Title:
Buying Into Japanese And German Exporters

Word Count:
650

Summary:
With the euro down nearly 15% this year and at a two-year low against the U.S. dollar, the world’s largest exporting nation is worth a good look. So is another country that has thriving exports in spite of a stronger currency. We’re talking about Japan and Germany, respectively, the world’s second- and third-largest economies.

The top lines at leading German industrial companies are rolling in with impressive numbers for an almost zero-growth economy. Quarterly sales at S...

Keywords:
etf, ishares, investment newsletter, investor newsletter, investing Japan, investing germany

Article Body:
With the euro down nearly 15% this year and at a two-year low against the U.S. dollar, the world’s largest exporting nation is worth a good look. So is another country that has thriving exports in spite of a stronger currency. We’re talking about Japan and Germany, respectively, the world’s second- and third-largest economies.

The top lines at leading German industrial companies are rolling in with impressive numbers for an almost zero-growth economy. Quarterly sales at Siemens rose 13%, the fastest since 2003. BMW’s sales rose by 11% in the third quarter, although high raw-material costs and pricing pressure resulted in weak net profits. A bright spot is Asia, where BMW expects to sell 150,000 cars per year by 2008.

Overall, German exports are up for the third-straight month and sales to countries outside of the European Union rose 18% annually from a year earlier. Clearly, the Germans are good at making stuff and selling it to the world, and the weaker euro is helping spur growth. Germany’s DAX stock index is taking notice and is up nearly 20% year-to-date.

Meanwhile, U.S. exports are up a paltry 2% since 2000. Although exports to China are up 35% during this same period, Americans are now buying seven times more from China than we are selling to them. A good reason why is that, according to research by Morgan Stanley's Stephen Roach, consumer spending represents 71% of America’s gross domestic product. The figure is 42% for China and 55% for Japan.

Speaking of Japan, the aftermath of the financial bubble has obscured the fact that it too, remains an exporting powerhouse, despite a currency that has risen more than 20% since 2002 and 13% this year alone. Just look at Japan’s current account surpluses over the past three years: $113 billion in 2002, $136 billion in 2003 and $172 billion in 2004. China is a major market, and despite political difficulties, bilateral trade between China and Japan now exceeds trade between Japan and America.

A majority of Japan’s exports are manufactured goods and components. Fifty percent of its exports to China in 2004 were electrical equipment and machinery, and its top exports to the world include autos, electronic components, optical instruments, imaging equipment and computer parts.

Much is made over China’s huge trade imbalance with America, which reached $126 billion in the first eight months of this year. No doubt a sizable share of Chinese exports to America are chock full of Japanese components. While some of these components were made in offshore facilities, many were made in Japan, which has been able to hold on to its industrial base better than America.

How do they do it? First, the Japanese are continually moving up the value-added curve and are careful to keep the R&D and manufacturing of sophisticated components close to home, while outsourcing the low-end to low-wage countries.

Secondly, even though China’s wages are about 5% of Japan’s, factory automation has lessened the importance of labor costs. For advanced high tech products, it accounts for only 10% to 15% of total costs. Having manufacturing closer to home also shortens new product lead times and increases cooperation between R&D and production teams leading to a crucial edge in staying ahead of its nimble competitors. Supply lines of 2,000 miles can be problematic.

Perhaps most important, there is the critical issue of protecting intellectual capital. Having research, development and production closer to headquarters better protects proprietary technologies.

Canon, Sharp, Hitachi, NEC and Toyota are all good plays on Japan’s manufacturing edge, while Sony will continue to lag until it boosts its R&D and catches up in product development.

The iShares MSCI Japan Index exchange-trade fund is an attractive option, since it has about 50% exposure to Japan’s manufacturing sector with an annual expense ratio of only 0.59%. Similarly in Germany, the iShares MSCI Germany Index is loaded with that country’s top exporters and would be an excellent proxy for overall German export growth.