ million and %)

A. FDI stock, excluding major financial centers 2001-2017



B. FDI distribution by destination country 2017



Notes: Japan: excluding FDI stock in the Cayman Islands. China: excluding FDI stocks in the Cayman Islands and the Virgin Islands.

Source: Japan: UNCTAD FDI database (2001-2012), Central Bank of Japan, JETRO FDI statistics. China, MOFCOM data. Statistical Yearbook of China, various years.

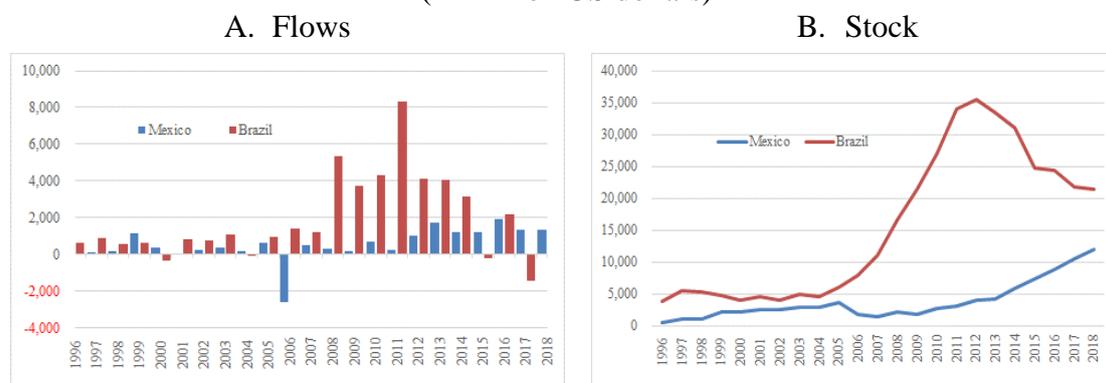
Despite a slack in 2014 and 2015, Japan’s FDI stock in LAC continued to rise. Brazil and Mexico have been the largest recipient countries in the region, while the “others” group accounting for 33% of the total. Even when FDI to “tax haven” countries is excluded, Japan’s FDI stock in LAC continues to grow and far exceeds that of China, based on Chinese official FDI statistics. It is noteworthy that Japan’s stock in Brazil remains high, while that in Mexico it continues to expand (Figure 5A and 5B). In the case of Japan, though the Cayman Islands is still the dominant destination, FDI to LAC is much more diversified in terms of recipient countries. FDI flows to Mexico has steadily increased in recent years, while those to Brazil show a trend of divestment (Figure 5B).

Aware of imperfections and distortions of FDI data as well as the methodological problems in estimating Chinese FDI in the LAC region, several scholars and regional institutions have attempted to estimate Chinese outward FDI to the region.¹ Estimates by Dussel Peters (2019), for example, differ significantly from figures by other national (central banks of Latin American countries or MOFCOM) and regional institutions (e.g. ECLAC), given that his estimates are based on the “materialized,” instead of “announced” FDI. ECLAC data are mostly based on national accounts and media coverage and reports on LAC countries. Another methodological problem is the treatment in statistics of mergers and acquisitions (M&As) as FDI substantially changes the magnitude of FDI, especially in the Chinese case.²

¹ Of total inflows to LAC in 2016, 73% came from either the United States (20%) or the European Union (53%). Of those from the EU, 12% came from the Netherlands and 8% from Luxembourg, which both offer tax advantages, meaning they are used as a base by transnational corporations from third countries so that the ultimate origin of funds from these two countries is not immediately clear.

² According to official statistics, China, which has ramped up its FDI outflows significantly, accounted for just 1.1%

Figure 5: Japan's FDI flows to and stock in Brazil and Mexico
(in million US dollars)



Source: Author's elaboration based on information from the Central Bank of Japan and JETRO FDI Statistics.

Dussel Peters (2019) shows that during 2000-2018, Chinese companies were engaged in 402 transactions in LAC countries, with accumulated FDI of US\$ 121.7 billion. The Chinese FDI stock in the LAC region estimated by Dussel Peters of approximately US\$ 120 billion at the end of 2018 is in the ballpark of the ECLAC's estimates (2018b) that close to US\$ 90 billion entered the region from China between 2005 and 2016, which represents approximately 5% of accumulated FDI inflows to LAC. ECLAC also suggests there was a marked increase in both the absolute value and in China's share in the FDI inflows to the region in 2017: the acquisition of Brazilian electricity companies by Chinese companies (more than US\$ 25 billion) had a significant impact on the 2017 figures. According to ECLAC (2014, 2017), Japan accounted for over 5% of the region's total FDI inflows between 2008 and 2013. FDI inflows from Japan in 2016 represented 3% of the total regional inflows in that year. Japan's FDI to Mexico accounted for 5-6% of total FDI received by the Azteca country during 2012-2016.

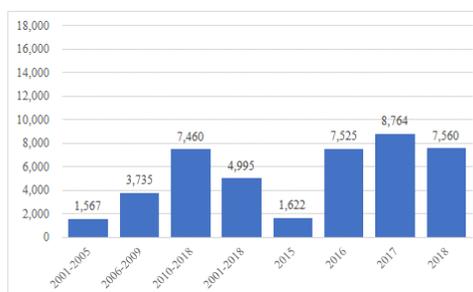
Admittedly, when compared to Chinese FDI, Japan's FDI flows to major FDI destinations in LAC has been smaller than that from China, especially since 2015 (Figure 5). However, Japan's flows have been more stable and diversified. ECLAC estimates Brazil probably has received 55% of investments made by Chinese companies in the region since 2005, followed by Peru, with 17%, and Argentina, 9%. Thus, the top three recipient countries account for 81% of Chinese FDI inflows to the region. In contrast, in the case of Japan's FDI, Brazil, Mexico, Chile, and Colombia also figure among major recipient countries (Table 3).

of inflows to the LAC region. This figure underestimates the amount of Chinese FDI in the LAC region; in fact, when the value of M&As in 2016 is taken into account, China was the fourth largest investor in the region after the United States, the European Union, and Canada (ECLAC 2017).

Table 3 and Figure 5: FDI flows of Japan and China to select Latin American countries 2000/1-2018
(US million dollars)

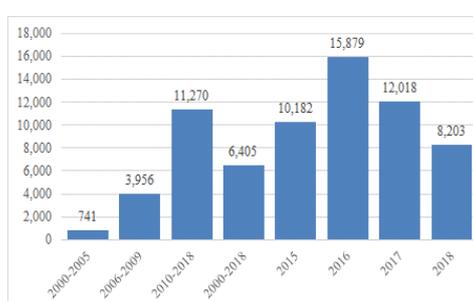
A. Japan*

	2001-2005	2006-2009	2010-2018	2001-2018	2015	2016	2017	2018
	Annual Avc.			Annual Flows				
Argentina	28	48	204	192	643	896	88	
Brazil	713	2,948	2,966	2,336	2,878	1,412	537	2,203
Chile	18	156	639	443	35	-217	825	
Colombia	-8	24	47	25	30	19	63	
Mexico	284	-394	1,194	508	1,772	1,778	1,657	1,321
Peru	19	52	12	23	0	0	0	
Subtotal of the above 6 countries	1,017	2,834	5,033	3,429	5,358	3,888	3,170	3,523
Other	550	901	2,427	1,567	-3,736	3,638	5,594	4,037
Total	1,567	3,735	7,460	4,995	1,622	7,525	8,764	7,560



B. China**

	2000-2005	2006-2009	2010-2018	2000-2018	2015	2016	2017	2018
	Annual Avc.			Annual Flows				
Argentina	0	0	154	65	0	215	1,413	513
Brazil	994	42	547	2,586	5,319	13,903	3,017	421
Chile	0	156	108	593	286	215	2,764	5,170
Mexico	94	33	69	380	1,001	81	2,733	398
Peru	0	181	43	335	11	211	73	1,109
Subtotal of the above 5 countries	688	411	921	4,492	6,617	14,625	10,000	7,611
Other	53	3,545	10,349	1,914	3,565	1,254	2,018	592
Total	741	3,956	11,270	6,405	10,182	15,879	12,018	8,203



Japan: Exclude FDI flows directed to the Cayman Islands.

Sources: Central Bank of Japan, JETRO statistics database. For the period 2001-2012, UNCTAD bilateral FDI statistics. Official statistics from Latin American authorities.

China's figures are taken from Dussel Peters (2019).

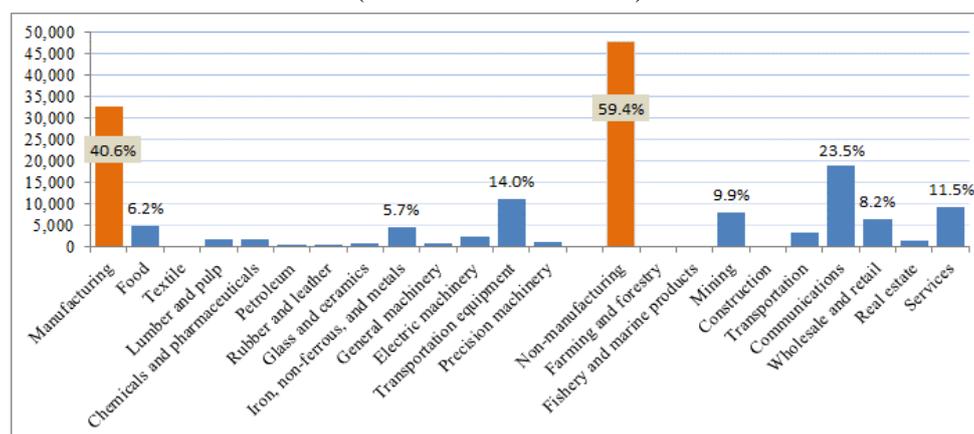
According to Dussel Peters (2019), Chinese FDI flows from 2017 onwards show a momentum significantly weaker than that of 2010-2016.³ The most recent analysis of FDI for LAC (ECLAC 2018a) — with information up to 2017— also shows a downward trend in the reception of FDI in the region since 2014, both due to the drop in international prices of raw materials and economic recessions of 2015 and 2016, particularly in Brazil. In the short and medium-term, Chinese FDI in the region is expected to settle at relatively low levels (see Table 3 and Figure 5).

More importantly, Japanese FDI has been far more diversified both in terms of industries and sectors. When financial and insurance services are excluded, 40% of Japan's FDI stock in LAC is in manufacturing, a stark difference from China's case (Figure 6). While China's investment has gone overwhelmingly to natural resource sectors, Japanese FDI is evenly split among the manufacturing, services, and primary sectors. Among the manufacturing sectors, the share of transport equipment is increasing, while in non-manufacturing, communication is gaining its importance. This scenario

³ The FDI for 2018 alone amounted to US\$ 8.2 billion, a sharp decline from a peak of US\$ 15.9 billion in 2016 and US\$ 12.0 billion in 2017. As a result of a declining trend in 2017 and 2018, the amount per transaction also declined to US\$ 178 million accordingly.

means Japanese firms are creating jobs and bringing new technologies in areas like cars in Mexico and ITC in Brazil.

**Figure 6: Japan’s FDI stock in LAC, by major sectors, 2018:
excluding financial services
(in million US dollars)**



Notes: Financial and insurance services are excluded in this analysis.

Source: Author’s elaboration on the basis of information from Central Bank of Japan.

ECLAC (2018a) shows in terms of the M&A transactions completed in 2017, China was the largest investor in the region. Although the country occupied the sixth position measured by number of M&A deals (15 for the year), the size of these investments — totaling US\$ 18 billion— accounted for 42% of the total. Dussel Peters (2019) also shows that in 2018, M&As consolidated themselves as the main type of Chinese FDI in Latin America, accounting for 62.4% of the FDI amount. The preceding might be interpreted that Chinese transnational corporations have shown a greater interest in acquiring capacities, technologies, and access to markets in relatively advanced economies in the region through the acquisition of strategic assets capable of delivering results in the short term. Therefore, the relative weight of “greenfield” investments might be declining, which, in turn, indicates Chinese FDI may not necessarily be contributing to capital formation of Latin American countries as expected.

The energy sector has been the main target of M&As by Chinese companies in LAC. Concerning the acquisitions by Chinese companies in the region, 49% of the total amount went to this sector and 12% to renewable energy. Meanwhile, mining and utilities accounted for 9% and 33% of the total, respectively (ECLAC 2018a). Manufacturing (8.6%) has been a minor recipient of the Chinese FDI (Dussel Peters 2019). In short, though Chinese FDI continues to diversify in Latin America, the recipient industries have still been concentrated in raw materials (60.0%) This sectoral distribution contrasts to the Japanese case in which the manufacturing sector is the dominant industry.

The presence of Japanese companies in Mexico's automobile and auto parts manufacturing industry exemplifies Japan's FDI sectoral diversification; the number of auto and auto-parts makers established with FDI from Japan totaled 204 companies in 2017, accounting for 15.3% of all foreign-affiliated companies of different nationalities (1,334 companies), after the United States (695 companies, 52%), and Germany (184 companies, 14%). Subsidiaries created in Mexico by FDI from Japanese parent companies in the United States are not counted in the 204 companies mentioned above; these companies in Mexico are included as investment from the United States or funded with indirect investment capital. In effect, when FDI is originating from third countries, the presence of Japanese companies in the Mexican automotive industry can be even greater (JETRO 2018).

C. Operations of Japanese companies' subsidiaries in LAC

The number of Japanese subsidiaries and affiliates operating overseas that participated in the survey on "Activities of Japanese Companies' Overseas Subsidiaries" for the fiscal year 2017 (from April 1/ 2017 to March 31/2018) conducted by the Ministry of Economy, Trade and Industry (Japan, METI 2019) reached some 25,000 worldwide in 2017. These subsidiaries and affiliates operated in a wide range of industries and do not include those in the financial and insurance or real estate industries. Roughly 67% of these (roughly 16,700 firms) were located in Asia, 30% in Mainland China alone. Some 11% were operating in the three NIEs³ (Taiwan Province of China, Republic of Korea and Singapore), and another 27% in ASEAN (4).⁴ The corresponding figures for North America and the EU were much lower, 13% and 11% of the total, respectively. During the same period, there were 1,409 subsidiaries and affiliates of Japanese firms operating in LAC that participated in the survey, representing 6% of the world total. In the LAC region, Brazil (306), Mexico (401) and Argentina (34) were the principal hosts of these companies.

Looking at the distribution by industry worldwide, out of the total (25,034 subsidiaries and affiliates), roughly 43% of Japanese affiliates (10,838 affiliates) were engaged in the manufacturing industries in FY2017, distributed as follows: transport equipment (2,354), chemicals (1,079), and information and communications (ITC) equipment (1,003), among others. The industrial distribution by the number of subsidiaries and affiliates in LAC shares the world pattern: out of the total (1,409), 400 affiliates were engaged in manufacturing, while the remaining 1,009 affiliates in the non-manufacturing industries (Table 4). Among the manufacturing industries, transportation equipment (183),⁵ chemicals (29), ITC equipment (26), and iron and steel (26), were the major recipient sectors of Japanese subsidiaries and affiliates. In non-manufacturing industries, the shares

⁴ ASEAN (4) comprises of Indonesia, Malaysia, Philippines, and Thailand.

⁵ The number of affiliates in transportation equipment in LAC (183) fared well, in relative terms, in comparison with the number of affiliates engaged in that sector of Mainland China (612), ASEAN (4) (655), and NIEs3 (94).

of transport and wholesale trade in total affiliate numbers were high.

LAC's subsidiaries and affiliates belong to a wide range of machinery industries⁶ with a total of 75 affiliates, a much smaller number than that in Mainland China (1,217), ASEAN (4) (660), and in NIEs3 (343). The numbers in and around the machinery industries in Asia reflects buoyant and complex supply chain networks that have been developing in that region. Interestingly, in the LAC, the number of subsidiaries and affiliates in natural-resource-related sectors was relatively small, but with much larger shares in sales and procurements (Japan, METI 2019).

Table 4: Major indicators by Japanese subsidiaries and affiliates operating in LAC, Fiscal Year 2017 (April 1, 2017-March 31, 2018)
(in US\$ million, percentages)

	Number of		Total		Total		Employees at Affiliates				Capital Investment		Ratio of Ordinary
	Affiliates		Sales		Procurements		Total Employees		Employees sent from Japanside	Share in Total	Investment Value	Share in Total	Profits to Sales (*)
	(No. firms)	(%)	(US\$ million)	(%)	(US\$ million)	(%)	(No. of employees)	(%)	(No. of employees)	(%)	(US\$ million)	(%)	(%)
All industries	1,409	100.0	102,834	100.0	68,085	100.0	345,747	100.0	2,836	1.5	6208.1	100.0	5.2
Manufacturing industries	400	28.4	63,659	61.9	43,198	63.4	227,441	65.8	1,601	1.0	1932.9	31.1	3.4
Food	17	1.2	2,148	2.1	957	1.4	12,602	3.6	68	0.6	45.8	0.7	8.9
Textiles	12		x				x		x	0.9	17.3		2
Lumber, wood, paper & pulp	5	0.4	987	1.0		0.0	5,259	1.5	20	0.4		0.0	18.8
Chemicals	29	2.1	1,297	1.3	597	0.9	3,224	0.9	43	2.1	40.6	0.7	22
Petroleum and coal	4	0.3	25	0.0	17	0.0	x		8	5.6			6.1
Ceramics, stone, and clay products	1						-		-				-
Iron and steel	23	1.6	3,879	3.8	1,781	2.6	9,920	2.9	98	1.1	92.9	1.5	1.5
Non-ferrous metals	9	0.6	1,235	1.2	786	1.2	3,987	1.2	x	0.9	84.9	1.4	10.4
Metal products	6	0.4	176	0.2	87	0.1	927	0.3	9	1.3		0.0	5.5
General-purpose machinery	18	1.3	536	0.5	313	0.5	5,422	1.6	50	1.2		0.0	4.1
Production machinery	9	0.6	493	0.5	202	0.3	2,207	0.6	x	3.9	28.2	0.5	2.8
Business-oriented machinery	7		x				x		15	0.2			0
Electrical machinery	15	1.1	528	0.5	346	0.5	4,601	1.3	34	1.5	14.6	0.2	3.4
Information & communications equipment	26	1.8	1,389	1.4	823	1.2	10,495	3.0	x	1.2	73.2	1.2	1.3
Transportation equipment	183	13.0	49,717	48.3	36,044	52.9	152,267	44.0	1,033	1.1	1343.6	21.6	2.4
Miscellaneous manufacturing industries	36	2.6	925	0.9	459	0.7	6,816	2.0	66	1.3	69.6	1.1	6.3
Non-manufacturing industries	1,009	71.6	39,175	38.1	24,886	36.6	118,306	34.2	1,235	4.1	4275.1	68.9	8.6
Agriculture, forestry and fisheries	20	1.4	510	0.5	189	0.3	4,087	1.2	22	1.7	13.6	0.2	13.7
Mining	30	2.1	3,413	3.3		0.0	2,879	0.8	82	4.4		0.0	31.9
Construction	9	0.6	270	0.3		0.0	210	0.1	36	18.8		0.0	-5.3
Information and communications	9		x		14	0.0	2,526	0.7	7	1.3			-16.5
Transport	381	27.0	5,283	5.1	3,084	4.5	9,641	2.8	164	2.0	1979.7	31.9	3.3
Wholesale trade	292	20.7	21,112	20.5	13,818	20.3	50,791	14.7	636	8.7	2050.6	33.0	3.7
Retail trade	13	0.9	791	0.8	578	0.8	1,448	0.4	10	2.0	3.0	0.0	-0.4
Services	126	8.9	3,398	3.3	5,152	7.6	38,494	11.1	243	2.4	14.7	0.2	-0.6
Miscellaneous non-manufacturing industries	129	9.2	x		1,136	1.7	8,230	2.4	35	9.5	46.0	0.7	24.5

Notes: (*) Ratio of ordinary profit to sales = Ordinary profits / Sales × 100.0 (Calculated based on overseas affiliates that responded to questionnaires for both ordinary profits and sales.)

Source: Author's elaboration based on information from Japan, METI (Ministry of Economy, Trade and Industry of Japan) (2019), "kaigai jigyo katsudo kihon chosa" [Basic (trend) survey of overseas business activities] No. 48.

The scale of business of Japanese subsidiaries and affiliates operating in LAC is impressive; total sales by these companies reached some 11.5 trillions of yen (approximately US\$ 103 billion) in FY2017 alone⁷ after reaching a peak of US\$ 148

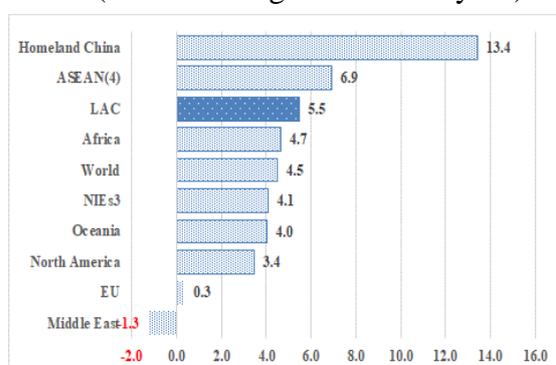
⁶ In this survey, the machinery industry includes general-purpose, production, business-oriented, electrical, and information & communications.

⁷ The sales are tabulated from the information by the companies who reported sales values to the survey. In the case of the Latin America and the Caribbean region, 1,067 companies, out of the total of 1,409 companies provided information

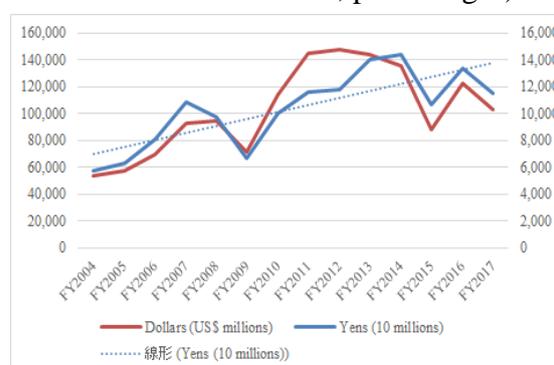
billion in 2012 until when commodity prices continued to rise.⁸ In spite of ups and downs, there is a clear rising trend in total sales, as can be observed in Figure 7B. Though total sales in LAC have been small in absolute terms when compared with those in Asia (Mainland China in particular) and other regions, total sales in LAC have been growing at a faster rate than those in Africa, NIEs3, Oceania, North America, and the Middle East during the 2004-2017 period, surpassed only by Mainland China and ASEAN (4) (Figure 7A).

**Figure 7: Sales by Japanese subsidiaries and affiliates operating in LAC
2004-2017**

**A. Total sales annual growth rates
2004-2017**
(annual average in terms of yens)



B. Total sales in LAC
(left scale: US\$ millions, right scale: 10 millions of Yen, percentages)



Source: Author's elaboration based on information from various issues of Japan, METI (Ministry of Economy, Trade and Industry of Japan), "kaigai jigyo katsudo kihon chosa" [Basic (trend) survey of overseas business activities].

By industry, manufacturing has represented more than 61% of total sales in LAC, while wholesale trade has been the largest non-manufacturing industry (20%). Operations by the *sogo-shosha* are supposedly included in the category of wholesales. The automotive sector has been the most buoyant, accounting for almost half of the total sales in 2017 (Table 4). In manufacturing, iron and steel, food, and ITC equipment, while in non-manufacturing, transport, mining, and services, were also important industrial sectors when measured in terms of sales.

In addition, Japanese companies in LAC are export-oriented, thereby contributing to foreign exchange earnings. In FY2017, more than 50% (some US\$ 53 billion) of total sales by Japanese affiliates operating in the LAC region were exported to third markets, while 44% were sold in domestic markets (US\$ 46 billion) (Figure 8C). Exports back to Japan (US\$ 5 billion) were only 5% of total sales made in that year. As can be observed from Figure 8A, the share of exports to third countries has increased over the years, while

on sales (Japan, METI 2019).

⁸ The sales amount for LAC represented only 3.8% of world sales (288 trillions of yen; approximately US\$ 2,567 billion) in FY2017.

the shares of domestic markets and exports to Japan have been declining since 2010. The three largest economies in the LAC region (Brazil, Mexico, and Argentina) are major sales markets for Japanese affiliates, with a respective share of 20%, 40%, and 7%.⁹ In sum, the overseas activities of Japanese affiliates in LAC are export-oriented to third market economies, which in turn sheds light on a very diversified nature of Japan's business engagement in LAC.

It is interesting to note that Brazil has been taken over by Mexico as the largest sales market destination: Brazil was by far the largest sales market in the LAC region, with a share of 64%, followed by Mexico (16%), and Argentina (3%) in FY2010. The preceding suggests Mexico has been integrated into GVCs, induced in part by Japanese companies. The rising importance of Mexico as a hub of business operations of Japanese companies in LAC is reflected in that major third-country export markets for Japanese affiliates operating in LAC are in North America (the United States and Canada), accounting for 44% of total third-country exports, followed by Europe (6%), Asia (4%), and the remaining regions that include proper Latin American countries (Mexico included) (46%) (Figure 8E). The foregoing suggests Latin American intra-regional market has become an important export destination for Japanese subsidiaries and affiliates.

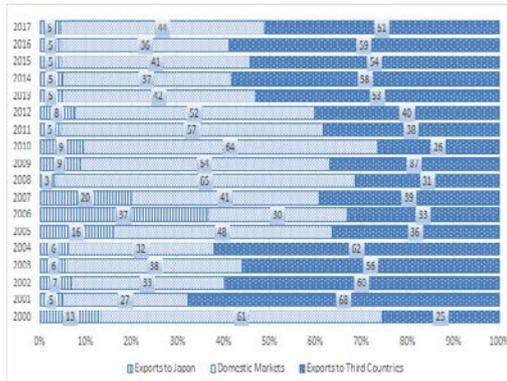
Export propensity towards third-country markets is particularly high for the automotive sector. Specifically, over 60% of total third-country exports (US\$ 53 billion) are accounted for by this sector (US\$ 34 billion). Of the total third-country auto exports, approximately 60% (US\$ 21 billion) were destined to North America, while 33% (US\$ 11 billion) to intra-regional LAC markets. The high export-propensity of Japanese affiliates in LAC suggests Mexico and Brazil —and to a lesser extent, Argentina— have become an important export platform to intra and extra-regional third markets, in addition to the sales in domestic markets based on the large market-size and increasing consumers' purchasing power.

As a reminder, exports to third-country markets by Japanese affiliates are not accounted for in Japanese trade statistics. For example, passenger cars fabricated by Japanese automakers such as Nissan, Honda, Toyota, and Mazda in Mexico are counted as Mexican exports to the United States. In this regard, the “third-market” orientation of the Japanese subsidiaries and affiliates is conducive to the creation of “intra-industry” trade (i.e. the exchange of similar products belonging to the same industry) and the development of supply-chain networks between, for example, Asia and Mexico and between the United States and Mexico. This intra-industry trade experience can be replicated in Brazil and elsewhere in the LAC region.

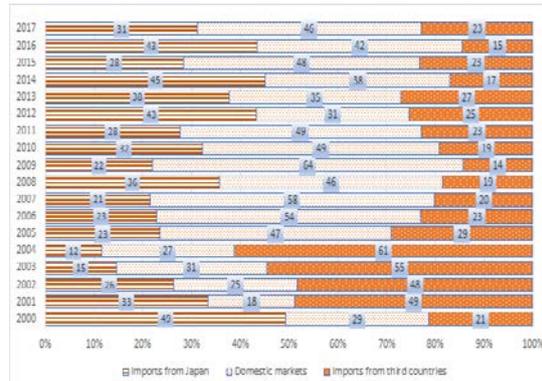
⁹ In Brazil, the highest sales in FY2017 were made in transportation equipment, chemicals, non-ferrous metals, and business-oriented machinery. In Mexico, transportation equipment accounted for over 70% of total sales, followed by iron and steel (5%).

Figures 8: Distribution of total sales and procurements in LAC by market destination, FY2001-FY2017
(In percentage of total sales %)

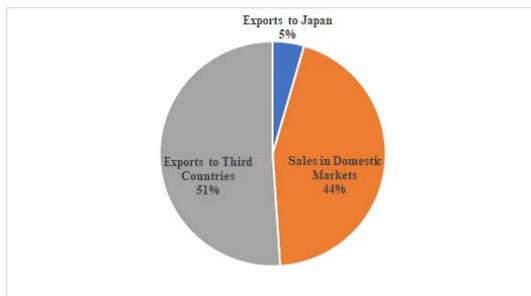
A. Composition of total sales by market destination 2001-2017
(In percentage of total sales of each year, %)



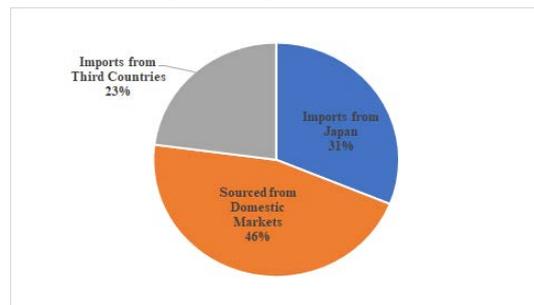
B. Composition of total procurements by market origin 2001-2017
(In percentage of total provisions of each year, %)



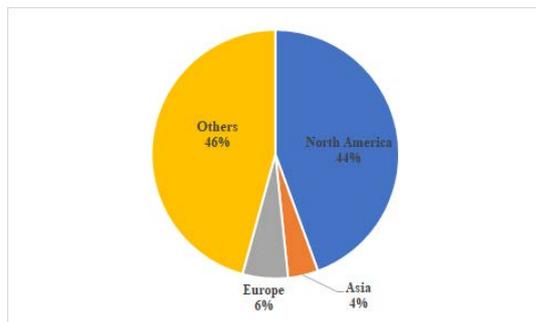
C. Composition of total sales by market destination FY2017
(In percentage of total sales %)



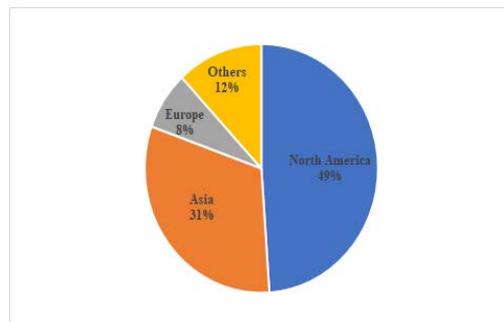
D. Composition of total procurements by market origin FY2017
(In percentage of total sales %)



E. Breakdown of exports to third countries FY2017
(In percentage of total exports to third countries %)



F. Breakdown of imports from third countries FY2007
(In percentage of total imports from third countries %)



Notes: Domestic sales ratio = Sales in domestic markets / Total sales of the region × 100.0.

Domestic procurement ratio = Domestic procurement (purchases) / Total procurement of the region (total purchases) × 100.0.

Source: Author's elaboration based on information from Japan, METI (Ministry of Economy, Trade and Industry of Japan) (2019), "kaigai jigyo katsudo kihon chosa" [Basic (trend) survey of overseas business activities] No. 48.

In addition to automobiles, a wide range of machinery, such as business-related machinery, electrical machinery, and ITC equipment, are exported to North American markets. Industries which show a relatively high export propensity include food and pulp and paper in the manufacturing industries, while in non-manufacturing, mining, forestry and fishery, transport, and wholesale trade. The preceding observations confirm LAC has transformed into one of the essential export platforms toward extra-regional and intra-regional markets for Japanese companies overseas where preferential market access provided by free trade agreements (FTAs) may be an important incentive for their business operations.

When looking at the distribution of procurements (purchases) by Japanese affiliates in LAC in FY2017, imports from Japan amounted to US\$ 21 billion, compared with US\$31 billion sourced from domestic markets, and US\$ 16 billion imported from third countries. Total procurements by Japanese affiliates in FY2017 amounted to US\$ 68 billion (Table 5). In relative terms, Japanese subsidiaries and affiliates operating in LAC make approximately half of their purchases from domestic sources, half of which are sourced from domestic firms and the remaining from other Japanese affiliates operating there (Figure 8D).

When procurements are made from Japan, in most cases, parent companies in Japan are involved. The procurements imported from third countries are less important, accounting for 23% of total procurements in FY2017. Third-country imports are sourced from North America, Asia, Europe, and from intraregional LAC markets (Figure 8F). By industry, as in the case of total sales, the transport equipment sector accounted for 53% of total procurements in FY2017, followed by wholesale trade with 20% of total procurements that year (Table 4). It is important to note the share of procurements from domestic markets is increasing. This trend, in turn, might suggest that operations of Japanese companies are increasingly integrated into regional value-chains (RVCs) in the LAC region.

In addition to sector diversification, Japanese FDI and operations of Japanese affiliates in LAC is conducive to employment creation. The most interesting aspect of Japan's FDI is that Japanese companies operating in LAC contribute to employment in some industries in a substantial manner: the number of employees directly hired by Japanese subsidiaries and affiliates in the region totaled approximately 346,000 employees in FY2017, 100,000 more than 250,000 posts recorded in FY2013. Some 66% (227,000) of the employed by Japanese companies in LAC worked in manufacturing, and 152,000 posts belonged to the automotive sector alone (Table 4). In non-manufacturing, wholesale and services sectors were major employers (Japan, METI 2019). The number of employees sent from Japanese parent companies represented only 1.5% of total employees. This figure might point to the possibility that these companies contribute to manpower training and technological

transfer.

The performance in capital investment and R&Ds activities by Japanese subsidiaries and affiliates operating in LAC fares relatively well when compared to the experiences in other regions. Capital investments made by Japanese subsidiaries and affiliates (479 affiliates investing in LAC) reached US\$ 6.6 billion as the annual average during FY2013-FY2017. In terms of capital-investment value per affiliate (total capital investment divided by the number of investing affiliates), the investment amount reached US\$ 13.8 million, surpassing that made in the EU, the Middle East, ASEAN (4) and NIEs³. A relatively large size of capital investment may be related to the region's specialization in the natural resources-related sectors, production structure of which are capital-intensive in most cases. In contrast, the size of capital investment by Japanese affiliates in East and South East Asia is smaller because Japanese firms in these countries have specialized in more labor-intensive and export-intensive activities such as textiles and confections, electronics (parts and components), and assembly operations.

Other indicators of performance, such as ordinary profits and R&D spending, indicate the subsidiaries and affiliates are equal to, or even better than those recorded worldwide. In terms of R&D spending, for example, LAC outperforms ASEAN (4) and NIEs³ countries; over 40 affiliates investing in R&D close to US\$ 300 million as the annual average during FY2013-FY2017. The R&D investment per affiliate totaled US\$ 6.4 million. Though surpassed by the performance in North America and the Middle East, the affiliates operating in LAC fare quite well when compared to their counterparts operating in the EU, or East or Southeast Asia.

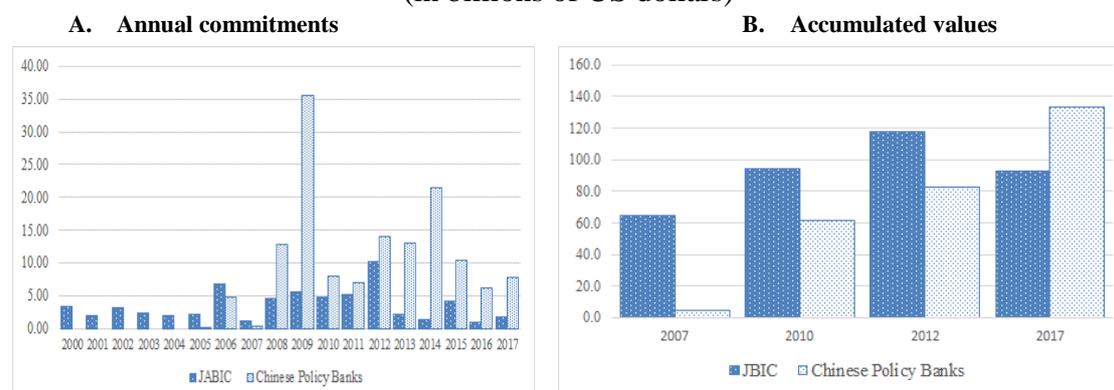
The performance in ordinary profits earned by Japanese affiliates in LAC during FY2004-FY2017 is characterized by high volatility. Specifically, the region shows the highest coefficients of variation among the regions under study.¹⁰ Meantime, net income earned by Japanese affiliates in LAC reached US\$ 3.3 billion (366 billion yen) in FY2017, up by 17% from the previous year. The amount of current retained earnings increased to US\$2.2 billion (283 billion yen), up by 17% from the previous year, while the balance of retained earnings amounted to US\$ 8.2 billion (917 billion yen), down by half from the previous year of US\$ 16.1 billion. The preceding indicates earnings of Japanese subsidiaries and affiliates in LAC fluctuate widely one year to the next. These fluctuations may have to do with macroeconomic “booms and bust” cycles countries of the region often suffer in addition to the skewed pattern of trade specialization in commodities, prices of which also fluctuate widely year to year.

¹⁰ Ordinary profits earned by Japanese affiliates in LAC in FY2017 amounted to US\$ 4.5 billion (505 billions of yen), more than 50% decline from the previous year of US\$ 9.5 billion, which accounted for 4% of total ordinary profits worldwide in that year. The ratio of ordinary profits to sales decreased to 5.2% in FY2017, down from 8.7% of the previous year. When compared to the performance of ratio of ordinary profits to sales of other regions in FY2017, LAC surpasses the world average, but underperforms Oceania, Middle East, and Mainland China.

C. Japanese finance to LAC

Japan has been a significant source of development finance for the LAC region; the present scale of JBIC's operations in Latin America rivals that of Chinese policy banks. JBIC's total commitment in loans, equity, and guarantees to the LAC region in FY 2012 amounted to 805 billion yen, approximately US\$ 10.1 billion (at the annual average exchange rate of 79.8 yens to a dollar of 2012), surpassing the World Bank support of US\$6.6 billion that year and nearing the US\$11.4 billion pledged by the Inter-American Development Bank (IDB) (Table 5). Although the rapid growth of lending to the LAC countries by the Chinese policy banks has outstripped that of JBIC since 2013, China's accumulated value of loans in the region equaled to that of JBIC in the same year, each estimated at US\$ 100 billion (Figure 9A and 9B). Loans by Chinese policy banks to LAC continued to expand in the following years, with accumulated loans reaching US\$ 133 billion in 2017, 30% more than that of JBIC. JBIC's accumulated values in dollar terms have been affected by yen's devaluations in recent years.

Figure 9: JBIC commitments (loan, equity participation, guarantees) vs. Chinese policy bank commitments, annual loans, and accumulated value in the LAC region (in billions of US dollars)



Notes: JBIC's values refer to Japan's fiscal year, while those of Chinese policy banks refer to the calendar year.

Source: Author's elaboration based on information from various JBIC Annual Reports, and Inter-American Dialogue (IAD), China- Latin America Financial Database.

It is noteworthy that JBIC's accumulated loans and equity investment to LAC countries had amounted to US\$ 58 billion in 2000, almost two decades ago. According to JBIC, the financial institution has been involved in 4,182 projects in the region. The preceding is very indicative of Japan's long-standing commitment to the development finance of the LAC region (see Table 5). In turn, LAC has been a major recipient of JBIC finance among developing regions; LAC has accounted for 17% (13,919 billions of yen: US\$ 124 billion) of JBIC's outstanding commitments as of March 31, 2018, more than 10% (1,400 billions of yen: US\$13 billion) of Southeast Asia, and 4% (510 billions of yen: US\$ 5 billion) of Africa (JBIC 2018).

Table 5: JBIC commitments (loan, equity participation, guarantees), annual loans, and accumulated value in the LAC region
(Billions of US dollars, Billions of yen)

	Export loans	Import loans	Overseas Investment loans	Untied loans	Guarantees	Equity participation	Loans, guarantees & equity		Loans & equity (excl. guarantees)	Loans and equity participation Accumulated			Exchange rate
	(1)	(2)	(3)	(4)	(5)	(6)	(Total) (1)-(6)		(1)-(4)+(6)	(1)-(4)+(6)			annual average
	(Bn of yen)	(Bn of yen)	(Bn of yen)	(Bn of yen)	(Bn of yen)	(Bn of yen)	(Bn of yen)	(Bn of dollars)	(Bn of yen)	Number	(Bn of yen)	(Bn of dollars)	(yen/dollar)
FY2000	45.7		229.4	55.3	33.1		363.5	3.4	330.4	3,690	6,231	57.8	107.77
FY2001	35.7		131.9	28.7	47.1		243.4	2.0	196.3	3,744	6,428	52.9	121.53
FY2002	28.3		82.1	156.8	119.9		387.1	3.1	267.2	3,796	6,696	53.4	125.39
FY2003	2.6		119.6	62.9	91.1		276.2	2.4	185.1	3,825	6,881	59.4	115.93
FY2004	1.7		141.1		56.3		199.1	1.8	142.8	3,861	7,033	65.0	108.19
FY2005	12.1	18.9	77.2	32.7	89.1		230	2.1	140.9	3,882	7,151	64.9	110.22
FY2006	32.6	3.6	366.3	4.4	343.1		750	6.4	406.9	3,910	7,557	65.0	116.3
FY2007	1		21.9	7.1	106.9		136.9	1.2	30.0	3,929	7,587	64.4	117.75
FY2008	1.7		214.5	53.1	200.8		470.1	4.5	269.3	3,959	7,857	76.0	103.36
FY2009	20.8		191.3	50.5	248.7		511.3	5.5	262.6	3,994	8,120	86.8	93.57
FY2010	11.6		149.2	14.9	241.6		417.3	4.8	175.7	4,021	8,304	94.6	87.78
FY2011	8.6		344.5	4.5	57.7		415.3	5.2	357.6	4,043	8,662	108.5	79.8
FY2012	23.5	18.1	645.7	70.2	47.9		805.4	10.1	757.5	4,083	9,420	118.1	79.79
FY2013	29.6		123.7	29.2	22.6	3.9	209	2.1	186.4	4,117	9,606	98.4	97.6
FY2014	5.1		104.4	14	12.6		136.1	1.3	123.5	4,133	9,730	91.8	105.94
FY2015	15.1		469.9	11.7	10.5		507.2	4.2	496.7	4,164	10,223	84.5	121.04
FY2016	0.1		3.3	2.8	82.8		89	0.8	6.2	4,171	10,228	94.0	108.79
FY2017	5.5		195.7				201.2	1.8	201.2	4,182	10,427	93.0	112.17

Notes: JBIC's values refer to Japan's fiscal year.

Source: Author's elaboration based on information from various JBIC Annual Reports.

JBIC has shown a strong disposition towards governments with market-friendly economic policies. Brazil and the Pacific Alliance countries (Chile, Colombia, Mexico, and Peru) have received a more significant share of new loans in recent years, while finance to Argentina and Venezuela has dried up since the mid-2000s (Figure 10A). As indicated earlier in this report, Brazil, Mexico, and Chile are Japan's top trading partners in the region. In the case of the Chinese banks, in contrast, Argentina, Brazil, Ecuador, and Venezuela have been major targets of their lending in the region since 2005, with Venezuela accounting for almost half of the accumulated commitments in 2017 (US\$ 62 billion). By recipient country, the accumulated amount of JBIC's loans and equity investment to Brazil surpassed, in dollar terms (US\$ 29.6 billion), that provided by Chinese policy banks (US\$ 28.9 billion). The accumulated amount received by Mexico from JBIC reached US\$ 20.1 billion, surpassing US\$ 1.0 billion from the Chinese policy banks. In sum, JBIC's portfolio is much more diversified than that of Chinese counterparts.

While a considerable percentage of JBIC's overseas lending supports the acquisition of energy and mineral resources by Japanese firms, Japan's official loans to LAC also support manufacturing. In addition, Japanese finance (from JBIC and JICA) has focused more extensively on workforce development, supply-chain development, and promotion of R&D and technology transfer compared to Chinese finance. JBIC is also actively reducing its focus on export promotion. JBIC has also started to put a new focus on so-

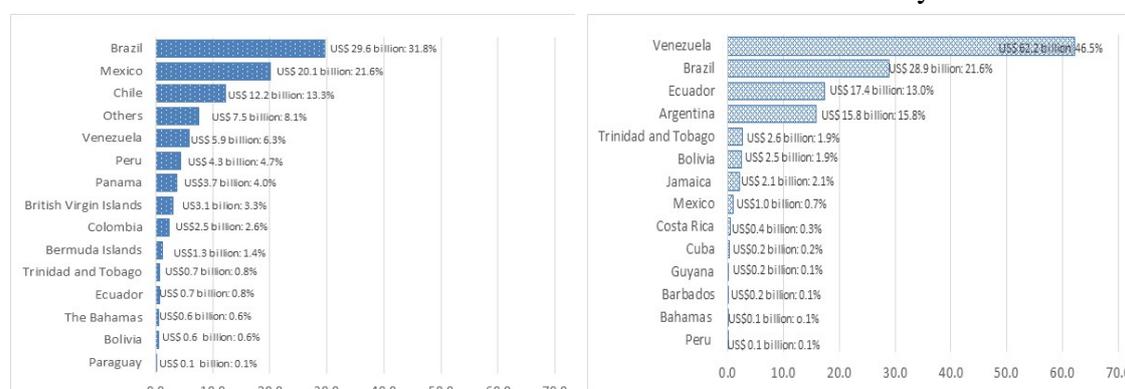
called “GREEN Operations,” which supports energy efficiency and quality infrastructure development. As an example, JBIC signed on November 2018, a loan agreement with the Central American Bank for Economic Integration (CABEI) as part of JBIC's “Global Facility to Promote Quality Infrastructure Investment for Environmental Preservation and Sustainable Growth.”¹¹ This credit line is co-financed with Mizuho Bank and other Japanese commercial banks, with JBIC providing a partial guarantee for the co-financed portion.

Figure 10: Country Distribution of Loan and Equity Participation Commitments, Accumulated 2017*/

(US\$ billion and percentages of total accumulated amount)

A. JBIC

B. Chinese Policy Banks



Notes. */ JBIC's values refer to FY2017, while those of Chinese Policy Banks refer to the calendar year, 2017.

Source: Author's elaboration based on information from various JBIC Annual Reports, and IAD China-Latin America Financial Database.

China policy banks provide finance in support of overseas M&As in strategic sectors such as energy, infrastructure, mining and others sectors; as of December 2018, over two-thirds of credit lines provided by these banks to LAC countries were destined to energy (US\$ 97 billion: 68% of the total), followed by infrastructure (US\$ 26 billion:18%), mining (US\$ 2 billion: 1.5%) and other sectors (US\$ 16 billion: 12%), respectively. In 2018, by contrast, JBIC issued approximately \$1.3 billion in finance to Argentina, Brazil, Central America, and Mexico. In 2018, China, issued just under \$7.7 billion in development bank finance to LAC, \$5 billion of which was given to Venezuela for oil-sector development. The remainder went to Argentina, Ecuador, and the Dominican Republic (Inter-American Dialogue webpage).¹²

¹¹ This credit line is intended to finance, through CABEI, smart energy projects such as maintenance and upgrading of energy transmission and distribution networks in Central America as part of GREEN operations.

¹² Since the beginning of 2019, to support Japan's long-term and stable procurement of copper, 1) the loan for Los Pelambres Copper Mine Expansion in Chile, 2) the loan for Quebrada Blanca Phase 2 Project in Chile, and 3) the loan for Quellaveco Copper Mine Development Project in Peru have been approved. JBIC also signed MOU with Petr oles Mexicanos, aimed at enhancing Japanese companies' participation in oil and gas development in Mexico. In the manufacturing sector, JBIC signed, in November 2018, a loan agreement with Molitec Steel Mexico, S.A. de C.V. (MSM) to finance the expansion of manufacturing equipment used in relation to MSM's manufacturing and sales of

It should also be emphasized that JBIC's and JICA's contributions represent only a fraction of aggregate Japanese finance in Latin America. During the debt crisis of the 1980s, the exposure of Japanese commercial banks in the case of large Latin American debtors was only second to that of the US commercial banks. In September 1986, the cumulative debt of Argentina, Brazil, Mexico, Chile, and Venezuela with Japanese banks reached US\$ 28.6 billion (ECLAC 1990). In recent years, Japanese bank claims on Latin American countries are on the rise. Most overseas loans are issued by one of three Japanese mega-banks: Mitsubishi UFJ Financial Groups, Mitsui Sumitomo Financial Group, and Mizuho Financial Group.

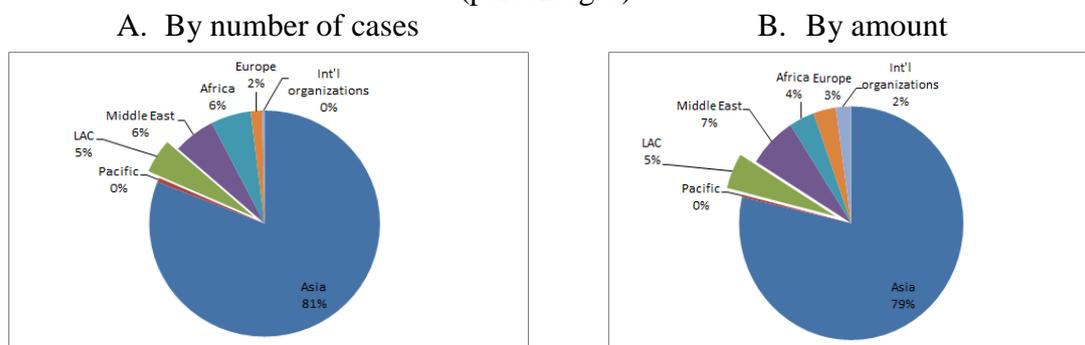
III. Significance of Japan's ODA for LAC

Japanese ODA has had a major presence in the LAC region over decades, while from Japan's perspective, the LAC region has been a relatively minor recipient. At present, Japanese ODA to LAC is modest in comparison to other donor nations. This situation reflects in part the region's average income is relatively high among developing countries; Argentina, Brazil, Chile, Mexico joined the group of high-income countries in January 2018. In terms of accumulated amounts, LAC has been a target region for JICA's loans, surpassing Africa (Figure 11A and 11B). Of a world total of 3,449 projects, 168 were targeted at LAC, while in terms of the amount granted, of a world total of US\$ 326.4 billion, US\$ 16.0 billion were destined to the LAC region. In FY2017 alone, LAC accounted for 2.5% of JICA's disbursement, with a total of US\$ 489 million (Table 6). Admittedly, Japan's ODA project profile varies widely from region to region, with emphasis on lower-income countries in Central America and the Caribbean.

The most important form of Japanese ODA that goes to the region has been technical cooperation, followed by concessional government loans (including those with a concessional element of less than 25%) and grants. Concessional loans are concentrated in Brazil, Mexico, and Peru. Currently, technical cooperation and loans are dominant components. In FY2017, LAC's share is higher for technical cooperation accounting for 8.4% of the world total, whereas that for loan aid is only 1.2%, and grant aid is 2.8% (Table 6). Despite relatively limited in scale, Japan's aid to the region tends to be wider-ranging than China's. China's ODA consists nearly entirely of concessional loans, usually from the Export-Import Bank of China (China Eximbank) to specific Latin American governments (Myers and Hosono 2019).

automobile components, in particular continuously variable transmission parts, in the state of Aguascalientes in West-Central Mexico. Similarly, JBIC signed on November 20, 2017, a loan with Ashimori Industria de Mexico, S.A. de C.V. (AIM), to build a second factory within the existing factory site of AIM for enhancing the production facility in the state of Guanajuato (from JBIC website).

Figure 11: Geographical distribution of accumulated Japanese ODA loans, FY2017 by number of cases and amounts (percentages)



Note: The original figures expressed in Japanese Yens are converted in US dollars using the exchange rate of 1 US dollars = 112.17 yens.

Source: Author's elaboration based on information from JICA Statistics on Program Results 2018.

Table 6: JICA disbursement Fiscal Year 2017 (ending March 31st), by aid type and by region (Millions of US dollars and percentages)

Types of Aid		Asia	Middle East	Africa	North and Latin America	Pacific	Europe	Others	Total
Technical Cooperation 1/	Amount	669	82	319	124	43	25	453	1,714
	Share (%)	36.7	5.8	23.6	8.4	2.4	1.4	21.8	100.0
Finance and investment Cooperation 2/	Amount	10,371	1,340	1,335	291	0	0	3,498	16,835
	Share (%)	79.6	7.2	5.3	1.2	0.8	5.0	1.0	100.0
Grants 3/	Amount	407	74	420	75	50	0	0	1,026
	Share (%)	43.0	3.2	43.3	2.8	6.7	1.0	0.0	100.0
Total (1+2+3)	Amount	11,447	1,496	2,075	489	93	25	3,951	19,576
	Share in Total (%)	70.3	7.6	10.6	2.5	0.5	0.1	20.2	100.0

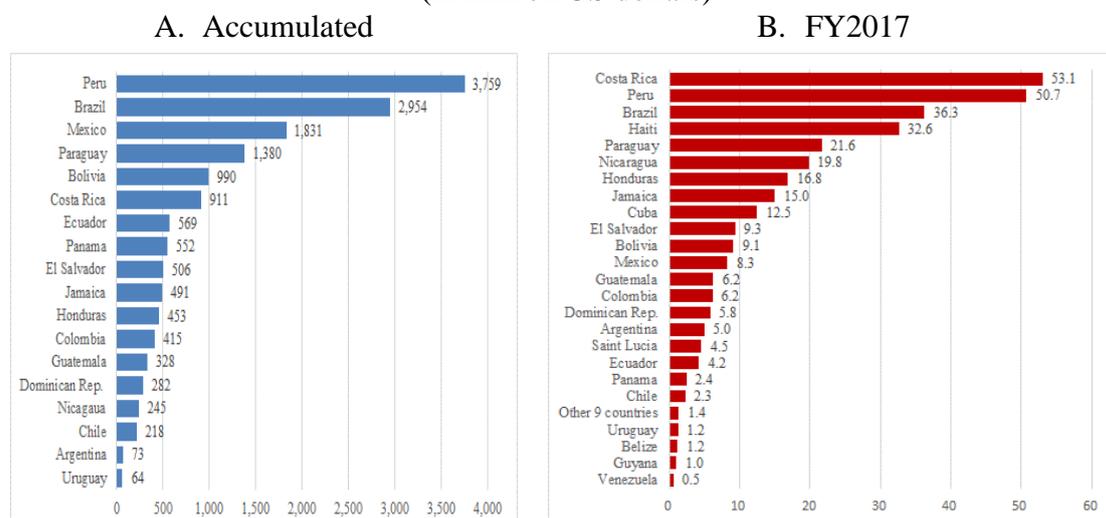
Note: The original figures expressed in Japanese yens are converted in US dollars using the exchange rate of 1 US dollar = 112.17 of yen.

*/ Technical Cooperation expenses include Technical Assistance expenses managed under the Finance and Investment Account budget but exclude administration costs. **/ Total commitment amounts of ODA Loan and Private-Sector Investment Finance. Commitments with the African Development Bank and the African Development Fund are included in "Africa" not "Others." ***/ Amount of concluded Grant Agreements. However, for projects running over several fiscal years, the maximum amount allowed for each fiscal year is counted for that fiscal year.

Source: Author's elaboration based on JICA Annual Report 2018.

When measured in accumulated accounts, Peru, Brazil, Mexico, and Paraguay have been major recipients of JICA's loans; these four countries accounted for 62% of the total amount as of March 31, 2018 (Figure 12A). In FY2017 alone, the major JICA aid recipient countries were Costa Rica, Peru, Brazil, Haiti, Paraguay, Nicaragua, and Honduras (see Figure 12B). Though small in absolute amount, small island states in the Caribbean have also been recipients of JICA aid.

Figure 12: JICA’s accumulated ODA loans and disbursement to LAC countries, FY 2017
(in million US dollars)



Note: The original figures expressed in Japanese Yens are converted in US dollars using the exchange rate of 1US dollars = 112.27 yen.

Source: Author’s elaboration based on JICA, and JICA Statistics on Program Results Report 2018.

Over the years, Japanese ODA has implemented projects of differing scale and scope in the LAC region. The aim of JICA’s recent aid to LAC can be said to be twofold: 1) focus on specific sectors while leveraging its accumulated assets gained through past cooperation; and 2) further strengthen friendly relations with Japan with intentions to working together on a global stage. In this context, JICA puts a priority on areas such as 1) quality infrastructure,¹³ 2) disaster risk reduction (DRR),¹⁴ 3) climate change measures,¹⁵ 4) reducing economic disparity,¹⁶ and 5) regional cooperation.¹⁷ JICA also

¹³ Specifically, in quality infrastructure, an exemplifying case is the implementation of the Rio Blanco–Siuna Bridges and the National Road Construction Project in Nicaragua under an ODA loan (4.94 billions of yen: US\$ 45 million), capitalizing on its many years of experience in constructing as many as 24 bridges by grant projects in the Central American country.

¹⁴ In the area of DRR, JICA and the Inter-American Development Bank (IDB) conducted joint research on the disaster resilience of infrastructure, and good practices in “quality infrastructure”. JICA also launched a technical cooperation project known as the Project for Safe and Resilient Cities for Earthquake and Tsunami Disaster in July 2017, in view of the severe damage caused by a major earthquake that hit Ecuador in April 2016.

¹⁵ With respect to climate change, in Bolivia, JICA is implementing the Laguna Colorada Geothermal Power Plant Construction Project, an ODA loan under the scheme of Co-financing for Renewable Energy and Energy Efficiency (CORE) with the IDB. In Ecuador, JICA supported prospecting for geothermal energy in the Preparatory Survey for Chachimbiro Geothermal Power Plant Construction Project.

¹⁶ JICA has started to apply in Central America the “Life Improvement Approach”, aimed at reducing economic and social disparities there. In Honduras and Nicaragua, JICA dispatched individual experts and launched a technical cooperation project in order to continue with the efforts to strengthen institutional capacities of local municipalities (JICA 2018a). In the area of human resources development, JICA launched the “Program of Japan Expert Development for Future Leaders in Latin America and the Caribbean, a program that offers opportunities to study in Japan.

¹⁷ In the area of regional cooperation, in October 2015, JICA agreed on an Action Plan with the Central American Integration System (SICA), a political and policy framework aimed at improving coordination among nations in Central America. This plan has five priority areas. In FY2017, JICA started regional cooperation projects in two of the five areas: logistics and mobility as well as the conservation of biodiversity and wetlands (JICA 2018a).

continues to work to strengthen ties with Nikkei communities and develop human resources who are familiar with Japanese affairs.

The target areas for JICA's aid mentioned above suggest the relationship between Japan and the LAC region has transformed from "Japan as donor and LAC as recipient" to "Japan-LAC global partner" over the years. Based on this transformation, Japanese Prime Minister Shinzo Abe, in a 2014 visit to Sao Paulo, announced three guiding principles of Japan's diplomacy vis-à-vis LAC region the three "Juntos!!" guideline. They are "Progre^{dir} juntos (progress together)"; reinforcement of economic relations, "Liderar juntos (lead together)"; partnering in the international arena, and "Inspirar juntos (inspire together)"; expansion of scale of people-to-people exchange and strategic communication.

An example of JICA's aid that fits into the "Progress Together" category is its \$US 50-million loan agreement with Amaggi Exportação e Importação Ltda. (Amaggi) for the "Agriculture Supply Chain Enhancement Project" in Brazil, as part of the Private Sector Investment Finance (PSIF) scheme. The Project aims to strengthen agricultural logistics and improve crop productivity in the Northern frontier in Brazil by developing infrastructures, providing advances, training to farmers, and purchasing grains, thereby contributing to sustainable agribusiness in the region. The project is the first JICA private finance transaction co-financed with Citibank, N.A.

A project that fits into the "Lead together" category is "Disaster Risk Reduction Training Program", also known as the KIZUNA Project. It aims to develop the capacity of personnel, notably researchers and administrative officers engaged in DRR, and to create a DRR network within the region. Chile is to be established as a hub for the development of human resources for DRR. JICA invites trainees from LAC countries to Chile to attend training programs and seminars on themes ranging from enhanced seismic resistance for bridges to disaster prevention plans for local communities with a view of enhancing the capabilities of 2,000 people over five years. The personnel trained under this program reached 3,776 persons as of 2017.

An exemplifying project that falls into the category of "Inspire together" is "Development of Harmful Algal Bloom Monitoring Methods and Forecast System for Sustainable Aquaculture and Coastal Fisheries" in Chile. This project aims to bring to light the complex mechanism of occurrence and termination of red tides and to develop a red tide dynamics forecast system under a consortium of research institutions on both sides.¹⁸ This project forms part of SATREPS (Science and Technology Research Partnership for Sustainable Development), a Japanese government program aimed at

¹⁸ The research institutions participating in this project include Japan Kyoto University, Okayama University, and Japan Fisheries Research and Education Agency (FRA), while Universidad de La Frontera, Universidad de Antofagasta, Universidad de Los Lagos, and Instituto de Fomento Pesquero (IFOP), and others from the Chilean side.

promoting international joint research. The program is structured as a collaboration project between the Japan Science and Technology Agency (JST), which provides competitive research funds for science and technology projects, and the Japan Agency for Medical Research and Development (AMED), which provides competitive research funds for medical research and development, while JICA provides ODA. Another example that falls into the category of Inspire together” is “Hazard Assessment of Large Earthquakes and Tsunamis in the Mexican Pacific Coast for Disaster Mitigation,” also part of SATREPS. It aims to assess the potential for megathrust earthquakes in the coastal region of the Guerrero state by establishing the first Mexican seafloor geodetic and seismic network to obtain slow earthquake data under a consortium of research institutions on both sides.¹⁹

With the intentions of working together to address the new and continuing challenges of the United Nations post-2015 era, Japan is pursuing various initiatives to achieve “quality” growth, which specifically means inclusive, sustainable and resilient growth for all, and thereby to eradicate extreme poverty by 2030 in the LAC region. Japan will do so based on the concept of human security by its guiding principle and by applying the new Development Cooperation Charter adopted in February 2015. Japan is promoting wide-ranging partnerships with the private sector in the fields of trade, finance, and technology while utilizing ODA as a catalyst to enhance such activities. This new focus of Japan on development finance bodes quite well with the post-2015 LAC’s Sustainable Development Goals (SDGs) vision.

IV. Concluding Remarks and policy recommendations

Japan’s economic and commercial relations with LAC go far beyond the mere exchange of industrial goods and commodities. LAC nations are increasingly viewed as essential economic and political partners as Japan promotes its model of cooperation and economic governance in the Asia-Pacific region and globally. In short, cooperation has been an integral part of the Japan-LAC relationship, demonstrating how interactions in the private sector open space for government-to-government cooperation, and vice versa. Japan’s engagement in LAC provides positive spillovers to LAC’s proper economic development process. Despite Japanese companies and banks navigating exceedingly complex trade and investment environments in the LAC region amid seismic shifts in the global economic and geostrategic landscape, Japan will remain committed to further strengthening the long-standing ties to the region with the same but more innovative approach.

¹⁹ Participants from the Japanese side are Kyoto University, University of Tokyo, Tohoku University, and Kobe University, while the institutions participating from the Mexican side include the Instituto de Geofísica, Universidad Nacional Autónoma de México (UNAM), and Centro Nacional de Prevención de Desastres (CENAPRED).

Although LAC's bilateral trade with Japan has not been as buoyant compared to China in recent years, Japan's trade relations with the region show several "qualitative" features, which distinguish Japan from other East Asian countries: 1) LAC export-basket to Japan is more diversified than that of China, with the former incorporating in the basket some non-traditional and manufactured products; 2) the export structure to Japan is more diversified in terms of exporting countries in LAC (in the case of China, the share of Brazil is quite high); and 3) the overall trade balance is more favorable for LAC countries with Japan. Some countries even register a trade surplus with Japan, and when the balance is negative, the size of the deficit is much smaller than for China. In the case of China, the deficit with Mexico has reached an alarming level, while Japan continues to expand its trade with the Aztec country, which has transformed into a major hub of global value chains, especially of the automotive industry.

An additional, yet more important feature of Japan's trade relations with LAC points to the importance of subsidiaries and affiliates of Japanese companies operating in the region. As argued in this paper, exports to third-country markets by these affiliates exceed by far LAC's bilateral exports to Japan, highlighting a very diversified and globalized nature of their business activities in the region. These companies show a high propensity to export, especially in the automotive sector in Mexico, and to a lesser extent in iron and steel, food, and ITC equipment in manufacturing, while transport, mining, and services in non-manufacturing. Thanks to the long-standing engagement in the manufacturing industries, their business operations are conducive not only to employment creation but also export expansion (thereby foreign exchange earnings) and global and regional value-chain developments in the region.

Keeping in mind the problematic methodological aspects in estimating Chinese FDI, Japan's FDI flows to LAC fare quite well with those from China. Japanese FDI stock in the region, excluding the financial centers, is estimated to have reached US\$ 70 billion in 2018. This figure compares favorably with estimates close to US\$ 90 billion from China between 2005 and 2016, which represents approximately 5% of accumulated FDI inflows to LAC. Though smaller than Chinese flows in recent years, Japan's FDI toward the region is more diversified in terms of recipient country and industry. In the Japanese FDI, Brazil has been gradually displaced by Mexico, as FDI to Mexico continues buoyant. Though Chinese FDI in the region started to diversify, the energy sector has been a major recipient industry, in which M&As has been increasingly used as a means of investment. The Japanese FDI is evenly split among the manufacturing, services, and primary sectors. Among the manufacturing sectors, the share of transport equipment is increasing, while in non-manufacturing, communication is gaining its importance. As a result, Japanese firms are creating jobs and bringing new technologies in areas like cars in Mexico and ITC in Brazil.

Japan has been a major source of development finance for the LAC region; the present scale of JBIC's operations in Latin America rivals those of major multilateral institutions and Chinese policy banks. JBIC has been involved in over 4,000 projects in the region. LAC has accounted for 17% of JBIC's outstanding commitments as of March 31, 2018, more than 10% of Southeast Asia, and 4% of Africa. The preceding is indicative of Japan's long-standing commitment to the development finance of the LAC region. JBIC's loan imbursement pattern is quite different from the Chinese policy banks, with the former towards governments with market-friendly economic policies, while most of the loans are designated to Argentina, Brazil, Ecuador, and Venezuela, which alone accounts for almost half of the accumulated commitments. In short, JBIC's portfolio is much more diversified than that of Chinese counterparts.

Japanese ODA has had a major presence in the LAC region over decades. Although the LAC region has been a relatively minor recipient in terms of aid amounts in recent years, LAC has been a target region for JICA's aid, surpassing Africa when measured in terms of accumulated amounts. Among different modalities of financing, the most important form of Japanese ODA that goes to the region has been technical cooperation. The recent projects in LAC put priority on areas such as 1) quality infrastructure, 2) disaster risk reduction (DRR), 3) climate change measures, 4) reducing economic disparity, and 5) regional cooperation. The nature and scope of JICA's activities in LAC suggest the relationship between Japan and the LAC region has transformed from "Japan as donor and LAC as recipient" to "Japan-LAC global partner" over the years. These projects are often undertaken with wide-ranging partnerships with the private sector and academic and research institutions, in the fields of trade, finance, and technology, while utilizing ODA as a catalyst to enhance such activities.

Strengthening commercial relations with Japan by reciprocally applying the public-private partnership (PPP) principle will assist LAC countries in addressing structural problems and challenges of long data. Latin America's production and export structure is still based on static comparative advantages than dynamic competitive ones. The region lags in international competitiveness, industrial amalgamation, innovation, R&D, education, and infrastructure. Productivity lags are huge, and there are large productivity gaps between and within sectors in each country (ECLAC 2010b, 2012). Japan's new approach focuses on diversification of products and firms and inclusive growth, promotion of clusters not only in manufacturing but also in natural resources, and participation in global and regional value chains of enterprises of different size.

Over two decades, Latin America has been witnessing three transformations in its commercial policy. One is the transformation of strategy based on trade openness to the internationalization of firms. The second is from trade and investment promotion to

participation in GVCs and RVCs, and the third is from the FTA to Public and Private Partnership (PPP). With this new policy orientation, the emphasis on the FTA has changed accordingly from i) market access to participation in GVCs; ii) rules of origin not as restrictions but advantages, via accumulation of origin between several FTAs; iii) the need to strengthen goods-services-investment links; iv) from commodity exports to technology and knowledge incorporated in natural-resources exports; and v) attracting FDI to promote value-chains in natural resource sectors (Rosales 2009). These policy changes not only point to vast possibilities that may lie ahead, but also lay the foundations for future regional cooperation with Japan, aimed at creating business alliances, enhancing cooperation in innovation and human capital in order to diversify trade, add greater value and knowledge to exports, and help create more stable and sustainable conditions for growth.

The economic partnership agreements (EPAs) signed by Japan seek to complement trade and investment liberalization with facilitation and cooperation. Although a major aim of the EPA is to assist and facilitate overseas operations of Japanese companies by improving the business environment at home and abroad, its scope goes beyond the domains of commercial interests. EPAs may be viewed as part and parcel of a policy of support for broadening production networks and value chains and for enhancing systemic competitiveness of the country and the region. In this way, the EPA complements ODA and other financial resources for cooperation. In sum, Japanese ODA is an important part of the cooperation provided for under the EPA.

For the Asia-Pacific Economic Cooperation (APEC) and non-APEC Latin American countries to resort to and take full advantage of benefits provided under an EPA, Japan should enhance the attractiveness of these agreements by significantly improving market access offers in agriculture that equal those being agreed upon in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) framework. At the same time, Japan needs to publicize and propagate the merits of the EPAs, which are different from the trade agreements signed by the United States, the European Union, or China. In the above respect, an important but often not fully appreciated feature, of the CPTPP is that this agreement incorporates, from the outset, development dimensions into trade negotiations.²⁰ Provisions provided in these chapters should be taken full advantage of to promote the development of Latin American GVCs and RVCs and the quality-infrastructure building. Japan can work together with Latin American countries to tackle these structural problems that these countries face by way of EPAs or CPTPP.

Together with the ODA, Japanese financial resources can play a decisive role in

²⁰ The CPTPP agreement has four chapters on cooperation: Cooperation and Capacity Building (Chapter 21), Competitiveness and Business Facilitation (Chapter 22), Development (Chapter 23), and Small and Medium-Sized Enterprises (Chapter 24).

creating a favorable trade-cum-investment climate. This goal can be achieved via the creation of infrastructure and the development of human resources, supply-chain, and cluster development, as well as innovation and scientific and technological development with intentions to participate more effectively in the global economy. Japan's ODA resources are limited and should be complemented by other Japanese financial resources public and private alike. This strategy, in turn, requires countries of the region set clear priorities and convey their technical cooperation and financial needs more explicitly to Japan.

Another area of mutual benefits is the strengthening of triangular cooperation between Japan and LAC countries. The triangular cooperation format might be encouraged, especially when new regional integration initiatives such as the Pacific Alliance, which have a strong cooperation agenda, are gaining force. In the future, it would also be worth considering cooperation arrangements that go beyond the region by including other extra-regional donors and recipients. The position of Japan as the main donor, both in Asia and LAC, should encourage new cooperation frameworks that might involve Asian countries like those of the Association of Southeast Asian Nations (ASEAN).

Concerning a more efficient and coordinated exploitation of comparative advantages, recent experiences show that value can be added to commodity exports and knowledge can also be incorporated. Although more difficult than in manufacturing sectors, it is also possible for Latin American firms to integrate commodities into production and marketing chains in the Asia-Pacific; this calls for a systemic approach that covers the production process, trade logistics, sea and air transport, and marketing and distribution in the final consumption market. To this end, strategic partnerships should be created to increase value-added throughout the production and marketing chain, and mutually beneficial technological partnerships should be developed by applying, for example, advanced technologies to agroindustry, mining, forestry, and fisheries. Japan offers vast experiences in these areas with Asian neighbor countries but also with some Latin American countries. These experiences can be replicated in LAC by the ODA and other financial resources. These areas are also good candidates for triangular cooperation schemes with countries inside and outside the LAC region.

It is of Japan's interest to promote greater trade and investment links between the Asia Pacific and non-APEC and non-CPTPP Latin American countries. Japan should act as interlocutor should Japan decide to act as a "bridge" between the Regional Comprehensive Economic Partnership Agreement (RCEP)²¹ and CPTPP toward the goal of realizing the Free Trade Area for Asia-Pacific (FTAAP). By doing so, Japan might be able to facilitate non-APEC Latin American countries' engagement in both CPTPP and

²¹ RCEP is an agreement under negotiation among the 10 ASEAN members as well as Australia, China, India, Japan, New Zealand, and the Republic of Korea.

RCEP. At the same time, Japan should support Latin American countries for their accession to RCEP when the membership is opened for extra-regional countries from Latin America. Even during RCEP negotiations, Japan might not only lift the quality of disciplines and rules in RCEP but also seek a model (template) typical of an agreement covering the entire Asia Pacific region, with a strong emphasis on development cooperation.

Most recently, during his 2018 visit to Argentina, Prime Minister Abe announced yet another initiative to enhance connectivity between Japan and LAC. Built on the previously articulated “Tres Juntos” guideline, this policy upgrade envisions a relationship built on three “pillars of connectivity”—economies, values, and wisdom. Regarding economic connectivity, Japan imagines “progressing together” with LAC through the mutual promotion of free and open economic systems, with emphasis on promotion of GVCs and quality infrastructure. Japan also envisions “leading together” with LAC on values connectivity by jointly supporting values-based and rules-based multilateralism. Moreover, knowledge connectivity is aimed at “inspiring together” through collaboration on the SDGs, employing innovative and evidence-based approaches to address regional development challenges. A new series of policy objectives uphold shared values with the region and support innovative solutions to development challenges in the LAC region. In this sense, countries of the LAC region are called upon to work together with the Japanese public and private sectors so that the new “connectivity” approach be mutually beneficial and at the same time supportive of SDGs, democracy, human rights, rules of law, and multilateralism.

A major focus of Japan’s new development assistance strategy is “quality growth”. To achieve quality growth, Japan is expected to assume a leading role in promoting quality infrastructure investment, which is the first target under Goal 9 of the United Nations SDGs. Quality infrastructure projects, in the Japanese government’s view, are those that are user and environmentally friendly, safe and disaster-resilient, and cost-effective in the long run. Quality infrastructure investments are those that fully respect each country’s development plan and enhance regional connectivity. Quality infrastructure cooperation creates jobs for local people and involves the transfer of technology and skills. LAC’s deficiency in infrastructure has been identified as a major bottleneck for the region to close the gaps in productivity and competitiveness with other regions and thereby achieve sustainable development. Establishing and/or strengthening public and private partnerships (PPP) with Japanese counterparts can help countries of the region to fill these gaps.

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