

## **Is Japan Getting Connected? How the New Economy is Reshaping International Transportation and Communications**

Alan Larson  
Department of State

I'll focus today on two themes. The first is how information technology (IT) can spur domestic growth and promote international trade by reducing transaction and distribution costs. The second is how old-style procedures and practices that remain unchanged in Japan—despite the advent of the new economy—can substantially offset the benefits IT could bring. These practices keep costs high, hurting Japanese companies and consumers and acting as obstacles to international trade. In this discussion I'll focus on the US-Japan agenda, particularly in four main areas: telecommunications, aviation, ports practices, and customs.

### The U.S. Perspective

In the United States, we have been working hard to foster a domestic and international environment conducive to the development of the Internet and e-commerce. We've encouraged private sector leadership, leaving it to markets, rather than government, to make important decisions about investments and technologies.

We have worked to eliminate unnecessary regulations and other barriers to e-commerce and transportation. The Telecommunications Act of 1996, which removed the last vestiges of monopoly telephone service in the U.S. and expanded competition and market access more than in any other part of the world, is a prime example.

We have deregulated air services at home and pursued liberalized bilateral aviation agreements abroad to encourage freer access to aviation markets around the world. These policies have cleared the way for air service to new cities, creating jobs and economic value far beyond the direct benefit of the service.

Our policies to make the telecommunications and air services sectors more market-oriented and competitive have been vital to the success of the New Economy. Consumers enjoy greater choice and lower prices. Information Technology has increased productivity, generating high growth and low inflation.

While information technology still accounts directly for only 8 percent of total jobs in the U.S., it appears to have generated nearly one-third of recent U.S. real economic growth, and has reduced our inflation by about one-third, as well, according to Department of Commerce studies.

## Telecom

Such observers as Alan Greenspan have pointed to widespread, reliable and affordable access to information technology and the internet as a significant source of the growth of the U.S.' "New" Economy, and the surge in productivity in our "Old" Economy. And the cost of telecommunication services is what determines the "admission fees" for using the internet. We have found that the surest way to keep telecom charges low and innovation high is to ensure vigorous competition among telecom services providers. We do this in part through the FCC – the Federal Communications Commission – an independent agency which has a mandate to protect the interests of consumers and prevent carriers' exercise of monopoly power.

Unfortunately, Japan does not have an independent telecommunications authority to protect consumers' interests – the Ministry of Post and Telecommunications is charged with both regulating and promoting corporate growth in the telecom sector and is hesitant to undertake changes which will hurt the revenues of the major player, NTT. And the Government of Japan, as NTT's major shareholder, also has a disincentive to reduce NTT's profits or threaten the value of its shares.

There is a price for this: Japanese consumers and companies pay two to three times more than their U.C. counterparts for internet services – even more, if you consider that most U.S. customers are allowed unlimited local calls and thus unlimited internet usage for a low monthly fee. It's clear that competition works – in the telecom service sectors in Japan which face competition, like long-distance and mobile phones, prices have dropped significantly and many new products have been introduced.

These are among the points we have raised in the U.S. telecom negotiations with Japan. NTT, which controls access to about 95% of Japan's end-users, continues to charge competitive carriers interconnection fees (that is, access fees to link up with the NTT system) which also are two to three times more expensive than in other developed countries – even after the reductions which we negotiated in July. And NTT still jealously inhibits physical access to its facilities, such as switch stations, telephone poles and cable conduits, in order to slow down the advances of competitive carriers in the Japanese market. To make matters worse, the Ministry of Construction enforces highly-unusual rules limiting by season and time of day the digging of ditches and laying of pipes for telecom infrastructure.

Overall, the Japanese government is still trying to pick technological winners and "plan" its way toward the internet future. But the technology is changing too fast for government planners to keep up with. For instance, well-intentioned Government planners have focused their development on ISDN standards and trying to get fiber-optic cable to each Japanese home. Markets, however, have jumped over ISDN and are moving rapidly toward DSL, cable modems and fixed wireless access, which don't require huge new wiring projects – unlike fiber to the home. There are now four million DSL lines in the U.S. – there are four thousand in Japan.

Japan, as a developed trading economy with a wealthy, well-educated workforce, is ideally poised to be a major player in e-commerce and the growing synergy between information technology, telecom/internet services and transportation. But Japan continues to lag behind the other developed nations in most measures of e-commerce readiness, and economic growth remains virtually flat, in part because of its failure to take full advantage of the productivity gains which are possible through a vibrant and competitive telecom environment.

This is doubly the pity because the Japanese government is right now running up the second highest level of government debt in the G-7, in an attempt to spur economic growth through old fashioned pork-barrel infrastructure projects of sometimes dubious value. At the same time, U.S., Japanese and European competitor carriers have told the U.S Embassy in Tokyo that they have not been able to spend hundreds of million of dollars they've budgeted to build telecom infrastructure in Japan, because o the regulatory obstacles I mentioned above.

We have found that governments alone simply cannot afford the enormous telecommunications infrastructure necessary to drive the information economy. But, if governments can create an environment that spurs competition and investment, the private sector will take care of much of the work.

### *Civil Aviation*

Nowhere has the marriage of the internet and transportation been more marked than in air cargo transport.

About 40% of the value of exports form the U.S. now moves via air cargo. In fact, some recent studies show that the air cargo industry is now expanding at a faster rate than are air passenger services. The information age has played an important role in that expansion. Online commerce demands efficient, global cargo networks – land, sea and air- that can deliver purchased goods quickly and at reasonable costs. And in the global information economy, many cargo carriers are going beyond just delivery of goods – they now provide online tracking services that allow customers to locate shipped goods anywhere in the cargo network.

Cargo has not been the only area in aviation that has benefited from the e-commerce boom. We also have seen a considerable impact on the passenger market.

In Europe, travel is *the* largest source of online retail revenue. One European regional carrier, EasyJet, estimates that 80% of its ticket purchasing is generated on-line.

Here in the U.S., web-based travel resources are expected to grow form what was a \$5 billion industry in 1998, to a \$30 billion industry by the end of 2001. Southwest Airlines has topped \$1 billion this year in online sales alone. The industry sold two to four percent of its tickets over the internet last year and there are estimates that that percentage will grow to 45 percent by 2004.

But in air cargo and passenger services, Ministry of Transport policies that constrain capacity and limit competition keep Japan a very high-cost place to do business. Landing fees at Narita, Haneda and Kansai are about five times higher than those at major U.S. international airports such as JFK and LAX. And landing and take-off slots at Tokyo's only international airport, Narita, are so tight that U.S. carriers can't even fly the flights they are allowed under our 1998 agreement.

These high costs and access limitations make Japanese airports less competitive as hubs vis-à-vis other airports in the region. It's in Japan's own interest to bring down costs and open up opportunities for the markets – not the government – to decide who the winners and losers should be.

We have been working with Japan and many other countries to eliminate barriers to cargo as well as passenger air services. Since 1992, we have negotiated 51 bilateral Open Skies air transport agreements around the world. These agreements promote the growth of international aviation by removing all restrictions on the frequency, capacity and pricing of passenger and cargo services. Most recently, at the APEC Leaders Meeting last month in Brunei, the United States and four of its APEC partners – Singapore, New Zealand, Chile and Brunei – announced agreement in principle on a Multilateral Open Skies Agreement. This agreement, which will be open for all countries to join, is an important step towards making Open Skies principles the accepted international standard in commercial aviation relations.

We recognize that not all countries may be ready to accept Open Skies at the same pace. Where a country is not prepared to allow Open Skies for passenger services, we will consider an Open Skies agreement limited to cargo services, such as the one that we negotiated last year with Australia. In some cases, we have concluded agreements that substantially liberalize bilateral air transportation, but fall short of full liberalization under Open Skies. Our 1998 agreement with Japan is a good example of such an accord.

Fundamentally, the U.S. wants to work to achieve Open Skies with all our bilateral aviation partners. As foreseen in our 1998 agreement, the United States and Japan last month resumed discussions on the further liberalization of our bilateral aviation relations. One important issue we will need to address regards the inability of our carriers to fully use the rights gained under the 1998 agreement due to slot constraints at Narita Airport. We are hopeful that the construction of a second runway at Narita offers an opportunity for our carriers to expand their access to levels foreseen under the 1998 agreement.

In these discussions, we will be looking for ways to expand our bilateral air transport agreement by phasing in Open Skies principles. Priority areas we will need to address include erasing the distinction under the current agreement between incumbent and non-incumbent carriers, removing severe route, frequency, and designation limits on non-incumbent all-cargo operators, liberalizing pricing restrictions, eliminating charter

quotas, removing restrictions on same-country code-sharing and improving conditions for service from Guam and Saipan to Japan.

We will also be urging our Japanese counterparts to consider adding provisions to our agreement that would encourage the development of integrated passenger intermodal services, similar to those we agreed to last month with Germany and France under our Open Skies bilateral agreements with those countries.

We urge Japan to join us in constructing an Open Skies environment that will benefit airlines, consumers, tourism, trade, investment and local communities in both countries.

### **Ports**

E-commerce ultimately translates into the flow of products and services, and a key part of international transportation is ocean shipping. Last year, Maritime Administrator Clyde Hart and I warned that antiquated and inefficient administration of the Japanese port system is fostering excessive costs that hinder Japan's foreign trade and work against the very port workers the rules are intended to protect. Shipping companies have bypassed Japan for lower-cost ports in neighboring countries.

Since then, Japan has begun to enact some reforms to its port Transportation Business Law. While an important first step, much remains to be done. Many of the burdensome rules for licensing and operating a port terminal are still in place. Not only does the law still set a minimum number of port workers that each stevedore company must employ, but the minimum level has been increased by fifty percent. In addition, carriers must still go through an arbitrary prior consultation procedure with the stevedore association to negotiate any significant changes in services. Labor unions have threatened to shut down any U.S. carrier that applies for a stevedoring license but the Japanese Government refuses to commit itself in advance to take any action against an illegal work action.

Experience in the United States and other countries shows that a competitive port service market yields more efficient services for shipping companies and creates new jobs for port workers. Japan needs to move forward with further port reform to establish the level of services that a great trading country like Japan and its trading partners need.

### **Customs Modernization**

As use of IT cuts transaction time and costs of international trade, other bottlenecks become increasingly apparent – and customs is a prime example.

You can't have just-in-time logistics without release-on-arrival customs.

Japan is an export powerhouse, efficient at sending products out of the country, Japan's challenge – especially with its huge trade surpluses with the U.S., the EU, and its

Asian neighbors – is to process imports into Japan as efficiently as Japan processes its exports.

To see whether Japan is meeting that challenge, it's useful to look at Japanese customs clearance procedures, and at how Japan is making use of IT to make its operations more efficient.

Foreign firms have long maintained that Japanese customs procedures have substantially inflated the costs of foreign goods in Japan.

The Japanese Government has addressed a number of the important problems raised by foreign exporters. For example, many importers are now able to clear air shipments as soon as the plane carrying cargo touches down. Japan allows certain importers to pay import taxes and duties after goods have been cleared. And bonded warehouses are now allowed outside of Narita airport, which has reduced costs somewhat through increased competition.

But in two important ways, Japanese policies give significantly less favorable treatment to imports than does the U.S.

The first is customs valuation. Whereas the U.S. calculates duty on an FOB basis, Japan uses the higher CIF valuation. That calculation is good for the Japanese Finance Ministry, in terms of tax revenue, but makes all imports in Japan more expensive.

The second is Japan's '*de minimis*' standard. The U.S. allows shipments valued under \$200 to enter duty free. For Japan, the ceiling is only 10,000 yen, about one hundred dollars. In this case, there may be little or no real gain to the Japanese Treasury, because the amount of duty collected on a single low-value shipment is so small that in many cases the cost of collecting the tax can exceed the value of the tax itself. And if Japan simply released these low-value shipments with our further processing, except as needed for law enforcement purposes, it could use those customs resources to cut release times for the balance of imports into Japan.

Today's theme is IT and international trade, and the degree to which IT is used to import procedures in Japan is addressed in a very interesting study by JETRO, the Japan External Trade Organization, issued in June 1999. In JETRO's survey of developed countries of the time between the arrival and removal of ocean-going freight, Japan clocked in at 29 hours, three or four times longer than any other country. The U.S. was 8 hours, by comparison.

JETRO said the longer time was the result of slow progress in introducing information technology. When JETRO did its report, it found that information systems linking port and harbor freight businesses, shipping companies, and banks were not linked to the Sea NACCS (pronounced: 'naks'), or Nippon Automated Cargo Clearance System. After the JETRO report was issued, Japan upgraded its Sea NACCS system. The U.S. Government welcomed that modernization, and we are very interested in the

Japanese Government's assessment of how increased use of IT has increased the efficiency of its customs processing system.

Using IT saves time and money, but it is not free, and when a government introduces a new system such as NACCS, it can expect questions on how the costs are parceled out. The Air NACCS system has generated significant efficiencies in clearing air cargo, and the system continues to improve. As Japan seeks to recover the costs, it's important that those affected – including the foreign firms using the system – participate in the process that leads to fee-setting. We hope the public corporation operating NACCS will publicize its proposals, invite comments, publish those comments, and explain how it responds to the comments it receives.

We hope the Ministry of Finance, which has the ultimate authority in determining new NACCS' fees, will also encourage public comment and take these into consideration when making its determination.

In its laudable efforts to adapt IT to the needs of its customers, NACCS has developed its own software to interface with users of the system. At the moment it is possible to use only the NACCS developed software. This will be quite expensive. In the spirit of promoting a more competitive and therefore less costly environment, we hope NACCS will give its users the information they need to develop their own software for this purpose, if they wish to do so. Or perhaps NACCS could move to a universal, web-based application.

### **Opportunities for Japan**

I believe inexpensive and interlinked telecommunication and transportation services will very effectively help Japan increase employment, stimulate personal consumption and revitalize now-struggling small- and medium-size enterprises. They will also help tie Japan's rural marketplace to the global marketplace, bringing growth to areas like Kyushu, Hokkaido, and Okinawa. Small companies could market to the world, and Japanese young people would not need to leave their hometown to find exciting modern jobs and a convenient lifestyle.

In the U.S. in the last decade, it has become less and less important where you are, whether as a consumer or a company. Companies have thrived in the U.S. in rural areas where land and labor is cheap, and young professionals are willingly choosing to relocate to inexpensive, smaller towns where the quality of life is high.

Some examples: **Gateway Computer Company**, which has many outlets in Japan, was founded in 1985 in a farmhouse in Iowa and soon moved to North Sioux City, South Dakota. Now it is a US\$8.6 billion company with 20,000 employees – 12,000 of which are in South Dakota. **Land's End** – which has an operation in Japan – is headquartered in Dodgeville, Wisconsin and 90% of their 8,800 employees live in Wisconsin. The Native-American **Navajo Nation** is located in a remote and rural part of Arizona and New Mexico. Through internet marketing they are expanding their market

for traditional products and arts, allowing their members who choose to live a traditional lifestyle to remain in their homeland while still reaping the benefits of marketing to the world.

The same could happen in Japan.

### **Best Practices for Today**

Increased transaction and distribution efficiency in Japan is good for Japanese businesses and consumers and good for Japan's trading partners. But reaping the benefits of these efficiencies will be difficult so long as the economy remains burdened by old-style regulations and practices.

I'll close by reviewing the U.S. agenda with Japan – much of which is drawn from suggestions by Japanese companies, academics, and government officials on what Japan needs to do to remain globally competitive.

1. Japan should make it cheaper to use telecommunications and the internet by increasing competition and more tightly regulating the traditional monopolist – NTT.
2. Don't try to pick winners or to direct investment flows – let the markets figure it out.
3. Liberalize civil aviation, including Open Skies.
4. Cut airport construction and operating costs, and increase capacities.
5. Put a halt to excessively restrictive labor and licensing regulations governing ports, which protect small numbers of Japanese workers in the short-term, while slowly strangling port usage over the longer-term.
6. Increase IT use in customs processing, and increase efficiencies and fairness by changing valuation methods and increasing de minimus levels.

Thank you very much.