Japan's Trade Balance and Income Balance

The trade policy of the Donald Trump administration in the United States has been causing bewilderment and confusion in many countries. For alleged national-security reasons, in March this year it drew up a policy of imposing high tariff rates on imports of steel and aluminum, at 25% and 10% respectively, announcing unilaterally that it would consider exemptions for countries that agree to engage in bilateral trade negotiations with the US. Also, taking aim at China, it declared that it would levy a 25% tariff on $50 billion-worth of imported goods from China in order to force a correction of the trade imbalance between the US and China. Japan is among the countries that are subject to the aforesaid high tariffs, but Japan's stance has been to give maximum priority to encouraging the US to rejoin the Trans-Pacific Partnership after having previously left it, its policy being to do its utmost to avoid negotiating a bilateral free-trade agreement of the kind desired by the US. The European Union has also been growing increasingly hostile toward US trade policy, taking a clear stance of adhering firmly to the principles of the free-trade system, while considering possible retaliatory tariffs and import restrictions. It appears that the sparks of flare-ups surrounding the US trade deficit are sputtering everywhere.

President Trump believes that the people who compose his political support base are missing out on sufficient job opportunities because other countries are employing unfair trade practices to steal markets both within the US and overseas. To him this is symbolized by the massive trade deficits that the US has been running year after year. Countering this, a view that is gaining traction in Japan is that since Japan is emerging from the stage of being a "trading nation" and is transforming itself into an "investment powerhouse," it should not be worrying itself about US trade policy but should be continuing to devote its efforts to direct foreign investment. Japan's overseas investment is indeed increasing from year to year, topping a thousand trillion yen last year, and the earnings of the overseas subsidiaries of Japanese companies reached a record high last year. It is also true that the surplus in Japan's primary income balance, which includes dividends, interest, and other gains from direct investment, currently accounts for most of the country's current-account surplus.

The time-series line graph in the figure shows Japan's trade balance and primary income balance. It can be observed that, in sharp contrast to a shifting of the trade balance deeply into deficit because of soaring crude oil and natural gas imports after the Great East Japan Earthquake in 2011, the primary income surplus has steadily been built up as Japan has stepped up direct investment overseas after experiencing trade frictions and a rise in the yen's value. As a result of the correction of the strong yen and the improvement in the energy situation, the trade balance has recently been moving into surplus, but nevertheless it remains at only around a quarter of the level of the surplus in the income balance. This indicates that the principal role of the current account balance is shifting to that of an income balance, and it is not surprising that the view is beginning to emerge that there is no need for excessive nervousness with regard to US trade policy.

Nevertheless, if we turn our attention to the bar graph in the figure, a somewhat different picture emerges. This shows not net balances but totals of exports and imports and totals of primary income balance credits and debits. Both of these have been recovering well since the global financial crisis of 2008, but the total of imports and exports has undergone more severe fluctuations than primary income balance credits and debits, and its future developments will naturally be an increasing focus of attention. Net balances are also important indicators, but from the perspective of the scale of economic activity and trade relationships between countries, both credits and debits are also important, and the most desirable state is surely that both of these expand in tandem with each other.

With regard to recent trends in US trade, exports and imports slumped as a result of the contraction of economic activity caused by the global financial crisis and the trade deficit narrowed, but since then imports have expanded as the economy has recovered, and the trade deficit has tended to widen. The president has concluded that this is not desirable, but apparently makes no mention of the total of exports and imports. The fact is that if we compare the total of exports and imports in 2009—in the immediate aftermath of the global financial crisis—and in 2017, whereas in Japan's case it has grown at an annual rate of 5.6%, in the case of the US the corresponding rate has been only slightly lower, at 5.0%. It would be a good thing if the president were also to take notice of this fact.

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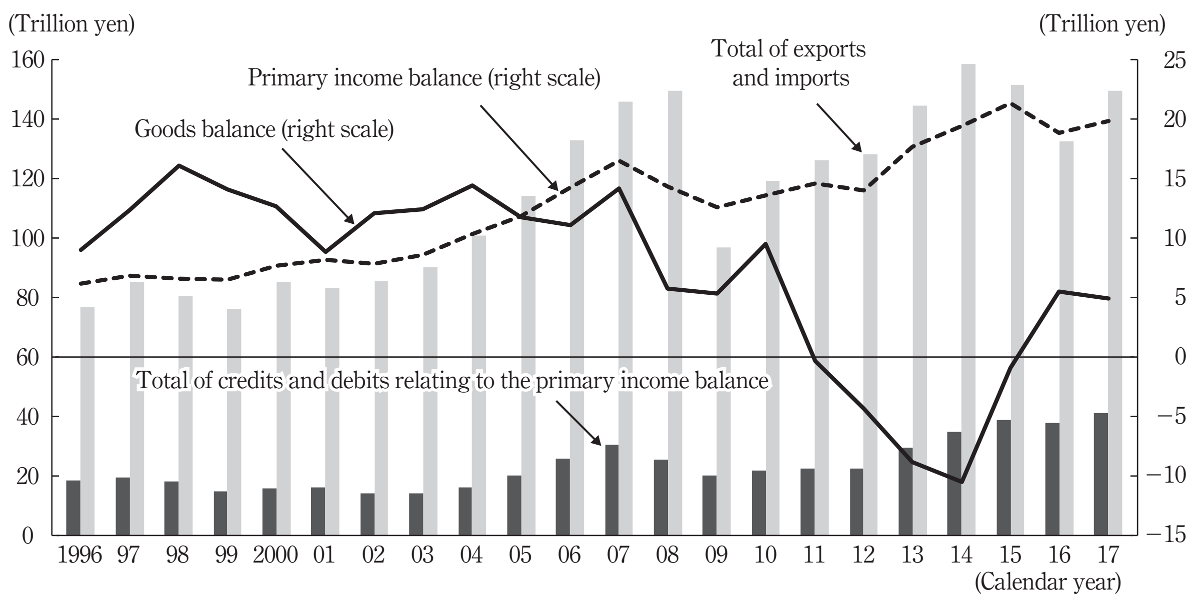

Notes: The trade balance is the balance of exports and imports of goods. The primary income balance is the balance of credits and debits of dividends, interest, etc., between parent and subsidiary companies (income from direct investment) and credits and debits of share dividends, bond interest (income from portfolio investment), etc.

Source: Ministry of Finance