

Trip Report for 1999 Industry-to-Industry Meetings in Japan

U.S. Delegation Participants:

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Overview:

AF&PA organizes and coordinates an annual industry-to-industry mission to Japan. The purpose of the mission is to have high-level meetings between representatives of the U.S. wood products industry, customer groups in Japan and the Japanese Government on the wood products market in Japan, including technical and trade policy issues.

This year the meetings were held in Tokyo, Japan on October 21-22. The full agenda for the mission is attached. The following is a summary of each of the meetings.

1. U.S. Embassy Briefing October 21, 1999 -- 9:30 - 10:30 a.m.

The comprehensive U.S. Embassy briefing focused on the economic outlook, political situation, opportunities for U.S. investment and business in Japan and the trade policy issues between Japan and the U.S.

The Japanese economy is in a fragile recovery with GDP growth up 2% in the first quarter and 0.2% in the second quarter. The U.S. Government estimates Japan's annual GDP growth for 1999 at 0.7%. In addition, housing starts are up. The Embassy noted that positive GDP growth most likely can be attributed to massive fiscal spending by the Japanese Government and that it is questionable whether real economic activity and growth would be taking place in the absence of the government stimulus package.

Prime Minister Obuchi is currently very popular with a 50% approval rating. Of particular note for our industry is the continuing trend toward housing deregulation. Embassy officials noted that while the Japanese Ministry of Construction was discussing regulatory changes in the housing sector at the central level, the effectiveness of these changes was not clear at the local level.

The U.S. and Japan share some general goals in the upcoming WTO Round. Both want a 3 year round; a balanced and broad agenda; progress on e-commerce; and a realistic scope for discussion. The major differences are agriculture, forest & fisheries products, anti-dumping and early harvest. The minor differences center on the investment negotiations, which the U.S. believes will not be successfully achieved in

the WTO and should be worked on in a different fora.

The Embassy's State Department representative, Larry Greenwood, is also responsible for working on USTR issues in Japan. Mr. Greenwood noted that within the Japanese bureaucracy, the EVSL/ATL is known as the "APEC trauma" or "APEC scar". Given that the Japanese never actually made any tariff offers in APEC on forest products and fish, they don't feel as though they are backing out of a commitment or being obstructionist. In addition, the other 6 sectors in the ATL hold little interest for Japan and there is not much they want out of the full round itself.

The political reality in Japan is that the power of the Keidanren (NAM-like business interests) pales in comparison to the power of the agriculture sector. Companies in Japan are negatively impacted on a daily basis by the high cost of agriculture subsidies and protectionism and can do nothing about it politically.

**2. Ministry of Construction (MOC) - General Housing Bureau
October 21, 1999 - 11:00 a.m. - 12:00 p.m.**

The meeting focused on technical issues surrounding revision to the Japanese Building Standards Law (BSL) and the implementation of performance-based standards; updates on the type approval processes and the new Housing Quality Assurance Law.

MOC continues to move toward implementation of the BSL with a deadline of June 2000 and will discuss its implementation plan in more detail at the November 1999 meeting of the Building Experts Committee (BEC). The U.S. industry is sending a delegation of 16 technical experts to participate in this meeting.

MOC indicated that they are working hard to identify the most critical sections of the new BSL for our industry and will make those sections available first to the U.S. and Canadian representatives for translation and review.

MOC reviewed the private inspection process put in place in May 1999, noting that several companies have been given approval to conduct these inspections. The criterion for the inspections is quite broad and MOC feels that this will lead to a strengthening of the Japanese housing stock.

Product approval processes under the new BSL will only be necessary for products used in new construction or remodeling efforts. There will be two types of approval processes: 1) Standard BSL Performance Approvals - which will be given by MOC-approved evaluation bodies; 2) Type Approval - for specific building type or project not specifically outlined in the BSL.

The evaluation body approval process has not even been discussed yet within MOC but is expected to be similar to that of the inspection bodies. An important change is that the Article 38 type-approvals will expire after 2 years and products will require recertification.

The Housing Quality Assurance Law passed the Diet in June 1998 and must be implemented by June 2000. This law is intended to promote higher quality housing construction in Japan. Some of the primary elements of the law and related regulations include the imposition of a 10-year warranty covering the fundamental structural elements of houses. Preparations are underway for a Japanese Housing Quality Standard - which would cover all parts of the house. Evaluation methods will be included in this new standard. While not directly connected with this law, the MOC has announced that Japanese builders will soon be required to provide a 10-year warranty. When questioned about the liability of U.S. suppliers under this system, the MOC noted that finding a way to determine fault and to limit liabilities was a difficult question that was under consideration. The Japanese legal system is not equipped to handle complaints and the majority of builders in Japan are very small -- so small in fact, that one major claim could certainly lead to bankruptcies.

Japanese builders may use more kiln-dried lumber in housing construction as a result of the housing assurance program. Japan's domestic wood products industry does not have adequate kiln capacity or capital to make improvements in the near future. Green lumber's tendency to buckle and warp will impact the builder's responsibilities under the new warranty system, particularly as the growing use of pre-cutters for the post & beam sector has cut down on the construction time significantly. The traditional 6 month housing construction time gave builders more opportunity to adjust or fix structural problems that developed as green lumber dried. Since the construction time has been dramatically cut, structural problems are occurring later in the process, often after builder has left the home to the buyers. Using kiln-dried products may reduce the likelihood of consumer complaints.

**3. Zenmokuren - All Japan Federation of Lumber Industries
October 21, 1999 - 1:15 p.m. - 2:15 p.m.**

The Zenmokuren, is the umbrella organization for the solid sawn forest products industry in Japan - both growers and processors. They have traditionally taken the opportunity of this meeting to explain the stance of the beleaguered Japanese industry on tariff and trade liberalization resistance.

Mr. Wako, the Executive Director of Zenmokuren noted that the Japanese industry was particularly concerned with "healthy house" issues in Japan and the need to work with the U.S. industry to expand the use of wood consumption in Japan. He shared data with the U.S. industry, showing a drop in the number of Japanese sawmills from 15,386 in 1993 to 13,496 in 1997 and a decline in plywood mills from 517 in 1993 to 420 in 1997. He also noted that 1998 saw the lowest number of housing starts in Japan in the past 15 years.

Zenmokuren is urging the Japanese government to accelerate their housing deregulation initiatives. They would like to see at least 1.3 million starts per year. They are concerned about the MOC's BSL revision and the Quality Assurance law and will be reviewing both very carefully.

He clarified the Japanese industry position on the ATL in the following way:

- Japanese industry will maintain its environmental and sustainable management concerns;
- Regard for the use of the natural resources such as the domestic forests, are critical.
- Log export bans and their impacts on domestic forest products industries continue to be a concern.
- Japanese forest products industry is suffering from lack of forest management.
- The standing timber has lost much value since the forests have been basically abandoned in favor of imported products.
- Japanese industry cannot fix the forest resource problems themselves.

When asked how many people would face losing their jobs if there was tariff liberalization in the forest products sector, Mr. Wako noted that number was "too scary" to contemplate. He suggested that we ask the Ministry of Agriculture Forestry and Fisheries (MAFF) when we met with them on October 22nd.

**4. Japan Lumber Importers Association
October 21, 1999 - 2:30 p.m. - 5:30 p.m.**

The annual meeting with the Japan Lumber Importers Association (JLIA) is the centerpiece of the U.S. mission agenda and allows for frank and open discussion about the current and future wood market in Japan including discussion of U.S. supply capability, Japanese demand and changes to the Japanese housing industry.

JLIA Chairman Tanaka presented a forecast for slow but positive growth over the next year and with yen appreciation, he noted a lessening of the financial and unemployment worries that were the main topic of discussion at last year's meeting.

Russian log imports have risen dramatically over the past year - increasing 29.4%, with Russia now seen as a good raw material supplier to Japan. 80% of the Russian larch logs were used in the production of Japanese plywood.

Solid sawn timber imports increased 9% from North America (over 1998 year-to-date figures) and 69% from European. Mr. Tanaka noted that European kiln-dried products have stable quality and price competitiveness against domestic wood and EU wood has gained a very positive reputation among Japanese importers and users. The Japanese feel that EU sawmills have a high capability to respond to the Japan market and trends.

Plywood imports increased 31.6% in the first half of 1999 but the market is still down due to Japanese overreaction to economic instability, Malaysian overproduction and the lowest number of housing starts in many years.

The JLIA believes MOC's new Housing Quality Assurance Law will force the Japanese industry to change dramatically to deliver a high-quality housing product to the Japanese consumer. The JLIA Chairman recognized that there was much that could be learned from the U.S. on these durability issues -- since he is aware that many homes in the U.S. are quite old yet still very comfortable.

JLIA noted three main reasons for the drop in imports from the U.S.

- North American industry consolidation disrupting supply.
- Booming North American housing market.
- Decrease in demand for green lumber (hemlock and others) and the change in the construction systems in Japan and the Housing Quality Assurance Law.

Builders used to specify certain species, now they are simply looking for quality and price to meet the new performance regulations. This will continue to impact the trading relationship and there is a hope that U.S. suppliers can meet the growing demand for kiln-dried lumber in Japan.

European lumber imports have benefited from a decrease in the extremely long lag-times for delivery. Northern Europe product will continue to increase market share in Japan as suppliers are perceived as willing and able to meet the Japanese need with exactly the quality and dimensions desired.

The U.S. industry gave an overview on the current global economic situation and provided the JLIA with detailed information about U.S. softwood, hardwood, panel, and engineered wood products, including production and consumption.

When asked about the JLIA position with regard to the ATL, JLIA Chairman Tanaka responded that, since JLIA was a private group of lumber importers with no government involvement, it would not be appropriate for them to make a comment on GOJ's position.

When asked whether Japanese industry had the capability or capital to build the number of kilns needed to supply the domestic market, JLIA Chairman Tanaka responded that it was still unclear whether the domestic industry, which has processing and facilities that are currently not cost-effective, would be in a position to supply the kiln dried lumber or whether they would have to rely on more imports.

NOTE: Directly following the JLIA meeting, the US industry hosted a reception for more than 150 Japanese. A complete list of invitees is attached to this report.

5. Ambassador Thomas Foley
October 22, 1999 -- 10:30 - 11:00 a.m.

Ambassador Foley gave mission members his view of the U.S.-Japan relationship. The loss of stature for the Japanese as a world economic power created an identity crisis which is now beginning to fade as the economy slowly recovers. This growing confidence will be critical over the coming year to see whether Japanese consumers begin to spend and restore economic strength outside of government-funded programs.

The U.S.-Japanese relationship is different than most any other diplomatic relationship around the world. The U.S. has always been far more explicit in making prescriptive policy demands to the Japanese than their other allies. Recent polling data shows that 78% of Japanese think that the U.S. is a reliable ally; most Japanese would like to get a U.S. education, and in general the Japanese have a positive view of security issues, and the general alliance and the American people. This has not always been the case -- in fact this poll showed a positive movement over the past three years.

Foley encouraged the delegation to continue its work noting that U.S. industry commitment and dedication to Japan was critical. Pursuit of the ATL is one of the Embassy's top priorities and he and the entire Embassy staff will continue to try to move the Japanese forward on these issues. Foley expressed the view that the Japanese would not change their minds on the ATL, and in fact, further entrenchment was likely to continue.

6. Ministry of Agriculture, Forestry and Fisheries
October 22, 1999 -- 11:30 - 12:30 p.m.

The U.S. delegation used this meeting to gain a better understanding of the MAFF position on the ATL. Director General, Sugata noted that of the total amount of wood used in Japan, only 20% was of domestic origin, a major shift from 40 years ago when over 90% was of Japanese origin. With regard to the ATL and any discussions and arguments on liberalization of the forest products sector, Sugata stated that the only thing the U.S. and Japan agree on is the need to "increase demand and consumption of wood products in Japan."

MAFF's argued that it must take all measures, including opposition to trade changes such as tariff elimination (as requested by the forestry sector), to "break the cycle of under-management and weak demand for forest products." Japan said it is currently "reviewing policies" on how to accomplish the reversal of the above "cycle."

Sugata maintained that environmental groups were making similar arguments as the Japanese Government and indicated that Japan would like to see the establishment of a trade rule in the WTO that allows each country to carry out policies that enable forest protection according to the needs of the public.

U.S. delegates noted that for the Japanese domestic industries for plywood and glulams, they source only 4% of their wood from Japan. Therefore, this is not a forestry protection issue; this argument is actually aimed at protecting Japanese manufacturers.

U.S. delegates asked how many jobs would be lost if tariffs were removed. MAFF indicated that it did not have that estimate but noted that there were 2.9 million forest owners in Japan and about 200,000 workers involved in processing industries.

MAFF is also questioning the future supply of kiln dried lumber which will surely increase given the Housing Quality Assurance Law. They did not know whether Japanese industry would be able to supply the kilns for the domestic need.

U.S. industry questioned MAFF about whether their forest policy review included looking at current species in the Japanese forests and exploring growth of alternative species which could be more easily managed, and also desired for use by the domestic industry. MAFF noted that they are looking at just these issues and would welcome any assistance in this regard from either the U.S. industry or U.S. Government.

**7. Judanren -- Federation of Housing Organizations
October 22, 1999 -- 2:00 - 3:00 p.m.**

Judanren's Executive Director, Mr. Ochi (former MOC Housing Production Division Director and Director of the Federation of Housing Organizations) reviewed how Japan's housing industry was reacting to the market's "Healthy House Theme" and new Housing Quality Assurance Act. Ochi's organization has both large and small companies and the industry looks at these themes as very positive for future growth of the housing market and consumer safety.

The Housing Quality Assurance Law was developed after the Hanshin earthquake of 1995 where so much destruction resulted from structurally defective workmanship. While large builders already carried a 10-year warranty program, the bulk of smaller builders do not, and the intent of the act is to kick "structurally defective" house construction out of the market and protect consumers' vested interest. Builders will be required to insure themselves. The cost for the warranty itself is 10% of the total value for the house.

Judanren has been taking the lead in developing guidelines for the "healthy house". The Healthy House Research Council has focused particularly on formaldehyde emissions, which are generally thought to be the most harmful to humans. Japanese consumers are demanding that builders be able to objectively prove that the materials used in the homes are safe. Since March, Judanren has been having talks with the producers to come to some agreement on these guidelines. He noted that since tatami is air-permeable, that sub-flooring must also meet these standards, as should all built-in furniture and fixtures. In cases where there is some coating for the furniture, a lower grade would be acceptable. Major housing companies will subscribe to these measures - however since the industry is so large, it will be impossible to claim 100% compliance.

In response to the Housing Quality Assurance Law, Judanren members have joined the Organization for Housing Warranty. That group will be able to assist the small to medium sized builder meet the warranty requirements as the larger companies will be able to provide their own warranties.

There was almost no opposition from the builders with regard to the installation of the warranty requirements.

**8. Ministry of Foreign Affairs
October 22, 1999 -- 3:30 -4:15 p.m.**

AF&PA representatives: Betsy Ward, Kris Marceca, Paul Boardman.

U.S. Embassy Representative: Mas Nagahama

MOFA hosts: Mr. Junichi Ihara, Director-Int'l Organizations Section, Mr. Tomoaki Ishigaki, Staffer from Ihara's group.

U.S. industry asked MOFA to clarify their strategy for tariff elimination of forest products in Seattle and the coming ATO Round.

MOFA gave AF&PA a paper presented by Prime Minister Obuchi to WTO Director-General Moore during their Tokyo meeting earlier that week stating Japan's official position on this issue.

Ihara's made two main points:

- o A meeting held that morning, involved Japanese lawmakers, GOJ officials (MAFF/MITI/MOFA) and domestic "agriculture and fisheries" industry groups to stress that Japan would not oppose tariff negotiations on forest products under a WTO Round as long as other GOJ-proposed issues and concerns (i.e. environmental concerns, resource sustainability) associated with tariff issues are addressed. Ihara reiterated that the Government of Japan is opposed to discussion of only tariff rates without due consideration of these other issues, and GOJ's position is very firm on this point.
- o Ihara quoted the MAFF position as one of extreme skepticism and precaution about giving away too many concessions all at once. This concern on MAFF's part was well founded, said Ihara, because of their earlier experiences during the Uruguay Round where MAFF was asked for concessions 3 times during the round ; once at the outset, once during the talks in progress, and finally toward the end of the round.

RECOMMENDATIONS:

Mission members met for a debrief and agreed to consider the following areas of improvement for next years' team:

- * Meet with a Post and Beam group. Zenkenren was mentioned.
- * More private company meetings to get business opinion leader's views: For example, a Misawa Homes to talk about their response to The Performance Based standards, etc. Also a wholesaler to talk about changing distribution. Maybe Tostem to talk about the new Insurance and Inspection system being implemented on a private level.
- * More active recruiting of US CEOs and company people.
- * JLIA presentation slides and handouts translated into Japanese. Units in Cubic Meters, Yen, etc.
- * Early and active input on the part of all the mission members for topic/agenda review, etc.