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Innovation: A New Focus for US-Japan Economic Cooperation

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In their April 30 statement outlining a new joint vision for US-Japan relations, President Barack Obama and Prime Minister Yoshihiko Noda advanced the goal of “enhancing economic growth and prosperity” through cooperation on “innovation, entrepreneurship...and science and technology.” This statement includes a wide range of commitments to expand existing engagement and initiate new developments in sectors driven by innovation, ranging from clean energy to space and cyber security. While emphasis in Washington and Tokyo often centers on the security aspects of the US-Japan relationship, opportunities to jointly develop and lead on innovation, entrepreneurship, science and technology should not be overlooked. Heightening focus on this area within US-Japan economic relations holds exciting potential for deepening ties as both countries work to meet shared challenges amidst an increasingly competitive global environment.

Sean Connell, Council on Foreign Relations-Hitachi Fellow at the Research Institute of Economy, Trade and Industry, Tokyo, explains that “While emphasis in Washington and Tokyo often centers on the security aspects of the US-Japan relationship, opportunities to jointly develop and lead on innovation, entrepreneurship, science and technology should not be overlooked.”

Turning Japan’s Innovation Capabilities into Growth: There is broad consensus that innovation is a primary driver of productivity and growth, generating new employment along with broader social and public benefits. In recent years both governments have made innovation a centerpiece of their respective domestic policies to boost job creation and economic revitalization. The Obama administration’s *Strategy for American Innovation* and the Japanese government’s “Innovation 25” agenda and “New Growth Strategy” take comprehensive approaches towards advancing innovation-driven growth. These include upgrading research, strengthening physical and digital infrastructures, investing in education, and developing policies to encourage breakthroughs for national strategic priorities.

While Japan is globally renowned as a leader in innovation concerning research and development (R&D) capabilities, policymakers continue to grapple with how to most effectively unleash these assets to support future prosperity—especially following two decades of stagnant growth and predicted future demographic decline. Policies once successful in promoting new growth sectors may no longer be effective or sustainable due to disruptive new technologies, leaps by regional competitors, and domestic fiscal and political constraints. One challenge facing Japan is what is widely regarded as a risk-averse and burdensome environment for entrepreneurs—who play an important role in bringing innovative technologies and services to market. Compared with other advanced economies, Japan has a relatively low entry and exit rate for new enterprises—an important indicator of innovative activity. Moreover, surveys show lower positive attitudes in Japan about starting a new business compared to the United States.

Trade and foreign direct investment are also significant drivers of innovation, bringing new technologies and knowledge across borders, and in turn spurring increased competition and development. However, Japan continues to have the lowest stock of inbound FDI among OECD member countries, and comparatively high regulatory and other non-tariff barriers to imports.



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Recent data on Japan’s economic performance during the last twenty years indicates the potential for boosting Japan’s innovation and growth strategies by addressing these constraints. A 2010 American Chamber of Commerce in Japan study found that from 1996 through 2006 foreign-owned companies in Japan and newly established Japanese firms were the only two groupings that consistently increased employment on a net basis. These and other challenges to Japan’s innovation and growth agenda are well recognized by Japanese policymakers and stakeholders, and are not unique to Japan. Overcoming them requires creative approaches, towards which end cooperative activities with the United States could present opportunities.

Innovation in the Bilateral Economic Relationship: The United States and Japan share a long history of co-evolution of innovation policies, going back to Japan’s rapid modernization during the Meiji Era. During the 1980s the United States focused attention on the perceived comparative strengths of Japan’s innovation system to identify strategies to improve American competitiveness, including *kaizen* (“continuous improvement”) production methods, Japan’s education system, and government-industry cooperation on R&D. More recently, Japan has introduced measures modeled on US initiatives successful in encouraging the commercialization of innovative technologies. These include the Small Business Innovation Research (SBIR) program and Bayh-Dole Act, both of which encourage private-sector commercialization of innovations derived from federally-funded research, including through university-industry collaboration. Furthermore, the success of US high-tech industry clusters such as Silicon Valley remains influential in discussions in Japan on encouraging new growth sectors and regional development. Moreover, both countries are increasingly finding converging interests in ensuring strong intellectual property protections and combating trends of economic nationalism, as competition in the Asia-Pacific region intensifies and emerging economies seek to boost their capabilities.

Opportunities for Cooperation: Initiatives listed in the April joint statement build upon extensive US-Japan cooperation around innovation, entrepreneurship, and science and technology at the government, private-sector, university and research institute levels. While too numerous to list all here, several offer potential channels through which the two countries could pursue new, creative approaches for collaboration. At the government level, frameworks including the Economic Harmonization Initiative and Internet Economy Dialogue offer platforms for working together to cultivate an environment most conducive to flows of trade and FDI that can foster innovation. Together with other forums like the Innovation and Entrepreneurship Dialogue, these provide opportunities to share best practices and experiences from broader national policies to strengthen key elements of the innovation infrastructure. Multilateral frameworks including APEC, international standards-setting bodies, and potentially the Trans-Pacific Partnership negotiations are other important venues for cooperation. These include removal of constraints for US and Japanese businesses to bring new technologies and services to global markets via improving regulatory coherence and transparency, aligning standards, and simplifying rules.

There is also strong potential for greater cooperation at the sub-national level. Hawai‘i and Okinawa are undertaking cooperative activities on clean energy, including evaluating and exchanging information on smart grid demonstration projects. A goal of this initiative is to develop systems that could be deployed to other remote communities. This offers a model for local governments to partner in harnessing innovation-focused solutions for community needs and growth, particularly as Japan works to revitalize the economy of the Tohoku region devastated by the March 11, 2011 earthquake.

Finally, there are vast networks linking people and institutions across both countries—from businesses to universities to civic and professional organizations—through which activities to foster innovation, entrepreneurship, and deployment of new technologies are already occurring. These networks are an incredible resource that could be further leveraged to encourage cooperation. Collectively, these dialogues, initiatives, and linkages should be viewed as elements of a comprehensive US-Japan agenda for partnership in innovation and growth, offering untapped possibilities for synergies and increased cooperation well into the 21st century.

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