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The 2006 Increase in U.S. Motor Vehicle Imports from Japan

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Abstract. Imports of motor vehicles (automobiles and light trucks) from Japan increased by one-third in volume from 2005 to 2006, rising to more than two million units, the highest yearly total since 1989. Some Members of Congress have expressed concern that the export of cars from Japan to the U.S. market has been assisted by a policy of the Japanese government to reduce the exchange rate of the yen. This could give producers based in Japan a trade advantage when they export vehicles to the U.S. market, in competition against those made in the United States. Alternative factors that may also explain the 2006 import increase are rising sales of imported subcompact vehicles, which are not built in the United States by any manufacturer, and a shortage of U.S. manufacturing capacity by two leading Japanese-owned automotive manufacturers. Toyota and Honda are now rapidly expanding their North American production, a development that may reduce net imports, but could further increase the competitive pressure on the Detroit-based "Big Three" manufacturers.





# The 2006 Increase in U.S. Motor Vehicle Imports from Japan

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#### **Summary**

Imports of motor vehicles (automobiles and light trucks) from Japan increased by one-third in volume from 2005 to 2006, rising to more than two million units, the highest yearly total since 1989. Some Members of Congress have expressed concern that the export of cars from Japan to the U.S. market has been assisted by a policy of the Japanese government to reduce the exchange rate of the yen. This could give producers based in Japan a trade advantage when they export vehicles to the U.S. market, in competition against those made in the United States. Alternative factors that may also explain the 2006 import increase are rising sales of imported subcompact vehicles, which are not built in the United States by any manufacturer, and a shortage of U.S. manufacturing capacity by two leading Japanese-owned automotive manufacturers. Toyota and Honda are now rapidly expanding their North American production, a development that may reduce net imports, but could further increase the competitive pressure on the Detroit-based "Big Three" manufacturers.

#### **Automotive Imports from Japan Rebound in 2006**

No trade issue in the last generation has likely been more sensitive than that of U.S. automotive imports from Japan. But even though the products of Japanese-based companies have continuously gained share in the U.S. domestic market, imports declined to a lower level in the 1990s. A renewed surge of Japanese imports occurred in 2006, as distinct from vehicles produced and assembled in North America by Japanese nameplate manufacturers. This contributed to a renewal of concerns in Congress about the competitiveness of the U.S.-based "Big Three" motor vehicle manufacturers, all of which have been suffering serious financial losses.

With the investment of automotive assembly plants in North America by Japan's major motor vehicle manufacturing companies, the level of imports from Japan declined substantially in the 1990s. From a peak of 3.6 million imported cars and trucks in 1986, the total fell to just over 1.25 million – more than two million fewer units – ten years later (see **Figure 1**). Thereafter, as Japanese companies continued to gain market share with a wider range of products in the U.S. market, imports from Japan began to increase again,

albeit marginally. According to Commerce Department data, imports from Japan averaged a little over 1.5 million units per year in 1996-2000, and close to 1.7 million units during the next five year period, 2001-05. But even though the number of units rose, Japan's share of U.S. imports from countries other than Canada and Mexico continued to decline. From a level as high as 93% in the early 1980s, Japan's share of such imports fell through the early 2000s, to less than 50% in 2003-05. In 2006, by contrast, Commerce data show that imports from Japan jumped by 35% in one year to about 2.2 million vehicles, and Japan's share of imports from outside the North American Free Trade Area (NAFTA) increased in that single year from 49% to 57% (**Figure 1**).

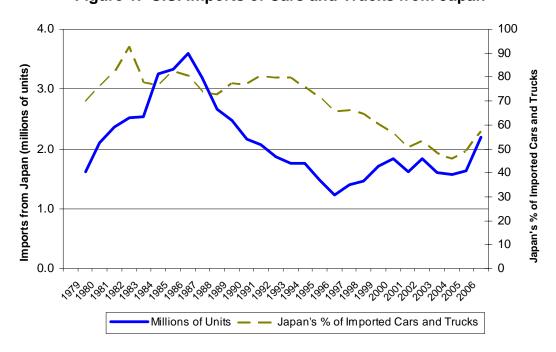


Figure 1. U.S. Imports of Cars and Trucks from Japan

Note: Excludes vehicles imported from Canada and Mexico.

**Sources:** (1979-1995) Motor Vehicle Mfrs. Assn./American Automobile Mfrs. Assn. *Motor Vehicle Facts & Figures*; (1996-2006) U.S. Dept. of Commerce Intl. Trade Adm., Office of Aerospace and Automotive Industries.

## Assertions That the Japanese Import Increase Is Linked to Undervalued Yen

The Automotive Trade Policy Council (ATPC), an organization supported by the Detroit-based Big Three (General Motors, Ford Motor Company, and the Chrysler Group of DaimlerChrysler), has consistently maintained that the Japanese currency, the yen, has been undervalued as an act of government policy to boost exports. Japan has carried out this policy, according to ATPC's analysis, by massive currency market intervention in 2000-04, by informal "guidance" to influence foreign currency markets since then, and

by a policy of exceptionally low interest rates.<sup>1</sup> The president of the United Auto Workers union, Ron Gettelfinger, estimates that, "The artificially low value of the Japanese yen against the dollar puts U.S.-made cars and trucks at disadvantage of between \$2,000 and \$9,000 per vehicle before a single sheet of metal is stamped or a single part is installed on a vehicle chassis."<sup>2</sup>

The allegedly undervalued yen exchange rate has been explicitly linked to the sharp increase in 2006 motor vehicle imports from Japan.<sup>3</sup> Four House committee and subcommittee chairs with jurisdiction over trade, commerce and financial policies on February 8, 2007, wrote Secretary of the Treasury Henry Paulson and noted that "from 2005 to 2006, imports of Japanese cars and trucks rose by more than 30 percent ... We are certain that the weak yen is also boosting Japanese exports in other economic sectors and is having a significant impact on many U.S. producers." They urged that he "press" the Japanese government to reverse the policy of maintaining a weak yen by raising interest rates and selling some of the massive reserves of dollars and euros Japan has accumulated through its market interventions.<sup>5</sup>

The yen has weakened since it reached a high point against the U.S. dollar in late 2004 and early 2005. At that time, the U.S. dollar only bought about about 103-104 yen. For the whole of 2004, the average value of the dollar was 108 yen, compared to almost 116 yen in 2003 and 125 yen in 2002 ( Japan's last major official intervention was early in 2004). The dollar strengthened to 110 yen in 2005, and about another 5% to 116 yen in 2006, for about an 11.5% overall gain above the post- 2000 low. In January-February 2007, the dollar did rise to more than 120 yen, but though this rise may affect the policy debate today, it could not have influenced 2006 trade results.<sup>6</sup> A rising dollar at these levels would have an immediate windfall effect on Japanese companies' profits, because U.S. dollar sales translate into relatively more yen. But the effect on longer-term product sourcing and planning may take longer to play out. There may have been more immediate causes of the short-term rise in Japanese imported vehicle sales in 2006 than the rise in the value of the yen. These notably may include capacity constraints on Japanese companies in North America and shifts in consumer demand in 2006.

<sup>&</sup>lt;sup>1</sup> ATPC. *The Economic Impact of Japanese Currency Manipulation* (Sept. 2006). The position of the U.S.-based automotive industry and this issue in general is discussed in CRS Report RL33178, *Japan's Currency Intervention: Policy Issues*, by Dick K. Nanto, especially p. 5. William Cline of the Peterson Institute for International Economics calculated in 2005 that a "reference rate" for the yen compatible with a "sustainable" level of the U.S. trade deficit would be 82, as opposed to recent rates of 120¥/US\$1.00. His colleague John Williamson has said that the excuse that Japan cannot afford adjustment because of weak domestic growth, "no longer looks compelling." See the latter's *Reference Rates and the International Monetary System* (Washington: Peterson Institute, 2007), pp. 48-49.

<sup>&</sup>lt;sup>2</sup> Ron Gettelfinger, "Speculation Won't Solve Pressing Auto Ills," *Detroit News* (Mar. 2, 2007).

<sup>&</sup>lt;sup>3</sup> James B. Treece, "Japanese Exports to U.S. Soar" Automotive News (Feb. 5, 2007).

<sup>&</sup>lt;sup>4</sup> Letter from Reps. Charles B. Rangel, John D. Dingell, Barney Frank and Sander Levin to Secretary of Treasury Paulson (Feb. 8, 2007).

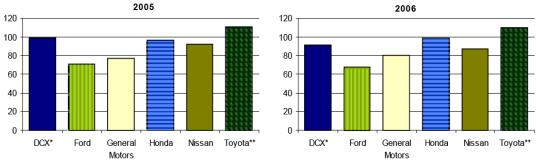
<sup>&</sup>lt;sup>5</sup> Ibid.

<sup>&</sup>lt;sup>6</sup> Exchange rate data from Federal Reserve Statistical series G.5 and G.5A.

#### **Capacity Constraints Affect Japanese Sourcing Decisions**

As will be shown later in detail, Toyota and Honda together accounted for virtually all of the net increase in U.S. motor vehicle imports from Japan. **Figure 2** illustrates that in 2005-06, these two companies were operating at or above their full North American manufacturing capacity. Toyota, which alone accounted for three-quarters of the net increase of more than 400,000 imports, operated at about 110% capacity in both 2005-06. During this period, the company opened a new truck plant in Texas (whose initial production runs began in late 2006, data not included in the figure), is building a second plant in Woodstock, Ontario and in early 2007 announced a new plant to be built in Tupelo, Mississippi. It has also bought Isuzu's half of a joint-venture plant in Indiana with Fuji Heavy Industries. Honda ran at 96% capacity in 2005, and 99% in 2006. As in the case of Toyota, they were stretched too thin in North America to immediately meet rising demand for certain products. Honda has announced a new assembly plant to be built in Greensburg, Indiana, after having opened and expanded a new plant in Alabama since 2001.

Figure 2. North American Automotive Assembly Capacity Utilization



<sup>\*</sup>excludes Mercedes Benz

Note: Based on "straight-time capacity" (two 8-hr. shifts/da., 235 da./yr.)

**Source:** Global Insight, *North American Light Vehicle Industry Forecast Report* (Nov. 2006), pp. A47-A50 for 2005 data; Jan. 2007, pp. A52-54 for 2006.

The third-largest Japanese motor vehicle company operating in the United States, and the only other one with more than a million units in annual sales, is Nissan. But Nissan's sales declined by 5% in 2006, and its capacity utilization fell from 92% to 87%. The company's imports from Japan also declined by 11% (see **Table 1** and **Figure 2**).

By comparison with Toyota and Honda, the two largest U.S.-based manufacturers, Ford and General Motors (GM), have experienced sales declines in some product lines, financial losses in 2005-06, much lower capacity utilization rates, and a need to close permanently some of their assembly plants. **Figure 2** illustrates that Ford operated at about 70% of capacity for the past two years. GM's rate actually increased slightly from 77% to 80% in 2006, but this was mainly due to a closure of plants with about 400,000 units of capacity, according to the source for the figure. The Chrysler Group's capacity utilization fell from 99% to 91%, but this was not enough to forestall a large inventory build-up of some vehicles, and the need to announce major production cutbacks and closures in early 2007.

<sup>\*\*</sup>excludes new San Antonio truck plant, incl. NUMMI joint venture, Fremont, CA.

#### **Japanese Firms Meet Shifting Consumer Demand with Imports**

**Table 1** shows that the net increase in 2006 imports from Japan was mostly due to strong U.S. demand for higher fuel economy models that could not be delivered by Japanese companies from their North American plants. This is especially true of Toyota:

- An increase of 81,000 imports of the RAV4, a "crossover" utility vehicle (CUV), that is Toyota's smallest vehicle of this type;
- 70,000 imported units of the subcompact Yaris, in its first year on the U.S. market;
- An increase of 42,000 imported units of the Corolla, Toyota's basic compact sedan, to supplement production in California;
- An increase of 17,000 imported units of Toyota's Scion brand, its entrylevel model.

Among Toyota's larger vehicles, only two saw a large gain in imports. One was the mid-size Camry sedan, of which about half of the net increase was the hybrid model that was then only made in Japan. However, the iconic Prius hybrid model, all of which are imported, by comparison showed no gain in sales at all. Also, Toyota introduced the FJCruiser, an imported SUV-type niche product that sold 56,000 units in its first year. All of Toyota's other mid-size and larger vehicles, including the Lexus brand, saw much smaller increases, or declines, in sales whether they were imported or produced in North America. Toyota plans to continue its stated strategy of increased North American sourcing. Besides the highly publicized new Tundra pickup truck now being built in Texas, Toyota will also bring the RAV4 to its new plant in Woodstock, Ontario. The Highlander SUV, currently imported, will be built at a new plant announced for Mississippi.

Imports of Honda vehicles from Japan increased by 70,000, mostly because of the introduction of the subcompact Fit (28,000 units) and the increased sales of the CR-V CUV (39,000 increased imports). Honda has begun to produce this vehicle in Ohio. As a Honda official stated, "Maintaining some level of imports gives Honda flexibility to adjust to changing economic conditions in the United States, while assuring a sustainable level of local [U.S.] employment." Smaller, but significant, import gains were also registered by Ford's Japanese affiliate, Mazda (27,000), and by Suzuki (19,000). The latter is Japan's fourth-largest motor company and a specialist in subcompact vehicles.

In summary, subcompacts are likely to be imported in the U.S. market from countries where they are sold in larger volumes. For example, GM's subcompact Chevrolet Aveo is imported from Korea, and Chrysler has negotiated a deal with Chery, a Chinese company, to produce a subcompact for North America. Otherwise, the Japanese companies' strategies would still appear to be to increase production in North America, while adding imports to supplement sales or to try out new products from Japan, where there is excess capacity, because the market there has been stagnating since the 1990s.

<sup>&</sup>lt;sup>7</sup> Letter of Edward B. Cohen, *Automotive News* (Feb. 19, 2007).

**Table 1. 2006 Changes in Japanese Motor Vehicle Imports** 

CRS-6

| Note: "Imports" not incl. vehicles from Canada or Mexico. | U.S. Sales (000s) |       |      |     | Imports (000s) |       |      |     |
|---|-------------------|-------|------|-----|----------------|-------|------|-----|
|   | 2005              | 2006  | Chg. | %   | 2005           | 2006  | Chg. | %   |
| TOYOTA -Tot.  | 2,260             | 2,543 | 283  | 13  | 861            | 1,180 | 319  | 37  |
| - Scion   | 156               | 173   | 17   | 11  | 156            | 173   | 17   | 11  |
| – Yaris   | 0                 | 70    | 70   | new | 0              | 70    | 70   | new |
| – Corolla   | 232               | 272   | 40   | 17  | 10             | 52    | 42   | 420 |
| – Camry*  | 432               | 448   | 16   | 4   | 29             | 85    | 56   | 193 |
| – FJCruiser   | 0                 | 56    | 56   | new | 0              | 56    | 56   | new |
| - RAV4  | 71                | 152   | 81   | 114 | 71             | 152   | 81   | 114 |
| – Lexus   | 303               | 322   | 19   | 6   | 235            | 246   | 11   | 5   |
| – Prius   | 108               | 107   | -1   | -1  | 108            | 107   | -1   | -1  |
| – Avalon  | 95                | 89    | -6   | -6  |                |       |      |     |
| – 4Runner   | 104               | 103   | -1   | -1  | 104            | 103   | -1   | -1  |
| – Highlander  | 137               | 130   | -7   | -5  | 137            | 130   | -7   | -5  |
| N.Ammade<br>SUVs, Trucks                                  | 503               | 500   | -3   | -1  |                |       |      |     |
| HONDA-Tot.**  | 1,462             | 1,509 | 47   | 3   | 234            | 304   | 70   | 30  |
| – Fit   | 0                 | 28    | 28   | new | 0              | 28    | 28   | new |
| - Accord*   | 369               | 354   | -15  | -4  | 19             | 32    | 13   | 68  |
| - Civic*  | 308               | 316   | 8    | 3   | 45             | 43    | -2   | -4  |
| - CR-V**  | 150               | 170   | 20   | 13  | 88             | 127   | 39   | 44  |
| – Acura   | 210               | 201   | -9   | -4  | 74             | 67    | -7   | -9  |
| NISSAN  | 1,077             | 1,019 | -58  | -5  | 225            | 214   | -11  | -5  |
| MAZDA   | 258               | 269   | 11   | 4   | 144            | 171   | 27   | 19  |
| SUBARU  | 196               | 201   | 5    | 3   | 87             | 92    | 5    | 6   |
| MITSUBISHI  | 124               | 119   | -5   | -4  | 43             | 36    | -7   | -16 |
| SUZUKI  | 82                | 101   | 19   | 23  | 82             | 101   | 19   | 23  |
| JAPAN -<br>TOTAL**  | 5,472             | 5,769 | 297  | 5   | 1,626          | 2,049 | 423  | 26  |

<sup>\*</sup>Imports include all hybrid types of this model.
\*\*Honda excluding CR-V imports from UK.

Source: Automotive News, (Jan. 8, 2007).